Between the lines...

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I. Corporate Insolvency Resolution can be initiated against a struck-off company

The National Company Law Appellate Tribunal (**"NCLAT"**) in ***Mr. Hemang Phophalia v. The Greater Bombay Co-operative Bank Limited and Another*** *(decided on September 05, 2019)* has held that a creditor can file an application requiring the restoration of the name of a dissolved/struck-off company in the register of companies for initiating a Corporate Insolvency Resolution Process (**"CIRP"**) against the said company.

Facts

The Greater Bombay Co-operative Bank Limited (**"Financial Creditor"**) filed an application under Section 7 of the Insolvency and Bankruptcy Code, 2016 (**"IBC"**) to initiate CIRP against Penguin Umbrella Works Private Limited (**"Corporate Debtor"**). National Company Law Tribunal, Mumbai Bench (**"NCLT, Mumbai"**) admitted the said insolvency application. An appeal was filed against the said order by Mr. Hemang Phophalia, Ex-Director and Shareholder of the Corporate Debtor (**"Appellant"**) as the name of the Corporate Debtor was struck-off from the register of companies and insolvency proceedings could not be initiated against a dissolved company.

Issue

Whether an application under Section 7 or 9 under IBC for initiating CIRP is maintainable against a Corporate Debtor, if the name of the Corporate Debtor is struck-off from the register of companies?

Arguments

Counsel appearing on behalf of the Appellant submitted that the name of the Corporate Debtor was struck-off from the register of companies under Section 248 of the Companies Act, 2013 (**"Companies Act"**), therefore, an application

under Section 7 of IBC against a non-existent company is not maintainable. It was further submitted that in view of initiation of the CIRP, the resolution professional will ask the Appellant, ex-Director and others to handover the records and assets of the Corporate Debtor, which are not available. It was also submitted that the Corporate Debtor is non-functional since a number of years. The Corporate Debtor does not have any assets or any employees. Therefore, the resolution professional cannot make the Corporate Debtor a going concern. Accordingly, the application under Section 7 is not maintainable.

The arguments of the respondent have not been provided in the judgment.

Findings of the NCLAT

NCLAT reproduced the relevant provisions of the Companies Act which deal with removal of names of companies from the register of companies as provided in Chapter XVIII of the Companies Act. As per Section 248(6) of the Companies Act, before passing an order to remove the name from the register of companies, the Registrar is to satisfy himself that sufficient provision has been made for realization of all amount due to the company and for the payment or discharge of its liabilities and obligations within a reasonable time and, if necessary, obtain necessary undertakings from the managing director, director or other persons in charge of the management of the company. As per the proviso thereof, notwithstanding the undertakings referred to in Section 248(6) of the Companies Act, the assets of the company are to be made available for payment or discharge of its liabilities and obligations even after the date of the order removing the name of the company from the register of companies. From Section 248(7) of the Companies Act, it is also clear that the liability, if any, of every director, manager or other officer who was exercising any power of management, and of every member of the company which is dissolved, shall continue and may be enforced as if the company had not been dissolved. Further, Section 250 of the Companies Act, also provides that after removal of the name of the company from the register of companies for the purpose of realizing the amount due to the company and for the payment or discharge of the liabilities or obligations of the company, the company shall not cease to be operational.

As per Section 252(3) of the Companies Act, if a company, or any member or creditor or workman thereof feels aggrieved by the company having its name struck off from the register of companies, the ***tribunal*** on an application made by the company, member, creditor or workman before the expiry of twenty years from the publication in the Official Gazette of the notice under sub-section (5) of Section 248, may, if satisfied that the company was, at the time of its name being struck off, carrying on business or in operation or otherwise it is just that the name of the company be restored to the register of companies and the tribunal may give such other directions and make such provisions as deemed just for placing the company and all other persons in the same position as nearly as may be as if the name of the company had not been struck off. The NCLAT held that the ***tribunal*** is the ***adjudicating authority*** in terms of Section 60(1) of the IBC. Hence, on one side it plays role of ***adjudicating authority*** and on the other, ***tribunal,*** under the Companies Act. Therefore, if an application is filed by a creditor (be it a financial creditor or an operational creditor) or workman (operational creditor) before the expiry of twenty years as prescribed, it is open to the adjudicating authority to give such directions and make such provisions as deemed just for placing the name of the

company and all other persons in the same position nearly as may be as if the name of the company had not been struck off. The name of the Corporate Debtor may be struck-off, but the assets may continue. In such a case and in view of the provisions of the Companies Act, the NCLAT held that the application under Sections 7 and 9 of the IBC will be maintainable against a company, even if the name of the company has been struck-off.

Decision of the NCLAT

Adjudicating authority which is also the tribunal is empowered to restore the name of a company and all other persons in their respective position for the purpose of initiation of CIRP under Sections 7 and 9 of the IBC based on the application, if filed by the creditors or workmen within twenty years from the date as prescribed under the provisions of the Companies Act. In the present case, the application under Section 7 was admitted, the Corporate Debtor and its directors, officers, etc. were deemed to have been restored.

VA View

Several companies opt for de-registration by removing their name from the register of companies instead of undergoing the protracted process of winding up. In order to successfully remove their name from the register of companies, the conditions of Section 248 of the Companies Act need to be complied with. Most importantly, the Registrar of companies needs to be satisfied that sufficient provisions have been made for the payment or discharge of all the liabilities of the company. Nevertheless, the Companies Act keeps the liability of directors, managers or other officers who were exercising any power of management and of every member of the company alive. Furthermore, Section 252(3) of the Companies Act also allows any aggrieved member, creditor or workman of the company to make an application to reverse the removal of the name of the company from the register of companies before the expiry of twenty years as prescribed in the Companies Act. The tribunal is required to exercise its discretion and be satisfied on one of these two counts for such an application to succeed (a) the company was at the time of striking off carrying on business or in operation or (b) it would be just that the company is restored.

In the present case, it was decided that the NCLT has been accorded the role of a ***tribunal*** under the Companies Act and the ***adjudicating authority*** under the IBC. Hereunder, NCLT, Mumbai considered it just for the purpose of initiation of the CIRP by the Financial Creditor against the Corporate Debtor to restore the name of the said Corporate Debtor in the register of companies. Therefore, this decision settles two important issues, namely: (1) applications under Section 252(3) of Companies Act for restoring the name of a struck-off company to initiate IBC proceedings against the said company is permissible; (2) creditors seeking to initiate CIRP against a dissolved debtor would not be required to first make an application for restoring the name of the dissolved company and then approach the NCLT for initiation of IBC proceedings; both can be done by way of a single application before the concerned NCLT.

II. Additional Evidence may be adduced under Section 34 of Arbitration and Conciliation Act only in exceptional circumstances

The Supreme Court in ***M/s. Canara Nidhi Limited v. M. Shashikala and Others*** *(decided on September 23, 2019)* held that in proceedings under Section 34 of the Arbitration and Conciliation Act, 1996 (**"Act"**), additional evidence can be permitted to be adduced only in exceptional circumstances.

Facts

M/s. Canara Nidhi Limited (**"Appellant"**) is a financial institution that had advanced a secured loan to M. Shashikala, (**"Respondent"**), the agreement of which was subject to an arbitration clause. On failure to repay the loan, the matter was referred to arbitration. Before the arbitrator, both the parties adduced oral and documentary evidence and an award was passed in the favor of the Appellant. In the Application under Section 34 of the Act in the Court of District Judge, Mangalore, the Respondent filed an application under Section 151 of the Civil Procedure Code (**"CPC"**) to permit the Respondent to adduce evidence against which the Appellant filed objections. The District Judge dismissed the application holding that there was no necessity of adducing fresh evidence and the grounds urged can be met by perusing the records of the arbitration proceedings.

The Respondent then filed writ petitions before the Hon'ble Karnataka High Court under Articles 226 and 227 of the Constitution of India, which relying on the decision in ***Fiza Developers and Inter-Trade Private Limited v. AMCI (India) Private Limited and Another [(2009) 17 SCC 796]*** (**"Fiza Developers"**) set aside the order of the District Judge, and directed the Judge to "recast the issues", allowing the Respondent to file affidavits of their witnesses and allow their cross-examination. Aggrieved by this judgment, the Appellant moved a Special Leave Petition before the Supreme Court.

Issue

Whether in an application under Section 34 of the Act seeking to set aside the arbitration award, the parties can adduce evidence to prove any of the specified grounds under sub-section (2) of Section 34 of the Act?

Arguments

The Appellant submitted that proceedings under Section 34 of the Act is summary in nature with a limited scope, and the validity of the award has to be decided on the basis of materials produced before the arbitrator, with no scope for adducing fresh evidence before the court. Further, the High Court misread the ratio of the Supreme Court in Fiza Developers, and in any event, no exceptional grounds for permission to lead fresh evidence in the proceedings under Section 34 were made out. Additionally, the High Court has erred in interfering with the order passed by the trial court.

The counsel for the Respondent reiterated the finding of the High Court and submitted that in order to prove the grounds stated in the application filed under Section 34, adducing additional evidence is necessary. It was submitted

that the scope of enquiry in the proceedings under Section 34 is restricted to a consideration whether any of the grounds mentioned, *inter alia,* in Section 34(2) were made out. The Respondent sought to adduce evidence to prove the grounds enumerated under Section 34(2)(a) of the Act as they were specific and therefore, necessarily need an opportunity to adduce evidence to plead and prove the grounds.

Further, the counsel for the Respondent submitted that in view of Rule 4(b) of the High Court of Karnataka Arbitration (Proceedings before the Courts) Rules, 2001, all the proceedings of the CPC shall apply to such proceedings filed under Section 34 of the Act, insofar as they could be made applicable.

Observations of the Supreme Court

The Hon'ble Supreme Court first pointed out that the Rule 4(b) of the Karnataka High Court Arbitration Rules are only procedural, and the Supreme Court in Fiza Developers made it clear that there is no wholesale or automatic import of all the provisions of the CPC into the proceedings under Section 34 of the Act as that will defeat the very purpose and object of the Act. It then considered the dicta in Fiza Developers which concerned whether the issues as contemplated under Order XIV Rule 1 of CPC should be framed in the application under Section 34 of the Act. The Court came to the conclusion that such framing of issues was not required in a Section 34 application, which proceeding is summary in nature. However, an opportunity to the aggrieved has to be afforded to prove the existence of any of the grounds under Section 34(2) of the Act, thus, allowing the filing of the affidavits.

The Supreme Court however, then observed that subsequent to the decision in Fiza Developers, section 34 was amended by Act 3 of 2016 adding sub-sections (5) and (6) that specified the time period of one year for the disposal of the application under Section 34. Additionally, noting the inconsistent practices subsequent to the Fiza Developers judgment, the Justice B. N. Srikrishna Committee suggested an amendment to Section 34(2)(a) of the Act substituting the words *'furnishes proof that'* with the words *'establishes on the basis of the Arbitral Tribunal's record that',* which was implemented by the Arbitration and Conciliation (Amendment) Act, 2019.

The Supreme Court then relied on its judgment in ***Emkay Global Financial Services Limited v. Girdhar Sondhi [(2018) 9 SCC 49]*** (**"Emkay"**) which stated that the Fiza Developers judgment must now be read in light of the amendments made in Section 34(5) and 35(6) of the Act, and noted that speedy resolution of arbitral disputes is the object of the Act and its amendments. Therefore, *"if issues are to be framed and oral evidence taken in a summary proceeding under Section 34, this object will be defeated."*

The Supreme Court in relying on Emkay thus, concluded that *"Section 34 application will not ordinarily require anything beyond the record before the arbitrator and that cross-examination of persons swearing in to the affidavits should not be allowed unless absolutely necessary."*

On applying the established principles, the Supreme Court concluded that there are no specific averments in the affidavit filed under Section 151 of the CPC as to the necessity and relevance of the additional evidence sought to be adduced. It did not indicate the aim of adducing additional evidence or state the specific documents or evidence required. Additionally, considering the objective of the Act, the summary nature of proceedings, and the fact that

parties had sufficient opportunity to adduce oral and documentary evidence, the Supreme Court noted that the grounds urged in the application can very well be considered by the evidence adduced in the arbitration proceedings, and that the Respondents have not made out grounds that it is an exceptional case to permit them to adduce evidence.

Further, the High Court directions amount to retrial on the merits of the issues decided by the arbitrator, and the High Court in exercise of its supervisory jurisdiction under Articles 226 and 227 of the Constitution, ought not to have interfered with the order of the District judge, when it did not suffer from perversity.

Decision of the Supreme Court

Allowing the appeals, the order passed by the High Court was set aside and the order of the District Judge was affirmed. The District Judge was directed to dispose of the application under Section 34 of the Act, expeditiously in accordance with law.

VA View

The Supreme Court has maintained the sanctity of the arbitration process by unconditionally stating the principle of "exceptional circumstances" to be applied to applications under Section 34 of the Act, in order to adduce additional evidence at that stage. Although the Supreme Court has not clearly enunciated what the principles of exceptional circumstances are, it has created ample safeguards by holding that the grounds under Section 34(2) of the Act will have to be proved from the record of the arbitral tribunal, and the need for new evidence to prove these grounds is an untenable submission. It has been further clarified that a summary procedure shall be applicable to Section 34 applications, and as the CPC does not strictly apply to such proceedings, leading evidence would be a matter of exception. Extraordinary factual circumstances will have to be demonstrated for this exception to be allowed by the courts.

III. NCLAT: Dissenting financial creditors cannot be discriminated against in a resolution plan

The National Company Law Appellate Tribunal (**"NCLAT"**) has, in the case of ***Hero Fincorp Limited v. Rave Scans Private Limited and Others*** *(dated September 17, 2019)* held that dissenting financial creditors cannot be discriminated against in a resolution plan.

Facts

Corporate Insolvency Resolution Process (**"CIRP"**) was initiated against Rave Scans Private Limited (**"Rave Scans"**) on January 25, 2017. Accordingly, on October 17, 2019, the National Company Law Tribunal, Principal Bench, New Delhi approved a revised resolution plan submitted by Mr. Rahul Jain, which was earlier passed by Rave Scan's committee of creditors which had approved the resolution plan with 78.55% of the votes in favour of the same. However, Hero Fincorp Limited (**"Hero Fincorp"**), which was a secured financial creditor of Rave Scans, challenged

the approval of the revised resolution plan before the NCLAT. Hero Fincorp stated that the revised resolution plan submitted and approved is discriminatory, as it treats similar creditors differently.

Issue

Whether the revised resolution plan submitted is discriminatory in nature against Hero Fincorp?

Arguments

The Appellant argued that Hero Fincorp, despite being a secured financial creditor, was discriminated against with respect to similarly situated secured financial creditors. It was argued that the other similarly situated secured financial creditors were provided with a higher percentage of their claim amount, whereas Hero Fincorp was provided with a lower percentage of the same.

The Respondent argued that the resolution plan in question was passed by 78.55% of the votes in favour of the same by the committee of creditors in its meeting held on March 13, 2019. Further, it was argued that as per the resolution plan, the successful resolution applicant has offered upfront payment of INR 54 crores as against the asset value (liquidation value) of INR 36 crores. Therefore, the amount payable to Hero Fincorp vide the revised resolution plan was higher than the liquidation value, which is the estimated realizable value of the assets of Rave Scans.

Observations of the NCLAT

The NCLAT perused the statement of settlement of the dues of the stakeholders and observed that Hero Fincorp has been provided with 32.34% of its claim, ostensibly because it has dissented with the revised resolution plan. It was also observed that other secured financial creditors have been provided a higher percentage of their claims. To illustrate the same, Tata Capital Financial Services Limited has been provided with 75.63% of its admitted claim and other financial creditors such as Indian Overseas Bank has been provided with 45% of its admitted claim, the Bank of Baroda was provided with 45% of its admitted claim and the Punjab National Bank has been provided with 45% of its admitted claim.

It was observed, that the Insolvency and Bankruptcy Board of India (Insolvency Resolution Process of Corporate Persons) (Fourth Amendment) Regulations, 2016, amended the provisions of Regulation 38 of the Insolvency and Bankruptcy Board of India (Corporate Insolvency Process of Corporate Persons) Regulations, 2016 (**"CIRP Regulations"**). Prior to the above amendment, Regulation 38(1)(c) of the CIRP Regulations stated that the resolution plan shall identify specific sources of funds that will be used to pay the liquidation value due to dissenting financial creditors and provide that such payment is made before any recoveries are made by the financial creditors who voted in favour of the resolution plan.

However, pursuant to the NCLAT's decision in the case of ***Central Bank of India v. Resolution Professional of the Sirpur Paper Mills Limited and Others*** *(dated September 12, 2019),* where it was held that no discrimination can be made between the financial creditors in the resolution plan on the ground that one has dissented and voted

against the resolution plan or the other has supported and voted in favour of the resolution plan, the Insolvency and Bankruptcy Board of India (Insolvency Resolution Process of Corporate Persons) (Fourth Amendment) Regulations, 2016 was passed, which deleted the above-mentioned Regulation 38(1)(c) of the CIRP Regulations.

Reference was also made to the Hon'ble Supreme Court's decision in the case of ***Swiss Ribbons Private Limited and Others v. Union of India and Others*** *(dated January 25, 2019)* where it was observed that:

"the NCLAT has, while looking into viability and feasibility of resolution plans as approved by the committee of creditors, always gone into whether the operational creditors are given roughly the same treatment as financial creditors, and if they are not, such plans are either rejected or modified so that the operational creditors' rights are safeguarded."

It was then observed that Insolvency and Bankruptcy Board of India has not provided for separate treatment to dissenting secured financial creditors who do not vote in favour of the resolution plan, and that the amended Regulation 38 of the CIRP Regulations does not discriminate against similarly situated creditors on basis of their affirmative/ dissenting vote on the resolution plan.

Decision of the NCLAT

The NCLAT held that the revised resolution plan in its current form was discriminatory in nature and is violative of Section 30(2)(e) of the Insolvency and Bankruptcy Code, 2016. However, the NCLAT did not set aside the approved plan, but gave the successful resolution applicant the opportunity to remove the discriminatory provisions of the revised resolution plan and provide for payment of 45% of Hero Fincorp's claim. It was also stated that if the successful resolution applicant does not make the abovementioned change, within one month of this order of the NCLAT, the order of the NCLT dated October 17, 2018 approving the resolution plan shall be set aside.

VA View

This judgment correctly stated that a resolution plan cannot discriminate against a creditor merely on the basis of the vote they cast. Now, resolution plans will have to provide for similar treatment to creditors irrespective of their vote.

Interestingly, while the NCLAT directed the successful resolution applicant to repay 45% of Hero Fincorp's claim in order to equate it with the claims filed by Indian Overseas Bank, Bank of Baroda and Punjab National Bank, it did not direct any changes to the money payable to Tata Capital Financial Services Limited, who were given 75.63% of their claim. This indicates that the NCLAT only was concerned in addressing negative discrimination, as the judgment was silent on the reasons for providing one secured financial creditor a higher percentage of his claims as compared to the other financial creditors.

IV. Inter-corporate deposit to fall outside the ambit of 'deposit' under the Maharashtra Protection of Interest of Depositors (in Financial Establishments) Act, 1999

In the recent judgment of ***Mr. Ashish Mahendrakar v. State of Maharashtra and Others*** *(decided on September 13, 2019),* the Hon'ble Bombay High Court declared that an inter-corporate deposit/loan,that is, a loan advanced/deposit made by a company with another company would not amount to a "deposit" within the meaning and for the purpose of the Maharashtra Protection of Interest of Depositors (In Financial Establishments) Act, 1999 (**"MPID Act"**).

Facts

Birla Power Solutions Limited (**"Company"**) had accepted deposits from 2009 to 2013. Shri Hajarimal Somai Memorial Trust (**"Trust"**) on March 09, 2012 had made a deposit of INR 1 crore with the Company. The deposit was to be repaid along with an interest of 10.75% per annum. The date of maturity of the deposit was March 08, 2013. However, the Company defaulted in the repayment of the principal amount and the interest.

Thus, Bhagwan Suryakant Seth filed a first information report against the Company, the managing director and other directors. Accordingly, an investigation was conducted and a charge-sheet was prepared. In the said charge-sheet, Mr. Ashish Mahendrakar (**"Petitioner"**), one of the authorized signatories for the Company, who had executed important documents of the Company, had been indicted as accused number 11. MPID Special Case No. 4 of 2014 is pending before the special court (**"MPID Case"**).

In the meantime, the State of Maharashtra (**"Respondent"**), exercising its powers under Sections 4, 8 and 12 of the MPID Act, had issued two attachment orders dated March 19, 2016 and November 24, 2016. Further, a forensic audit was conducted with relation to the amounts accepted by the Company. The outstanding amount stated in the forensic audit included the amounts payable to the Trust.

Issue

Whether an inter-corporate deposit/loan registered under the provisions of the Companies Act, 1956 would amount to a deposit within the meaning and for the purpose of the MPID Act?

Arguments

The counsel appearing for the Petitioner contended that an inter-corporate deposit/loan would fall outside the purview of the MPID Act and would be governed by the Companies Act, 2013 (**"Companies Act"**) and its rules. The definition of 'deposit' under Section 2(c) of the MPID Act, if properly construed, does not include inter-corporate deposits. Further, the counsel for the Petitioner asserted that inclusion of the inter-corporate deposits in the outstanding amount of the forensic audit and the consequent attachment orders by taking into account the

outstanding amount is legally impermissible and therefore, requested the Bombay High Court to quash the names of the inter-corporate deposit holders/lenders from the list of depositors in the MPID Case.

The Petitioner submitted that the object of the MPID Act was to protect the interests of the public, that is, the middle class and poor people, from companies who would swindle their deposits by offering unprecedented higher rates of interests and awards. The aim of the MPID Act was not to govern inter-corporate debts or transactions. Secondly, the Petitioner submitted that inter-corporate transactions are regulated by the Companies Act. On the other hand, Chapter V of the Companies Act and the Companies (Acceptance of Deposits) Rules, 2014 (**"Rules"**) regulate the acceptance of deposits. In the definition of the term 'deposits' in the Rules, inter-corporate deposits have been specifically excluded. Lastly, it was stated by the Petitioner that since the Companies Act has been enacted by the central legislature, the provisions of the Companies Act, the rules framed thereunder, and other central legislations cannot be overridden by the provisions of the MPID Act, which has been enacted by the state legislature.

On the other hand, the counsel for the Respondent had submitted that the present matter lacked substance since the Petitioner did not have any locus to file the matter. This was because none of the attached properties were of the Petitioner. The Respondent further submitted, that the definition of 'deposits' in the MPID Act had an exhaustive list of exclusions and inter-corporate deposits was not part of this exclusion list. Therefore, MPID Act did govern inter-corporate deposits. Lastly, the Respondent had submitted that the purpose of the MPID Act was to provide an effective mechanism to help the investors, whether a corporate or non-corporate, who has been duped by the financial establishments.

Observations of the Bombay High Court

The Bombay High Court observed that the Petitioner was arraigned in the charge-sheet as an accused, and thus, the Petitioner did have locus to file the present matter. The Bombay High Court then reviewed the definition of 'deposit' as per the MPID Act, which stated that term deposit covers receipt of money or acceptance of any valuable commodity, except those which have been specifically excluded in the definition.

Further, the Bombay High Court observed that the statement of objects and reasons in a statute cannot determine the true meaning and effect of the provisions of such statute, but it may provide a gainful reference for understanding the background of the legislation, the state of affairs that preceded the enactment, the attendant and surrounding circumstances in relation to the statute and the mischief which the statute sought to curb.

The Bombay High Court relied on ***New Horizons Sugar Mills Limited v. Government of Pondicherry through Additional Secretary and Another [(2012) 10 SCC 575]*** wherein the Supreme Court dealt with issues of the

objects behind the enactment of, and the legislative competence to enact, the Tamil Nadu Act, the Maharashtra Act and the Pondicherry Act. The apex court had stated:

"In addition to the above, it has also to be noticed that the objects for which the Tamil Nadu Act, the Maharashtra Act and the Pondicherry Act were enacted, are identical, namely, to protect the interests of small depositors from fraud perpetrated on unsuspecting investors, who entrusted their life savings to unscrupulous and fraudulent persons and who ultimately betrayed their trust.

The three enactments referred to hereinabove, were framed by the respective legislatures to safeguard the interests of the common citizens against exploitation by unscrupulous financial establishments mushrooming all over the country. That is, in fact, the main object indicated in the Statement of Objects and Reasons of the three different enactments....We have to keep in mind the beneficial nature of the three legislations which is to protect the interests of small depositors."

The Bombay High Court thus observed, that MPID Act and the enactments passed by other state legislatures were to protect the interests of the depositors. On reviewing the MPID Act, no distinction had been made between a corporate and an ordinary deposit. Further, the term 'depositor' had not been defined under the MPID Act.

The Bombay High Court also observed that a corporate entity while making a business decision should have a feel of the financial market. The entity should weigh in a number of factors before making such a decision such as the creditworthiness of the other company, the business model of such company, the financial condition and the corporate structure and governance of the company. Moreover, the company should check whether such other company would be able to honour its financial commitment. A company, having key personnel should make an informed decision and should not be easily lured by a mere promise of higher percentage of return on investments. According to the Bombay High Court, this was the reason why inter-corporate deposits were excluded from the definition of deposits in the Companies Act and its Rules.

Another angle taken by the Bombay High Court was that if the corporate depositors are clubbed with other depositors as investors, then this would be detrimental to the small time depositors as, if such corporate depositor would compete with the small depositors and claim pari passu distribution, then the small depositors would be deprived of realization of their money to the full potential.

Decision of the Bombay High Court

The Bombay High Court held that an inter-corporate deposit/loan would not amount to a "deposit" within the meaning and for the purpose of the MPID Act. Thus, the petition was allowed and the inter-corporate loan for the proceedings leading to the MPID Case would not be taken into consideration for such proceedings.

VA View

The Bombay High Court has justly observed that the MPID Act is to protect the rights of the small investors, that is, the middle and poor class and not that of the companies, which are expected to make informed decisions after due diligence and not be easily lured by mere promise of high returns on investments unlike an unsuspecting small time depositor. The intent of the MPID Act is to protect the interests of small depositors, who invest their life's earnings and savings in schemes for making profit which are floated by unscrupulous individuals and companies, both incorporated and unincorporated. More often than not, the investors end up losing their entire deposits. Thus, the remedy provided by the MPID Act is for small investors and not for enforcement of rights of one corporate entity against another.

Further, Section 186 of the Companies Act provides for loan and investment by a company to another company. The remedy for a company having deposited in another company and where such company has failed to repay the depositor company, would be regulated by section 186 of the Companies Act and not the MPID Act.

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