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Between the lines...

A BRIEFING ON LEGAL MATTERS OF CURRENT INTEREST

KEY HIGHLIGHTS

* **Supreme Court:** Rents receivable can be assigned by a debtor to a creditor as actionable claim.

* **Supreme Court:** The constitutional validity of provisions of IBC pertaining to the personal guarantors upheld.

* **NCLAT:** An operational creditor who is a participant in meetings of the CoC has no right to seek a copy of the information memorandum.

* **Kerala High Court:** An insolvency application filed by satisfying the statutory procedural requirements and without any defects, gives effect to moratorium, and mere uploading of an application cannot be taken as filing of an application under Section 96 of IBC.

I. Supreme Court: Rents receivable can be assigned by a debtor to a creditor as actionable claim.

The Supreme Court, *vide* its judgment dated October 19, 2023, in the matter of ***Infrastructure Leasing and Financial Services Limited v. HDFC Bank Limited and Another [Civil Appeal No(s). 4708 of 2022]***, has held that rents receivable can be assigned by a debtor to a creditor as actionable claim and dismissed an appeal assailing the impugned order dated May 13, 2022 ("**Impugned Order**") passed by the National Company Law Appellate Tribunal, New Delhi ("**NCLAT**").

Facts

Housing Development Finance Corporation Limited ("**HDFC**") extended a credit facility of INR 400 Crores to Infrastructure Leasing and Financial Services Limited ("**ILFS**"/ "**Appellant**") by way of a sanction letter dated June 22, 2018. Further, a Master Facility Agreement ("**MFA**") was executed between HDFC and ILFS for securing the aforesaid credit facility. The MFA stipulated creation of an escrow account with HDFC Bank Limited ("**Escrow Bank**"/ "**Respondent**"). Further, an Assignment Agreement dated June 25, 2018 ("**Assignment Agreement**") was executed between HDFC and ILFS. In terms of the Assignment Agreement, HDFC and ILFS had agreed that the authorized indebtedness of ILFS as per MFA, by way of the aforesaid credit facility together with the interest thereon was payable from the gross income and revenue to be derived from the operation of their business centre services agreements/ lease /leave and license agreement(s). It was further agreed that 'all the receivables derived/ to be derived from the operation of the borrower's contracts, a sufficient portion of which, to pay the principal and interest as and when the same shall become due' in terms of the MFA was assigned and pledged and was 'set aside for that purpose on the same day'. Power of Attorney was also executed between HDFC and ILFS ("**POA**").

Further, pursuant to a petition filed on October 1, 2018 by the Union of India under Section 241 (*Application to Tribunal for relief in cases of oppression, etc.*) and Section 242 (*Powers of Tribunal*) of the Companies Act, 2013, the National Company Law Tribunal, Mumbai ("**NCLT**") had ordered to supersede the existing board of directors of ILFS. Consequently, a new board of directors was constituted to take charge of the affairs of ILFS. However, by a subsequent order dated October 12, 2018, NCLT had declined to grant moratorium sought by the Union of India, similar to moratorium in terms of Section 14 (*Moratorium*) of the Insolvency and Bankruptcy Code, 2016 ("**Code**"). Thereafter, by order dated October 15, 2018 ("**NCLAT Order**"), NCLAT had granted appropriate reliefs in the nature of moratorium. Inter alia, the aforesaid order included stay on any action to foreclose, recover or enforce any security interest created over the assets of ILFS or those of its 348 group companies as well as stay on the acceleration, premature withdrawal or other withdrawal, invocation of any term loan, corporate loan, bridge loan, commercial paper, debentures, fixed deposits, guarantees, letter of support, commitment or comfort and other financial facilities or obligations availed by ILFS and its 348 group companies.

By e-mail dated October 16, 2018, ILFS informed the Escrow Bank about the NCLAT Order. On October 19, 2018, HDFC instructed the Escrow Bank to transfer monthly instalments from the escrow account to HDFC's account. On October 23, 2018, ILFS informed HDFC about the NCLAT Order. Further, by letter dated October 27, 2018, ILFS called upon HDFC to reverse the debit of INR 6.24 Crores and credit the aforesaid amount back to ILFS. HDFC replied to the aforesaid letter addressed by ILFS, thereby stating that receivables (that is, rents) in respect of the secured property were assigned by ILFS in favour of HDFC and the asset ceased to belong to ILFS. Further, on January 4, 2019, ILFS

called upon HDFC to reverse the amount debited by the Escrow Bank in the escrow account. Thereafter, by order dated February 4, 2019, NCLAT directed the Union of India and ILFS to approach Justice (Retired) Mr. D.K. Jain to seek supervision on the operation of the resolution process. Thereafter, pursuant to restrain orders being sought against banks and financial institutions from debiting accounts of ILFS and its group entities, on August 8, 2019, NCLAT passed an order to the effect that if any bank/ financial institution has debited any amount in violation of NCLAT Order, it will be open to Union of India and/or ILFS to apprise Justice Mr. D.K. Jain and seek appropriate reliefs.

Pursuant thereto, ILFS made a representation before Justice Mr. D.K. Jain on August 28, 2019. Accordingly, Justice Mr. D.K. Jain issued show cause notices to HDFC as well as the Escrow Bank. In response to the show cause notice, the Escrow Bank stated that the receivables stood assigned in favour of HDFC and monies received were not the assets of ILFS. Thereafter, a personal hearing was granted to the parties, pursuant to which, on May 12, 2020, Justice Mr. D.K. Jain recommended the Escrow Bank and HDFC to maintain the status quo in the escrow account till a final view was taken on the application filed by ILFS. In view thereof, the Escrow Bank ceased to debit any amount from the escrow account. Thereafter, on July 3, 2020, Justice Mr. D.K. Jain passed a final order holding that the actions of HDFC and Escrow Bank in debiting the amount from the escrow account amounted to violation of the order passed by NCLAT and thus, HDFC and the Escrow Bank were directed to purge themselves within two weeks. In view of the aforesaid final order passed by Justice Mr. D.K. Jain, HDFC assailed the aforesaid order before NCLAT and sought the same be set aside. Whereas, ILFS sought direction from NCLAT that INR 112,79,18,348/- appropriated from its accounts towards debt service payments were in violation of the NCLAT Order as well as the final order passed by Justice Mr. D.K. Jain.

By the Impugned Order, NCLAT held that in so far as the amount of receivables deposited in the escrow account were sufficient to meet the principal and interest (payable by ILFS) assigned by the said borrower to HDFC, no proprietary interest continued with ILFS nor could it exercise any right over that part of the escrow account which was assigned. However, NCLAT did not accede to the contention raised by ILFS that there was no assignment of the receivables, but only the creation of security interest in the receivables. Further, NCLAT observed that since there was an express assignment of lease rental, sufficient to meet the principal and interest payments, the *"assignment has to be accepted as assignment"* in favour of HDFC and that pledge in the Assignment Agreement did not take away the nature of the transaction documents which was assignment. NCLAT further held that the NCLAT Order did not negate the Assignment Agreement nor did it take away the proprietary right of HDFC in the lease rental receivables. However, the right over receivables deposited in the escrow account to the extent they were in excess of principal and interest, was retained by ILFS and any amount in excess of the said principal and interest transferred to or debited in HDFC's account needed to be reversed, after adjusting the shortfall in debiting any interest or principal of any earlier months.

Aggrieved by the Impugned Order, ILFS approached the Supreme Court challenging the same.

Issue

Whether the credit facility and other ancillary loan documents executed by ILFS, pursuant to which rents payable to ILFS stood passed over to HDFC, amounts to assignment and stands outside the purview of an "asset" owned by ILFS.

Arguments

Contentions of the Appellant:

It was contended by the Appellant that MFA and other agreements executed between parties clearly indicate that the credit facility advanced to ILFS was loan repayable within 96 months. The security interest was created by ILFS and the receivables were in the nature of security for repayment of the aforesaid credit facility. Further, escrow account was created in the Escrow Bank for the purpose of facilitating the repayment of principal and interest as per the repayment schedule. However, there was no transfer of title in the receivables from ILFS to HDFC. Further, the Appellant emphasized upon the order passed by Justice Mr. D. K. Jain and submitted that HDFC and Escrow Bank were obliged to return the amount debited to the tune of INR 112,79,18,348/-.

Further, the Appellant argued that the Lease Rental Discounting facility ("**Lease Rental Discounting**") as relied upon by HDFC is a type of term loan offered with security of rental income. Further, none of the clauses from the relevant documents executed between parties contain any element or mention of the sale and purchase of the debt of ILFS. Hence, the aforesaid transaction is a loan transaction leading to creation of security interest and not a sale of debt at all.

Further, it was submitted that from the provisions of the Assignment Agreement and MFA, it is absolutely clear that receivables were charged in favour of HDFC only for securing the obligations of ILFS under MFA and for the purpose of facilitation of repayment and it did not amount to a transfer of the legal title over such receivables which continues to vest with ILFS.

Contentions of the Respondent:

It was contended by the Respondent that a bare reading of the transaction documents makes it clear that the facility extended to ILFS is a Lease Rental Discounting, which is significantly different from a traditional loan transaction. It was further submitted that a Lease Rental Discounting involves the assignment/ sale of the rent receivables by the landlord to the financing entity at a discounted value in terms of the transaction documents. Hence, the assigned receivables are the property of HDFC and ILFS has no right/ title or interest in the monies/ receivables/ amount deposited in the escrow account. It was submitted that the transaction is not covered within the purview of NCLAT Order, as it was restricted to the assets of ILFS, whereas assigned receivables pursuant to Lease Rental Discounting belong to HDFC.

Observations of the Supreme Court

The Supreme Court observed that by virtue of POA executed by ILFS on June 25, 2018, ILFS had irrevocably nominated, constituted and appointed HDFC as its true and lawful attorney on its behalf and that the relevant clauses of the POA enabled HDFC to *appropriate the proceeds received towards the discharge of the aforesaid facility* and *to receive all rents and all other sums in respect of such premises*.

Further, the Supreme Court relied upon a plethora of judgments including ***Yellapu Uma Maheshwari v. Buddha Jagadheeswararao [(2015) 11 SCR 849]*** and ***Assam Small Scale Industries Development Corporation Limited v. J.D. Pharmaceuticals [2005 Supp (4) SCR 232]*** to conclude that in order to understand the nature of transactions entered into between parties, the same has to be determined on the basis interpretation of the transaction documents in its entirety and the substance therein and not merely on the nomenclature given in the transaction documents.

In particular, the Supreme Court observed that Lease Rental Discounting is a new kind of financial agreement by which a banker allows credit facilities to a commercial property owner, whereby it can be ensured that the asset owner is given access to credit. In such an arrangement, a substantial portion or the entire rent or receivables which the owner would be entitled to are made-sold or assigned, absolutely to the creditor bank with the intention that the borrower's liabilities are discharged automatically from the proceeds payable in respect of the property. Considering that the owner is a debtor of the bank, the latter becomes the creditor of the tenant or the lessee as the case may be.

Further, the Supreme Court observed that the relevant clauses from the Assignment Agreement clearly set aside the rents payable to ILFS, in favour of the assignee, that is, HDFC. Further, relevant clause from the escrow agreement records that all receivables to which the borrower would be entitled would be deposited in the escrow account and further, that, the lessees or tenants of the properties owned by the borrower be instructed to pay such an amount in the escrow account itself. Furthermore, the escrow agreement authorizes only the lender (that is, HDFC) to instruct the Escrow Bank to transfer the amounts and permits the Escrow Bank to appropriate amounts towards adjustment arising out of the facility liability. Further, the POA categorically entitles HDFC to appropriate the proceeds deposited towards the discharge of the borrower's liability under the aforesaid facility. Hence, the bank/ lender virtually steps into the shoes of the borrower and by the terms of the POA is also authorized to let out the premises in case due to an unforeseen situation an existing lessee or tenant vacates it or is unable to pay.

Hence, basis conjoint reading of all relevant transaction documents and ascertaining their interpretation in its entirety, the Supreme Court arrived at the conclusion that parties intended assignment of debt, that is, the rents payable.

Further, the Supreme Court considered it necessary to determine as to whether such amounts payable on a future date are to be considered property and, therefore, capable of transfer. In this regard, it was observed that as per Section 5 (*"Transfer of property" defined*) of the Transfer of Property Act, 1882, all manner of property is capable of transfer. Furthermore, Section 6 (*What may be transferred*) of the Transfer of Property Act, 1882 provides as to what kinds of properties or actions are not transferable, that is, *personal claims* in the nature of tortious claims and *choices in action* cannot be transferred.

Thereafter, the Supreme Court analyzed the definition of actionable claims as envisaged under the provisions of the Transfer of Property Act, 1882 as well as Sections 130 (*Transfer of actionable claim*), 131 (*Notice to be in writing, signed*) and 132 (*Liability of transferee of actionable claim*) of the Transfer of Property Act, 1882 which deal with transfer of actionable claims. Upon in-depth analysis, Supreme Court arrived at the conclusion that rents receivable can be assigned by a debtor to a creditor as actionable claim.

Decision of the Supreme Court

In view of the submissions made by parties and the above-mentioned observations, Supreme Court held that in the present case, the rents payable by the tenants, lessees and licensees are debts, which stood transferred to HDFC.

Therefore, Supreme Court held that rents receivable can be assigned by a debtor to a creditor as actionable claim. In view of the aforesaid decision, the present appeal filed by ILFS stood dismissed.

VA View: The present judicial pronouncement rendered by the Supreme Court gives clarity on those issues which were unsettled and hence, are no more res integra.

More particularly, this judgment sets outs the precedent that when a borrower avails credit facilities and executes an assignment agreement by way of Lease Rental Discounting which is secured against the rent receivables from the property in question, would tantamount to transfer of right, title and interest in the rental amounts in favour of the lender and not merely creation of security interest. Therefore, Supreme Court has clarified that rents receivable can be assigned by a debtor to a creditor and the same shall come within the purview of actionable claim as per the provisions of the Transfer of Property Act, 1882.

II. Supreme Court: The constitutional validity of provisions of IBC pertaining to the personal guarantors upheld.

The Supreme Court, in its judgement dated November 9, 2023, in the matter of ***Dilip B. Jiwrajka v. Union of India and Others [Writ Petition (Civil) No. 1281 of 2021]*** (decided along with multiple other similar tagged-along writ petitions on similar legal issue), has upheld the constitutional validity of provisions of the Insolvency and Bankruptcy Code, 2016 ("**IBC**") pertaining to insolvency resolution process of personal guarantors.

Facts

In the present case, the constitutional validity of Sections 95 (*Application by creditor to initiate insolvency resolution process*), 96 (*Interim moratorium*), 97 (*Appointment of resolution professional*), 98 (*Replacement of resolution professional*), 99 (*Submission of report by resolution professional*) and 100 (*Admission or rejection of application*) of IBC were challenged *vide* three hundred and eighty-four petitions under Article 32 (*Remedies for enforcement of rights conferred by this Part*) of the Constitution of India ("**Constitution**"). The Supreme Court did not reproduce the individual facts of each case as it was deciding the constitutionality of the said provisions of IBC.

Notably, by way of background, in the matter of ***Lalit Kumar Jain v. Union of India [(2021) 9 SCC 321]***, the Supreme Court has, *inter alia*, held that the liability of a guarantor is not discharged merely on the discharge of the Corporate Debtor.

For the purpose of reference herein, Mr. Dilip B. Jiwrajka shall be referred to as the "**Petitioner**" and Union of India shall be referred to as the "**Respondent**".

Issue

Whether the provisions of Sections 95 to 100 of IBC are unconstitutional and violate the principles of natural justice.

Arguments

Contentions of the Petitioner:

It was submitted by the Petitioner that there must be determination of existence of debt by a judicial body before appointment of a resolution professional and an action initiated by the resolution professional.

Further, the Petitioner contended that an automatic interim moratorium should not commence upon filing of a petition under Section 95 of IBC.

Petitioner contended that the fundamental aspect as to whether the jurisdiction to entertain an application under Chapter III of Part III (*Insolvency resolution and bankruptcy for individuals and partnership firms*) of IBC exists, must be determined at the threshold by giving the debtor or personal guarantor an opportunity to be heard and that such jurisdictional question ought to be determined prior to appointment of resolution professional under Section 97(5) of IBC itself.

Further, Petitioner sought natural justice by a judicial body at the stage of Section 97(1) of IBC and it was contended that prior to the appointment of a resolution professional, without incorporating a requirement for a hearing before the adjudicating authority, Sections 95 to 100 of IBC would be arbitrary and violative of Article 14 (*Equality before law*) of the Constitution.

Contentions of the Respondent:

It was contended by the Respondent that adding an intermittent stage, as suggested by the Petitioner, for the adjudicating authority to decide a 'jurisdictional question' would result in the dislocation of the very scheme of IBC pertaining to observance of stringent timelines.

It was contended by the Respondent that the requirement of observing the principles of natural justice arises under Section 100 of IBC at the adjudicatory stage and not under Section 97 of IBC. Hence, the compliance pertaining to natural justice at a stage prior to Section 100 of IBC would result in dislocation of the entire scheme of IBC. Further, at the stage of an application under Sections 94 (*Application by debtor to initiate insolvency resolution process*) or 95 of IBC, no adjudication takes place. Additionally, no significant consequence on a debtor or personal guarantor takes place before the adjudication under Section 100 of IBC. Hence, there is no breach of natural justice under Chapter III of Part III of IBC.

Additionally, the Respondent submitted that the function of a resolution professional under Section 99 of IBC is not of adjudicatory nature as it does not bind the adjudicating authority. Rather the resolution professional's purpose under Part III of IBC is merely to collate the facts and submit a report along with recommendations to the adjudicating authority.

It was submitted by the Respondent that the object of corporate insolvency resolution process ("**CIRP**") under Part II (*Insolvency resolution and liquidation for corporate persons*) of IBC and in Chapter III of Part III of IBC is completely distinct as Part II of IBC deals with the resolution of corporate insolvency and Part III of IBC deals with the resolution and bankruptcy of individuals and partnership firms. Therefore, Chapter III of Part III of IBC has contemplated appointment of a resolution professional straightaway preceding the adjudicatory function by an adjudicatory body.

Respondent also submitted that a distinction exists between a moratorium under Section 14 (*Moratorium*) of IBC and an interim-moratorium under Section 96 of IBC as it is for the benefit of

guarantor or debtor and does not impose embargo on alienation of assets, legal rights or beneficial interest of the debtor.

Respondent submitted that the constitutional validity of a statute which the Parliament is competent to enact cannot be challenged on the basis an alleged ground of misuse of a provision in a particular case.

Observations of the Supreme Court

The Supreme Court while rendering its judgement divided the judgement into parts which are as follows:

Part I: Comparative Analysis of Parts II and III of IBC:

It was observed by the Supreme Court that the object of CIRP under Part II and in Chapter III of Part III of IBC is completely distinct in nature as Part II of IBC deals with insolvency resolution and liquidation for corporate entities. On the other hand, Part III of IBC deals with insolvency resolution and bankruptcy for individuals and partnership firms. Further, it was observed by the Supreme Court that there exists considerable difference in the provisions of Parts II and III of IBC relating to the role and functions of a resolution professional, even though both use the expression 'resolution professional'. Section 5(27) (*Definitions*) of IBC provides that a resolution professional, for the purposes of Part II, means an insolvency professional appointed to conduct the CIRP or the pre-packaged insolvency resolution process, as the case may be, and to include an interim resolution professional.

The role of Adjudicating Authority:

The Supreme Court was of the view that the resolution professional does not possess an adjudicatory function in terms of the provisions of Section 99 of IBC and there has been no provision made in Part III of IBC empowering the resolution professional to take over the assets or the business which is being carried on by the individual or the partnership. The role of resolution professional under Section 99 of IBC is that of a facilitator. The role of the resolution professional is purely recommendatory in nature and cannot bind the creditor, the debtor or the adjudicating authority.

The Supreme Court also noted that Section 14(1)(b) of IBC empowers the adjudicating authority to declare a moratorium restraining the transfer, encumbrance, alienation or disposal by the corporate debtor of any of its assets or any legal right or beneficial interest therein. Further, the moratorium under Section 14 of IBC operates on the order passed by an adjudicating authority whereas the purpose of the moratorium under Section 96 of IBC is protective in nature.

The Supreme Court in respect to the role of the adjudicating authority, held that after the submission of a recommendatory report by the resolution professional, the adjudicating authority's adjudicatory functions begins. Hence, the Supreme Court provided its observation pertaining to the role of the resolution professional, the imposition of the moratorium as well as the stage at which the function of the adjudicating authority comes into play, under Parts II and III of IBC.

Part II: Applicability of the principles of natural justice:

The Supreme Court analysed the ambit of Section 99(4) of IBC which is prefaced by the words "*for the purposes of examining an application*". It implies that when the resolution professional is empowered to seek information or explanation in connection with the application, such information or explanation must be relevant to and bearing a connection with the nature of the application itself. Such power to seek any information or any explanation is concerned with the nature of the application submitted under Sections 94 or 95 of IBC.

The right for filing such representation is sufficient compliance of the principles of natural justice which postulates the concept of *audi alterum partem*, that is, an opportunity of being heard to a person who is liable to be affected by an investigation, enquiry, proceeding or action. Therefore, the Supreme Court observed that the assertion by the Petitioner in relation to the violation of natural justice principle holds no merit.

Part III: Challenge to the constitutional validity of the provisions of IBC:

While interpreting Part II of IBC, the Supreme Court has drawn inference of the requirement for granting an opportunity to a debtor before initiating the insolvency resolution process against them. It was observed by the Supreme Court that Section 100 of IBC does not explicitly mention a hearing for a debtor. However, the requirement of a hearing for a debtor must be read into Section 100 of IBC. To support this observation, the Supreme Court held that in legal interpretation, when a statute is silent on a specific aspect, such as hearing, for which there is no explicit prohibition, the Supreme Court may imply or read in such a requirement. Therefore, the lack of explicit mention of a hearing in a provision does not automatically make it unconstitutional because such a requirement can be read into the statute.

The resolution professional in exercise of his duty under Section 99 of IBC may not embark on a roving enquiry into the affairs of the debtor or personal guarantor. The information sought by the resolution professional from the creditor, debtor, or third parties must be relevant to the examination of the application of insolvency resolution process. The Supreme Court observed that the proportionality test devised for privacy under Article 21 (*Protection of life and personal liberty*) of the Constitution is met by the virtue of vesting such powers in the resolution professional along with his duty to keep such information confidential. Additionally, the nature of the role of resolution professional, the powers of resolution professional, as well as its nexus with the legislation's legitimate aim also leads to the conclusion that the provisions of Sections 95 to 100 of IBC are compliant with Article 14 of the Constitution. Therefore, an adjudicatory decision-making process of the nature which has been suggested by the Petitioner would not be implicated under Section 97(5) of IBC, since to accept the submission of the Petitioner would render the provisions of Sections 99 and 100 of IBC otiose.

Decision of the Supreme Court

The Supreme Court held that at the stages envisaged under Sections 95 to 99 of IBC, there is no involvement of judicial adjudication. The resolution professional appointed under Section 97 of IBC serves a facilitative role of collating all the facts relevant to the examination of the application for the commencement of the insolvency resolution process which has been preferred under Sections 94 or 95 of IBC. Additionally, the report to be submitted to the adjudicatory authority is recommendatory in nature on whether to accept or reject the application.

The Supreme Court held that there is no violation of natural justice under Sections 95 to 100 of IBC as the debtor is not deprived of an opportunity to participate in the process of the examination of the

application by the resolution professional. The Supreme Court also held that until the adjudicating authority decides under Section 100 of IBC whether to accept or reject the application, no judicial determination takes place and the adjudicatory authority must observe the principles of natural justice while exercising its jurisdiction under Section 100 of IBC for the purpose of determining whether to accept or reject the application. The Supreme Court held that the purpose of interim-moratorium under Section 96 of IBC is to protect the debtor from further legal proceedings.

It was held by the Supreme Court that the provisions of Sections 95 to 100 of IBC are not unconstitutional as they do not violate Articles 14 and 21 of the Constitution.

VA View: In the present case, the Supreme Court highlights the underlying spirit of IBC which is concerned with observance of stringent time lines under IBC as time bound resolution of insolvency constitutes the heart and soul of the provisions of IBC. The Supreme Court in this case has analyzed the scheme of IBC in-depth in light of the constitutional validity of the provisions of IBC and with the backdrop of the principle of natural justice.

The Supreme Court has rightly highlighted the role and functions of an adjudicating authority and the purpose of the interim-moratorium under Section 96 of IBC. This judgement ultimately settles and puts an end to the questions being raised pertaining to the similar set of issues and challenging the constitutional validity of certain provisions of IBC.

Further, on account of the present batch of writ petitions being sub-judice before the Supreme Court and status quo order of the Supreme Court in some of these writ petitions, the Adjudicating Authority was not in a position to proceed further and admit the personal guarantors in insolvency. However, pursuant to pronouncement of this judgment, the cases and mechanism of personal insolvency as envisaged under IBC will be proceeded expeditiously and the personal guarantors will no longer take shelter of pendency of constitutional challenge before the Supreme Court to evade the process of law.

III. NCLAT: An operational creditor who is a participant in meetings of the CoC has no right to seek a copy of the information memorandum.

The National Company Law Appellate Tribunal, Principal Bench, New Delhi ("**NCLAT**"), in its order dated October 10, 2023, in the matter of ***Vinay Kumar Singhal, Resolution Professional for M/s. PG Advertising Private Limited v. Mahesh Bajaj [Comp. App. (AT) (Ins) No. 645 of 2023]***, has held that an operational creditor, who was merely a participant in the meetings of the committee of creditors ("**CoC**"), would have no right to seek a copy of the information memorandum.

Facts

Mr. Tulsi Nandan Kant Bansal, the financial creditor of M/s. PG Advertising Private Limited ("**Corporate Debtor**"), filed an application under Section 7 (*Initiation of corporate insolvency resolution process by financial creditor*) of the Insolvency and Bankruptcy Code, 2016 ("**IBC**") seeking resolution of an amount of INR 1,05,00,000/-, which was due from the Corporate Debtor to such

financial creditor. The said application was admitted by the National Company Law Tribunal, New Delhi ("**NCLT**") on October 18, 2022, and corporate insolvency resolution process ("**CIRP**") was initiated against the Corporate Debtor. Following this, a moratorium was imposed, and Mr. Vinay Kumar Singhal ("**Petitioner**") was appointed as the interim resolution professional.

During the pendency of the CIRP, Mr. Mahesh Bajaj ("**Respondent**"), one of the operational creditors of the Corporate Debtor, representing 10% of the total debt owed by the Corporate Debtor, filed an application before the NCLT for issuance of directions to the Petitioner for providing the information memorandum and other relevant documents to him, since he was a participant of the CoC. The NCLT, *vide* its order dated May 3, 2023 ("**Impugned Order**"), instructed the Petitioner to deliver a copy of the information memorandum along with the other relevant documents to the Respondent, despite the fact that the Respondent was merely a participant and not a member of the CoC.

Aggrieved by the Impugned Order, the Petitioner filed the present appeal before the NCLAT, urging the NCLAT to set aside the Impugned Order.

Issue

Whether a copy of the information memorandum can be ordered to be given to an operational creditor, who is merely a participant in the meeting of the CoC and not a member.

Arguments

Contentions of the Petitioner:

The Petitioner submitted that the term 'member' has neither been defined in IBC nor in the Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 ("**CIRP Regulations**"). Whilst referring to Section 21(2) (*Committee of creditors*) of IBC, the Petitioner submitted that the CoC must essentially comprise of all the financial creditors of a corporate debtor and that an operational creditor was not a member.

The Petitioner further referred to Section 24 (*Meeting of committee of creditors*) of IBC, and submitted that Section 24(3) of IBC provides for the issuance of notice of each meeting of the CoC and Section 24(3)(c) of IBC deals with the issuance of notice to the operational creditors of the corporate debtor or their representatives. The Petitioner submitted that while Section 24(4) of IBC provides the operational creditors or their representatives with a right to attend the CoC meeting, it does not provide them with a right to vote at such meeting. Further, Section 24(8) of IBC stipulates that the meeting of the CoC must be conducted in a specific manner, as enumerated in the CIRP Regulations.

The Petitioner referred to Regulation 2(1)(d) (*Definition*) of CIRP Regulations which defines 'committee' as a CoC established under Section 21 of IBC and to Regulation 2(1)(l) of CIRP Regulations which defines 'participant' as a person entitled to attend a meeting of the CoC under Section 24 of IBC, or any other person authorized by the CoC to attend the meeting.

The Petitioner argued that as per Regulation 36(4) (*Information memorandum*) of the CIRP Regulations, the resolution professional of the corporate debtor must share the information memorandum with the members of the CoC, upon receiving an undertaking from the member of the CoC to the effect that such member shall maintain confidentiality of the information and shall not use

such information to cause an undue gain or loss to itself or any other person. The Petitioner contended that there was no provision, either in IBC or the CIRP Regulations for giving information memorandum to the participants in the meeting of the CoC, and that the NCLT had committed an error in passing the Impugned Order on the ground that there was no such prohibition under the legislature. The Petitioner concluded its arguments by submitting that reliance by the NCLT on the case of ***Vijay Kumar Jain v. Standard Chartered Bank and Others [Civil Appeal No. 8430 of 2018]*** ("**Vijay Kumar Jain Case**"), at the time of passing the Impugned Order, was not sustainable since the said case had altogether different facts and dealt with the supply of resolution plan to the erstwhile member of the board of directors as a participant of the CoC.

Contentions of the Respondent:

Respondent submitted that there was no error in the Impugned Order, and hence did not call for any interference by the NCLAT. Respondent submitted that while the definition of 'member' is conspicuous by its absence in both IBC and the CIRP Regulations and the definition of 'participant' has been given only in the CIRP Regulations, it did not mean that the information memorandum and other documents cannot be supplied to the Respondent.

Respondent referred to Regulations 21(2) (*Contents of the notice for meeting*) and 21(3)(iii) of the CIRP Regulations and submitted that it was essential to supply to each member of the meeting of the CoC, copies of all documents, which are relevant for the matter to be discussed and issues to be voted upon at the meetings of the CoC. Respondent further referred to Regulation 24(2)(e) (*Conduct of meeting*) of the CIRP Regulations to contend that the meeting of the CoC cannot be convened without supplying an agenda with all the relevant material for the said meeting.

Respondent, in order to support its submissions, relied on the Vijay Kumar Jain Case, wherein the Hon'ble Supreme Court had held that although the erstwhile board of directors of the corporate debtor were not members of the CoC, they had a right to participate in each and every meeting held by the CoC, and also had a right to discuss along with members of the CoC all resolution plans that were presented at such meetings of the CoC. The Hon'ble Supreme Court also opined that even though persons such as operational creditors have no right to vote and were merely participants in meetings of the CoC, they would still have a right to be given a copy of the resolution plans before such meetings are held so as to effectively comment on the same to safeguard their interest, as operational creditors of the corporate debtor.

Observations of the NCLAT

The NCLAT observed that the Respondent had admitted that he was merely a participant to the CoC meeting. Further, it was an admitted fact that there is no definition of 'member' provided in IBC or in the CIRP Regulations, albeit repeatedly used in IBC as well as the CIRP Regulations. The NCLAT observed that while both IBC and the CIRP Regulations are silent about the supply of the information memorandum to a participant of a CoC meeting, the legislature has made a provision for providing a copy of the information memorandum to the member of the CoC and the resolution applicant of the corporate debtor. In this regard, the NCLAT further observed that since IBC and the CIRP Regulations are totally silent about the supply of the information memorandum to the participant of the CoC meeting, it has to be inferred that the legislature has made a provision for providing a copy of the information memorandum to the member of the CoC and the resolution applicant but not to the participant of the CoC meeting, as the Respondent. Therefore, the finding of the NCLT that since there

is no express prohibition in IBC or the CIRP Regulations for providing the information memorandum to an operational creditor (as a participant of the CoC meeting) was totally erroneous and unsustainable.

The NCLAT observed that the NCLT wrongly relied on the Vijay Kumar Jain Case, at the time of passing the Impugned Order, as there was no reasonable nexus attached with the supply of information memorandum to the participant as the Respondent. Further, although the Hon'ble Supreme Court, in the Vijay Kumar Jain Case, had opined that the expression 'documents' was a wide expression which would include resolution plans, the information memorandum which was one of its own kind could not be referred to as a document which had to be given to the participant of the meeting of the CoC, especially when there was no such provision under the legislature.

Decision of the NCLAT

In view of the above, the NCLAT set aside the Impugned Order and held that the Respondent being a participant in the meeting of the CoC had no right to seek a copy of the information memorandum.

VA View: Through this judgement, the NCLAT has clarified the position under IBC on an operational creditor's right to seek a copy of information memorandum, and has rightly observed that while the legislature has made a provision to provide a copy of the information memorandum to the 'members' of the CoC, there is no provision for providing a copy of such information memorandum to the 'participants' in meetings of the CoC.

The NCLAT has rightly held that since IBC and the CIRP Regulations are totally silent on the supply of the information memorandum to the participant of the CoC meeting, it has to be inferred that the legislature has made a provision for providing a copy of the information memorandum to only the members of the CoC and the resolution applicant (and not to the participant of the CoC meeting, as the Respondent in the instant case).

IV. Kerala High Court: An insolvency application filed by satisfying the statutory procedural requirements and without any defects, gives effect to moratorium, and mere uploading of an application cannot be taken as filing of an application under Section 96 of IBC.

The Kerala High Court ("**Kerala HC**"), by its judgment pronounced on November 17, 2023, in the matter of ***Jeny Thankachan v. Union of India and Others [WP(C) No. 31502 of 2023]***, has held that the mere uploading of an application cannot be taken as filing of an application under Section 96 (*Interim Moratorium*) of the Insolvency and Bankruptcy Code, 2016 ("**IBC**"). The filing of an application is legal and acceptable only when it is filed without any defects, satisfying the statutory procedural requirements of filing and when the adjudicating authority numbers the application. The Kerala HC further held that unless there is any repugnancy between the provisions of IBC and the provisions of Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 ("**SARFAESI Act**"), there is no question of IBC overriding the provisions of the SARFAESI Act in totality.

Facts

Jeny Thankachan ("**Petitioner**") is a sleeping partner of Hawking Technologies India LLP ("**Respondent No. 3**"/ "**Corporate Debtor**"). The Corporate Debtor obtained a bank loan of an amount of INR 65,10,000/- from IndusInd Bank Limited ("**Respondent No. 4**") for which the Petitioner was a guarantor. The Corporate Debtor defaulted in repayment of the loan and the account of the partnership was rendered non-performing asset on October 31, 2022. Thereafter, Respondent No. 4 initiated proceedings under Section 13 (*Enforcement of security interest*) of the SARFAESI Act and issued a notice to the Corporate Debtor and the Petitioner (being a guarantor).

Respondent No. 4 approached the Chief Judicial Magistrate under Section 14(1) (*Chief Metropolitan Magistrate or District Magistrate to assist secured creditor in taking possession of secured asset*) of the SARFAESI Act. The Chief Judicial Magistrate passed an order dated May 5, 2023 appointing an Advocate Commissioner to assist Respondent No. 4 to take possession of the schedule property. The Petitioner, at this stage, filed an application dated August 21, 2023 for initiating insolvency resolution process under Section 94 (*Application by debtor to initiate insolvency resolution process*) of IBC before the National Company Law Tribunal, Kochi ("**Respondent No. 2**"/ "**NCLT**"). On August 23, 2023, NCLT assigned diary number 1386/2023 to the application submitted by the Petitioner.

The present petition by the Petitioner is to obtain a stay on the proceedings initiated by Respondent No. 4 and the Chief Judicial Magistrate under the SARFAESI Act and to seek a declaration, as to the effect, that provisions of IBC shall have an overriding effect over the provisions of SARFAESI Act.

Issue

Whether the filing of an application under Section 94 of IBC would by itself trigger a stay on the proceedings initiated by Respondent No. 4 and the Chief Judicial Magistrate under the SARFAESI Act as contemplated under Section 96(1)(b)(i) of IBC.

Arguments

Contentions of the Petitioner:

The Petitioner submitted that action to foreclose, recover or enforce any security interest under the SARFAESI Act shall be deemed to have been stayed by virtue of Section 96(b) of IBC upon the Petitioner filing an application under Section 94 of IBC. Placing reliance on Section 238 (*Provisions of this Code to override other laws*) of IBC and Government order dated November 15, 2019, by which the provisions in relation to personal guarantors to corporate debtors have come into force, the Petitioner contended that the provisions of IBC shall have overriding effect over the SARFAESI Act and as such the proceedings under SARFAESI Act should be stayed.

The Petitioner further submitted that the loan agreement has not been executed between the Petitioner, and Respondent No. 4, but between the Corporate Debtor and Respondent No. 4, and since the property proceeded against by Respondent No. 4 is a joint family property of the Petitioner, of which half the share is not liable to be proceeded against pursuant to order dated May 5, 2023.

Contentions of the Respondent:

Respondent No. 4 while applying the ratio laid in the case of ***State Bank of India v. B. Ramakrishnan [2018 17 SCC 394]*** ("**Ramakrishnan Case**"), wherein it was held that moratorium under Section 14 (*Moratorium*) of IBC, on admission of insolvency petition would not be extended to personal guarantor of the corporate debtor, contended that interim moratorium under Section 96 of IBC would not be applicable to the Petitioner in the present case, who is the personal guarantor of the Corporate Debtor. Respondent No. 4 further asserted that since the application filed by the Petitioner under Section 94 of IBC was not assigned a regular case number by the NCLT, the provisions under Section 96 of IBC did not even apply to the Corporate Debtor.

Observations of the Kerala HC

The Kerala HC observed the difference in the provisions of moratorium in case of corporate insolvency resolution process and in cases relating to individuals and partnership firms. An order of declaration of moratorium by the adjudicating authority is necessary in the former, while the latter operates automatically by operation of law. The Kerala HC observed that Sections 96 and 101 (*Moratorium*) of IBC need to be construed strictly, since legal actions and proceedings initiated by the creditor against the debtor are stayed, and consequently, creditors are left disabled and disentitled.

The Kerala HC further discussed the overriding nature of IBC over the SARFAESI Act. It opined that Section 238 of IBC cannot be applied in the case of SARFAESI Act, since IBC and SARFAESI Act operate in different areas of law. Further, on this point, the Kerala HC discerned that unless there is any repugnancy between the provisions of IBC and the SARFAESI Act, there is no question of IBC overriding the provisions of the SARFAESI Act in totality. The Kerala HC relied upon judgment pronounced in the matter of Ramakrishnan Case and reiterated that since protective provisions of IBC do not extend to personal guarantor of corporate debtor, the securitization proceedings against personal guarantors of corporate debtors can continue under the SARFAESI Act.

Decision of the Kerala HC

The Kerala HC held that since the Petitioner's application is not duly numbered by the NCLT, the Petitioner's contention that the Respondents cannot proceed with the securitisation proceedings under the SARFAESI Act and interim moratorium under Section 96 of IBC is in force, is rejected.

VA View: The present judgment of the Kerala HC is a significant judicial pronouncement in the realm of insolvency law.

The Kerala HC has held that the personal guarantors of corporate debtors cannot use the provisions of IBC as a shield to escape from the claims of creditors. Section 96 of IBC must be construed strictly, since the operation of interim and final moratorium under Sections 96 and 101 of IBC have serious repercussions, that is to say legal actions and proceedings pending against the debtor are stayed and the creditors of the debtor are not able to initiate any legal proceeding in respect of any debt. The Kerala HC further clarified that an application will be deemed proper only when it is filed without any defects and by satisfying the statutory procedural requirements of filing and when the adjudicating authority numbers the application.

The Kerala HC has further clarified that even though Section 238 of IBC provides for an overriding effect over other laws, it cannot oust the operation of the SARFAESI Act in totality in absence of any repugnancy between the provisions of IBC and the SARFAESI Act.

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