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Insolvency And Bankruptcy Code, 2016

IBC and Limitation

by Rohit Suri

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Insolvency and Bankruptcy Code, 2016

by Rohit Suri

Limitation

Acknowledgement Of Debt In The Balance Sheet

There have been a slew of judgements dealing with the point of limitation under the IBC. This follows the judgment passed by the Apex court in the case of B.K. Educational Services Pvt. Ltd. v. Parag Gupta & Associates” passed in Civil Appeal No. 23988 of 2017 reported in (2019) 11 SCC 633.

The Hon’ble NCLAT in Gautam Sinha v. Uv Asset Reconstruction Company Limited (2020 PLRIJ e@journal 40) was considering mention in the balance Sheet would tantamount to an Acknowledgement of Debt. It held that principle of law laid down is that statement in the balance sheet indicating liability is to be read along with the Directors’ report to see whether both so read would amount to an acknowledgement.

On facts the tribunal held that the Auditor stated that its own opinion and according to the information and explanations given that the Company has not defaulted in the repayment of loan or borrowings
to the financial institution. What was further recorded is statement of fact that bank has declared the Corporate Debtor NPA and proceedings are pending before DRT. In effect, Company claimed to the Auditors that Company has not defaulted in the repayment of loans or borrowings. This cannot be read as Acknowledgement.

While considering “Sheetal Fabrics versus Coir Cushions Ltd.” reported as 2005 SCC OnLine DEL 247 and Judgement in the matter of “In re. Padam Tea Company Ltd.” AIR 1974 Calcutta 170 it held that the Balance Sheet would be required to be read with Directors’ Report. In the present case there does not appear to be any acknowledgement of debt as the statement recorded by the Auditor with regard to the pending litigation in the facts of the present matter, could not be read as an acknowledgement by Company under Section 18 of the Limitation Act. The tribunal was not deliberating whether entry in Balance Sheet can be termed Acknowledgement in law. In the tribunals even if it was to be considered that contents in Balance Sheet could be read as acknowledgment even then it did not find that the Corporate Debtor acknowledged as such the liability to pay the alleged outstanding debt.

Whether SARFAESI and DRT proceeding can be considered for computing period of limitation.

Whether an offer of OTS can be considered as Acknowledgement of Debt
Whether payment of an amount by guarantor would give rise to a cause of action under IBC

Whether the application under Section 7 of the IBC is a suit for the purposes of the Limitation Act, 1963.

Whether CIRP proceedings can continue where there is No Acknowledgement in last 3 years.

The Hon’ble NCLAT in Bimalkumar Manubhai Savalia v. Bank of India (2020 PLRIJ e@journal 46) has considered the issue of affect of OTS, Payment of amount by guarantor and pendency of SARFAESI and DRT proceeding on the point of limitation.

Facts: Insolvency and Bankruptcy Code, 2016, Section 7, application by financial creditor. Date of default in statutory form-1, as per the rules, shown as 05.11.2014. Application filed before the Adjudicating Authority on 30.08.2018. Reliance placed by bank-financial creditor on letter issued by Corporate Debtor dated 28.04.2016 and letter dated 01.06.2016 with regard to the settlement. Letter dated 28.04.2016 was issued ‘without prejudice’. However, second letter dated 01.06.2016 the word ‘without prejudice’. Plea that letter dated 01.06.2016 can be treated as an acknowledgement of debt by the Corporate Debtor, negated. Plea that Guarantor paid certain amounts transferring the same to the account of the Corporate Debtor on 01.04.2017, would extend limitation, negated. Transfer of amount by guarantor can be treated as an acknowledgement for the purposes of limitation. Application barred by limitation. Corporate Debtor is released from the rigor of
Corporate Insolvency Resolution Process and action taken by IRP/RP and Committee of Creditor, if any, in view of the impugned order set aside. IRP/RP will hand back the records and management of the Corporate Debtor to the Promoter’s/Directors of the Corporate Debtor. Matter is remitted back to Adjudicating Authority to decide the fee and costs of “Corporate Insolvency Resolution process” payable to IRP/RP which shall be borne by the Bank.

The tribunals views are summarised as:

a. SARFAESI and DRT proceeding

_Insolvency and Bankruptcy Code, 2016, Section 7 – Limitation - SARFAESI and DRT proceeding will not extend the period of limitation since those proceedings are independent and as per section 238 of IBC, the Insolvency and Bankruptcy Code is a complete Code and will have overriding effect on other laws - Held, therefore, the proceedings initiated or pending in DRT, either initiated under SARFAESI or under debts and due to Banks and Financial Institutions cannot be taken into account for the purposes of Limitation - Limitation Act, 1963 - Banking – IBC._

b. OTS

_Insolvency and Bankruptcy Code, 2016, Section 7 - OTS not accepted by financial creditor shall not extend period of limitation – Banking - IBC._

_Held, OTS was not accepted by the Financial Creditor, therefore, the same cannot be treated as an acknowledgement in view of Section_
18 of the Limitation Act, 1963 – OTS Proposal on 28.04.2016 prior to the OTS Proposal i.e., 01.06.2016 - Application filed before the Adjudicating Authority on 30.08.2018 - First OTS offer was given by using the words as “without prejudice” in Second OTS Proposal dated 01.06.2016 there is no use of word “without Prejudice”- Plea that second OTS Proposal dated 01.06.2016 can be treated as an acknowledge for the purpose of limitation - we are not inclined to accept such submission – Application barred by limitation.

C. Payment of amount by guarantur

Insolvency and Bankruptcy Code, 2016, Section 7 – Limitation – Payment of amount by guarantur shall not extend period of limitation.

Held, Plea that Guarantor paid certain amounts transferring the same to the account of the Corporate Debtor on, would extend limitation, negated. Transfer of amount by guarantur can be treated as an acknowledgement for the purposes of limitation. Stand of the Financial Creditor /bank that the period of limitation will get extended from the date of payment of amount by the Guarantor cannot be a ground and the limitation will not get extended.

d. Section 7 of the IBC is not a suit and is an Application under the IBC which falls under the category of Application in para II of 3rd division of the Limitation Act, 1963

Article 19 of the Limitation Act will fall under the category of first
division of schedule which applies to the suits. However, Section 7 of the IBC is not a suit and as held by Hon’ble Supreme Court, Section 7 is an Application under the IBC which falls under the category of Application in para II of 3rd division, Therefore, Article 137 will apply to the Applications filed under Section 7 & 9 of the IBC

e. No Acknowledgement in last 3 years

Insolvency and Bankruptcy Code, 2016, Section 7 – Limitation - There is no acknowledgement issued by Corporate Debtor prior to expiry of 3 years or from the date of default - Therefore, the Application filed by the Financial Creditor /bank before the Adjudicating Authority is beyond the period of limitation.
MSME and SARFAESI

by Er. Sandeep Suri

Framework for revival and rehabilitation of Micro, Small and Medium Enterprises of Reserve Bank of India dated 17.3.2016

Whether the company of the plaintiffs falls under Micro, Small and Medium Enterprises or not would be a question of fact to be debated before the trial Court at the relevant stage with reference to the evidence to be led by the parties - Trial Court dismissed the application filed by the plaintiffs under Order 39 Rules 1 and 2 CPC on the ground that no prima facie case is made out for grant of temporary injunction as jurisdiction of Civil Court is barred under Section 34 of the SARFAESI Act - Lower Appellate Court, on the basis of guidelines of Reserve Bank of India dated 17.3.2016, reversed the order of the trial Court on the ground that under the aforesaid guidelines, a framework for revival and rehabilitation of Micro, Small and Medium Enterprises having loan limits upto 25 crores is provided and for that the case should have been sent to the Committee before initiating any appropriate action under the SARFAESI Act – Revision of bank dismissed.

Trial Court dismissed the application filed by the plaintiffs under Order 39 Rules 1 and 2 CPC on the ground that no prima facie
case is made out for grant of temporary injunction as jurisdiction of Civil Court is barred under Section 34 of the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act. Lower Appellate Court, on the basis of guidelines of Reserve Bank of India dated 17.3.2016, reversed the order of the trial Court on the ground that under the aforesaid guidelines, a framework for revival and rehabilitation of Micro, Small and Medium Enterprises having loan limits upto 25 crores is provided and for that the case should have been sent to the Committee before initiating any appropriate action under the SARFAESI Act. Whether the company of the plaintiffs falls under Micro, Small and Medium Enterprises or not would be a question of fact to be debated before the trial Court at the relevant stage with reference to the evidence to be led by the parties. For grant of temporary injunction, three principles are required to be appreciated i.e. existence of prima facie case, balance of convenience and irreparable loss to be caused in the event of non grant of temporary injunction.

**Court having no jurisdiction can pass interim order till such time issue of jurisdiction is decided by the Court on merits.**

Civil Procedure Code 1908 (V of 1908), Order 39 Rules 1 and 2 - Temporary injunction - Court having no jurisdiction can pass interim order till such time issue of jurisdiction is decided by the Court on merits. For grant of temporary injunction, three principles are required to be appreciated i.e. existence of prima facie case, balance of convenience and irreparable loss to be caused in the
event of non grant of temporary injunction. At this stage no consideration on merits can be made by any Court except to consider the case on the basis of prima facie consideration. Court having no jurisdiction can pass interim order till such time issue of jurisdiction is decided by the Court on merits. Basakhi Ram v. Suresh Kumar, (1998-2)119 P.L.R. 344, and Tayabbhai M Bagasarwalla v. Hind Rubber Industries Pvt.Ltd., A.I.R. 1997 S.C. 1240 relied

(2020-1)197 Punjab Law Reporter 256 (Punjab And Haryana High Court)
Banks Prior Mortgage and the IT Act

by Kriti Sharma Avasthi

Where bank has a prior charge, the property can not be attached under the Income Tax Act

The Apex court was dealing with the provision of the Income Tax Act, 1961, R. 2 of Schedule II (notice), R 16(2) and R. 48 (Attachment) where the Mortgaged property was sold under the provisions of the Recovery Of Debts Due To Banks And Financial Institution Act, 1993 where subsequently Attachment was ordered by the Tax Authorities.

Property in dispute was mortgaged by B to the Bank in 2000 and the DRT passed an order of recovery against the B in 2002 wherein recovery certificate was issued immediately, pursuant to which an attachment order was passed prior to the date on which notice was issued by the Tax Recovery Officer under Rule 2 of Schedule II to the Act - Notice under Rule 2 was issued on 11.02.2003, and the property in dispute was attached under Rule 48 on 17.06.2003, whereas the sale by the recovery officer DRT took place on 09.12.2004 and the sale certificate was issued on 14.01.2005 – Though sale was conducted after the issuance of the notice as well as the attachment order passed by in 2003, the fact remains that a
charge over the property was created much prior to the notice issued
- Finding of High Court that Rule 16(2) is applicable on the ground
  that the actual sale took place after the order of attachment set aside
- High Court failed to take into account the fact that the sale of the
  property was pursuant to the order passed by the DRT with regard to
  the property over which a charge was already created prior to the
  issuance of notice on 11.02.2003 - Order of attachment set aside

Charge over the property was created in favour of the bank
much prior to the issuance of notice under Rule 2 of Schedule II to
the Act by Tax Recovery Officer and Attachment under Rule 48 and
the Property was sold in auction by Recovery Officer, DRT after
decree passed under the RDDB Act, 1993. The Sale of the
property was pursuant to the order passed by the DRT with regard
to the property over which a charge was already created prior to the
issuance of notice under Rule 2 of Schedule II of Income Tax Act,
1961. The court was pleased to restrain Tax Recovery Officer from
enforcing the attachment order. (M/S. Connectwell Industries Pvt.
Ltd. V. Union of India 2020 SCoJ 151)
SARFAESI – Whether criminal proceedings can continue where action is taken under Sarfaesi.

by Kaveesh Kailey

In K. Virupaksha & Anr. v. State Of Karnataka & Anr. (2020 SCeJournal 142), the Hon’ble Apex court was seized of a matter of a quashing of an FIR arising out of an action taken by the bank in selling the mortgaged property.

Loanee after dismissal of the application under section 17 of the Sarfaesi Act, before the DRT filed the a criminal complaint against the bank and its officers and the auction purchaser alleging that the sale of the mortgaged property has been carried out fraudulently for a much lower value in connivance with each other. The court held that the criminal complaint appears to be an intimidatory tactic and an afterthought which is an abuse of the process of law and Quashed the same.

Held, in the matter of present nature if the grievance as put forth is taken note and if the same is allowed to be agitated through a complaint filed at this point in time and if the investigation is allowed
to continue it would amount to permitting the jurisdictional police to redo the process of Sarfaesi wherein application has been dismissed by the DRT, DRAT and the writ by the High Court and which would be in the nature of reviewing the order passed by the learned Single Judge and the Division Bench in the writ proceedings by the High Court and the orders passed by the competent Court under the SARFAESI Act which is neither desirable nor permissible and the banking system cannot be allowed to be held to ransom by such intimidation. Therefore, the present case is a fit case wherein the extraordinary power is necessary to be invoked and exercised.

It held that under Securitisation and Reconstruction of Financial Assets and Enforcement of Securities Interest Act, 2002, Section 32 an Immunity from prosecution for action taken in good faith has been provided. That aspect of the matter qua Sale of property at a low value is also an aspect which can be examined in the proceedings provided under the SARFAESI Act and Criminal proceeding would not be sustainable. Exposing the bank and its officials even on that count to the proceedings before the Investigating Officer or the criminal court would not be justified.

It further went on to hold that SARFAESI Act is a complete code in itself which provides the procedure to be followed by the secured creditor and also the remedy to the aggrieved parties including the borrower. In such circumstance if there is any discrepancy in the manner of classifying the account of the appellants as NPA or in the manner in which the property was valued or was auctioned, the DRT is vested with the power to set aside such auction at the stage after the secured creditor invokes the power under Section 13 of
SARFAESI Act.

The court however added a caveat that action taken by the Banks under the SARFAESI Act is neither unquestionable nor treated as sacrosanct under all circumstances but if there is discrepancy in the manner the Bank has proceeded it will always be open to assail it in the forum provided.
No Defamation everytime a Criminal Complaint is dismissed

by Geetika Kapur

Whether an officer of a company can be prosecuted for defamation Complaint was filed by the bank under Section 138 of the Negotiable Instruments Act, which was dismissed. Accused filed a complaint under Section 499/500 IPC. In a criminal trial, the finding regarding acquittal is recorded by the Court on the basis of the evidence on record. The court held that merely because the Court comes to the conclusion that no offence is made out, does not give a handle to the accused to launch the defamation proceedings against the complainant.

If such process is allowed, then in every case, after the acquittal, there would be an eventual and/or consequential initiation of the proceedings under Section 499/500 IPC.

While considering the provisions contained in Section 499/500 IPC which are penal in nature, a Magistrate has to take into account if the requirement of mensrea which is a mandate for a criminal defamation punishable under Section 500 IPC, was present while committing such offence. Trial Court did not appreciate the contents of the complaint and the material placed on record by the
respondent/complainant along with the complaint in the right perspective while taking cognizance of the offence under Section 500 IPC and passing the consequential summoning order.

Mens-rea, the court held, a mandatory prerequisite for the offence of defamation is clearly missing in the complaint filed by the respondent under Section 499/500 IPC. Bank or its employees cannot be in any case held to have committed an offence under Section 500 IPC because, the most essential ingredient of the said offence i.e. ‘mensrea’ would be missing as a Bank or its employees.

*ICICI Bank Ltd. v. Kusum Aggarwal (2020-1)197 PLR 454 (This case was handled by our partner Sandeep Suri)*
SARFAESI and IBC, 2016

by Puneet Tuli

Financial Creditor can proceed simultaneously under SARFAESI Act, 2002 as well as under I&B Code

Insolvency and Bankruptcy Code, 2016, Section 238 - Financial Creditor can proceed simultaneously under SARFAESI Act, 2002 as well as under I&B Code - The non-obstante clause of the I&B Code will prevail over any other law for the time being in force – IBC.

The NCLAT while dealing with the interplay between the two acts has held that Financial Creditor can proceed simultaneously under SARFAESI Act, 2002 as well as under I&B Code. Section 238 of I&B Code provides that the provisions of this code shall have effect, notwithstanding anything inconsistent therewith contained in any other law for the time being in force or any instrument having effect by the virtue of any such law. Thus, the non-obstante clause of the I&B Code will prevail over any other law for the time being in force. Punjab National Bank v. M/s Vindhya Cereals Pvt. Ltd. - (2020 PLR Important Judgements e@journal 37 (NCLAT))
Negotiable Instruments Act,
1881

by Tushar Arora

Fine Can Not Be Reduced

In V. Rao Gulur v. Sreehari Rao B. Kodikal. (2020 PLR Important Judgements e@journal 34) it is held that the Section provides that if any person commits an offence under Section 138 of the Act, he shall be punished with imprisonment for a term which may extend to two years or with fine which may extend to twice the amount of the cheque or with both. The word used in the said Section is “shall” which indicates that the Court is not having any discretion to exercise power and reduce the fine amount. Only discretion which has been granted under the said Section is that it can impose sentence upto two years or both the sentence as well as fine or it can impose only fine. While imposing sentence, word used is “may” which gives discretion and Court can impose sentence lesser than two years. But there is no discretion to reduce the imposing a fine. No reasons have been assigned for the lesser sentence of fine imposed under Section 138 of the Act when section itself mandates that the sentence will be double the cheque amount.
Vicarious Liability of Director

To make the Director responsible or liable for the vicarious liability, strict compliance of the statutory requirements was required.

In Amandeep Kaur v. Videocon Industries Ltd ((2020-1)197 PLR 640), petitioner was not the Director of the Company, when the cheque in question was issued nor the petitioner was, thus, responsible for the conduct of the business of respondent company at the relevant time. There was no specific averment in the complaint regarding the role of the petitioner as a Director and/or one of the Directors of the accused-company. The court held that there should be a clear and unambiguous allegation as to how the concerned Director i.e. petitioner was in-charge of and was responsible for the conduct and affairs of accused company. No specific notice having been issued to the petitioner, which is the requirement of the mandate of the law – To make the Director responsible or liable for the vicarious liability, strict compliance of the statutory requirements was required. No vicarious liability could be fastened upon her in the context of Section 141 of the Act for the offence under Section 138 of the Act.
Consumer Protection Act, 1986. Forum has no power to extend the time for filing Reply beyond the period of 45 days

By Chaitanya Suri, (Intern)

Constitution Bench of the Supreme Court of India (Justice Arun Mishra, Justice Indira Banerjee, Justice Vineet Saran, Justice M. R. Shah and Justice S. Ravindra Bhat) in New India Assurance Company Limited v. Hilli Multipurpose Cold Storage private limited decided on 04.03.2020 (2020 SCeJournal 171) has held that District Forum has no power to extend the time for filing the response to the complaint beyond the period of 15 days in addition to 30 days as is envisaged under Section 13 of the Consumer Protection Act. Commencing point of limitation of 30 days under Section 13 of the Consumer Protection Act would be from the date of receipt of the notice accompanied with the complaint by the opposite party, and not mere receipt of the notice of the complaint. Wherever limitation is provided, either for filing response/written
statement or filing an appeal, it is the copy of the plaint or the order/award which is to be served on the party concerned after which alone would commence the period of limitation.

Commencing point of limitation of 30 days, under the aforesaid provisions, would be from the date of receipt of notice accompanied by a copy of the complaint, and not merely receipt of the notice, as the response has to be given, within the stipulated time, to the averments made in the complaint and unless a copy of the complaint is served on the opposite party, he would not be in a position to furnish its reply. Mere service of notice, without service of the copy of the complaint, would not suffice and cannot be the commencing point of 30 days under the aforesaid Section of the Act.

We may, however, clarify that the objection of not having received a copy of the complaint along with the notice should be raised on the first date itself and not thereafter, otherwise if permitted to be raised at any point later would defeat the very purpose of the Act, which is to provide simple and speedy redressal of consumer disputes.

_Hooghly Mills Company Ltd. v. State Of West Bengal (Reported in 2020 SCEJournal 34)_
IBC : Has the Genie left the bottle

By Er. Sandeep Suri

The procedure and system prescribed under the *Insolvency and Bankruptcy Code, 2016* (IBC) was designed to save jobs and protect companies from dying in the case of financial difficulties, however it has ended up perpetuating joblessness instead by encouraging promoter replacement (through NCLT) as a first step.

The Indian Bankruptcy Code was passed for two primary reasons, to help banks recover their dues from companies that have failed to pay back their loans, and to prevent such companies from dying so as to limit job losses.

The note circulated by the Ministry of Finance, has raised several Red Flags and perhaps the most damaging is the question mark which has been raised on the competency and integrity of the RPs (Resolution professionals) itself as well as Bankers, which has placed several companies on the death row.
Why the Alarm!

**Liquidation under IBC : 73.6%**

More than half of the cases admitted to the National Company Law Tribunal (NCLT) are been liquidated as recovery through resolution continues to elude creditors, latest data released by the Insolvency and Bankruptcy Board of India (IBBI) showed. The same has resulted in thousands of loss of jobs, According to IBBI's latest figures*:

- Closed cases : 1,351
- Resolved cases : 190 (14%)
- Average haircut : 57%

**Liquidation : 780 (58%)**

The figures for the *Third quarter, 2020* paint a much more appalling picture:

- Closed cases: 182
- Resolved cases : 30 (16.4%)
- Haircuts : 88%

**Liquidation : 134 (73.6%)**

*(source The Hindu)*
What is an NPA

RBIs, Master Circular- Income Recognition, Asset Classification, Provisioning and Other Related Matters – UCBs deals with Non-performing Assets (NPA) under clause 2. An asset becomes non-performing when it ceases to generate income for the bank. Earlier an asset was considered as non-performing asset (NPA) based on the concept of 'Past Due'. A 'non performing asset' (NPA) was defined as credit in respect of which interest and / or installment of principal has remained 'past due' for a specific period of time. An amount is considered as past due, when it remains outstanding for 30 days beyond the due date. However, with effect from March 31, 2001 the 'past due' concept has been dispensed with and the period is reckoned from the due date of payment. With a view to moving towards international best practices and to ensure greater transparency, '90 days' overdue norms for identification of NPAs have been made applicable from the year ended March 31, 2004. Any amount due to the bank under any credit facility, if not paid by the due date fixed by the bank becomes overdue.

As such, with effect from March 31, 2004, a non-performing asset has been classified as loan or an advance where:

(i) Interest and / or installment of principal remain overdue for a period of more than 90 days in respect of a Term Loan.
(ii) The account remains ‘Out of order’ for a period of more than 90 days, in respect of an Overdraft / Cash Credit (OD/CC). An account is treated as 'out of order' if the outstanding balance remains continuously in excess of the sanctioned limit / drawing power. In cases where the outstanding balance in the principal operating account is less than the sanctioned limit / drawing power, but there are no credits continuously for 90 days or credits are not enough to cover the interest debited during the same period, these accounts are treated as 'out of order’.

(iii) The bill remains overdue for a period of more than 90 days in the case of bills purchased and discounted,

(v) Any amount to be received remains overdue for a period of more than 90 days in respect of other accounts.

A non performing asset (NPA) is a loan or advance for which the principal or interest payment remained overdue for a period of 90 days (in most cases). Companies that have failed to pay back their loans within a 90 day period from their due date are declared NPA.

The inability of the promoter to pay the loan amount within this short window can happen due to a variety of reasons such as economic slowdown, stringent pollution regulations, changes in government policy, promoter committing fraud amongst others. In only 10% of such cases is promoter fraud the reason and majority of the time the alternate factors are responsible.
Role of Resolution Professionals under the scanner

Once a company has been sent to NCLT, a resolution professional (usually a CA) is appointed to run the company, thereby replacing the board and the promoters.

_In the case of smaller companies such professionals are usually unable to successfully run these companies due to their lack of industry and sectoral knowledge. This invariably leads to unit shut downs and job losses for its employees._

I as a lawyer or a Company Secretary, with no knowledge of running a company may pass an examination based on my capacity of rote learning, however the same would not overnight bestow me with the supreme power to understand the nitty gritty of a pharmaceutical, dairy or steel manufacturing company.

_Resolution - professionals even end up misusing their new found absolute control_

In some cases, the resolution - professionals even end up misusing their new found absolute control and power by colluding with the promoters and the bank officials to make money on the side by taking advantage of these reasonably large businesses. Resolution professionals being paid a monthly remuneration which may be several times the income they may have been earning otherwise is
not unknown, infact the same has become the rule. The RPs have been commanding Monthly Fees which may put the salary of a highly qualified and experienced professional in the particular trade/industry to shame. Earlier discussed in hushed tones but now views being exchanged openly in legal circles talk unkindly of the “Cuts” being entered into to appoint Lawyers and Chartered Accountants for the company as per the discretion of the powers that be.

Role of Bankers : No proactive effort for Revival

Once faced with an NPA, Banks instead of arriving at a balanced resolution, end up referring the matter freely to the NCLT as the concerned bank officers find that a safer option rather than the option of taking the onus upon themselves and thereby making themselves vulnerable to a CVC/CBI or other inquiry at a later stage.

As a result, most banks (especially public sector banks), are using NCLT as escape route rather than a tool to empower and keep companies running.

While such a system was designed to save jobs and protect companies from dying in the case of financial difficulties, it has ended up perpetuating joblessness instead by encouraging promoter replacement (through NCLT) as a first step. Bankers seem to
suggest that when it comes to taking haircut they prefer decision making through NCLT rather than sticking out their neck to endorse a resolution plan outside court process. This is ironical since Bankers are fully aware that pre-NCLT solutions may clearly workout better, in terms of overall recovery. Even in the NCLT it is the Committee of creditors which is the banks themselves which are finally taking the call.

Around 19,000 cases have been referred to NCLT and 10,000 have been admitted. Managements have been taken over and original promoters shunted out. These companies are being run by Resolution professionals, (at times even more than one, simultaneously).

While there have been successes in the cases of some large companies and a few smaller accounts as well, majority of smaller companies are in a very vulnerable position. The collapse of so many companies will cause an exponential job loss and thereby further the economic slowdown.

Intent of various regulations to restructure companies lost in the numbers game

The present times require that bankers ensure that under no condition are companies forced into closure and job losses furthered. Handholding and sharing of domain expertise is called for. Public
Sector bankers have immense experience, it should not be allowed to go waste just to show a better NPA figure on the 31st March.

Empowered decision making and a capacity to take bold calls based on conscientious decision making in the interest of the country and its economy without the fear of being questioned by Investigative Authorities can go a long way in terms of restructuring the ecosystem.

The IBC process was meant to serve as a deterrent, incentivizing promoters to pay up or reach a deal with lenders, rather than end up in the NCLT, with the risk of losing their companies.

**MSME regulations – a case in study.**

The government has provided various platforms so as to promote an amicable resolution to help revive the company. For example, to keep the MSME sector robust, the Ministry of Micro, Small and Medium Enterprises, Government of India, vide their Gazette Notification dated May 29, 2015 had notified a ‘Framework for Revival and Rehabilitation of Micro, Small and Medium Enterprises’ to provide a simpler and faster mechanism to address the stress in the accounts of MSMEs and to facilitate the promotion and development of MSMEs. The same has been subsequently adopted by the Reserve Bank of India vide circular No. RBI/2015-16/338 FIDD.MSME & NFS.BC.No.21/06.02.31/2015-16 March 17, 2016 named as Framework for Revival and Rehabilitation of Micro, Small and Medium Enterprises (MSMEs). The framework provides for identification of insipient stress by Banks or creditors - Before a loan
account of a Micro, Small and Medium Enterprise turns into a Non-Performing Asset (NPA), banks or creditors are required to identify incipient stress and refer the matter to a Standing Committee (which also includes independent members) for arriving at a Corrective Action Plan. The options under Corrective Action Plan by the Committee include Rectification, Restructuring, Recovery in that order. However bankers have known to give all these guidelines a go bye and instead of even referring the matter to the committee have been merely referring accounts for Recovery. This inspite of RBI’s “Master Direction – Reserve Bank of India (Lending to Micro, Small & Medium Enterprises (MSME) Sector) - Directions, 2017” dated July 24, 2017 dealing with the Debt Restructuring Mechanism for MSMEs, and RBI’s circular dealing with “Micro, Small and Medium Enterprises (MSME) sector – Restructuring of Advances” dated January 1, 2019, “Interest Subvention Scheme for MSMEs” dated February 21, 2019. Bankers own Code of Banks Commitment To Micro And Small Enterprises are not followed.

All these provide for a platform to help the MSME stand on its feet again, however inspite of the intent shown by the Government to protect and help out this Sector, bankers have prevented the real intention of the policy makers to provide succour and relief and have found recovery instead of handholding as an easier alternative.

**SARFAESI – Where did "Reconstruction" vanish**

The Securitisation And Reconstruction Of Financial Assets And Enforcement Of Security Interest Act, 2002, is a case in point.
The Stated Objects and Reasons of the Act was to regulate securitisation and “Reconstruction” of financial assets and enforcement of security interest and for matters connected therewith or incidental thereto. The provisions of the Act was to enable banks and financial institutions to realise long-term assets, manage problem of liquidity, asset liability mismatches and improve recovery by exercising powers to take possession of securities, sell them and reduce non-performing assets by adopting measures for recovery or “Reconstruction”. The act aims inter alia in facilitating reconstruction of financial assets. However Bankers have exercised powers under the Sarfaesi Act only for recovery and perhaps never for “Reconstruction”.

*In the authors view if the real intention of these Acts and Regulations was followed, the need to promulgate the IBC would never have arisen.*

A Wake Up Call

It’s a wake up call for the central body – RBI – to ensure that its circulars are implemented by banks in the spirit what they were formed for. Its time the bankers are not allowed to flout RBI circulars at will.

The NCLT infrastructure is proving woefully inadequate for the quantum of cases flooding the system. The lack of established legal precedents, which will only build up over time, also makes litigation
under the IBC framework elaborate and time-consuming. The critical change in the new guidelines, which makes it significantly stringent for banks is the accelerated provision that will have to be created if the asset is not resolved in a timely manner and is not referred to NCLT. Such a high provision requirement and its impact on banks' profitability will nudge them to refer cases to NCLT, if a quick resolution is not in sight.

The shortcomings we saw under the Recovery of Debts and Bankruptcy Act, 1993 (earlier known as the Recovery of Debts Due to Banks and Financial Institutions Act, 1993) has reared its head again.

Suggestions

The note circulated by the Ministry of Finance, dated 1.2.2020 under F No. 3/2/2020-BOA-II, in Solution Proposed has suggested that banks be persuaded not to push companies with a loan amount less than 200 Cr to NCLT, and instead should be encouraged to work with the current promoters to find long term solutions (even offering a One Time Settlement scheme) to ensure that under no condition are companies forced into closure and job losses furthered. It has also suggested empowering decision making to enable Bankers to take such calls without the fear.
Steps need to be taken to protect against the closure of companies and loss of jobs.

It is a thinking which needs to change.

Has the Genie left the bottle? No, not yet!
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