THIS WEEK'S **COMPANY CASES–ONLINE** VOLUME 10

CONTENTS

SUBJECT INDEX

NATIONAL COMPANY LAW APPELLATE TRIBUNAL ORDERS

Insolvency resolution—Application by financial creditor—Application admitted on finding that default committed in discharging liability—Justified—Insolvency and Bankruptcy Code, 2016, s. 7—RANVIR RANJIT *v.* VIJAY R. VAKHARIA ... 490

——Collation of claims—Financial creditor—Loan granted by creditor to corporate debtor guaranteed by pledge of shares held by another—On invocation of pledge, creditor becoming owner of shares with right to sell shares and appropriate its value towards amount due—To that extent creditor cannot make any claim—Order of Adjudicating Authority affirmed—Insolvency and Bankruptcy Code, 2016, s. 18(b)—Indian Contract Act, 1872, s. 176—PTC INDIA FINANCIAL SERVICES LTD. *v.* VENKATESWARLU KARI ... 456

NATIONAL COMPANY LAW TRIBUNAL ORDERS

Insolvency resolution—Application by financial creditor—Admissibility of electronic records—Certificate of requirement—Not mandatory—E-mail communications relied upon by financial creditors sent from device in possession of corporate debtor—Court can give relaxation in interest of justice—Indian Evidence Act, 1872, s. 65B—Insolvency

CASES JUDICIALLY NOTICED IN THIS PART

Bhartiya Seva Samaj Trust *v.* Yogeshbhai Ambalal Patel [2012] AIR 2012 SC 3285 **relied on** in Vijay R. Vakharia *v.* Rayala Corporation P. Ltd. [2020] 10 Comp Cas–OL 465 (NCLT)

Innoventive Industries Ltd. *v.* ICICI Bank [2017] 205 Comp Cas 57 (SC) **relied on** in Vijay R. Vakharia *v.* Rayala Corporation P. Ltd. [2020] 10 Comp Cas–OL 465 (NCLT)

Konakalla Venkata Satyanarayana *v.* State Bank of India [1975] AIR 1975 AP 113 **relied on** in Vijay R. Vakharia *v.* Rayala Corporation P. Ltd. [2020] 10 Comp Cas–OL 465 (NCLT)

Kundan Lal Rallaram *v.* Custodian, Evacuee Property, Bombay [1961] AIR 1961 SC 1316 **relied on** in Vijay R. Vakharia *v.* Rayala Corporation P. Ltd. [2020] 10 Comp Cas–OL 465 (NCLT)

Life Insurance Corporation of India *v.* Escorts Ltd. [1986] 59 Comp Cas 548 (SC) **relied on** in Vijay R. Vakharia *v.* Rayala Corporation P. Ltd. [2020] 10 Comp Cas–OL 465 (NCLT)

Manladina *v.* Sukhdeo Bose [1933] AIR 1933 Nagpur 224 **relied on** in Vijay R. Vakharia *v.* Rayala Corporation P. Ltd. [2020] 10 Comp Cas–OL 465 (NCLT)

NSL Nagapatnam Power and Infratech Ltd., *In re* [2020] 10 Comp Cas-OL 434 (NCLT) **affirmed** in PTC India Financial Services Ltd. *v.* Venkateswarlu Kari [2020] 10 Comp Cas–OL 456 (NCLAT)

Sumeet Ahuja *v.* Union Bank of India [2019] 7 Comp Cas-OL 169 (NCLAT) **relied on** in Vijay R. Vakharia *v.* Rayala Corporation P. Ltd. [2020] 10 Comp Cas–OL 465 (NCLT)

Vijay R. Vakharia *v.* Rayala Corporation P. Ltd. [2020] 10 Comp Cas-OL 465 (NCLT) **affirmed** in Ranvir Ranjit *v.* Vijay R. Vakharia [2020] 10 Comp Cas–OL 490 (NCLAT)

COMPARATIVE TABLE OF CASES REPORTED IN THIS VOLUME

Asterisks indicate cases which have not been reported in other journals.

Page	Court	Other Journals
		PART 1 — 3-7-2020
1	NCLT	* * *
5	NCLT	* * *
9	NCLT	* * *
26	NCLT	* * *
51	NCLAT	* * *
55	NCLT	* * *
57	NCLT	* * *
62	NCLAT	* * *
72	NCLT	* * *
82	NCLAT	* * *
		PART 2 — 10-7-2020
99	NCLT	* * *
122	NCLAT	[2019] 152 SCL 10 ; 102 taxmann.com 63
131	NCLT	* * *
139	NCLAT	* * *
148	NCLT	* * *
153	NCLAT	* * *
180	Bom	* * *
		PART 3 — 17-7-2020
221	NCLT	* * *
240	NCLT	* * *
248	NCLT	* * *
253	NCLAT	* * *
262	NCLAT	* * *

272	NCLAT	[2019] 112 taxmann.com 264 ; [2020] 154 CLA 47 ; 157 SCL 360
		PART 4 — 24-7-2020
364	NCLAT	* * *
374	SC	* * *
394	NCLT	* * *
402	NCLAT	* * *
408	NCLT	* * *
		PART 5 — 31-7-2020
424	NCLAT	* * *
432	NCLAT	* * *
438	NCLAT	* * *
448	NCLT	* * *
459	NCLT	* * *
466	NCLT	* * *
477	NCLT	* * *
489	NCLT	* * *
501	NCLAT	* * *
506	NCLT	* * *
520	Mad	* * *
		PART 6 — 7-8-2020
541	Mad	* * *
572	NCLAT	* * *
580	NCLT	* * *
590	NCLAT	[2019] 152 SCL 47 ; 108 taxmann.com 13
		PART 7 — 14-8-2020
625	SC	* * *
		PART 8 — 21-8-2020
758	SC	* * *

CONTENTS OF THIS PART

REPORTS OF CASES : 705—784

Supreme Court Cases :

STATUTES AND NOTIFICATIONS : 65—72

Circulars :

MCA Circulars :

SEBI Circulars :

Rules :

Regulations :

SUBJECT INDEX TO CASES REPORTED IN THIS PART

SUPREME COURT

Penalty—Directors—Liability—Foreign exchange—Contravention by company—Non-executive director—Must be shown to have been in charge of and responsible for conduct of company's business at relevant time—Reasonable opportunity for making representation must be given before adjudication—Failure to consider director's written representation that he was not responsible for conduct of affairs of company—Penalty set

CASES JUDICIALLY NOTICED IN THIS PART

National Small Industries Corp. Ltd. *v.* Harmeet Singh Paintal [2010] 154 Comp Cas 313 (SC) **distinguished** in Shailendra Swarup *v.* Deputy Director, Enforcement Directorate [2020] 221 Comp Cas 758 (SC)

S. M. S. Pharmaceuticals Ltd. *v.* Neeta Bhalla [2005] 127 Comp Cas 563 (SC) **relied on** in Shailendra Swarup *v.* Deputy Director, Enforcement Directorate [2020] 221 Comp Cas 758 (SC)

Shailendra Swarup *v.* Director, Enforcement Directorate [2011] 162 Comp Cas 346 (Delhi) **reversed** in Shailendra Swarup *v.* Deputy Director, Enforcement Directorate [2020] 221 Comp Cas 758 (SC)

CUMULATIVE TABLE OF CASES REPORTED

PARTS 1 to 8

(Cases reported in this part are marked with asterisks)

(Contd. on Cover page 3)

course of business", reference made by the appellants to the decision of the High Court of Australia in *Downs Distributing Co. Pty Ltd.* v. *Associated Blue Star Stores Pty Ltd. (in liquidation)* [1948] 76 CLR 463 (Australia), could be usefully recounted as under :

> "As was pointed out in *Burns* v. *McFarlane*[1] the issues in sub-section (2)(b) of section 95 of the Bankruptcy Act, 1924-1933 are '(1) good faith ; (2) valuable consideration ; and (3) ordinary course of business'. This last expression it was said 'does not require an investigation of the course pursued in any particular trade or vocation and it does not refer to what is normal or usual in the business of the debtor or that of the creditor'. It is an additional requirement and is cumulative upon good faith and valuable consideration. It is, therefore, not so much a question of fairness and absence of symptoms of bankruptcy as of the everyday usual or normal character of the transaction. The provision does not require that the transaction shall be in the course of any particular trade, vocation or business. It speaks of the course of business in general. But it does suppose that according to the ordinary and common flow of transactions in affairs of business there is a course, an ordinary course. *It means that the transaction must fall into place as part of the undistinguished common flow of business done, that it should form part of the ordinary course of business as carried on, calling for no remark and arising out of no special or particular situation*." (emphasis[2] supplied)

25.6.2. Taking up the transactions in question, we are clearly of the view that even when furnishing a security may be one of normal business practices, it would become a part of "ordinary course of business" of a particular corporate entity only if it falls in place as part of "the undistinguished common flow of business done" ; and is not arising out of "any special or particular situation", as rightly expressed in *Downs Distributing Co. Pty Ltd.* v. *Associated Blue Star Stores Pty Ltd. (in liquidation)* [1948] 76 CLR 463 (Australia). Though we may assume that the transactions in question were entered in the ordinary course of business of bankers and financial institutions like the present respondents but on the given set of facts, we have not an iota of doubt that the impugned transactions do not fall within the ordinary course of business of the corporate debtor JIL. As noticed, the corporate debtor has been promoted as a special purpose vehicle by JAL for construction and operation of Yamuna Expressway and for development of the parcels of land along with the expressway for residential, commercial

1. See [1940] 64 CLR 108 (Australia).
2. Here printed in italics.

and other use. It is difficult to even surmise that the business of JIL, of ensuring execution of the works assigned to its holding company and for execution of housing/building projects, in its ordinary course, had inflated itself to the extent of routinely mortgaging its assets and/or inventories to secure the debts of its holding company. It had also not been the ordinary course of financial affairs of JIL that it would create encumbrances over its properties to secure the debts of its holding company. In other words, we are clearly of the view that the ordinary course of business or financial affairs of the corporate debtor JIL cannot be taken to be that of providing mortgages to secure the loans and facilities obtained by its holding company ; and that too at the cost of its own financial health. As noticed, JIL was already reeling under debts with its accounts with some of the lenders having been declared NPA ; and it was also under heavy pressure to honour its commitment to the home buyers. In the given circumstances, we have no hesitation in concluding that the transfers in questions were not made in ordinary course of business or financial affairs of the corporate debtor JIL.

25.7. The submissions that security was disclosed in the annual reports or that none of the creditors expressed dissent are of no effect because such disclosure or want of objection by creditors, by themselves, do not operate as estoppel against anybody nor would take the transaction out of the purview of the legal fiction predicated in section 43, if it is otherwise of a preference at a relevant time. Similarly, the distinction between "NPA" and "wilful default" ; the submission that NPA could be regularised ; and further the submission that the mortgages were created before JIL was declared NPA, are hardly of any bearing on the question as to whether the impugned transactions had been in the ordinary course of business or financial affairs of JIL. Thus, reference to the decisions like that in *Keshavlal Khemchand and Sons P. Ltd.* v. *Union of India* [2015] 4 SCC 770[1] is not of any consequence and need not be dilated upon. The answer to this question, in our view, could only be in the negative. That is to say that the impugned transactions had not been in the ordinary course of business or financial affairs of JIL.

25.8. Therefore, the answer to question (v) as referred in paragraph 20 is that the impugned transactions are not of excepted transfers in terms of sub-section (3) of section 43 of the Code.

The concern expressed by lenders of JAL is legally untenable

26 The argument of lenders, that holding the transactions in question as preferential would result in impacting large number of transactions

1. See [2015] 190 Comp Cas 452 (SC).

undertaken by the bankers/financial institutions, of financing in the ordinary course of their business ; and the consequences may be devastating and irreversible on the economy, has only been noted to be rejected.

26.1. It needs hardly any emphasis that in the ordinary course of their business, when the bankers or financial institutions examine any proposal for loan or advance or akin facility, they are supposed to, and they indeed, take up the exercise commonly termed as "due diligence"[1] so as to study the viability of the proposed enterprise as also to ensure, inter alia, that the security against such loan/advance/facility is genuine and adequate ; and would be available for enforcement at any point of time. Given the nature of transaction, the lenders must prefer a clean security to justify the transaction as being in the ordinary course of their business. In the same exercise, in the ordinary course of their business, if they are at all entering into a transaction whereby a third party security, including that of a subsidiary company, is to be taken as collateral, they are obliged to undertake further due diligence so as to ensure that such third party security is a prudent and viable one and is not likely to be hit by any law. In that sequence, they remain under obligation to assure themselves that such third party whose security is being taken, is not already indebted or in red and is not likely to fail in dealing with its own indebtedness. In the context of the IBC, such requirement is moreover imperative on a bare look at the provisions contained in Part II thereof. Interesting it is to notice on the facts of the present case that in fact, several of the respondent lenders are shown to be the direct creditors of JIL too, to the extent of the advances made to JIL. They and the co-respondents cannot plead ignorance about the actual state of affairs and financial position of JIL. Despite such knowledge, if they chose to take the business risk of accepting security from JIL and that too, for securing the loans/advances/facilities made over to JAL, who was a directly related party of JIL for being its holding company, they themselves remain responsible for present legal consequences.

Summation : The transactions in question are hit by section 43 of the IBC

For what has been discussed hereinabove, we are clearly of the view that **27** the transactions in question are hit by section 43 of the Code and the

1. As regards the present context, the term "due diligence" is explained in P. Ramanatha Aiyar's *Advanced Law Lexicon* (5th edition-Volume 2, page 1654) in the following :
"The detailed review of the borrower/issuer's overall position, which is supposed to be undertaken by the lead manager of a new financing in conjunction with the preparation of legal documentation.
Analysis of the financial status and prospects of company before it receives a major investment of capital. It is usually carried out by an independent accountant."

Adjudicating Authority, having rightly held so, had been justified in issuing necessary directions in terms of section 44 of the Code in relation to the transactions concerning property Nos. 1 to 6. The NCLAT, in our view, had not been right in interfering with the well-considered and justified order passed by the NCLT in this regard.

Search and commandeering of preference at a relevant time

28 Although we have analysed the transactions in question on the anvil of section 43 with reference to the submissions made and the facts of the present case but, before moving on to other aspects, we deem it appropriate to point out the manner in which the provisions concerning preference at a relevant time are expected to be applied, particularly by the resolution professional, in a given case. It could be readily recapitulated that as per the charging parts of section 43, i. e., sub-sections (4) and (2) thereof, a corporate debtor shall be deemed to have given preference at a relevant time if the twin requirements of clauses (a) and (b) of sub-section (2) coupled with the applicable requirements of either clause (a) or clause (b) of sub-section (4), as the case may be, are satisfied. However, even if the requirements of sub-sections (4) and (2) are satisfied, a transaction may not be regarded as an offending preference if it falls in either or both of the exceptions provided by sub-section (3) of section 43.

28.1. Looking to the legal fictions created by section 43 and looking to the duties and responsibilities per section 25, in our view, for the purpose of application of section 43 of the Code in any insolvency resolution process, what a resolution professional is ordinarily required to do could be illustrated as follows :

(1) In the first place, the resolution professional shall have to take two major but distinct steps. One shall be of sifting through the entire cargo of transactions relating to the property or an interest thereof of the corporate debtor backwards from the date of commencement of insolvency and up to the preceding two years. The other distinct step shall be of identifying the persons involved in such transactions and of putting them in two categories ; one being of the persons who fall within the definition of "related party" in terms of section 5(24) of the Code and another of the remaining persons.

(2) In the next step, the resolution professional ought to identify as to in which of the said transactions of preceding two years, the beneficiary is a related party of the corporate debtor and in which the beneficiary is not a related party. It would lead to bifurcation of the identified transactions into two sub-sets : One concerning related party/parties and other concerning unrelated party/parties with each sub-set requiring different analysis. The

sub-set concerning unrelated party/parties shall further be trimmed to include only the transactions of preceding one year from the date of commencement of insolvency.

(3) Having thus obtained two sub-sets of transactions to scan, the steps thereafter would be to examine every transaction in each of these sub-sets to find : (i) as to whether the transaction is of transfer of property or an interest thereof of the corporate debtor ; and (ii) as to whether the beneficiary involved in the transaction stands in the capacity of creditor or surety or guarantor qua the corporate debtor. These steps shall lead to shortlisting of such transactions which carry the potential of being preferential.

(4) In the next step, the said shortlisted transactions would be scrutinised to find if the transfer in question is made for or on account of an antecedent financial debt or operational debt or other liability owed by the corporate debtor. The transactions which are so found would be answering to clause (a) of sub-section (2) of section 43.

(5) In yet further step, such of the scanned and scrutinised transactions that are found covered by clause (a) of sub-section (2) of section 43 shall have to be examined on another touchstone as to whether the transfer in question has the effect of putting such creditor or surety or guarantor in a beneficial position than it would have been in the event of distribution of assets per section 53 of the Code. If answer to this question is in the affirmative, the transaction under examination shall be deemed to be of preference within a relevant time, provided it does not fall within the exclusion provided by sub-section (3) of section 43.

(6) In the next and equally necessary step, the transaction which otherwise is to be of deemed preference, will have to pass through another filtration to find if it does not answer to either of clauses (a) and (b) of sub-section (3) of section 43.

(7) After the resolution professional has carried out the aforesaid volumetric as also gravimetric analysis of the transactions on the defined coordinates, he shall be required to apply to the Adjudicating Authority for necessary order/s in relation to the transaction/s that had passed through all the positive tests of sub-section (4) and sub-section (2) as also negative test of sub-section (3).

28.2. On a motion made by the resolution professional after and in terms of the exercise aforesaid, the Adjudicating Authority, in its turn, shall have to examine if the referred transaction answers to all the descriptions noted above and shall then decide as to what order is required to be passed, for avoidance of the impugned transaction or otherwise.

28.3. In our view, looking to the legal fictions created by section 43 and looking to the duties and responsibilities of the resolution professional and the Adjudicating Authority, ordinarily an adherence to the process illustrated hereinabove shall ensure reasonable clarity and less confusion ; and would aid in optimum utilization of time in any insolvency resolution process.

Other aspects of the application made by IRP—allegations of transactions being undervalued and fraudulent

29 Having found that the transactions in question cannot be countenanced, for being of preference during a relevant time to a related party ; and having approved the order passed by the NCLT in that regard, we do not consider it necessary to deal with the other length of arguments advanced by learned counsel for parties on the questions as to whether the transactions are undervalued and/or fraudulent too. In the totality of circumstances, we would prefer leaving the said questions at that only, while also leaving all the related questions of law open ; to be examined in an appropriate case.

29.1. However, we are impelled to make one comment as regards the application made by the IRP. It is noticed that in the present case, the IRP moved one composite application purportedly under sections 43, 45 and 66 of the Code while alleging that the transactions in question were preferential as also undervalued and fraudulent. In our view, in the scheme of the Code, the parameters and the requisite enquiries as also the consequences in relation to these aspects are different and such difference is explicit in the related provisions. As noticed, the question of intent is not involved in section 43 and by virtue of legal fiction, upon existence of the given ingredients, a transaction is deemed to be of giving preference at a relevant time. However, whether a transaction is undervalued requires a different enquiry as per sections 45 and 46 of the Code and significantly, such application can also be made by the creditor under section 47 of the Code. The consequences of undervaluation are contained in sections 48 and 49. Per section 49, if the undervalued transaction is referable to sub-section (2) of section 45, the Adjudicating Authority may look at the intent to examine if such undervaluation was to defraud the creditors. On the other hand, the provisions of section 66 related to fraudulent trading and wrongful trading entail the liabilities on the persons responsible therefor. We are not elaborating on all these aspects for being not necessary as the transactions in question are already held preferential and hence, the order for their avoidance is required to be approved ; but it appears expedient to observe that the arena and scope of the requisite enquiries, to find if the transaction is undervalued or is intended to defraud the creditors or had been of

wrongful/fraudulent trading are entirely different. Specific material facts are required to be pleaded if a transaction is sought to be brought under the mischief sought to be remedied by section 45/46/47 or section 66 of the Code. As noticed, the scope of enquiry in relation to the questions as to whether a transaction is of giving preference at a relevant time, is entirely different. Hence, it would be expected of any resolution professional to keep such requirements in view while making a motion to the Adjudicating Authority.

29.2. In the present case, it is noticed that the NCLT in its detailed and considered order essentially dealt with the features of the transaction in question being preferential at a relevant time but recorded combined findings on all these three aspects that the impugned transactions were preferential, undervalued and fraudulent. Appropriate it would have been to deal with all these aspects separately and distinctively.

29.3. We are conscious of the fact that the IBC is comparatively a new legislation and various aspects expected therein are in the progression of taking proper shape, particularly in the adjudicatory processes envisaged. Having said so, we would leave this aspect at that only, while expecting all the concerned to be more attentive to the scheme, object and requirements of the provisions contained in the Code.

Second issue : Whether lenders of JAL could be categorised as financial creditors of JIL

Preliminary and background

The discussion and summation in the foregoing paragraphs and con- **30**
clusion on the first issue itself would have been the end of the matter because the transactions in question stand disapproved as being preferential. However, there remains another significant issue to be adjudicated herein, which, though not adverted to by the NCLAT, is indeed involved in these matters.

30.1. The issue is as to whether the lenders of JAL could be categorised as financial creditors of JIL for the purpose of the IBC ?

The issue aforesaid was raised before the NCLT by two of the respond- **31**
ent-banks, namely, ICICI Bank Ltd., and Axis Bank Ltd., by way of separate applications under section 60(5) of the Code, seeking to question the decision of IRP rejecting their claims to be recognized as financial creditors of the corporate debtor JIL on account of the securities provided by JIL for the facilities granted to JAL. The NCLT rejected the applications so filed, by way of its orders dated May 9, 2018 and May 15, 2018 respectively, while concluding that on the strength of the mortgages created by the corporate

debtor JIL, as collateral security of the debts of its holding company JAL, the applicants cannot be treated as financial creditors of the corporate debtor JIL.

31.1. The aforesaid orders dated May 9, 2018 and May 15, 2018 were questioned before the NCLAT by the said lenders of JAL in Comp. App. (AT) (Insolvency) No. 353 of 2018 and Comp. App. (AT) (Insolvency) No. 301 of 2018 respectively. These appeals formed part of the bunch of appeals decided by the NCLAT by way of the impugned common order dated August 1, 2019 and, as per the final result recorded therein, these two appeals also stand allowed. However, fact of the matter remains that nothing has been discussed by the NCLAT in the impugned order dated August 1, 2019 as regards the subject-matter of these two appeals, i. e., as to whether the said lenders of JAL could be categorised as financial creditors of JIL or not ; and the entire discussion in the impugned order and the final conclusion therein had only been in relation to the order dated May 16, 2018 that was passed by the NCLT on the application for avoidance filed by IRP.

31.2. The appellant of Civil Appeal D. No. 32881 of 2019, IIFCL, apart from raising other contentions, has also questioned this aspect of the order impugned that the aforesaid two appeals, involving the issue as to whether the mortgagees of the corporate debtor could be taken as financial creditors, have been allowed by the NCLAT without recording any findings and without any discussion in that regard.

31.3. Though, ordinarily, such omission in the impugned order dated August 1, 2019 might have resulted in the matter being remitted to the Appellate Tribunal for appropriate consideration and finding but, as aforesaid, in the entire process, adherence to the time limit is also of significance ; and in view of the fact that learned counsel for the respective parties have advanced elaborate submissions on the merits of the issue as to whether such lenders of JAL could be treated as financial creditors of the corporate debtor JIL and have invited the decision of this court, we deem it just, proper and expedient to finally decide the relevant questions in this regard.

31.4. We may, of course, reiterate that in view of the conclusion that we have reached in relation to the principal issue, the transactions in question are denuded of their value and worth, per the force of the order by the NCLT under section 44 of the Code, which has been approved by us. To be more specific, the security interests created by the corporate debtor JIL over the properties in question stand discharged in whole. Therefore, the respondent-lenders cannot claim any status as creditors of the corporate debtor JIL and there could arise no question of their making any claim to

be treated as financial creditors as such. However, for its relevance, we deem it appropriate to determine the issue as to whether the lenders of JAL, because of creation of the mortgages in question, could be treated as financial creditors of JIL, independent of the finding that the transactions in question are hit by section 43 of the Code.

Before proceeding further, apposite it would be to take note of the rea- **32** sons assigned by the NCLT in its impugned orders for rejecting the claim of two of the lender banks to be treated as financial creditors of JIL.

Reasoning and findings of NCLT

The Adjudicating Authority, NCLT, in its order dated May 9, 2018 as **33** passed on the application moved by ICICI Bank Ltd., with reference to the nature of transaction in question, whereby JIL had extended collateral security towards the facility extended to its holding company JAL as also with reference to the definition and connotations of the expressions "financial debt" and "financial creditor" as occurring in the IBC, essentially proceeded to find that in such a transaction, as regards the corporate debtor JIL, no consideration for time value for money was involved ; and hence, the transaction in question did not qualify as "financial debt" qua the corporate debtor JIL. The NCLT, inter alia, observed as under :

> "9. In the present case undisputedly corporate debtor has mortgaged its property for creating collateral security for the debt of its holding company JAL. The corporate debtor is not a borrower, it has created a mortgage in favour of financial institutions for creating collateral security for the money borrowed by its holding company JAL. In the said transaction time value of money is not involved. The corporate debtor's liability is not regarding the debt owed by its holding company JAL. In case of default in making payment by the principal borrower, for which security interest has been created by the corporate debtor by mortgaging its property in favour of applicant-bank, the debt amount can be realized from the sale of the mortgaged property but not from the corporate debtor, i. e., Jaypee Infratech Ltd. . . .
>
> 9.2 In this case, the applicant has not disbursed the debt along with interest against the consideration for the time value of money. It is also not the case of the applicant that the corporate debtor has borrowed money against payment of interest from the applicant. It is also not the case that the corporate debtor has raised any amount from the applicant under any credit facility. It is not the case of the applicant that there is any liability towards the corporate debtor in respect of any lease or higher purchase contract. It is further not the case of an applicant that any receivables been sold or discounted. It is further

not the case of the applicant that any amount has been raised for the corporate debtor under any other transaction having the commercial effect of borrowing to the corporate debtor. It is not the case of the applicant that any derivative transaction has been entered with the corporate debtor. It is also not the case of the applicant that any counter indemnity obligation in respect of a guarantee, indemnity, bond, documentary, letter of credit or any other instrument issued by a bank or a financial institution for the corporate debtor. Further, no amount of any liability in respect of any of the guarantee or indemnity for any of the items referred to above has been issued by the corporate debtor."

33.1. The NCLT also distinguished the decision of this court in the case of *Rajkumari Kaushalya Devi* v. *Bawa Pritam Singh*, AIR 1960 SC 1030, as relied upon by learned counsel for the applicant, while pointing out the distinct context of the said decision and while observing that the connotations of the expressions "debt", "financial debt", "financial creditor" and "creditor" in the present context would be limited to the definitions given in the Code. The NCLT further distinguished the decision of the Gujarat High Court in the case of *State Bank of India* v. *Smt. Kusum Vallabhdas Thakkar* [1991] SCC Online Guj 14, while again pointing out that in the present case, the corporate debtor has created a mortgage of its property in favour of a third party without any consideration for time value of money.

33.2. Yet further, the NCLT rejected the contentions that the transaction in question could be termed as either "guarantee" or "indemnity" while observing, inter alia, as under :

"13. The contention of the applicant that mortgage created by the corporate debtor can be termed as either a guarantee or indemnity is not tenable. In terms of the mortgage deeds the corporate debtor has created a mortgage over its immovable properties, which is either money borrowed against payment of interest nor indemnity or a guarantee as claimed by the applicant and therefore, the same does not fall within the definition of the financial debt in terms of section 5(8) of the IBC. It is stated that the corporate debtor has neither issued any guarantee nor has provided an indemnity to the applicant in respect of the financial assistance granted to JAL.

14. The resolution professional further submitted that the mortgage deed shows that the corporate debtor has only agreed to create a mortgage in favour of the applicant towards the financial assistance granted to its holding company, i. e., JAL. On perusal of mortgage it is clear that the corporate debtor has neither given any guarantee to

repay or any indemnity qua the repayment of the loans granted by the applicant to JAL. The definition of mortgage debt as per the mortgage deed dated March 7, 2017 is as under :

'Mortgage debt shall mean the principal amount of the facility, all interest therein additional interest, default interest, liquidated damages, fees, costs, charges, expenses, any other amounts due and payable to secured parties under the transaction documents, premia on prepayment, costs, charges, and expenses and other monies whatsoever stipulated in or payable together with other debts and liabilities of JAL to lender under the transaction document and/or these presents.'

It is important to point out that section 124 of the Indian Contract Act defines a 'Contract of Indemnity' as being a contract by which one party promises to save the other from loss caused to him by the conduct of the promisor himself or by the conduct of any other person. In the instant case, as per the mortgage deed the repayment obligation of the loan granted to JAL by the applicant is upon JAL as stated above and therefore, no contract of indemnity as claimed by the applicant has been entered even by conduct of the corporate debtor, and therefore, the contention of the applicant that the applicant is a financial creditor of the corporate debtor is completely untenable in law."

33.3. While observing that in the scheme of the Code and CIRP Regulations thereunder, the claims are invited from the creditors of the corporate debtor, i. e., financial creditors, operational creditors and other creditors, and not from any person or creditors of the holding company of the corporate debtor ; and while further observing that the resolution professional had rightly observed that the mortgages in questions were not like guarantee or indemnity, the NCLT observed that the basic ingredient of financial debt, i. e., "debt along with interest disbursed against time value of money" was lacking in the impugned transactions. The NCLT also referred to the interpretation of the expression "financial creditors" by NCLAT in the case of *Nikhil Mehta and Sons* v. *AMR Infrastructure Ltd.*[1], Company Appeal (AT) (Insolvency) No. 7 of 2017 and endorsed the decision of IRP while holding that :

"15. On the above basis, we are of the view that the resolution professional has correctly rejected the claim of the applicant on the ground that the applicant is not a financial creditor of the corporate

1. See [2018] 2 Comp Cas-OL 88 (NCLAT).

debtor concerning the mortgages and the mortgaged debt. The resolution professional has rightly observed that guarantee and indemnity are distinct documents under the relevant laws and the mortgages executed by the corporate debtor are not like guarantee and indemnity. The basic ingredient of the financial debt as defined under the Code is that debt along with interest disbursed against time value of money lacks in the impugned transaction."

33.4. Accordingly, the NCLT rejected the application of ICICI Bank Ltd., by way of its order dated May 9, 2018 while concluding as under :

"Therefore, by the mortgage created by the corporate debtor, as collateral security by the debt of its holding company, i. e., Jaiprakash Associates Ltd. ('JAL') in favour of the applicant, i. e., ICICI Bank, the applicant cannot be treated as financial creditor of the corporate debtor. Therefore in our view, resolution professional has rightly rejected the claim of the applicant, which was filed by the applicant in the capacity of financial creditors of the corporate debtor, i. e., Jaypee Infratech Ltd. ('JIL')."

33.4.1. Thereafter, the other application filed by Axis Bank Ltd., was rejected by the NCLT on May 15, 2018 while following the earlier order dated May 9, 2018.

34 As noticed, the aforesaid orders dated May 9, 2018 and May 15, 2018 were questioned in two appeals before the NCLAT by the said lenders of JAL ; and the said appeals stand allowed in the impugned order dated August 1, 2019 without any discussion as regards the issue involved therein. We have heard learned counsel for the parties at length in relation to this issue too, and, in the circumstances of the case, as noticed, we had indicated prima facie view in the order dated December 10, 2019[1], that such lenders of JAL cannot be categorised as financial creditors of JIL and had stayed the operation of impugned order to that extent.

Rival submissions

35 Having noticed the relevant background, we may now take note of the contentions of learned counsel for the parties in regard to the issue under consideration.

Submissions on behalf of the appellant

36 It has essentially been argued on behalf of the appellant IIFCL that as per sub-section (7) of section 5 of the Code, only such creditor could be the "financial creditor" of the corporate debtor to whom a "financial debt" is owed by the corporate debtor ; and, as per sub-section (8) of section 5 of

1. Reproduced in paragraph 7 hereinbefore.

the Code, the key requirement of a financial debt is "disbursal against the consideration for the time value of money", which includes the events or modes of disbursement as enumerated in sub-clauses (a) to (i) of section 5(8). It is submitted that in the present case, the lenders of JAL having not disbursed any debt against the consideration for the time value of money to the corporate debtor JIL, the corporate debtor does not owe any "financial debt" to such lenders ; and the transactions in question do not fall within the brackets of "financial debt" only for the reason that the corporate debtor JIL created mortgages as collateral security in favour of lender banks for the money borrowed by JAL. Concisely put, the submission is that in the said mortgage transactions, disbursal against the consideration for the time value of money qua the corporate debtor JIL being not involved, the lenders of JAL are not the "financial creditors" of JIL and cannot be included in the committee of creditors[1], as to be constituted per section 21 of the Code.

36.1. It is further submitted that the said lenders of JAL have no right to demand the mortgage money from the corporate debtor nor is the corporate debtor JIL under any liability to pay the same ; and mere holding of security interest, which too had not been extended for direct disbursement of any credit to JIL, cannot make the JAL lenders as financial creditors of JIL within the meaning of the IBC. Learned counsel for the appellant has referred to the judgment and order dated December 22, 2017 by the NCLAT in *Dr. B. V. S. Lakshmi* v. *Geometrix Laser Solutions P. Ltd.*[2], Company Appeal (AT) (Insolvency) No. 38 of 2017, to substantiate this submission.

36.2. It is contended on behalf of the appellant that though the definition of "financial debt" extends to include various types of transactions, yet it does not include a mortgage, as could be gathered from a plain and simple reading of the said provision. Counsel for the appellant has further relied on the judgment of this court in *Swiss Ribbons*[3], wherein the concept of "financial creditor" has been explicated to mean and include a person who has direct engagement in the functioning of corporate debtor right from the beginning, while assessing the viability of corporate debtor ; and who would also engage in restructuring of debts and reorganising the corporate business in case of financial stress. With reference to the case at hand, it is submitted that mere holding of security interest, not meant for

1. "CoC" for short.
2. See [2018] 3 Comp Cas-OL 61 (NCLAT).
3. See [2019] 213 Comp Cas 198 (SC).

direct disbursement of any credit to corporate debtor JIL, cannot convert the lenders of JAL into the financial creditors of JIL.

36.2.1. It is also contended that the respondents, the lenders of JAL to whom mortgages were extended by the corporate debtor JIL, could at best be construed as plain creditors, who are entitled to file Form F and to specify their security in column 8 thereof ; and in any case, they cannot become financial creditors of JIL.

36.2.2. It is further contended that a secured creditor under the Code can be a financial creditor under two circumstances, i. e., (i) when corporate debtor directly avails a debt from the creditor and such a debt is a secured debt ; and (ii) if corporate debtor furnishes a guarantee to any person. Learned counsel for the appellant submits that a mortgagee, who has not disbursed any debt to the corporate debtor, may be a secured creditor because of the corporate debtor creating a security to secure the payment of a third party but cannot be a financial creditor of the corporate debtor within the meaning of section 5(8) of the Code.

36.3. Elaborating on the submissions relating to the nature of transactions, learned counsel for the appellant has strenuously argued that "mortgage" is not included within the framework of section 5(8) of the Code and its sub-clauses (a) to (i) ; and that "financial debt" is limited only to the transactions enumerated thereunder and its coverage cannot be enlarged while interpreting the provision. It is also argued that "mortgage" cannot be deemed to mean "guarantee", for a mortgagor has no intentions to undertake to discharge the liability of a third person in case of his default in repayment of debts. In other words, only where the debtor and the mortgagor are the same person that the mortgagor would be liable to pay his debts and else, the mortgage itself does not create a pecuniary liability. Moreover, in the present case, when there is a tripartite contract wherein, the mortgagor and debtor are different, the impugned transactions do not satisfy the ingredients of section 126 of the Contract Act, as JIL has not undertaken specifically to discharge the liability of JAL nor has entered into a "contract of guarantee" with the lenders of JAL nor has provided any indemnity ; and therefore, the corporate debtor JIL is not bound by any liabilities and obligations incurred by JAL. To support the contention that liability always flows from debt and not from the security created under the mortgage, learned counsel for the appellant has also relied on several decisions including that in *Ram Chand Sur* v. *Iswar Chandra Giri* (61 IC 539).

36.4. It is submitted that a general reference to the transaction documents would not be sufficient to fasten liability for JIL to pay any outstanding debt of JAL because any payment obligation has to be unequivocal and

ought to be of specific undertaking to discharge such obligations ; and that general words of incorporation or general covenant in some mortgage deeds cannot bind JIL to all the terms and conditions of the documents, particularly any liability to incur JAL's indebtedness by fastening payment obligations. It is further submitted that when the intention of parties is ascertained with reference to the terms of documents and all the surrounding factors, it cannot be inferred that JIL undertook the liability to discharge the indebtedness of JAL when it was itself reeling under financial stress, was declared NPA and had surmounting liabilities towards home buyers and its own lenders. With reference to the financial statements of JIL, it is pointed out that therein, it was specifically disclosed that the mortgages had been provided as a security for the financial assistance availed by JAL but such mortgages were not declared either as contingent or as direct liability. It is also submitted that the common loan agreement between JIL and its lenders, including the appellant, contained negative covenants prohibiting JIL from creating, assuming or incurring any additional indebtedness or from encumbering any property or creating any security on the assets of JIL. The sum and substance of such submissions had been that the corporate debtor JIL could have neither incurred a liability to discharge the indebtedness of JAL nor it had done so under the mortgages in question.

36.5. As regards the decision of this court in *Committee of Creditors of Essar Steel India Ltd*. v. *Satish Kumar Gupta* [2019] SCC Online SC 1478[1], as relied upon by the respondents, learned counsel for the appellant has submitted that the generalised assertion on the part of the respondents, that per the force of the said decision, a secured creditor ipso facto becomes financial creditor, is not a correct appreciation of the ratio thereof. It is submitted that in the scheme of the Code, a secured creditor could also be a financial creditor under two circumstances : First, when the corporate debtor directly avails a debt from the creditor and such debt is secured by a security interest like in the form of a charge or mortgage or hypothecation ; and such a creditor, the secured one, is regarded as financial creditor because of direct disbursement of debt to the corporate debtor ; and secondly, when the corporate debtor furnishes guarantee to any person, such person would also become a financial creditor and a secured creditor by virtue of sub-clause (i) of section 5(8) of the Code, of course, such guarantee may even be to secure the debt obligation of a third party. However, according to counsel for the appellant, when the corporate debtor creates

1. Hereinafter also referred to as the case of *Essar Steel—Committee of Creditors of Essar Steel India Ltd.* v. *Satish Kumar Gupta* [2020] 219 Comp Cas 97 (SC).

mortgage to secure payment obligation of a third party, without disbursement of any debt to itself (the corporate debtor), the mortgagee, even if becoming a secured creditor because of creation of mortgage, could only be described as "indirect secured creditor" and cannot be treated as a "direct secured creditor" so as to become a "financial creditor" because, the mortgage transaction is not envisaged to be a "financial debt" in section 5(8) with its sub-clauses (a) to (i).

36.5.1. It is submitted that *Essar Steel*[1] envisages the position and priorities of secured creditors, mainly in the context of a creditor who has disbursed direct debt to the corporate debtor and has secured its debt by a security interest, who should have priority over unsecured creditors of the corporate debtor. However, the said decision, according to learned counsel, cannot be read to the effect that even the indirect secured creditor be also necessarily construed as financial creditor. It is submitted that the crux of the said decision is that creditors not similarly situated cannot be at par ; that the arrangements of the corporate debtor with its creditors must be taken into consideration ; and that the aim of equitable treatment is based on the notion that creditors with similar legal rights should be treated evenly while receiving distribution in accordance with their relative ranking and interest. It is submitted that *Essar Steel*[1] cannot be read as laying down the law that even the lenders of third party, who hold mortgages from the corporate debtor, be also treated as such secured creditors who would fall within the sect of "financial creditors".

36.6. Learned counsel for the appellant would further submit that existence of a security interest is not relevant while construing whether a creditor is financial creditor or not because, in the composition of CoC, even a non-secured creditor could also be a financial creditor, if the ingredients of section 5(8) of the Code are satisfied. It is also argued that the financial facilities availed by JAL from the respondents were not utilized for any business operation of JIL and hence, the respondents cannot be construed as financial creditors of JIL.

Submissions on behalf of the respondents

37 Learned counsel for the contesting respondents have made elaborate submissions in support of the counter-assertion that on account of security provided by the corporate debtor JIL, the respective lenders have become financial creditors of JIL for the purpose of proceedings under the Code. We may briefly summarise the principal facets of the contentions urged on behalf of the main contesting respondents in this regard as infra.

1. See [2020] 219 Comp Cas 97 (SC).

Axis Bank

37.1. It has been strenuously argued on behalf of this respondent that the nature and character of a "mortgage" is such that it secures a debt ; and in the present case, the mortgage in question, as made by JIL, had been to secure the debt obligations of its holding company JAL. With reference to section 58 of the Transfer of Property Act and the decision of this court in *Prithvi Nath Singh* v. *Suraj Ahir* [1963] 3 SCR 302 as also the decision of Mysore High Court in *Dasappa* v. *Jogiah*, ILR 1964 Karn 545, it is submitted that the purpose of "mortgage" is to secure a debt ; and with reference to the decision in *Manik Chand Raut* v. *Baldeo Chaudhary* [1949] SCC Online Patna 64, it is also contended that mortgage, by its very nature, presupposes existence of a debt and the transaction by which a debt is extinguished is not a mortgage but a sale. Further, with reference to the aforementioned decision of this court in the case of *Rajkumari Kaushalya Devi* v. *Bawa Pritam Singh*, AIR 1960 SC 1030, it is contended that a mortgage debt creates pecuniary liability upon the mortgagor ; and that a mortgagor who transfers an interest in immovable property so as to secure a debt, incurs a mortgage debt. With reference to the decision of Delhi High Court in the case of *State Bank of India* v. *Samneel Engineering Co.* [1995] 35 DRJ 485 (Delhi), it is further submitted that a mortgage is both a promise by a debtor to repay the loan as well as a real property right ; of course, the right being intended to secure the due payment of the debt ; and a suit on a mortgage is essentially a suit for recovery of a debt.

37.1.1. With reference to principles aforesaid, it is contended that a mortgage debt is a "debt" within the meaning of section 3(11) of the Code ; that a debt can be classified to be a debt due from "any person" and not necessarily restricted to the borrower alone. The aforementioned decision of Gujarat High Court in *State Bank of India* v. *Smt. Kusum Vallabhdas Thakkar* [1991] SCC Online Guj 14 has again been referred to submit that Indian Law recognizes that a person, other than the borrower, can also execute a mortgage to secure the debt of the borrower. In this context, learned counsel for the respondent has also relied upon the provisions contained in section 126 of the Contract Act, to contend that JIL stands in the position of a guarantor for the debts owed by JAL. Learned counsel has also referred to an order dated March 13, 2019 in M. A. No. 1584 of 2019 in C. P. No. 402 of 2018 as passed by the NCLT (Mumbai Bench) in the case of *SREI Infrastructure Finance Ltd.* v. *Sterling International Enterprises Ltd.*[1], wherein it is held that a third party mortgagor, who mortgages the property to secure the financial obligation of another party, stands in the

1. See [2020] 221 Comp Cas 580 (NCLT).

position of a guarantor ; and the mortgagee is a financial creditor of the third party mortgagor. In the case at hand, it is submitted, the corporate debtor JIL stands in the position of a guarantor with respect to the security provided to this respondent and hence, the impugned mortgage transactions are covered within the meaning of section 5(8)(i) of the Code.

37.1.2. It is also submitted that looking to the nature of transaction in question, the question whether JAL has defaulted on repayment and consequently, the security is to be invoked is irrelevant for the purposes of the issue at hand ; and whether JAL committed default or not is not decisive of the question as to whether the mortgage debt in question is financial debt or not.

37.1.3. It is further submitted that in the present case, the mortgage transactions were executed to secure the payment of debts/liabilities of JAL ; and that such creation of mortgage undoubtedly is a "security interest" as defined in section 3(31) of the Code inasmuch as, a security interest includes any creation of right/title/interest/claim in property for the purpose of securing the payment or performance of an obligation ; and also includes a mortgage. Hence it is contended that the respondent-bank comes within the ambit of "secured creditor" per section 3(30) of the Code.

37.1.4. It is emphasised by learned counsel for this respondent that a mortgage debt constitutes a "financial debt" within the meaning of section 5(8) of the Code even if no amount is directly disbursed to the corporate debtor. While relying on the decision of this court in *Pioneer Urban*[1], it is contended that the definition of "financial debt" under section 5(8) of Code has been given an extended meaning so as to include the situations which may not directly involve disbursal against the consideration for time value money.

37.1.5. Further, with reference to the aforementioned UNCITRAL Legislative Guide on Insolvency Law and the decisions of this court in the cases of *Essar Steel*[2] and *Swiss Ribbons*[3], it is submitted that a holistic interpretation of the Code would support the position that the respondent, being a secured creditor and a financial creditor, should be included in CoC so as to protect its security interest.

37.2. The submissions and contentions made on behalf of this respondent largely cover the stand of other respondents too. Hence, we may only notice, in brief, the other or additional part of major submissions on behalf of other respondents, while avoiding repetition.

1. See [2019] 217 Comp Cas 1 (SC).
2. See [2020] 219 Comp Cas 97 (SC).
3. See [2019] 213 Comp Cas 198 (SC).

Standard Chartered Bank

37.3. It is submitted on behalf of this respondent that the terms envisaged in the mortgage deed dated May 24, 2016 make it abundantly clear that the corporate debtor JIL had unequivocally promised to pay to this respondent the debts/liabilities owed by JAL in accordance with the terms and conditions of the secured financing documents executed between this respondent and JAL[1]. Hence, it is contended that though the claim of this respondent is limited to the extent of the value of the properties mentioned in the Schedule to the mortgage deed but, to that extent, it remains a financial creditor of JIL.

37.3.1. As regards similar arguments with respect to section 58 of the Transfer of Property Act, that a mortgage presupposes the subsistence of a debt and hence it is a secured debt, apart from above referred decisions, learned counsel has also referred to the decision in *Pomal Khanji Govindji* v. *Brajlal Karsandas Purohit* [1989] 1 SCC 458.

37.3.2. It is contended that when the objective of the Code is to revive the corporate debtor, the resolution plan ought to contain all claims against the corporate debtor, whether matured or not, so that if the liability again creeps in, the company may be prevented from being dragged into insolvency or liquidation proceedings. It is further submitted that this respondent, who is holding public money, ought to be a part of CoC ; and its absence in CoC would be defeating the very object of the Code because the resolution plan may provide for various measures which might take away the security interest created in favour of this respondent ; and without its participation, the entire process would be prejudicial to the interest of this respondent. It is submitted that as per the ratio in *K. Sashidhar* v. *Indian Overseas Bank* [2019] SCC Online SC 257[2] read with the decision in the case of *Essar Steel*[3], once a resolution plan is approved by the wisdom of the CoC, the same cannot be challenged and looking to the scheme of the Code, presence of the mortgagees like this respondent in the CoC of JIL is necessary and is rather unavoidable.

ICICI Bank

37.4. On behalf of this respondent, it is maintained that in view of section 5(8)(i) read with section 5(8)(a) of the Code, the creation of impugned mortgage had resulted in creation of a "financial debt" as defined under the Code, for the transaction being akin to that of a "guarantee" as defined under section 126 of the Contract Act. Again, with reference to the decision

1. Clause B and B(a) of the mortgage deed produced as annexure-1 at pages 8-43.
2. See [2019] 213 Comp Cas 356 (SC).
3. See [2020] 219 Comp Cas 97 (SC).

in *State Bank of India* v. *Smt. Kusum Vallabhdas Thakkar* [1991] SCC Online Guj 14, it is submitted that even a third party mortgage leads to creation of an implied guarantee with an obligation to pay the mortgage debt. In other words, since the definition of "financial debt" is not exhaustive, any transaction which is akin to creation of a guarantee would come under the purview of the definition of "financial debt" and as such, the mortgage provided by the corporate debtor JIL, being akin to the guarantee, would be squarely within the definition of "financial debt". It is further submitted that in the given scenario, this respondent takes on the role of a "financial creditor" of the corporate debtor JIL within the meaning of section 5(8)(i) of the Code and hence, ought to be admitted as a member of the CoC.

37.4.1. It is submitted on behalf of this respondent that on a holistic reading of the mortgage deeds, it is clear that "exclusive mortgages" were executed in favour of this respondent with express clauses whereby, the corporate debtor JIL had undertaken to either discharge the debt or to ensure repayment of facilities extended to JAL and in the event of default, this respondent shall have the right to sell the mortgaged properties. Such stipulations, it is contended, clearly put the respondent in the category of "financial creditors".

37.4.2. With reference to the duties of IRP as laid out in the Code, and with analysis of the definition of "claim" as found in section 3(6) of the Code, it is submitted that the definition of "claim" is wide enough to include all stakeholders of the corporate debtor, even if a claim had not matured on the date of insolvency commencement. The *Report of Banking Law Reform Committee* has also been referred in this regard.

37.4.3. It is further submitted that regulations 12, 13 and 14 of the Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 require the IRP to admit all claims, including contingent claims, as on the insolvency commencement date ; that as per section 29 of the Code, the IRP ought to prepare an information memorandum for formulating a resolution plan ; that as per regulation 37 of the CIRP Regulations, the insolvency resolution of the corporate debtor should include sale of all or part of the assets, irrespective of whether they are subject to security interest and satisfaction or modification of any security interest ; and that sub-section (4) of section 30 of the Insolvency and Bankruptcy (Amendment) Act, 2019 clarifies that priority of secured creditors has to be considered. With reference to the processes so envisaged by the Code, it is contended that the secured creditors like the respondent cannot be kept away from the class of financial creditors.

Central Bank of India

37.5. Apart from the submissions carrying essentially the substance as abovenoted, it is also contended that this respondent, being a secured creditor, would be entitled to enforce its security interest in the mortgaged property upon vacation of the order of moratorium in terms of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002[1] ; and that the resolution plan, without including the secured creditors, would be unenforceable, as the secured creditors will then seek enforcement against mortgage property under the SARFAESI Act. It is, therefore, contended that the secured creditor, like the respondent, needs to be recognized as financial creditor, and thereby a participant in CoC of the corporate debtor JIL.

Bank of Maharashtra

37.6. While going in tandem with the submissions aforesaid, it is asserted on behalf of this respondent that the corporate debtor JIL is under a pecuniary obligation to discharge the liability in view of the Indenture of Mortgage (IOM) dated December 29, 2016 which is a contract of guarantee and, therefore, the relationship between the parties cannot be classified merely as that of mortgagor and mortgagee, but is also of a guarantor and guarantee which, in turn, is covered under section 5(8) of the Code and thereby, this respondent is a "financial creditor" within the meaning of section 5(7) of the Code.

Unique position of financial creditor—as explained in Swiss Ribbons

Having taken note of the rival contentions on the issue as to whether **38**
the lenders of JAL could be categorised as "financial creditors" of JIL for the purpose of CIRP in question, gist of the matter is as to whether the subject transactions could be categorised as "financial debts" within the meaning of section 5(8) of the Code so as to confer the status of "financial creditors" upon the respondents, lenders of JAL.

38.1. The expressions "financial creditor" and "financial debt" as occurring in the Code have come up for consideration before this court in several decisions, including those in the abovementioned cases of *Swiss Ribbons*[2] (decided on January 25, 2019), *Pioneer Urban*[3] (decided on August 9, 2019) and *Essar Steel*[4] (decided on November 15, 2019), which have been referred to and relied upon by learned counsel for the parties for one proposition or another. In fact, the observations as occurring in the last of the

1. Hereinafter also referred to as "the SARFAESI Act".
2. See [2019] 213 Comp Cas 198 (SC).
3. See [2019] 217 Comp Cas 1 (SC).
4. See [2019] 219 Comp Cas 97 (SC).

said decisions, in the case of *Essar Steel*[1], as relied upon by learned counsel for the respondents, are based on those occurring in the decision in *Swiss Ribbons*[2].

39 As indicated hereinbefore, the law declared by this court in the case of *Swiss Ribbons*[2], while rejecting the contentions that classification between financial creditor and operational creditor was discriminatory and violative of article 14, shall have some bearing on the claim of the respondent-lenders for being treated as financial creditors of JIL. Having regard to the submissions made, it shall now be pertinent to take note of the relevant aspects from the said decision in requisite details.

39.1. The broad features of the expressions used in sections 5(7) and (8) of the Code in defining the terms "financial creditor" and "financial debt" were indicated by this court in the case of *Swiss Ribbons*[2] in the following[3] :

> "A perusal of the definition of 'financial creditor' and 'financial debt' makes it clear that a financial debt is a debt together with interest, if any, which is disbursed against the consideration for time value of money. It may further be money that is borrowed or raised in any of the manners prescribed in section 5(8) or otherwise, as section 5(8) is an inclusive definition. On the other hand, an 'operational debt' would include a claim in respect of the provision of goods or services, including employment, or a debt in respect of payment of dues arising under any law and payable to the Government or any local authority."

39.2. The unique position assigned to a "financial creditor", who plays a crucial role in insolvency resolution process as against the role of other creditors, has been extensively explained by this court in the case of *Swiss Ribbons*[2], albeit in the context of its differentiation with the category of "operational creditor", in the following[4] :

> "According to us, it is clear that most financial creditors, particularly banks and financial institutions, are secured creditors whereas most operational creditors are unsecured, payments for goods and services as well as payments to workers not being secured by mortgaged documents and the like. The distinction between secured and unsecured creditors is a distinction which has obtained since the earliest of the Companies Acts both in the United Kingdom and in this

1. See [2019] 219 Comp Cas 97 (SC).
2. See [2019] 213 Comp Cas 198 (SC).
3. See page 247 of 213 Comp Cas.
4. See pages 252 and 270 of 213 Comp Cas.

country. Apart from the above, the nature of loan agreements with financial creditors is different from contracts with operational creditors for supplying goods and services. *Financial creditors generally lend finance on a term loan or for working capital that enables the corporate debtor to either set up and/or operate its business*. On the other hand, contracts with operational creditors are relatable to supply of goods and services in the operation of business. Financial contracts generally involve large sums of money. By way of contrast, operational contracts have dues whose quantum is generally less. In the running of a business, operational creditors can be many as opposed to financial creditors, who lend finance for the set-up or working of business. *Also, financial creditors have specified repayment schedules, and defaults entitle financial creditors to recall a loan in totality*. Contracts with operational creditors do not have any such stipulations. Also, the forum in which dispute resolution takes place is completely different. Contracts with operational creditors can and do have arbitration clauses where dispute resolution is done privately. Operational debts also tend to be recurring in nature and the possibility of genuine disputes in case of operational debts is much higher when compared to financial debts. A simple example will suffice. Goods that are supplied may be substandard. Services that are provided may be substandard. Goods may not have been supplied at all. All these qua operational debts are matters to be proved in arbitration or in the courts of law. On the other hand, financial debts made to banks and financial institutions are well documented and defaults made are easily verifiable.

Most importantly, financial creditors are, from the very beginning, involved with assessing the viability of the corporate debtor. They can, and therefore do, engage in restructuring of the loan as well as reorganisation of the corporate debtor's business when there is financial stress, which are things operational creditors do not and cannot do. Thus, preserving the corporate debtor as a going concern, while ensuring maximum recovery for all creditors being the objective of the Code, financial creditors are clearly different from operational creditors and therefore, there is obviously an intelligible differentia between the two which has a direct relation to the objects sought to be achieved by the Code . . .

Since the financial creditors are in the business of money-lending, banks and financial institutions are best equipped to assess viability

and feasibility of the business of the corporate debtor. Even at the time of granting loans, these banks and financial institutions undertake a detailed market study which includes a techno-economic valuation report, evaluation of business, financial projection, etc. Since this detailed study has already been undertaken before sanctioning a loan, and since financial creditors have trained employees to assess viability and feasibility, they are in a good position to evaluate the contents of a resolution plan. On the other hand, operational creditors, who provide goods and services, are involved only in recovering amounts that are paid for such goods and services, and are typically unable to assess viability and feasibility of business. The BLRC Report, already quoted above, makes this abundantly clear." (emphasis[1] supplied)

39.3. The enunciation aforementioned illuminates the reasons as to why at all a financial creditor is conferred with a major, rather pivotal, role in the processes contemplated by Part II of the Code. It is the financial creditor who lends finance on a term loan or for working capital that enables the corporate debtor to set up and/or operate its business ; and who has specified repayment schedules with default consequences. The most important feature, as this court has said, is that a financial creditor is, from the very beginning, involved in assessing the viability of the corporate debtor who can, and indeed, engage in restructuring of the loan as well as reorganisation of the corporate debtor's business when there is financial stress. Hence, a financial creditor is not only about in terrorem clauses for repayment of dues ; it has the unique parental and nursing roles too. In short, the financial creditor is the one whose stakes are intrinsically interwoven with the well-being of the corporate debtor.

Financial debt—ratio of Pioneer Urban

40 Having imbibed the basic features associated with a "financial creditor", we need to examine as to who could at all fall in this category. In order to address this core question, delving into the finer connotations of the expression "financial debt", as defined in section 5(8) of the Code is, obviously, necessary. As noticed, while defining "financial creditor" and "financial debt" in section 5(7) and section 5(8) of the Code, both the expressions "means" and "includes" have been used. As per the definition, while "financial creditor" means a person to whom a "financial debt" is owed, it also includes a person to whom such debt has been legally assigned or transferred to. Obviously, a comprehension of this definition of "financial

1. Here printed in italics.

creditor" cannot be complete without taking into account as to what is the meaning assigned to the expression "financial debt". Again, the term "financial debt" has also been defined with the expressions "means" and "includes". A "financial debt" means a debt along with interest, if any, which is disbursed against the consideration for the time value of money ; and it includes the money borrowed or raised or protected in any of the manners prescribed in sub-clauses (a) to (i) of section 5(8).

The larger parts of the expressions employed in the definition of **41** "financial debt" in clause (8) of section 5 of the Code with their connotations were explicated in *Pioneer Urban*[1] by a three-Judge Bench of this court ; and, in view of the contentions urged, it would be appropriate to take a deeper look into the exposition of law by this court, while also keeping in view the plain basic principle that a decision of the court is required to be understood in the context of the facts and issues involved therein.

41.1. In the case of *Pioneer Urban*[1], this court was concerned with the challenge to the constitutional validity of amendments made to the Code pursuant to a report dated March 26, 2018 prepared by the Insolvency and Bankruptcy Law Committee. The amendments were essentially to the effect of putting the allottees of real estate projects into the sect of "financial creditors" and thereby investing them with the rights and entitlement to trigger the proceedings under section 7 of the Code against the real estate developers and to be represented in the committee of creditors. In the background of such amendments had been certain important decisions/orders by NCLAT and by this court. One had been the order dated July 21, 2017 by the NCLAT in the case of *Nikhil Mehta and Sons* v. *AMR Infrastructure Ltd.* [2017] SCC Online NCLAT 859[2], where it was held that the amount raised by the developers had the commercial effect of a borrowing and the allottees of such developers were financial creditors within the meaning of section 5(7) of the Code. The other one had been the order dated September 11, 2017 passed by this court in *Chitra Sharma* v. *Union of India*[3] whereby, a representative of the home buyers was appointed to participate in the meetings of the committee of creditors for protection of their interests. Yet another order was passed by this court on November 22, 2017 on practically the same lines, qua another group of builders in the case of *Bikram Chatterjee* v. *Union of India* [2019] 8 SCC 527. In the wake of such orders, the Insolvency Committee Report suggested for

1. See [2019] 217 Comp Cas 1 (SC).
2. See [2018] 2 Comp Cas-OL 88 (NCLAT).
3. See [2018] 210 Comp Cas 609 (SC).

amendment to the Code that ultimately culminated into the Insolvency and Bankruptcy (Second Amendment) Act, 2018. The amendments were made, inter alia, with insertion of *Explanation* to sub-clause (f) of section 5(8) of the Code and with the co-related insertion of sub-section (6A) to section 21 as also with further insertion of section 25A in the Code. These amendments were under challenge in *Pioneer Urban*[1]. Several contentions were urged before this court questioning the treatment of allottees as financial creditors. In this context and in the wake of such issues this court dealt with the contentions related with section 5(8), particularly sub-clause (f) thereof. The relevant part of the consideration of this court in *Pioneer Urban*[1] under the heading "Interpretation of section 5(8)(f) of the Code" needs to be noticed and is extracted as under[2] :

> "Section 5(8)(f) of the Code has been set out in the beginning of this judgment. What has been argued by learned counsel on behalf of the petitioners is that *section 5(8)(f)*, as it originally stood, is an exhaustive provision which must be read noscitur a sociis, and if so read, sub-clause (f) must take colour from the other clauses of the provision, all of which show that the sine qua non of a 'financial debt' is a loan of money made with or without interest, which must then be returned as money. This, according to learned counsel for the petitioners, is clear from even a cursory reading of section 5(8). Secondly, according to learned counsel for the petitioners, by no stretch of imagination, could an allottee under a real estate project fall within section 5(8)(f), as it originally stood and the *Explanation* must then be read prospectively, i. e., only on and from the date of the Amendment Act. Several sub-arguments were made on the effect of deeming fictions generally and on the functions of an *Explanation* to a section. Let us address all of these arguments . . .
>
> Thus, in order to be a 'debt', there ought to be a liability or obligation in respect of a 'claim' which is due from any person. 'Claim' then means either a right to payment or a right to payment arising out of breach of contract, and this claim can be made whether or not such right to payment is reduced to judgment. Then comes 'default', which in turn refers to non-payment of debt when whole or any part of the debt has become due and payable and is not paid by the corporate debtor. Learned counsel for the petitioners relied upon the judgment in *Union of India* v. *Raman Iron Foundry* [1974] 2 SCC

1. See [2019] 217 Comp Cas 1 (SC).
2. See page 101 of 217 Comp Cas.

231, and, in particular relied strongly upon the sentence reading (SCC page 243, paragraph 11) :

'11. Now the law is well-settled that a claim for unliquidated damages does not give rise to a debt until the liability is adjudicated and damages assessed by a decree or order of a court or other adjudicatory authority.'

It is precisely to do away with judgments such as *Union of India* v. *Raman Iron Foundry* [1974] 2 SCC 231 that 'claim' is defined to mean a right to payment or a right to remedy for breach of contract whether or not such right is reduced to judgment. What is clear, therefore, is that a debt is a liability or obligation in respect of a right to payment, even if it arises out of breach of contract, which is due from any person, notwithstanding that there is no adjudication of the said breach, followed by a judgment or decree or order. The expression 'payment' is again an expression which is elastic enough to include 'recompense', and includes repayment. For this purpose, see *Himachal Pradesh Housing and Urban Development Authority* v. *Ranjit Singh Rana* [2012] 4 SCC 505 (at paragraphs 13 and 14 therein), where the Webster's *Comprehensive Dictionary (International edition) Volume 2 and the Law Lexicon* by P. Ramanatha Aiyar (2nd edition, Reprint) are quoted.

The definition of 'financial debt' in *section 5(8)* then goes on to state that a 'debt' must be 'disbursed' against the consideration for time value of money. 'Disbursement' is defined in the *Black's Law Dictionary* (10th edition) to mean :

'1. The act of paying out money, commonly from a fund or in settlement of a debt or account payable. 2. The money so paid ; an amount of money given for a particular purpose.'

In the present context, it is clear that the expression 'disburse' would refer to the payment of instalments by the allottee to the real estate developer for the particular purpose of funding the real estate project in which the allottee is to be allotted a flat/apartment. The expression 'disbursed' refers to money which has been paid against consideration for the 'time value of money'. In short, the 'disbursal' must be money and must be against consideration for the 'time value of money', meaning thereby, the fact that such money is now no longer with the lender, but is with the borrower, who then utilises the money. Thus far, it is clear that an allottee 'disburses' money in the

form of advance payments made towards construction of the real estate project. We were shown the Dictionary of Banking Terms (2nd edition) by Thomas P. Fitch in which 'time value for money' was defined thus :

'present value : today's value of a payment or a stream of payment amount due and payable at some specified future date, discounted by a compound interest rate of Discount Rate. Also called the time value of money. Today's value of a stream of cash flows is worth less than the sum of the cash flows to be received or saved over time. Present value accounting is widely used in Discounted Cash Flow analysis.' (emphasis[1] supplied)

That this is against consideration for the time value of money is also clear as the money that is 'disbursed' is no longer with the allottee, but, as has just been stated, is with the real estate developer who is legally obliged to give money's equivalent back to the allottee, having used it in the construction of the project, and being at a discounted value so far as the allottee is concerned (in the sense of the allottee having to pay less by way of instalments than he would if he were to pay for the ultimate price of the flat/apartment) . . .

What is clear from what Shri Venugopal has read to us is that a wide range of transactions are subsumed by paragraph (f) and that the precise scope of paragraph (f) is uncertain. Equally, paragraph (f) seems to be a 'catch all' provision which is really residuary in nature, and which would subsume within it transactions which do not, in fact, fall under any of the other sub-clauses of section 5(8).

And now to the precise language of section 5(8)(f). First and foremost, the sub-clause does appear to be a residuary provision which is 'catch all' in nature. This is clear from the words 'any amount' and 'any other transaction' which means that amounts that are 'raised' under 'transactions' not covered by any of the other clauses, would amount to a financial debt if they had the commercial effect of a borrowing. The expression 'transaction' is defined by section 3(33) of the Code as follows :

'3. (33) "transaction" includes an agreement or arrangement in writing for the transfer of assets, or funds, goods or services, from or to the corporate debtor ;'

1. Here printed in italics.

As correctly argued by the learned Additional Solicitor General, the expression 'any other transaction' would include an arrangement in writing for the transfer of funds to the corporate debtor and would thus clearly include the kind of financing arrangement by allottees to real estate developers when they pay instalments at various stages of construction, so that they themselves then fund the project either partially or completely.

Sub-clause (f) section 5(8) thus read would subsume within it amounts raised under transactions which are not necessarily loan transactions, so long as they have the commercial effect of a borrowing. We were referred to Collins *English Dictionary and Thesaurus* (2nd edition, 2000) for the meaning of the expression 'borrow' and the meaning of the expression 'commercial'. They are set out hereinbelow :

'borrow-vb 1. to obtain or receive (something, such as money) on loan for temporary use, intending to give it, or something equivalent back to the lender. 2. to adopt (ideas, words, etc.) from another source ; appropriate. 3. Not standard. to lend. 4. (intr) Golf. To putt the ball uphill of the direct path to the hole : make sure you borrow enough . . .

commercial.-adj. 1. of or engaged in commerce. 2. sponsored or paid for by an advertiser : commercial television. 3. having profit as the main aim : commercial music. 4. (of chemicals, etc.) unrefined and produced in bulk for use in industry. 5. a commercially sponsored advertisement on radio or television.'

A perusal of these definitions would show that even though the petitioners may be right in stating that a 'borrowing' is a loan of money for temporary use, they are not necessarily right in stating that the transaction must culminate in money being given back to the lender. The expression 'borrow' is wide enough to include an advance given by the homebuyers to a real estate developer for 'temporary use' i. e., for use in the construction project so long as it is intended by the agreement to give 'something equivalent' to money back to the homebuyers. The 'something equivalent' in these matters is obviously the flat/apartment. Also of importance is the expression 'commercial effect'. 'Commercial' would generally involve transactions having profit as their main aim. Piecing the threads together, therefore, so long as an amount is 'raised' under a real estate agreement, which is done with profit as the main aim, such amount would be subsumed

> within section 5(8)(f) as the sale agreement between developer and home buyer would have the 'commercial effect' of a borrowing, in that, money is paid in advance for temporary use so that a flat/apartment is given back to the lender. Both parties have 'commercial' interests in the same—the real estate developer seeking to make a profit on the sale of the apartment, and the flat/apartment purchaser profiting by the sale of the apartment. Thus construed, there can be no difficulty in stating that the amounts raised from allottees under real estate projects would, in fact, be subsumed within section 5(8)(f) even without adverting to the *Explanation* introduced by the Amendment Act . . .
>
> That this amendment is in fact clarificatory is also made clear by the Insolvency Committee Report, which expressly uses the word 'clarify', indicating that the Insolvency Law Committee also thought that since there were differing judgments and doubts raised on whether homebuyers would or would not be included within section 5(8)(f), it was best to set these doubts at rest by explicitly stating that they would be so covered by adding an *Explanation* to section 5(8)(f). Incidentally, the Insolvency Law Committee itself had no doubt that given the 'financing' of the project by the allottees, they would fall within section 5(8)(f) of the Code as originally enacted."

41.1.1. It is, therefore, evident that this court, even while interpreting sub-clause (f) of section 5(8) on the question as to whether an allottee under a real estate project could fall thereunder, analysed the gamut of the relevant expressions of "disbursement", "borrowing" and "time value of money", being the root ingredients of "financial debt" within the meaning of the Code.

41.1.2. It is significant to notice that in the case of *Pioneer Urban*[1], one line of arguments on behalf of the petitioners, who led challenge to the amendments, had been that the use of expression "means and includes" in section 5(8) was indicative that the provision was exhaustive and in that position, alien subject-matter such as home buyers could not have been inserted therein. The decision of this court in the case of *P. Kasilingam* v. *P. S. G. College of Technology* [1995] (Supp) 2 SCC 348 was relied upon by the petitioners wherein, this court had rejected an argument that the expression "means and includes" indicated that the definition was inclusive in nature and would also cover the categories which were not

1. See [2019] 217 Comp Cas 1 (SC).

mentioned therein. In *P. Kasilingam* v. *P. S. G. College of Technology* [1995] (Supp) 2 SCC 348, this court had said that the use of the word "means" indicates that the definition is a hard and fast definition and no other meaning could be assigned to the expression than is put down in the definition. As regards the word "includes", this court said that it enlarges the meaning of the expression defined so as to comprehend not only such things as they signify according to their natural import but also those things which the clause declares that they shall include. Further, this court said that the words "means and includes", on the other hand, indicate "an exhaustive explanation" of the meaning which, for the purposes of the Act, must invariably be attached to these words or expressions. On the other hand, another decision of this court in *Krishi Utpadan Mandi Samiti* v. *Shankar Industries* [1993] (Supp) 3 SCC 361 was referred on behalf of the respondents wherein, the court had considered a definition clause whereby the expression "agricultural produce" was defined to mean such items of produce of agriculture, horticulture, viticulture, apiculture, sericulture, pisciculture, animal husbandry, or forest as specified in the Schedule and then, the definition included therein admixture of two or more of such items, and further included any such item in processed form and yet further included specific items like gur, rub, shakkar, khandsari and jaggery. While examining such definition in *Krishi Utpadan Mandi Samiti* v. *Shankar Industries* [1993] (Supp) 3 SCC 361, the court proceeded to say that under the rules of interpretation, when the words "means and includes" are used in a definition, they are to be given a wider meaning and are not exhaustive or restricted to the items contained therein. This statement of law in *Krishi Utpadan Mandi Samiti* v. *Shankar Industries* [1993] (Supp) 3 SCC 361 was held by the three-Judge Bench of this court in *Pioneer Urban*[1] to be not that of good law for it ignored the earlier precedents of larger and co-ordinate Benches and was also out of sync with the later decisions on the same point. However, and at the same time, the arguments on behalf of the petitioners, that sub-clauses (a) to (i) of section 5(8) of the Code must necessarily reflect the fact that the financial debt could only be a debt disbursed against the consideration for the time value of money and which permeates sub-clauses (a) to (i), was also not accepted as a matter of statutory interpretation while observing that the expression "and includes" speaks of the subject-matter which may not necessarily be reflected in the main part of the definition. These observations of the court,

1. See [2019] 217 Comp Cas 1 (SC).

after reproduction of the relevant extracts from the referred decisions, read as under[1] :

> "This statement of the law, as can be seen from the quotation hereinabove, is without citation of any authority. In fact, in *Jagir Singh* v. *State of Bihar* [1976] 2 SCC 942 at paragraphs 11 and 19 to 21 and *Mahalakshmi Oil Mills* v. *State of Andhra Pradesh* [1989] 1 SCC 164, at paragraphs 8 and 11 (which has been cited in *P. Kasilingam* v. *P. S. G. College of Technology* [1995] (Supp) 2 SCC 348 this court set out definition sections where the expression 'means' was followed by some words, after which came the expression 'and includes' followed by other words, just as in the *Krishi Utpadan Mandi Samiti* v. *Shankar Industries* [1993] (Supp) 3 SCC 361. In two other recent judgments, *Bharat Co-operative Bank (Mumbai) Ltd.* v. *Co-operative Bank Employees Union* [2007] 4 SCC 685, at paragraphs 12 and 23 and *State of West Bengal* v. *Associated Contractors* [2015] 1 SCC 32 at paragraph 14, this court has held that wherever the expression 'means' is followed by the expression 'and includes' whether with or without additional words separating 'means' from 'includes', these expressions indicate that the definition provision is exhaustive as a matter of statutory interpretation. It has also been held that the expression 'and includes' is an expression which extends the definition contained in words which follow the expression 'means'. *From this discussion, two things follow.* Krishi Utpadan Mandi Samiti *v.* Shankar Industries [1993] (Supp) 3 SCC 361 *cannot be said to be good law in so far as its exposition on 'means' and 'includes' is concerned*, as it ignores earlier precedents of larger and co-ordinate Benches and is out of sync with later decisions on the same point. Equally, Dr. Singhvi's *argument that sub-clauses (a) to (i) of section 5(8) of the Code must all necessarily reflect the fact that a financial debt can only be a debt which is disbursed against the consideration for the time value of money, and which permeates sub-clauses (a) to (i), cannot be accepted as a matter of statutory interpretation, as the expression 'and includes' speaks of subject-matters which may not necessarily be reflected in the main part of the definition.*" (emphasis[2] supplied)

41.1.3. In the end, however, this court rejected the contentions urged on behalf of the petitioners while accepting other line of submissions on

1. See page 110 of 217 Comp Cas.
2. Here printed in italics.

behalf of the respondents that the Legislature is not precluded by way of amendment from inserting words into what may even be an exhaustive definition and while observing that an exhaustive definition is exhaustive only for the purposes of interpretation of a statute by the courts. This court said[1] :

> "In any event, as was correctly argued by learned Additional Solicitor General Mrs. Madhavi Divan, the Legislature is not precluded by way of amendment from inserting words into what may even be an exhaustive definition. What is an exhaustive definition is exhaustive for purposes of interpretation of a statute by the courts, which cannot bind the Legislature when it adds something to the statute by way of amendment. On this score also, there is no substance in the aforesaid argument."

41.1.4. This court ultimately found that the Explanation was added by the Amendment Act only to clarify the doubt that had arisen as to whether home buyers/allottees were subsumed within section 5(8)(f) of the Code. In essence, the amendment in question was interpreted to be clarificatory in nature so as to put beyond doubt that allottees are to be regarded as financial creditors within the enacting part of section 5(8)(f) of the Code. The Amendment Act was upheld with this court holding as under[2] :

> "In the present case, it is clear that the deeming fiction that is used by the *Explanation* is to put beyond doubt the fact that allottees are to be regarded as financial creditors within the enacting part contained in section 5(8)(f) of the Code.
>
> It was also argued that an explanation does not enlarge the scope of the original section and for this purpose *S. Sundaram Pillai* v. *V. R. Pattabiraman* [1985] 1 SCC 591 was relied upon. This very judgment recognises, in paragraph 46, that an explanation does not ordinarily enlarge the scope of the original section. But if it does, effect must be given to the legislative intent notwithstanding the fact that the Legislature has named a provision as an explanation. (See *Hiralal Rattanlal* v. *State of U. P.* [1973] 1 SCC 216 at 225, followed in paragraph 51 of *S. Sundaram Pillai* v. *V. R. Pattabiraman* [1985] 1 SCC 591). *In any case, it has been found by us that the Explanation was added by the Amendment Act only to clarify doubts that had arisen as to whether homebuyers/allottees were subsumed within section 5(8)(f).*

1. See page 111 of 217 Comp Cas.
2. See page 120 of 217 Comp Cas.

The Explanation added to section 5(8)(f) of the Code by the Amendment Act does not in fact enlarge the scope of the original section as homebuyers/allottees would be subsumed within section 5(8)(f) as it originally stood as has been held by us hereinabove. As a matter of statutory interpretation, that interpretation, which accords with the objects of the statute in question, particularly when we are dealing with a beneficial legislation, is always the better interpretation or the 'creative interpretation' which is the modern trend of authority, and which is reflected in the concurring judgment of *Eera (through Dr. Manjula Krippendorf)* v. *State (NCT of Delhi)* [2017] 15 SCC 133 paragraphs 122 and 127. This argument must, therefore, also be rejected.

We, therefore, hold that allottees/homebuyers were included in the main provision, i. e., section 5(8)(f) with effect from the inception of the Code, the Explanation being added in 2018 merely to clarify doubts that had arisen." (emphasis[1] supplied)

41.1.5. For taking into comprehension the ratio of *Pioneer Urban*[2] and for its application to the question at hand, appropriate it would be to recount the basic principles expounded and explained by a three-Judge Bench in the case of *Haryana Financial Corporation* v. *Jagdamba Oil Mills* [2002] 3 SCC 496 that the observations of the court in a judgment are always required to be read in the context in which they appear. This court has said (page 508) :

"19. Courts should not place reliance on decisions without discussing as to how the factual situation fits in with the fact situation of the decision on which reliance is placed. Observations of courts are not to be read as Euclid's theorems nor as provisions of the statute. These observations must be read in the context in which they appear. Judgments of courts are not to be construed as statutes. To interpret words, phrases and provisions of a statute, it may become necessary for judges to embark upon lengthy discussions but the discussion is meant to explain and not to define. Judges interpret statutes, they do not interpret judgments. They interpret words of statutes, their words are not to be interpreted as statutes. In *London Graving Dock Co. Ltd.* v. *Horton* [1951] AC 737 (HL) (at page 761) Lord MacDermot observed (All ER page 14C-D) :

1. Here printed in italics.
2. See [2019] 217 Comp Cas 1 (SC).

'The matter cannot, of course, be settled merely by treating the ipsissima verba of Willes J., as though they were part of an Act of Parliament and applying the rules of interpretation appropriate thereto. This is not to detract from the great weight to be given to the language actually used by that most distinguished judge.'

20. In *Home Office* v. *Dorset Yacht Co. Ltd.* [1970] 2 All ER 294 (HL), Lord Reid said (at All ER page 297g-h), 'Lord Atkin's speech . . . is not to be treated as if it were a statutory definition. It will require qualification in new circumstances'. Megarry, J. in *Shepherd Homes Ltd.* v. *Sandham (No. 2)* [1971] 1 WLR 1062 (Ch D) observed : 'One must not, of course, construe even a reserved judgment of even Russell, L.J. as if it were an Act of Parliament'. And, in *British Railways Board* v. *Herrington* [1972] 2 WLR 537 (HL) Lord Morris said (All ER page 761c) :

'There is always peril in treating the words of a speech or a judgment as though they were words in a legislative enactment, and it is to be remembered that judicial utterances are made in the setting of the facts of a particular case.'

21. Circumstantial flexibility, one additional or different fact may make a world of difference between conclusions in two cases. Disposal of cases by blindly placing reliance on a decision is not proper."

41.1.6. Read as a whole and with reference to its context, it is but clear that in *Pioneer Urban*[1] this court has not enunciated that the scope of the expression "financial debt" be read as if to encompass any debt of whatsoever nature. Rather, a submission made therein, with reference to the decision in *Krishi Utpadan Mandi Samiti* v. *Shankar Industries* [1993] (Supp) 3 SCC 361, that "and includes" part in a definition may lead to it being extensive, was rejected by this court while holding that the said decision was not a good law. However, the other extreme of submissions, seeking restrictive interpretation with reference to "means" part of the definition, was also not accepted and, in that context, the court observed that the expression "and includes" speaks of subject-matters which may not necessarily be reflected in the main part of the definition. Obviously, there could be several subject-matters which may not, as such, be found squarely manifested in the expressions employed in the "means" part of a definition and could be reasonably found in the "includes" part. However, it has not been laid down as a rule of statutory interpretation that

1. See [2019] 217 Comp Cas 1 (SC).

the "includes" part could stand alone, disjunct from and totally alien to the "means" part.

The expressions "means and includes" in the definition clauses—effect

42 Looking to the frame of the Code, where the significant expressions "financial creditor" and "financial debt" have been defined with the words "means" and "includes", we may further refer to the principles of construction of such a definition clause in a statute. Tersely put, the law remains settled that where a word is defined to "mean" something, the definition is prime facie restrictive and exhaustive. On the other hand, where the word defined is declared to "include" something more, the definition is prima facie extensive. However, a little difficulty arises when the definition contains both the words "means" and "includes"[1].

42.1. As noticed, in the case of *Pioneer Urban*[2], a suggestion made on behalf of the respondents with reference to the decision in *Krishi Utpadan Mandi Samiti* v. *Shankar Industries* [1993] (Supp) 3 SCC 361, that when the words "means and includes" are used in a definition, they are to be given a wider meaning and are not exhaustive or restricted to the items contained therein, was not accepted by this court ; and the statement of law in *Krishi Utpadan Mandi Samiti* v. *Shankar Industries* [1993] (Supp) 3 SCC 361 was held to be not that of good law for it ignored the earlier precedents of larger and co-ordinate Benches and was also out of sync with the later decisions on the same point. However, the other extreme of interpretation, as canvassed by the petitioners, that a financial debt could only be a debt which is disbursed against the consideration for the time value of money, and such requirement pervades all sub-clauses (a) to (i), was also not accepted as a matter of statutory interpretation by this court while observing that the expression "and includes" speaks of subject-matters which may not necessarily be reflected in the main part of the definition. Thus, it is evident that this court did not accept either of the extremities suggested by the parties in *Pioneer Urban*[2] for interpretation and implication of the expressions "means and includes" in a definition clause of the statute. Significantly, in *Pioneer Urban*[2], none of the extremities had any bearing on the conclusion because, eventually, the amendment in question

1. *Craise on Statue Law* (Seventh edition-Indian reprint 1999 page 213) has stated this feature as follows :
"There are two forms of interpretation clause. In one, where the word defined is declared to 'mean' so and so, the definition is explanatory and prima facie restrictive. In the other, where the word defined is declared to 'include' so and so, the definition is extensive, e. g., 'sheriff' includes 'undersheriff'. Sometimes the definition contains the words 'mean and include', which inevitably raises a doubt as to interpretation."
2. See [2019] 217 Comp Cas 1 (SC).

was held to be only clarificatory in nature ; and this court held that the Explanation added to section 5(8)(f) of the Code by the Amendment Act did not enlarge the scope of the original section.

42.2. Various features of the process of interpretation while dealing with such definition clauses were explained by this court in the case of *Delhi Development Authority* v. *Bhola Nath Sharma* [2011] 2 SCC 54 in the following :

> "25. The definition of the expressions 'local authority' and 'person interested' are inclusive and not exhaustive. The difference between exhaustive and inclusive definitions has been explained in *P. Kasilingam* v. *P. S. G. College of Technology* [1995] (Supp) 2 SCC 348 in the following words (SCC page 356, paragraph 19) :
>
> '19. A particular expression is often defined by the Legislature by using the word "means" or the word "includes". Sometimes the words "means and includes" are used. The use of the word "means" indicates that "definition is a hard-and-fast definition, and no other meaning can be assigned to the expression than is put down in definition. (See *Gough* v. *Gough* [1891] 2 QBD 665 (CA) ; *Punjab Land Development and Reclamation Corporation Ltd.* v. *Labour Court* [1990] 3 SCC 682, SCC page 717, paragraph 72). The word "includes" when used, enlarges the meaning of the expression defined so as to comprehend not only such things as they signify according to their natural import but also those things which the clause declares that they shall include. The words "means and includes", on the other hand, indicate "an exhaustive explanation of the meaning which, for the purposes of the Act, must invariably be attached to these words or expressions". (See *Dilworth* v. *Commissioner of Stamps* [1899] AC 99 (PC) (Lord Watson) ; *Mahalakshmi Oil Mills* v. *State of Andhra Pradesh* [1989] 1 SCC 164, SCC page 170, paragraph 11). The use of the words "means and includes" in rule 2(b) would, therefore, suggest that the definition of "college" is intended to be exhaustive and not extensive and would cover only the educational institutions falling in the categories specified in rule 2(b) and other educational institutions are not comprehended. In so far as engineering colleges are concerned, their exclusion may be for the reason that the opening and running of the private engineering colleges are controlled through the Board of Technical Education and Training and the Director of Technical Education in accordance with the directions issued by the AICTE from time to time.'

26. In *Bharat Co-operative Bank (Mumbai) Ltd.* v. *Co-operative Bank Employees Union* [2007] 4 SCC 685 this court again considered the difference between the inclusive and exhaustive definitions and observed (SCC page 695, paragraph 23) :

'23. . . . when in the definition clause given in any statute the word "means" is used, what follows is intended to speak exhaustively. When the word "means" is used in the definition . . . it is a "hard-and-fast" definition and no meaning other than that which is put in the definition can be assigned to the same . . . On the other hand, when the word "includes" is used in the definition, the Legislature does not intend to restrict the definition : it makes the definition enumerative but not exhaustive. That is to say, the term defined will retain its ordinary meaning but its scope would be extended to bring within it matters, which in its ordinary meaning may or may not comprise. Therefore, the use of the word "means" followed by the word "includes" in (the definition of "banking company" in) section 2(bb) of the ID Act is clearly indicative of the legislative intent to make the definition exhaustive and would cover only those banking companies which fall within the purview of the definition and no other.'

27. In *N. D. P. Namboodripad* v. *Union of India* [2007] 4 SCC 502 the court observed (SCC page 509, paragraph 18) :

'18. The word "includes" has different meanings in different contexts. Standard dictionaries assign more than one meaning to the word "include". *Webster's Dictionary* defines the word "include" as synonymous with "comprise" or "contain". Illustrated *Oxford Dictionary* defines the word "include" as : (i) comprise or reckon in as a part of a whole ; (ii) treat or regard as so included. Collins *Dictionary of English Language* defines the word "includes" as : (i) to have as contents or part of the contents ; be made up of or contain ; (ii) to add as part of something else ; put in as part of a set, group or a category ; (iii) to contain as a secondary or minor ingredient or element. It is no doubt true that generally when the word "include" is used in a definition clause, it is used as a word of enlargement, that is to make the definition extensive and not restrictive. But the word "includes" is also used to connote a specific meaning, that is, as "means and includes" or "comprises" or "consists of". (emphasis[1] in original)

1. Here printed in italics.

28. In *Hamdard (Wakf) Laboratories* v. *Deputy Labour Commissioner* [2007] 5 SCC 281 it was held as under (SCC page 294, paragraph 33) :

'33. When an interpretation clause uses the word "includes", it is prima facie extensive. When it uses the word "means and includes", it will afford an exhaustive explanation to the meaning which for the purposes of the Act must invariably be attached to the word or expression'."

42.3. In the case of *Black Diamond Beverages* v. *CTO* [1998] 1 SCC 458[1], while examining a definition that carried both "means" and "includes" expressions, this court pointed out that the natural meaning of the "means" part of the definition is not narrowed down by the "includes" part. This court extracted the definition in question and said[2] :

"The 1954 Act generally provides for levy of a single-point tax at the first stage on commodities notified under section 25 of that Act. On the other hand, the 1941 Act is a general statute providing for multipoint levy of sales tax on commodities not covered by the 1954 Act. Sub-clause (d) of section 2 of the 1954 Act reads as follows :

'2. (d) "sale-price" used in relation to a dealer means the amount of the money consideration for the sale of notified commodities manufactured, made or processed by him in West Bengal, or brought by him into West Bengal from any place outside West Bengal, for the purpose of sale in West Bengal, less any sum allowed as cash discount according to trade practice, but *includes* any sum charged for containers or other materials for the packaging of notified commodities ;' (emphasis[3] supplied)

We shall first deal with the contention of the appellants' counsel based upon the non-inclusion of 'freight charges' in the definition of sale price in section 2(d) of the 1954 Act.

It is clear that the definition of 'sale price' in section 2(d) uses the words 'means' and 'includes'. The first part of the definition defines the *meaning* of the word 'sale price' and must, in our view, be given its ordinary, popular or natural meaning. The interpretation thereof is in no way controlled or affected by the second part which 'includes'

1. See [1997] 107 STC 219 (SC).
2. See page 222 of 107 STC.
3. Here printed in italics.

certain other things in the definition. This is a well-settled principle of construction. *Craies on Statute Law* (7th edition, 1.214) says :

'An interpretation clause which extends the meaning of a word does not take away its ordinary meaning . . . Lord Selborne said in *Robinson* v. *Local Board of Barton-Eccles* [1883] 8 AC 798, AC at page 801 :

'An interpretation clause of this kind is not meant to prevent the word receiving its ordinary, popular, and natural sense whenever that would be properly applicable, but to enable the word as used in the Act . . . to be applied to something to which it would not ordinarily be applicable'. (emphasis[3] supplied)

Therefore, the inclusive part of the definition cannot prevent the main provision from receiving its natural meaning."

The essentials for financial debt and financial creditor

43 Applying the aforementioned fundamental principles to the definition occurring in section 5(8) of the Code, we have not an iota of doubt that for a debt to become "financial debt" for the purpose of Part II of the Code, the basic elements are that it ought to be a disbursal against the consideration for time value of money. It may include any of the methods for raising money or incurring liability by the modes prescribed in sub-clauses (a) to (f) of section 5(8) ; it may also include any derivative transaction or counter-indemnity obligation as per sub-clauses (g) and (h) of section 5(8) ; and it may also be the amount of any liability in respect of any of the guarantee or indemnity for any of the items referred to in sub-clauses (a) to (h). The requirement of existence of a debt, which is disbursed against the consideration for the time value of money, in our view, remains an essential part even in respect of any of the transactions/dealings stated in sub-clauses (a) to (i) of section 5(8), even if it is not necessarily stated therein. In any case, the definition, by its very frame, cannot be read so expansive, rather infinitely wide, that the root requirements of "disbursement" against "the consideration for the time value of money" could be forsaken in the manner that any transaction could stand alone to become a financial debt. In other words, any of the transactions stated in the said sub-clauses (a) to (i) of section 5(8) would be falling within the ambit of "financial debt" only if it carries the essential elements stated in the principal clause or at least has the features which could be traced to such essential elements in the principal clause. In yet other words, the essential element of disbursal, and that too against the consideration for time value of money, needs to be found in the genesis of any debt before it may be treated as "financial

debt" within the meaning of section 5(8) of the Code. This debt may be of any nature but a part of it is always required to be carrying, or corresponding to, or at least having some traces of disbursal against consideration for the time value of money.

As noticed, the root requirement for a creditor to become financial cre- **44**
ditor for the purpose of Part II of the Code, there must be a financial debt which is owed to that person. He may be the principal creditor to whom the financial debt is owed or he may be an assignee in terms of extended meaning of this definition but, and nevertheless, the requirement of existence of a debt being owed is not forsaken.

It is also evident that what is being dealt with and described in section **45**
5(7) and in section 5(8) is the transaction vis-a-vis the corporate debtor. Therefore, for a person to be designated as a financial creditor of the corporate debtor, it has to be shown that the corporate debtor owes a financial debt to such person. Understood this way, it becomes clear that a third party to whom the corporate debtor does not owe a financial debt cannot become its financial creditor for the purpose of Part II of the Code.

Expounding yet further, in our view, the peculiar elements of these **46**
expressions "financial creditor" and "financial debt", as occurring in section 5(7) and (8), when visualised and compared with the generic expressions "creditor" and "debt" respectively, as occurring in section 3(10) and (11) of the Code, the scheme of things envisaged by the Code becomes clearer. The generic term "creditor" is defined to mean any person to whom the debt is owed and then, it has also been made clear that it includes a "financial creditor", a "secured creditor", an "unsecured creditor", an "operational creditor", and a "decree-holder". Similarly, a "debt" means a liability or obligation in respect of a claim which is due from any person and this expression has also been given an extended meaning to include a "financial debt" and an "operational debt".

46.1. The use of the expression "means and includes" in these clauses, on the very same principles of interpretation as indicated above, makes it clear that for a person to become a creditor, there has to be a debt, i. e., a liability or obligation in respect of a claim which may be due from any person. A "secured creditor" in terms of section 3(30) means a creditor in whose favour a security interest is created ; and "security interest", in terms of section 3(31), means a right, title or interest or claim of property created in favour of or provided for a secured creditor by a transaction which secures payment for the purpose of an obligation and it includes, amongst

others, a mortgage. Thus, any mortgage created in favour of a creditor leads to a security interest being created and thereby, the creditor becomes a secured creditor. However, when all the defining clauses are read together and harmoniously, it is clear that the Legislature has maintained a distinction amongst the expressions "financial creditor", "operational creditor", "secured creditor" and "unsecured creditor". Every secured creditor would be a creditor ; and every financial creditor would also be a creditor but every secured creditor may not be a financial creditor. As noticed, the expressions "financial debt" and "financial creditor", having their specific and distinct connotations and roles in insolvency and liquidation process of corporate persons, have only been defined in Part II whereas the expressions "secured creditor" and "security interest" are defined in Part I.

47 A conjoint reading of the statutory provisions with the enunciation of this court in *Swiss Ribbons*[1], leaves nothing to doubt that in the scheme of the IBC, what is intended by the expression "financial creditor" is a person who has direct engagement in the functioning of the corporate debtor ; who is involved right from the beginning while assessing the viability of the corporate debtor ; who would engage in restructuring of the loan as well as in reorganisation of the corporate debtor's business when there is financial stress. In other words, the financial creditor, by its own direct involvement in a functional existence of corporate debtor, acquires unique position, who could be entrusted with the task of ensuring the sustenance and growth of the corporate debtor, akin to that of a guardian. In the context of insolvency resolution process, this class of stakeholders namely, financial creditors, is entrusted by the Legislature with such a role that it would look forward to ensure that the corporate debtor is rejuvenated and gets back to its wheels with reasonable capacity of repaying its debts and to attend on its other obligations. Protection of the rights of all other stakeholders, including other creditors, would obviously be concomitant of such resurgence of the corporate debtor.

47.1. Keeping the objectives of the Code in view, the position and role of a person having only security interest over the assets of the corporate debtor could easily be contrasted with the role of a financial creditor because the former shall have only the interest of realising the value of its security (there being no other stakes involved and least any stake in the corporate debtor's growth or equitable liquidation) while the latter would, apart from looking at safeguards of its own interests, would also and simultaneously be interested in rejuvenation, revival and growth of the corporate debtor. Thus understood, it is clear that if the former, i. e., a person having

1. See [2019] 213 Comp Cas 198 (SC).

only security interest over the assets of the corporate debtor is also included as a financial creditor and thereby allowed to have its say in the processes contemplated by Part II of the Code, the growth and revival of the corporate debtor may be the casualty. Such result would defeat the very objective and purpose of the Code, particularly of the provisions aimed at corporate insolvency resolution.

47.2. Therefore, we have no hesitation in saying that a person having only security interest over the assets of corporate debtor (like the instant third party securities), even if falling within the description of "secured creditor" by virtue of collateral security extended by the corporate debtor, would nevertheless stand outside the sect of "financial creditors" as per the definitions contained in clauses (7) and (8) of section 5 of the Code. Differently put, if a corporate debtor has given its property in mortgage to secure the debts of a third party, it may lead to a mortgage debt and, therefore, it may fall within the definition of "debt" under section 3(10) of the Code. However, it would remain a debt alone and cannot partake the character of a "financial debt" within the meaning of section 5(8) of the Code.

The respondent mortgagees are not the financial creditors of corporate debtor JIL

Indisputably, the debts in question are in the form of third party security **48**
; said to have been given by the corporate debtor JIL so as to secure the loans/advances/facilities obtained by JAL from the respondent-lenders. Such a "debt" is not and cannot be a "financial debt" within the meaning of section 5(8) of the Code ; and hence, the respondent-lenders, the mortgagees, are not the "financial creditors" of the corporate debtor JIL.

Though several decisions have been cited on behalf of the respondent- **49**
lenders to contend that they do fall within the definition of "financial creditor" but for what has been discussed hereinabove, it does not appear necessary to dilate upon all of them. However, it would be appropriate to take note of the relevant decisions strongly relied upon by the respondents as infra.

Much emphasis is laid on behalf of the respondents on the observations **50**
occurring in another three-Judge Bench decision of this court in the case of *Essar Steel*[1] and predominantly on the observation therein, that "secured creditors as a class are subsumed in the class of financial creditors". Again, the decisions of the court are required to be understood with reference to the context. In the case of *Essar Steel*[1], the questions before the court related to the roles of resolution applicant, resolution professional and

1. See [2020] 219 Comp Cas 97 (SC).

committee of creditors constituted under the Code and the jurisdiction of Adjudicating Authority as also the Appellate Tribunal in questioning the resolution plans. The constitutional validity of the Insolvency and Bankruptcy (Amendment) Act, 2019 was also under challenge. The problem arose essentially with the decision of NCLAT holding that in a resolution plan, there could be no difference amongst the creditors in that, a financial creditor and operational creditor deserve equal treatment under a resolution plan. It was in the setup of such background that in *Essar Steel*[1], this court made the observations relied upon by the respondents.

50.1. The referred observations in the case of *Essar Steel*[1] are essentially based on the earlier observations occurring in the case of *Swiss Ribbons*[1]. As noticed, the decision in *Swiss Ribbons*[1] was rendered by this court when constitutional validity of various provisions of the Code was put to challenge. In *Essar Steel*[1], this court reiterated the enunciations in *Swiss Ribbons*[1] in paragraph 55 in the following[2] :

"Financial creditors are in the business of lending money. The RBI report on Trend and Progress of Banking in India, 2017-18 reflects that the net interest margin of Indian banks for the financial year 2017-18 is averaged at 2.5 per cent. Likewise, the global trend for net interest margin was at 3.3 per cent. for banks in the USA and 1.6 per cent. for banks in the UK in the year 2016, as per the data published on the website of the bank. Thus, it is clear that financial creditors earn profit by earning interest on money lent with low margins, generally being between 1 to 4 per cent. Also, financial creditors are capital providers for companies, who in turn are able to purchase assets and provide a working capital to enable such companies to run their business operation, whereas operational creditors are beneficiaries of amounts lent by financial creditors which are then used as working capital, and often get paid for goods and services provided by them to the corporate debtor, out of such working capital. On the other hand, market research carried out by India Brand Equity Foundation, a trust established by the Ministry of Commerce and Industry, as regards the Oil and Gas sector, has stated that the business risk of operational creditors who operate with higher profit margins and shorter cyclical repayments must needs be higher. Also, operational creditors have an immediate exit option, by stopping supply to the corporate debtor, once corporate debtors start defaulting in payment. Financial creditors may exit on their long-term loans, either upon repayment of the full amount or upon default, by recalling the entire loan facility and/or enforcing the security interest which is a

1. See [2019] 213 Comp Cas 198 (SC).
2. See page 168 of 219 Comp Cas.

time consuming and lengthy process which usually involves litigation. Financial creditors are also part of a regulated banking system which involves not merely declaring defaulters as non-performing assets but also involves restructuring such loans which often results in foregoing unpaid amounts of interest either wholly or partially. All these differences between financial and operational creditors have been reflected, albeit differently, in the judgment of *Swiss Ribbons*[1]"

50.2. In the relevant part, the court found that the NCLAT had fallen in grave error in reading paragraph 77 in *Swiss Ribbons*[1] de hors the earlier paragraphs. In that context this court said[2] :

> "By reading paragraph 77 de hors the earlier paragraphs, the Appellate Tribunal has fallen into grave error. Paragraph 76 clearly refers to the *UNCITRAL Legislative Guide* which makes it clear beyond any doubt that equitable treatment is only of similarly situated creditors. This being so, the observation in paragraph 77 cannot be read to mean that financial and operational creditors must be paid the same amounts in any resolution plan before it can pass muster. On the contrary, paragraph 77 itself makes it clear that there is a difference in payment of the debts of financial and operational creditors, operational creditors having to receive a minimum payment, being not less than liquidation value, which does not apply to financial creditors. The amended regulation 38 set out in paragraph 77 again does not lead to the conclusion that financial and operational creditors, or secured and unsecured creditors, must be paid the same amounts, percentage wise, under the resolution plan before it can pass muster. Fair and equitable dealing of operational creditors' rights under the said Regulation involves the resolution plan stating as to how it has dealt with the interests of operational creditors, which is not the same thing as saying that they must be paid the same amount of their debt proportionately. Also, the fact that the operational creditors are given priority in payment over all financial creditors does not lead to the conclusion that such payment must necessarily be the same recovery percentage as financial creditors. So long as the provisions of the Code and the Regulations have been met, it is the commercial wisdom of the requisite majority of the committee of creditors which is to negotiate and accept a resolution plan, which may involve differential payment to different classes of creditors, together with

1. See [2019] 213 Comp Cas 198 (SC).
2. See page 172 of 219 Comp Cas.

negotiating with a prospective resolution applicant for better or different terms which may also involve differences in distribution of amounts between different classes of creditors.

Indeed, by vesting the committee of creditors with the discretion of accepting resolution plans only with financial creditors, operational creditors having no vote, the Code itself differentiates between the two types of creditors for the reasons given above. Further, as has been reflected in *Swiss Ribbons*[1], most financial creditors are secured creditors, whose security interests must be protected in order that they do not go ahead and realise their security in legal proceedings, but instead are incentivised to act within the framework of the Code as persons who will resolve stressed assets and bring a corporate debtor back to its feet. Shri Sibal's argument that the expression 'secured creditor' does not find mention in Chapter II of the Code, which deals with the resolution process, and is only found in Chapter III, which deals with liquidation, is for the reason that secured creditors as a class are subsumed in the class of financial creditors, as has been held in *Swiss Ribbons*[1]. Indeed, regulation 13(1) of the 2016 Regulations mandates that when the resolution professional verifies claims, the security interest of secured creditors is also looked at and gets taken care of."

50.3. While strongly relying upon one of the observations occurring in *Essar Steel*[2], that secured creditors as a class are subsumed in the class of financial creditors, learned counsel for the respondents would assert that secured creditors do become financial creditors. The submission remains untenable for more than one reason. First, the submission itself proceeds on the same shortcoming as was existing in the NCLAT's decision that was disapproved by this court in *Essar Steel*[2], i. e., reading of a line in a judgment disjunct from the context. Secondly, in the decisions above referred, this court has never expanded the scope of "financial debt" as envisaged by section 5(8) of the Code. Thirdly, the case of an indirect secured creditor, i. e., the person having in its hand only the security interest over the property of the corporate debtor but with no corresponding involvement in the finances and growth of the corporate debtor, was never under consideration in the said decisions.

50.4. We may usefully elaborate a little. On a contextual reading of the expositions in *Essar Steel*[2] and *Swiss Ribbons*[1], it is but clear that the court had examined the status of direct secured creditor of the corporate debtor

1. See [2019] 213 Comp Cas 198 (SC).
2. See [2020] 219 Comp Cas 97 (SC).

and there had not been any occasion to examine the features related with an indirect secured creditor, who is neither involved in assessing the viability of the corporate debtor nor in lending finances to the corporate debtor for setting up the business. As noticed, the prime, rather only, area of interest of such indirect secured creditor is in recovery of its debt and not in reorganization of the corporate debtor's business. Thus understood, it is absolutely clear that the class of secured creditors indicated by this court in *Essar Steel*[1] and *Swiss Ribbons*[2], as being subsumed in financial creditors, is only that of such secured creditors who are directly engaged in advancing credit to the corporate debtor and not the indirect creditors who had extended any loan or facility to a third party but had taken a security from the corporate debtor, whose resolution is under consideration.

50.5. Hence, we are undoubtedly of the view that the decisions in *Swiss Ribbons*[2] and *Essar Steel*[1] do not enure to the benefit of the respondents ; rather on the principles enunciated therein, they only operate against the respondents.

The case of *State Bank of India* v. *Smt. Kusum Vallabhdas Thakkar* **51**
[1991] SCC Online Guj 14 has also been repeatedly referred by the respondents in support of their contentions that because of the transactions of mortgage, the corporate debtor JIL owes them the mortgage debt as a guarantee obligation and hence, it falls within the ambit of "financial debt" within the meaning of section 5(8) of the Code.

51.1. We may have a close look at the relevant background aspects of the said case of *State Bank of India* v. *Smt. Kusum Vallabhdas Thakkar* [1991] SCC Online Guj 14. Therein, the appellant-bank had advanced a loan to the firm of which, husband of the respondent was the proprietor. The respondent had executed an agreement in favour of the appellant-bank to the effect that so long as her husband's firm was indebted to the bank, she would execute, by way of collateral security, a legal mortgage of the immovable property, being a flat belonging to her, with or without possession, in favour of the bank within 14 days of issuance of written requisition for such execution. Later on, when the bank called upon the respondent to execute the mortgage as per the agreement, she declined to do so and hence, a suit for specific performance and in the alternative for damages was filed by the appellant-bank. The trial court, however, dismissed the suit while holding, inter alia, that the agreement in question was without consideration. The suit was dismissed on certain other grounds too with which we are not concerned herein.

1. See [2020] 219 Comp Cas 97 (SC).
2. See [2019] 213 Comp Cas 198 (SC).

51.2. In appeal by the bank, the High Court, while holding that the agreement to create a mortgage was specifically enforceable, proceeded to examine the question as to whether the promise to create mortgage, if given by a third party and not by the borrower, is for consideration and is valid. The High Court held that by making the promise, the respondent had agreed to provide collateral security and thereby to discharge the liability to a third party in case of his default. The court observed that such guarantee was limited to the security offered and no personal liability by the promisor ; and thus, the promisor became a surety and referred to sections 126, 127 and 128 of the Contract Act.

51.3. With reference to section 128 of the Contract Act, the court pointed out that the liability of a surety is ordinarily co-extensive with that of the debtor but in the case at hand, such liability of the surety was as otherwise provided by the contract ; and such liability of the respondent was to the extent of securing the dues by creation of mortgage. The court said that as the principal debtor could create a mortgage of his immovable property, a third person could also agree to create a mortgage so as to secure the dues of the principal debtor. As regards the consideration, the court said that though no direct consideration had flowed from the appellant to the respondent but, in such tripartite agreement, anything done for the benefit of the principal debtor is sufficient consideration to the surety for giving guarantee. For their relevance, we may notice the relevant parts of paragraphs 12, 13, 14, 17 and 21 of the said decision in *State Bank of India* v. *Smt. Kusum Vallabhdas Thakkar* [1991] SCC Online Guj 14 as follows :

> "12. The next question that arises is whether such promise to create a mortgage, if given by a third party and not by the borrower or the principle debtor, is for consideration and is valid. The learned trial Judge has held that for creating mortgage, the mortgagor must be a debtor and must have right to redeem mortgage on payment of the debt and since the present defendant was not the debtor, she could not create a mortgage in respect of that debt and that the mortgagor should be a debtor and there must be a relationship of debtor and creditor, the mortgage being a security for the debt. The learned trial Judge has also held that there was no consideration for giving this promise of executing the mortgage. Both these aspects are interrelated. By making the promise by exhibit 20, defendant has agreed to provide collateral security of a legal mortgage to secure repayment of all the moneys due from Nitin Pharmaceuticals. Thus, the defendant has promised to discharge the liability of a third person (the debtor)

in case of his default. This guarantee is limited to the security offered by the promisor, namely, the mortgage and no further personal liability is taken by the promisor. Thus, the promisor has became a surety and this would be an agreement to offer security for due performance of that promise and to that extent. Sections 126, 127 and 128 of the Contract Act read as follows : . . .

13. The liability of the surety is co-extensive with that of the debtors. However, in the present case, the liability of the surety is as otherwise provided by the contract exhibit 20. Therefore, the liability of the defendant is as provided in the agreement and to that extent of securing dues by a creation of mortgage, no personal liability is accepted by the surety. It is, therefore, fallacious to say that the defendant is not a debtor and, therefore, the defendant could not have created a mortgage in favour of the creditor. The defendant has rendered himself liable to the dues of Nitin Pharmaceuticals by agreeing to provide security in the form of mortgage for the dues. Just as the principal debtor can create a mortgage of his immovable properties, a third person can also agree to create a mortgage so as to secure the dues of the principal debtor. In that manner, he becomes a surety to the extent of the security or the mortgage. If that were not so, the present commercial and banking transactions would not be possible and would be hampered to a great extent. In the present day world of commerce, a person may not have sufficient security to offer for obtaining advances from financial institutions even though satisfying the requirements. In such cases, he draws upon resources of others by asking them to give guarantee and also security for the performance of that guarantee and it is a perfectly legitimated and legal way of conducting such commercial transactions. In fact, Chapter VIII of the Contract Act deals with indemnity and guarantee and provides for this kind of tripartite arrangement.

14. As regards consideration, it is true that no direct consideration has flowed from the plaintiff to the defendant who has made the promise to create a mortgage. But in such tripartite arrangement, anything done for the benefit of the principal debtor is a sufficient consideration to the survey for giving guarantee as expressly provided in section 127 of the Contract Act. Thus, even though there is no consideration to the third party-surety for mortgages, the consideration of having done anything for the benefit of the principal debtor is a sufficient consideration . . .

17. In the present case, the consideration that anything done for the benefit of the principal debtor is a sufficient consideration to the surety. Anything done in the present case is that the loans advanced to the principal debtor who is the husband of the present defendant. She has agreed to give collateral security to secure the dues in default of payment by her husband. Apart from the close relationship of husband and wife, there is substantial consideration by having advanced the loan . . .

21. Thus, the plaintiff not enforcing the claim against the principal debtor or even the third person may be sufficient consideration by the debtor or third person to give security for the debt and the consideration for such promise is that by such forbearance, the creditor is delayed and the debtor or third party is benefited. It is also seen that even in absence of express promise to forbear, a simple forbearance from enforcing the claim can be held to have been implied in the present case. This promise and agreement was given in 1975 and it is clear that thereafter for two years, the claim was not pressed which shows that there is actual forbearance against the principal debtor after this exhibit 20 was executed. Thus, even under the English Law, this consideration is held to be good and sufficient consideration. Under Indian Law, which is significantly different from English Law of Contract, past consideration or the consideration towards third person is statutorily held to be good consideration as defined in section 2(d) and as mentioned in section 127 of the Contract Act. The observation of the learned trial Judge that as the husband of the defendant had to pay Rs. 5 lakhs to the plaintiff, the writing exhibit 20 which is subsequently obtained is without consideration, is patently erroneous. In the present case, it is amply clear that the principal debtor was a defaulter in meeting his financial obligations to the bank and the bank had noticed the irregularities in his accounts and the, bank could have proceeded against the principal debtor to effect recovery. At that stage, at the instance of the principal debtor-husband, wife comes forward and agrees to give collateral security obviously to secure forbearance against the principal debtor. Thus, at the desire of the promisor (defendant) the bank has abstained from enforcing its claim against the principal debtor and has forborne itself from suing the husband. Such forbearance is sufficient and valid consideration for the promise made by the defendant to agree to create mortgage and give collateral security. The learned Trial Judge is in

error in observing that 'an act done at the desire of third party is not a consideration'. It must, therefore, be held that the suit agreement exhibit 20 is for sufficient and valid consideration and is valid and enforceable."

51.4. The said decision in *State Bank of India* v. *Smt. Kusum Vallabhdas Thakkar* [1991] SCC Online Guj 14, at best, leads to the position that a promise to create a mortgage, even if given by a third party and not by the borrower would be deemed to be for consideration; that even if no direct consideration had flown from the plaintiff to the defendant who made the promise to create the mortgage, anything done for the benefit of the principal debtor would be sufficient consideration to the surety for giving guarantee as provided under section 127 of the Contract Act. When the creditor abstained from enforcing the claim against the principal debtor because of such promise to create mortgage by the defendant, such forbearance was held to be sufficient and valid consideration. It is difficult to stretch the ratio of the said decision so as to be applied to the issue at hand concerning the definition of "financial debt" under section 5(8) of the Code, which conspicuously omits mortgage ; and which requires "disbursement" against "the consideration for the time value of money" as the lead elements. As said, the respondent-lenders of JAL, while holding the mortgages in their hands, as said to have been executed by the corporate debtor JIL, may be carrying a security interest and may be the creditors who may claim to be falling within the terminology "secured creditors", yet cannot become "financial creditors" of the corporate debtor JIL who is not owing any "financial debt" to them. The decision in *State Bank of India* v. *Smt. Kusum Vallabhdas Thakkar* [1991] SCC Online Guj 14 does not make out a case in favour of the respondents, the lenders of JAL.

Another decision forming the mainstay of the respondents had been **52**
that in the case of *Rajkumari Kaushalya Devi* v. *Bawa Pritam Singh,* AIR 1960 SC 1030. The relevant background aspects of the said case had been that the appellant had executed two usufructuary mortgages with respect to the two properties situated in Feroozepore city in favour of the respondent while also taking the same property on lease on the very same date in 1946. On default in effecting payments by the appellant, the respondents filed an application under section 13 of the Displaced Persons (Debts Adjustment) Act 70 of 1951[1] seeking recovery of the principal amount together with arrears of rental. While omitting other

1. "Act 70 of 1951" for short.

aspects which may not be relevant, noticeable it is for the present purpose that one of the points for consideration in the case had been as to whether the liability created under the said mortgage was a "debt" within the meaning of section 2(6) of the Act 70 of 1951. It was contended on behalf of the appellant that such liability under the mortgage was not a pecuniary liability and, therefore, section 2(6) did not apply to a mortgage debt.

52.1. The argument aforesaid was rejected by this court after taking note of the definition of "debt" as occurring in the said enactment. The principal part of the said definition, relevant for the present purpose read as under (page 1031 of AIR 1960 SC) :

> "'Debt' means any pecuniary liability, whether payable presently or in future, or under a decree or order of civil or revenue court or otherwise, or whether ascertained or to be ascertained, which . . ."

52.2. This court, inter alia, observed, with reference to the definition aforesaid as occurring in the Act 70 of 1951 and the definition of "mortgage" as occurring in the Transfer of Property Act, as under (page 1031 of AIR 1960 SC) :

> "3. The main contention of the appellant in this connection is that a mortgage debt is not a pecuniary liability and therefore does not fall within the definition of debt at all. We are of opinion that there is no force in this contention. The words 'pecuniary liability' will cover any liability which is of a monetary nature. Now the definition of a mortgage in section 58 of the Transfer of Property Act 4 of 1882, shows that though it is the transfer of an interest in specific immovable property, the purpose of the transfer is to secure the payment of money advanced or to be advanced by way of loan or to secure an existing or future debt or the performance of an engagement which may give rise to a pecuniary liability. The money advanced by way of loan, for example, which is secured by a mortgage, obviously creates a pecuniary liability. It is true that a mortgage in addition to creating the pecuniary liability also transfers interest in the specific immovable property to secure that liability ; none the less the loan or debt to secure which the mortgage is created will remain a pecuniary liability of the person creating the mortgage. Therefore a mortgage debt would create a pecuniary liability upon the mortgagor and would be covered by the definition of the word 'debt' in section 2(6) . . ."

52.3. The proposition aforesaid, being related with the definition of "debt" as occurring in the said enactment (Act 70 of 1951), cannot have a direct application in the present case. In any event, the said decision cannot be taken as an authority governing the transaction where there is no direct debt of the mortgagor himself.

The other citations, on various terminologies related with mercantile law **53** and mortgage transactions, do not advance the cause of the respondents because of distinct and rather peculiar requirements of section 5(8) of the Code. Of course, the decision of the NCLT in *SREI Infrastructure Finance Ltd.* v. *Sterling International Enterprises Ltd.*[1] stands disapproved for what we have held hereinabove. Equally, the other submissions about the contents of the documents in question as also the entitlement of the respondent-lenders to invoke the security or to take up the proceedings under SARFAESI Act, etc., do not, in any event, make the transactions in question "financial debts" within the meaning of section 5(8) of the Code. Such submissions have only been noted to be rejected.

Summation on second issue

For what has been discussed hereinabove, on the issue as to whether **54** lenders of JAL could be treated as financial creditors, we hold that such lenders of JAL, on the strength of the mortgages in question, may fall in the category of secured creditors, but such mortgages being neither towards any loan, facility or advance to the corporate debtor nor towards protecting any facility or security of the corporate debtor, it cannot be said that the corporate debtor owes them any "financial debt" within the meaning of section 5(8) of the Code ; and hence, such lenders of JAL do not fall in the category of the "financial creditors" of the corporate debtor JIL.

Conclusion

Accordingly, and in view of the above, these appeals are allowed to the **55** extent and in the manner that :

(1) The impugned order dated August 1, 2019 as passed by the NCLAT in the batch of appeals is reversed and is set aside.

(2) The appeals preferred before the NCLAT against the order dated May 16, 2018 as passed by the NCLT on the application filed by the IRP, are dismissed ; and consequently, the order dated May 16, 2018 so passed by the NCLT is upheld in regard to the findings that the transactions in question are preferential within the meaning of section 43 of the Code. The

1. See [2020] 221 Comp Cas 580 (NCLT).

directions by the NCLT for avoidance of such transactions are also upheld accordingly.

(3) The appeals preferred before the NCLAT against the orders passed by the NCLT dated May 9, 2018 and May 15, 2018 on the applications filed by the lender banks are also dismissed and the respective orders passed by the NCLT are restored with the findings that the applicants are not the financial creditors of the corporate debtor-Jaypee Infratech Ltd.

Acknowledgment

56 While closing on these appeals, we put on record our thanks and compliments to learned counsel for the respective parties as also their associates and researchers for erudite and scholarly presentation of their respective view points, in oral as also in written submissions and in rendering invaluable assistance to the court in dealing with the vast variety of questions involved in these matters.

[2020] 221 Comp Cas 758 (SC)

[IN THE SUPREME COURT OF INDIA]

SHAILENDRA SWARUP

v.

DEPUTY DIRECTOR, ENFORCEMENT DIRECTORATE

ASHOK BHUSHAN and **R. SUBHASH REDDY** JJ.

July 27, 2020.

HF ▶ Appellant

PENALTY—DIRECTORS—LIABILITY—FOREIGN EXCHANGE—CONTRAVENTION BY COMPANY—NON-EXECUTIVE DIRECTOR—MUST BE SHOWN TO HAVE BEEN IN CHARGE OF AND RESPONSIBLE FOR CONDUCT OF COMPANY'S BUSINESS AT RELEVANT TIME—REASONABLE OPPORTUNITY FOR MAKING REPRESENTATION MUST BE GIVEN BEFORE ADJUDICATION—FAILURE TO CONSIDER DIRECTOR'S WRITTEN REPRESENTATION THAT HE WAS NOT RESPONSIBLE FOR CONDUCT OF AFFAIRS OF COMPANY—PENALTY SET ASIDE—FOREIGN EXCHANGE REGULATION ACT, 1973, SS. 8, 50, 51, 68.

The necessary ingredient for proceeding against a director of a company for contravention of provisions of the Foreign Exchange Regulation Act, 1973, shall be that at the time offence was committed, the director was in charge of and responsible to the company for the conduct of the business of the

company. The liability to be proceeded against for the offence under section 68 of the Act depends on the role one plays in the affairs of the company and not on mere designation or status.

Section 68(1) of the Act creates a legal fiction, i. e., "shall be deemed to be guilty". The legal fiction is activated on fulfilment of the conditions contained in the section. The words "every person who, at the time of the contravention was committed, was in charge of, and was responsible to, the company for the conduct of business" have to be given some meaning and purpose. The provision cannot be read to mean that whosoever was a director of a company at the relevant time when the contravention took place, shall be deemed to be guilty of the contravention. Had the Legislature intended that all the directors irrespective of their role and responsibilities shall be deemed to be guilty of contravention, the section could have been worded in different manner. When a person is proceeded against for committing an offence and is to be punished, necessary ingredients of the offence as required by section 68 should be present.

For imposing a penalty under section 50 of the Act, the adjudicating officer is required to hold an enquiry after giving the person a reasonable opportunity for making a representation in the matter. Even though the Act does not contemplate the filing of a written complaint but in proceedings contemplated by section 51, the person who has to be proceeded against has to be informed of the contravention for which penalty proceedings are initiated. The expression "after giving that person a reasonable opportunity for making a representation in the matter" occurring in section 51 itself contemplates due communication of the allegations of contravention and unless the allegations contain the complete ingredients of the offence within the meaning of section 68, it cannot be said that a reasonable opportunity for making a representation in the matter has been given to the person, who is to be proceeded against.

A person in the commercial world having a transaction with company is entitled to presume that the directors of the company are in charge of the affairs of the company. The presumption of a person in the commercial world is a rebuttable presumption and when the adjudicating authority proceeds to impose a penalty for a contravention of the Act, the essential ingredients constituting an offence under the Act read with section 68 have to be communicated to the person proceeded against to enable him to make effective representation in the matter.

The Enforcement Directorate initiated proceedings against a company and its directors, including the appellant for violation of the Act. The Deputy

Director issued to show-cause notices to all concerned for contravention of section 51 of the Act. The company replied to the show-cause notice through its company secretary. The Directorate of Enforcement decided to hold proceedings as contemplated in section 51 of the Act and fixed a date for personal hearing. The appellant submitted a detailed reply to the notice for personal hearing. He had stated that he was a practising advocate of the Supreme Court and was only a part-time, non-executive director of the company and he was never in the employment of the company nor had an executive role in the functions of the company. He further stated that the he was never in charge of nor ever responsible for the conduct of business of the company. Along with the reply an affidavit of the company secretary that the appellant who was the director of the company was only a part-time, director and never in charge of the day-to-day business of the company was also filed. The company also submitted a reply. The Deputy Director after hearing the appellant and other directors of the company passed an order imposing a penalty of Rs. 1,00,000 on the appellant for contravention of section 8(3) read with 8(4) and section 68 of the Act. The Appellate Tribunal for Foreign Exchange dismissed the appeal filed by the appellant and the High Court affirmed the order. On further appeal :

Held, *allowing the appeal, that the High Court committed an error in observing that the plea taken by the appellant in its reply dated October 29, 2003 was an afterthought, since, no such plea was taken in reply to the show-cause notice. Although the notice dated February 19, 2001 was addressed to the company and all its directors, the reply was given only by the company secretary and none of the directors had given any reply. The notice dated February 19, 2001 was issued by the Deputy Director, Enforcement Directorate to decide whether the adjudication proceedings as contemplated in section 51 should be held against the directors for contravention. When the Deputy Director decided to hold the adjudication proceedings under section 51 of the Act the reply given in response to the notice dated October 8, 2003 was statutorily required to be considered under section 51 of the Act. The reply could not have been ignored by an erroneous assumption that it was an afterthought as had been done by the High Court. October 29, 2003 was the date fixed by the adjudicating officer for personal hearing of the directors. The representation dated October 29, 2003 was the first representation submitted by the appellant before the adjudicating officer during the course of personal hearing. The statement of the person called for a personal hearing even though given in the form of written representation and was required to be considered by the adjudicating officer. Otherwise the personal hearing would become an*

empty formality and meaningless, specially when what was said by the appellant in his representation dated October 29, 2003 in no manner contradicted the reply sent by the company secretary. The written representation submitted by the appellant required due consideration and the High Court erred in discarding it as an afterthought. The affidavit of the company secretary dated July 4, 2003 clearly stating that the appellant who was director of the company was only a part time director of the company and was never in charge of the day-to-day business of the company was very much on the record of the adjudicating officer and the High Court erred in holding that the material was not filed before the adjudicating officer or the Appellate Tribunal. The High Court had erroneously discarded the plea of the appellant that he was part-time, non-executive director as afterthought and did not consider it. The adjudicating officer had imposed the penalty without returning a finding that it was the appellant who was liable for contravention of the provisions of section 8(3), (4) and section 68 of the Act. The Appellate Tribunal had also not considered the plea of the appellant and making general observation that the management of the company was to be handled by the board of directors. The appellant being director was held guilty without a finding that the appellant was not a part-time, non-executive director and was responsible for the conduct of business of the company at the relevant time. In another order which was passed on February 13, 2004 by the Deputy Director in adjudication proceedings although with regard to different period, the plea of the appellant that he was only a part-time, non-executive director and not responsible of the conduct of business of the company was accepted and notice was discharged against the appellant. The order dated February 13, 2004 although relating to a different period had categorically noticed the status of the appellant as part-time non-executive director. There had to be some reasons for taking a contrary view by the adjudicating officer in the order dated March 31, 2004 with regard to affairs of the same company. The adjudicating officer had erroneously imposed penalty on the appellant for the alleged offence under section 8(3), (4) and section 68 of the Act and it had been erroneously affirmed both by the Appellate Tribunal and the High Court. The penalty set aside.

S. M. S. PHARMACEUTICALS LTD. *v.* NEETA BHALLA [2005] 127 Comp Cas 563 (SC) *relied on*.

NATIONAL SMALL INDUSTRIES CORP. LTD. *v.* HARMEET SINGH PAINTAL [2010] 154 Comp Cas 313 (SC) *distinguished*.

Decision of the Delhi High Court in SHAILENDRA SWARUP *v.* DIRECTOR, ENFORCEMENT DIRECTORATE [2011] 162 Comp Cas 346 (Delhi) *reversed*.

Cases referred to :

National Small Industries Corp. Ltd. *v.* Harmeet Singh Paintal [2010] 154 Comp Cas 313 (SC) (paras 31, 35)

Pooja Ravinder Devidasani *v.* State of Maharashtra [2015] 190 Comp Cas 106 (SC) (para 31)

Rangachari (N.) *v.* Bharat Sanchar Nigam Ltd. [2007] 137 Comp Cas 198 (SC) (paras 32, 33, 34, 40)

S. M. S. Pharmaceuticals Ltd. *v.* Neeta Bhalla [2005] 127 Comp Cas 563 (SC) (paras 27, 29, 32, 33, 34, 38)

Saroj Kumar Poddar *v.* State (NCT of Delhi) [2007] 137 Comp Cas 837 (SC) (para 33)

Shailendra Swarup *v.* Director, Enforcement Directorate [2011] 162 Comp Cas 346 (Delhi) (para 1)

Wahi (N. K.) *v.* Shekhar Singh [2007] 137 Comp Cas 939 (SC) (para 31)

Criminal Appeal No. 2463 of 2014.

Appeal from the judgment and order dated November 18, 2009 of the Delhi High Court in Crl. A. No. 575 of 2008. The judgment of the Delhi High Court is reported as *Shailendra Swarup* v. *Director, Enforcement Directorate* [2011] 162 Comp Cas 346 (Delhi).

C. A. Sundaram and *Kailash Vasdev*, Senior Advocates (*Ms. Rohini Musa*, *Jagjit Singh Chhabra*, *Saksham Maheshwari* and *Abhishek Gupta*, Advocates with them) for the appellant.

K. M. Nataraj, Additional Solicitor General (*Ms. Shirin Khajuria*, *Ms. Ranjana Narayan* and *B. Krishna Prasad*, Advocates with him) for the respondent.

JUDGMENT

The judgment of the court was delivered by

1 ASHOK BHUSHAN J.—This appeal has been filed against the judgment of Delhi High Court dated November 18, 2009[1] dismissing the criminal appeal filed by the appellant by which appeal the judgment dated March

1. See *Shailendra Swarup* v. *Director, Enforcement Directorate* [2011] 162 Comp Cas 346 (Delhi).

26, 2008 of the Appellate Tribunal for Foreign Exchange in Appeal No. 622 of 2004 filed by the appellant was challenged.

Brief facts of the case giving rise to this appeal are : 2

2.1 Modi Xerox Ltd. (MXL) was a company registered under the Companies Act, 1956 in the year 1983. Between the period June 12, 1985-November 21, 1985, 20 remittances were made by the company-MXL through its banker Standard Chartered Bank. The Reserve Bank of India issued a letter stating that despite reminder issued by the authorised dealer, MXL had not submitted the Exchange Control copy of the custom bills of entry/postal wrappers as evidence of import of goods into India. Enforcement Directorate wrote to MXL in the year 1991-93 for supplying invoices as well as purchase orders. MXL on July 9, 1993 provided for four transactions and chartered accountant's certificates for balance 16 amounts for which MXL's bankers were unable to trace old records dating back to 1985. MXL amalgamated and merged into Xerox Modicorp Ltd. (hereinafter referred to as "XMC") on January 10, 2000. A show-cause notice dated February 19, 2001 was issued by the Deputy Director, Enforcement Directorate to MXL and its directors, including the appellant. The show-cause notice required to show cause in writing as to why adjudication proceedings as contemplated in section 51 of the Foreign Exchange Regulation Act, 1973 (hereinafter referred to as the "FERA, 1973") should not be held for contravention. Xerox Modi Corporation Ltd. (successor of MXL) replied the show-cause notice dated February 19, 2001 vide its letter dated March 26, 2001. The Directorate of Enforcement decided to hold proceedings as contemplated in section 51 of the FERA, 1973 read with sections 3 and 4 of section 49 of the FEMA and fixed October 22, 2003 for personal hearing. Notice dated October 8, 2003 was sent to MXL and its directors. Notice dated October 8, 2003 was replied by the appellant vide its detailed reply dated October 29, 2003. In the reply the appellant stated that he is a practicing advocate of the Supreme Court and was only a part-time, non-executive director of MXL and he was never in the employment of the company nor had executive role in the functions of the company. It was further stated that the appellant was never in charge of nor ever responsible for the conduct of business of the company. Along with the reply an affidavit of the company secretary dated July 4, 2003 that the appellant who was the director of erstwhile company-XML was only a part-time, director of the said company and never in charge of the day-to-day business of the company was also filed. The MXL has also submitted a reply dated October 29, 2003. The Deputy

Director, Enforcement Directorate after hearing the appellant, other directors of the company passed an order dated March 31, 2004 imposing a penalty of Rs. 1,00,000 on the appellant for contravention of section 8(3) read with 8(4) and section 68 of the FERA, 1973.

2.2 Aggrieved by the order dated March 31, 2004 imposing penalty of Rs. 1,00,000 on the appellant, Appeal No. 622 of 2004 was filed by the appellant before the Appellate Tribunal for Foreign Exchange which appeal came to be dismissed by the Appellate Tribunal on March 26, 2008. Against the order of the Appellate Tribunal dated March 26, 2008, Criminal Appeal No. 575 of 2008 was filed by the appellant in the Delhi High Court. The Delhi High Court by the impugned judgment dated November 18, 2009 has dismissed the appeal of the appellant, questioning which judgment this appeal has been filed.

3 The High Court, in criminal appeal, during pendency of the appeal has stayed the order of penalty. This court while issuing notice on February 19, 2010 in the present appeal had also stayed the order of penalty imposed on the appellant.

4 We have heard Shri C. A. Sundaram, learned senior counsel for the appellant and Shri K. M. Nataraj, learned Additional Solicitor General for the respondent.

5 Shri C. A. Sundaram, learned senior counsel for the appellant submits that the High Court dismissed the appeal of the appellant holding that reply dated October 29, 2003 of the appellant taking the plea that he was only a part-time director was only an afterthought. The High Court further held that the affidavit dated July 4, 2003 of the company secretary relied by the appellant does not appear to have been filed either before the adjudicating authority or the Appellate Tribunal and no such plea had been taken in the earlier communications. Shri Sundaram submits that the High Court committed error in dismissing the appeal of the appellant whereas neither there was any material nor any specific case of the Department that the appellant was in charge of and responsible for the conduct of business of the company. The mere fact of company-MXL in its reply to the notice dated February 19, 2001 having given the names of the 13 persons as directors of MXL does not amount to stating that all the directors were responsible for the conduct of business of the company. The appellant could have been prosecuted and punished for the contravention of the provisions of the FERA, 1973 only after returning a finding that it was the appellant who was responsible for the conduct of business during the relevant period when remittances in question were made by MXL. The Appellate Tribunal without recording any finding that the appellant was in charge of the

affairs of the company held the appellant liable, observing that there is nothing on record to show that any restriction was placed on the powers of the appellants as directors of the company with reference to subject transactions. The adjudicating authority although noticed the detailed reply given by the appellant dated October 29, 2003 but without returning any finding that the appellant was director who was responsible for working of MXL at the relevant time imposed the penalty only relying on the letter of the company secretary where names of the persons who were in the board of directors were mentioned.

Shri Sundaram further submits that with regard to a subsequent transaction, proceedings were initiated against the appellant in respect to transaction of MXL where the plea of the appellant that he was only a part-time, non-executive director and had no executive role or function in the company was accepted and proceedings were dropped in so far as the appellant is concerned by order dated February 13, 2004 which order clearly noticed the status and role of the appellant. 6

The learned Additional Solicitor General refuting the submissions of counsel for the appellant contends that penalty has rightly been imposed on the appellant. He submits that admittedly the appellant was director during the relevant period which fact was admitted too in the reply given to the show-cause notice. The show-cause notice was issued against all the directors including the appellant and no effort has been made by the appellant to disprove the allegations made against him. The learned Additional Solicitor General submits that there needs no specific complaint in proceedings of the FERA, 1973 as opposed to complaint under the Negotiable Instruments Act, 1881. When the proceedings have been initiated under section 51 of the FERA, 1973, the burden is on the appellant to prove that he had no role to play on behalf of the company. 7

Learned counsel for the parties have placed reliance on few decisions of this court which shall be referred to while considering the submissions of the parties in detail. 8

From the submissions made by the parties and materials on records following points arise for determination in this appeal : 9

> "(1) Whether the plea taken by the appellant in its reply dated October 29, 2003 that he was only a part-time, non-executive director and was never in charge of nor even responsible for the conduct of business of the company at the relevant time was an afterthought, since, in the reply given by the company secretary dated March 26, 2001 no such plea was taken ?

(2) Whether the appellant has not brought any material on record either before the adjudicating authority or the Appellate Tribunal to prove that he was only a part-time, non-executive director not responsible for the conduct of business of the company at the time of commission of the offence ?

(3) Whether the adjudicating authority, Appellate Tribunal and the High Court erred in holding contravention of provisions of section 8(3) and (4) and section 68 of the FERA, 1973 by the appellant without their being any material that the appellant was responsible for the conduct of business of the company at the time of commission of the offence and without recording any specific findings to that effect ?"

Point No. 1

10 As noted above, the High Court has rejected the plea of the appellant that he was part-time, non-executive director not responsible for the conduct of business of the company at the relevant period on the ground that the above plea is an afterthought since in reply given by the company secretary to show-cause notice dated February 19, 2001 no such plea was taken.

11 We may first notice the show-cause notice dated February 19, 2001. The show-cause notice dated February 19, 2001 was given to the MXL and all directors of MXL and along with show-cause notice annexure B was a list of directors of MXL where the name of the appellant was also included at Serial No. 12. It is relevant to notice following portion of the show-cause notice :

"And whereas it further appears that S/Shri—as per annexure B proprietor, partner(s)/manager/secretary of the said company/firm has been responsible/supervisor/in charge of the said company/firm for the conduct of business of the company/firm at the relevant time when the aforesaid import was made as such he/she/they has/have rendered himself/herself/themselves liable also to be proceeded against under section 50 of the Foreign Exchange Regulation Act, 1973 (46 of 1973).

Now therefore, the said M/s. Modi Xerox Ltd., as well as its directors of the above address are hereby required to show cause in writing (in duplicate) within thirty days from the date of receipt of this memorandum as to why adjudication proceedings as contemplated in section 51 of the Foreign Exchange Regulation Act, 1973 (46 of 1973) should not be held against them for the aforesaid contravention."

The show-cause notice, thus, asked the directors to show cause as to **12** why adjudication proceedings as contemplated in section 51 of the FERA, 1973 should not be held against them. The reply to the said notice was sent only by the company through acting company secretary dated March 26, 2001. The Deputy Director, Enforcement Directorate after considering the reply to show cause by XMC's vide letter dated March 26, 2001 decided to hold adjudication proceedings as contemplated in section 51 of FERA, 1973. Adjudication notice dated October 8, 2003 was issued by the Deputy Director, Enforcement asking the directors to appear for personal hearing on October 22, 2003. It is relevant to reproduce the contents of the notice dated October 8, 2003 which are to the following effect :

"DIRECTORATE OF ENFORCEMENT
FOREIGN EXCHANGE MANAGEMENT
MINISTRY OF FINANCE
DEPARTMENT OF REVENUE
GOVERNMENT OF INDIA

Head Quarters Office,
6th Floor Lok Nayak Bhawan,
Khan Market, New Delhi-110 003.

F. No. T4. 20/DZ/2001/DD(AV)VM/4571 Date 8-10-2003

From

The Deputy Director of Enforcement

To

M/s. Modi Xerox Ltd.
Ground Floor, Hemkunt Tower,
98, Nehru Place,
New Delhi-19.
And its directors (as per first attached).

Dear Sir/Madam,

Subject : Adjudication proceedings in respect of Memo No. T-4/20/D2/2001 (SCN.) dated 19-2-2001

This is to inform you that after considering the cause shown by you in/as you have failed to reply to the abovementioned memorandum the Deputy Director of Enforcement is of the opinion the adjudication proceeding as contemplated in section 51 of the FERA, 1973 read with

sections 3 and 4 of section 49 of the FEMA, 1999 should be held against you in accordance with the procedure laid shown in Rules of the Adjudication Proceedings and Appeal Rules, 1974 and has accordingly fixed this case for personal hearing before him on October 22, 2003 (October 22, 2003) at 12:30 p.m. in the office of this Directorate at the abovementioned address.

Now, therefore, you are hereby given an opportunity to present yourself either personally or through your lawyer or other authorised representative before the Deputy Director of Enforcement for personal hearing on the aforesaid date, time and place.

You may please note that in case you fail to appear before the Adjudication Authority on the aforesaid date he may proceed with the enquiry in your absence and pass Adjudication Order on the basis of material and evidence available to him.

Your attention in this connection is invited to the provisions to rule 3 of the Adjudication Proceedings and Appeal Rules, 1974 read with sections 3 and 4 of section 49 of the FEMA, 1999 whereby in case it is decided to hold Adjudication Proceedings personal hearing of the case could be waived at your request. In case you prefer to waive personal hearing you may intimate accordingly so that the case may be decided without your personal attendance on the basis of available evidence.

Yours faithfully,

Sd/-

For Deputy Director."

13 We may also notice the provisions of section 51 of the FERA, 1973, which is to the following effect :

"51. *Power to adjudicate.*—For the purpose of adjudging under section 50 whether any person has committed a contravention of any of the provisions of this Act (other than those referred to in that section) or of any rule, direction or order made thereunder, the adjudicating officer shall hold an inquiry in the prescribed manner after giving that person a reasonable opportunity for making a representation in the matter and if, on such inquiry, he is satisfied that the person has committed the contravention, he may impose such penalty as he thinks fit in accordance with the provisions of that section."

The provisions of section 51 as noted above oblige the adjudicating officer to hold an inquiry in the prescribed manner after giving that person a reasonable opportunity for making a representation in the matter. **14**

When the notice dated October 8, 2003 was given for adjudication proceedings it was obligatory for the adjudicating officer to give opportunity for making representation. In response to the notice dated October 8, 2003 the appellant has submitted a detailed reply dated October 29, 2003. In his reply the appellant apart from other facts stated following : **15**

> "1. The undersigned is a practicing advocate of the hon'ble Supreme Court of India and was only a part-time, non-executive director of erstwhile Modi Xerox Ltd., and was never in its employment nor ever had any executive role or function in the said company. Further the undersigned was never in charge of nor ever responsible for the conduct of the business of the company MXL nor did the noticee ever had any executive role or function in the company.
>
> 2. The undersigned noticee had not at any stage been involved in any discussions or decisions relating to the import by the said company and never issued any instructions to any banker or any other functionary of MXL to get any remittance affected out of India for any import.
>
> 3. The notices was neither in charge of nor ever responsible for conduct of the day-to-day business of MXL."

The representation dated October 29, 2003 was, thus, first representation submitted by the appellant in response to adjudication notice and the plea taken by the appellant that he was only a part-time, non-executive director of erstwhile MXL and was never in charge of nor even responsible for the conduct of business of the company was the plea taken first time by the appellant and could not have been termed either as afterthought or denied consideration. The High Court committed error in observing that plea taken by the appellant in its reply dated October 29, 2003 was afterthought, since, no such plea was taken in reply to the show-cause notice dated February 19, 2001. As noted above the notice dated February 19, 2001 although was addressed to the company and all its directors, the reply was given only by the company secretary and none of the directors has given any reply. The notice dated February 19, 2001 was issued by the Deputy Director, Enforcement Directorate to decide as to whether the adjudication proceedings as contemplated in section 51 should be held against the directors for contravention. When the Deputy Director decided to hold the adjudication proceedings under section 51 **16**

reply given in response to the notice dated October 8, 2003 was statutorily required to be considered under section 51 and the said reply could not have been ignored or knocked down by an erroneous assumption that it was an afterthought as has been done by the High Court. October 29, 2003 was the date fixed by the adjudicating officer for personal hearing of the directors. The appellant had not submitted any reply to show-cause notice dated February 19, 2001 which though was addressed to the company and all directors and the reply was sent only by the company secretary on March 26, 2001. The representation dated October 29, 2003 was the first representation submitted by the appellant before the adjudicating officer during course of personal hearing. What is said by a person who is called for personal hearing even though given in the form of written representation dated October 29, 2003 required to be considered by the adjudicating officer otherwise the personal hearing shall become an empty formality and meaningless, specially when what was said by the appellant in his representation dated October 29, 2003 in no manner contradicted the reply March 26, 2001 sent by the company secretary. We, thus, are of the considered opinion that the written representation dated October 29, 2003 submitted by the appellant required due consideration and the High Court erred in discarding it as an afterthought.

Point No. 2

17 We may further note that the High Court in its judgment has observed that affidavit relied upon by the appellant dated July 4, 2003 of the company secretary had not been filed either before the adjudicating authority or the Appellate Tribunal nor any such plea was taken in the earlier communications. This has been observed in paragraph 17 of the impugned judgment, which is to the following effect[1] :

> "It was only as an afterthought and later on that the petitioner in his subsequent reply dated October 29, 2003 took up a plea that he was only a part time director and relied upon an affidavit dated July 4, 2003 of the company secretary Mukesh Dugar which even otherwise does not appear to have been filed either before the adjudicating authority or the Appellate Tribunal. No such plea had been taken in any of the earlier communications."

18 The above view of the High Court is neither correct nor based on materials on the record.

1. See page 351 of 162 Comp Cas.

The adjudicating officer in its order dated March 31, 2004 has noted the reply dated October 29, 2003 on behalf of the appellant. The reply dated October 29, 2003 has been brought on the record of the paper book as annexure P4. In paragraph 10(1) of the reply dated October 29, 2003 the affidavit filed by the company secretary has been relied which was also enclosed with the reply as annexure C. Affidavit of the company secretary dated July 4, 2003 which was enclosed with the reply was to the following effect : **19**

"AFFIDAVIT

I, Mukesh Dugar son of Shri S. R. Dugar and presently the Company Secretary and Head-Legal of Xerox Modicorp Ltd., having its registered office at 109, Shivalik Apartments, Sector 3, Noida, Distt. Gautam Budh Nagar, Uttar Pradesh do hereby solemnly affirm and state as follows :

1. That Modi Xerox Ltd., has since been merged into Xerox Modicorp Ltd., vide orders dated January 10, 2000 and January 21, 2000 of the hon'ble Allahabad High Court.

2. That Mr. Shailendra Swarup, who was a director of the erstwhile Modi Xerox Ltd., was only a part time director of the said company and was never in charge of the day-to-day business of the company.

Place : Gurgaon Sd/-

Date : July 4, 2003 Deponent

Verification

Verified that the contents of this affidavit are true to the best of my knowledge and no part of it is false and nothing material has been concealed therein.

Signed and verified at Gurgaon on this 4th day of July, 2003.

Deponent."

Thus, the affidavit of the company secretary dated July 4, 2003 clearly stating that the appellant who was director of the erstwhile MXL was only a part time director of the said company and was never in charge of the day-to-day business of the company was very much on the record of the adjudicating officer and the High Court erred in holding that the said material was not filed before the adjudging authority or the Appellate Tribunal. **20**

The High Court, thus, discarded the plea of the appellant that he was part-time, non-executive director as afterthought and did not consider the **21**

same on the ground that the affidavit dated July 4, 2003 relied by the appellant was not filed which, as noted above, is not correct. There was nothing on record brought on behalf of the Department that the above plea of the appellant was incorrect and it was the appellant who was responsible for the conduct of business of the company at the relevant time.

22 We, thus, are of the view that the material was brought by the appellant on the record that he was a part-time, non-executive director not in charge of the affairs of the company at the relevant time, which was erroneously refused to be considered.

Point No. 3

23 The adjudicating authority has in its order dated March 31, 2004 noted the reply dated October 29, 2003 filed on behalf of the appellant and adjudicating authority has extracted several paragraphs of the reply of the appellant. Paragraph 10 of the reply has been extensively quoted by the adjudicating authority specially sub-paragraphs (1), (2) and (3) which are to the following effect :

> "10. It is prayed that the proceedings initiated may kindly be dropped on the following amongst other main grounds, which are set out hereinafter without prejudice to one another and are in addition to the facts and submission set forth hereinabove :
>
> (1) That the notice was a decorative part time non-executive director and the board meetings attended by him have only been in his capacity as a part-time non-executive director and not in any other capacity. The noticee was never in the employment of the company and never ever had nay executive role or function in the company. A copy of the affidavit filed by the noticee with his reply to show-cause notice No. T-4/337/DZ/2002, dated May 28, 2002 of the company secretary of XMC at the time to its swearing confirming that the noticee was only a part-time director of MXL and was never in charge of the day-to-day business of MXL is enclosed herewith and marked as annexure C. This notice has been never engaged in the day-to-day conduct of the business of MXL. He has never entered into any import agreement. He has never issued any instructions to any person or the bank for causing any remittance abroad and as such he is not responsible for liable at all in any manner.
>
> (2) It is respectfully submitted that the documents enclosed with MXL's reply of December 4, 1991, December 25, 1991, December 25, 1991 and July 9, 1993 and XMC's reply dated March 26, 2001 will

establish that goods have been imported against the remittances mentioned in the annexure and they had been duly reported to Reserve Bank of India and there is no evidence of goods not having been imported.

(3) This noticee was never in charge of the day-to-day business of MXL and had no knowledge of the transactions in respect of which the above referred show-cause notice dated October 8, 2003 had been issued much less any intent or knowledge of alleged contraventions as set forth therein. The certificates of compliances given by MXL management to the Board prove and establish that the contraventions alleged in the above referred notice and the subject memorandum, in any view of the matter if occurred, were without the knowledge and had nothing to do with the transactions in question, the question of this noticee committing consciously or deliberately any contravention of the FERA or any other law or regulations does not arise and no penalty can in law be imposed on this noticee. The adjudication proceedings are otherwise not maintainable in law."

After noticing the above plea of the appellant, the adjudicating authority **24** has noticed that letter dated March 26, 2001 of the company secretary where he has given the names of 13 directors and after noticing the aforesaid 13 directors the adjudicating authority has recorded its conclusion in following words :

"I have also gone through the replies received from other directors and found that they were not responsible for the day-to-day activities of the company and were not the directors during the relevant period which was between June 12, 1985 to November 21, 1985 and they were the nominees of IFCI, GIC, ICICI, UTI and IDBI respectively, hence, I drop the charges against the directors except S/Shri Bhupinder Kumar Modi, Umesh Kumar Modi, John Rodger Miligan, James Campbell White and Shailendra Swarup who were directors at relevant time and responsible for working of the M/s. Modi Xerox Ltd., I hereby find them guilty and impose a penalty of Rs. 1,00,000 (rupees one lakh only) each on S/Shri Bhupinder Kumar Modi, Umesh Kumar Modi, John Rodger Miligan, James Campbell White and Shailendra Swarup and Rs. 5,00,000 (rupees five lakhs only) on M/s. Modi Xerox Ltd., for contravention of section 8(3) read with section 8(4) and section 68 of the FERA, 1973, I also find the other directors were not joined the company at relevant time when the transaction had taken place and were not

responsible for the conduct of the company, hence I drop the charges against S/Shri Laurence Lyndon Haddon, Stephen Lawrence Tiemey, Bernard Fournier, R. S. Lodha, R. P. Goel, Jan Williams Van Erde, Chaman Lal Turki Dhar, Ramesh C. Vash, S. K. Jain, K. P. Narasimhan, Sunil Mitra, Sundershan Lal, R. K. Mahajan, C. G. Parekh, Kari Kumar and Usha Ranjan Saha."

25 There is no consideration of pleas of the appellant as has been extracted by the adjudicating officer himself as noted above specially in paragraph 10(1), 10(2) and 10(3) of the reply. The adjudicating officer has not even held that the pleas taken by the appellant were untenable. The adjudicating officer, thus, has imposed the penalty without returning a finding that it was the appellant who was liable for contravention of the provisions of section 8(3), (4) and section 68 of the FERA, 1973. The order of the adjudicating officer, thus, is unsustainable on the above ground also.

26 The Appellate Tribunal has also not considered the above plea of the appellant and by making general observation that management of the company is to be handled by the board of directors, hence, the appellant being director is held guilty. No finding has been returned by the Appellate Tribunal that the appellant was not a part-time, non-executive director and was responsible for the conduct of business of the company at the relevant time.

27 We may also notice few judgments of this court some of which have also been referred to by learned counsel for the parties. A three-Judge Bench judgment in *S. M. S. Pharmaceuticals Ltd.* v. *Neeta Bhalla* [2005] 8 SCC 89[1], had occasion to consider the provisions of section 141 of the Negotiable Instruments Act, 1981 which provisions are pari materia to section 68 of the FERA, 1973. Section 68 of the FERA, 1973 deals with Offences by companies and is to the following effect :

"68. *Offences by companies.*—(1) Where a person committing a contravention of any of the provisions of this Act or of any rule, direction or order made thereunder is a company, every person who, at the time of the contravention was committed, was in charge of, and was responsible to, the company for the conduct of business of the company as well as the company, shall be deemed to be guilty of the contravention and shall be liable to be proceeded against and punished accordingly :

1. See [2005] 127 Comp Cas 563 (SC).

Provided that nothing contained in this sub-section shall render any such person liable to punishment if he proves that the contravention took place without his knowledge or that he exercised all due diligence to prevent such contravention.

(2) Notwithstanding anything contained in sub-section (1), where a contravention of any of the provisions of this Act or of any rule, direction or order made thereunder has been committed by a company and it is proved that the contravention has taken place with the consent or connivance of, or is attributable to any neglect on the part of, any director, manager, secretary or other officer of the company, such director, manager, secretary or other officer shall also be deemed to be guilty of the contravention and shall be liable to be proceeded against and punished accordingly.

Explanation.—For the purposes of this section—

(i) 'company' means any body corporate and includes a firm or other association of individuals ; and

(ii) 'director', in relation to a firm, means a partner in the firm."

In the Negotiable Instruments Act, 1881 initially there was no provision **28**
regarding offences by companies and by Act 66 of 1988 section 141 was inserted in the Negotiable Instruments Act, 1881 which provision is to the following effect :

"141. *Offences by companies.*—(1) If the person committing an offence under section 138 is a company, every person who, at the time the offence was committed, was in charge of, and was responsible to, the company for the conduct of the business of the company, as well as the company, shall be deemed to be guilty of the offence and shall be liable to be proceeded against and punished accordingly :

Provided that nothing contained in this sub-section shall render any person liable to punishment if he proves that the offence was committed without his knowledge, or that he had exercised all due diligence to prevent the commission of such offence :

Provided further that where a person is nominated as a director of a company by virtue of his holding any office or employment in the Central Government or State Government or a financial corporation owned or controlled by the Central Government or the State

Government, as the case may be, he shall not be liable for prosecution under this Chapter.

(2) Notwithstanding anything contained in sub-section (1), where any offence under this Act has been committed by a company and it is proved that the offence has been committed with the consent or connivance of, or is attributable to, any neglect on the part of, any director, manager, secretary or other officer of the company, such director, manager, secretary or other officer shall also be deemed to be guilty of that offence and shall be liable to be proceeded against and punished accordingly.

Explanation.—For the purposes of this section,—

(a) 'company' means any body corporate and includes a firm or other association of individuals ; and

(b) 'director', in relation to a firm, means a partner in the firm."

29 A bare reading of section 141 of the Negotiable Instruments Act, 1881 indicates that sub-section (1) and sub-section (2) of section 141 are pari materia to section 68 of the FERA, 1973 which was already in the statute. This court in *S. M. S. Pharmaceuticals Ltd.* v. *Neeta Bhalla* [2005] 8 SCC 89[1] had occasion to consider the requirements of section 141. In paragraph 4 this court lays down following[2] :

"The normal rule in the cases involving criminal liability is against vicarious liability, that is, no one is to be held criminally liable for an act of another. This normal rule is, however, subject to exception on account of specific provision being made in statutes extending liability to others. Section 141 of the Act is an instance of specific provision which in case an offence under section 138 is committed by a company, extends criminal liability for dishonour of cheque to officers of the company. Section 141 contains conditions which have to be satisfied before the liability can be extended to officers of a company. Since the provision creates criminal liability, the conditions have to be strictly complied with. The conditions are intended to ensure that a person who is sought to be made vicariously liable for an offence of which the principal accused is the company, had a role to play in relation to the incriminating act and further that such a person should know what is attributed to him to make him liable. In other words, persons who had nothing to do with the matter need

1. See [2005] 127 Comp Cas 563 (SC).
2. See page 569 of 127 Comp Cas.

not be roped in. A company being a juristic person, all its deeds and functions are result of acts of others. Therefore, officers of a company who are responsible for acts done in the name of the company are sought to be made personally liable for acts which result in criminal action being taken against the company. It makes every person who at the time the offence was committed, was in charge of and was responsible to the company for the conduct of business of the company, the company, liable for the offence. The proviso to the sub-section contains an escape route for persons who are able to prove that the offence was committed without their knowledge or that they had exercised all due diligence to prevent commission of the offence."

This court held that the criminal liability arises from being in charge of **30** and responsible for the conduct of the company at the relevant time. Elaborating the requirement for a person to be made liable under section 141 this court laid down following in paragraphs 10 and 12[1] :

"While analysing section 141 of the Act, it will be seen that it operates in cases where an offence under section 138 is committed by a company. The key words which occur in the section are 'every person'. These are general words and take every person connected with a company within their sweep. Therefore, these words have been rightly qualified by use of the words 'who, at the time the offence was committed, was in charge of and was responsible to the company for the conduct of the business of the company, as well as the company, shall be deemed to be guilty of the offence. etc.'. What is required is that the persons who are sought to be made criminally liable under section 141 should be at the time the offence was committed, in charge of and responsible to the company for the conduct of the business of the company. Every person connected with the company shall not fall within the ambit of the provision. It is only those persons who were in charge of and responsible for conduct of business of the company at the time of commission of an offence, who will be liable for criminal action. It follows from this that if a director of a company who was not in charge of and was not responsible for the conduct of the business of the company at the relevant time, will not be liable under the provision. The liability arises from being in charge of and responsible for conduct of business of the company at the relevant time when the offence was committed and not on the basis of merely

1. See page 573 of 127 Comp Cas.

holding a designation or office in a company. Conversely, a person not holding any office or designation in a company may be liable if he satisfies the main requirement of being in charge of and responsible for conduct of business of a company at the relevant time. Liability depends on the role one plays in the affairs of a company and not on designation or status. If being a director or manager or secretary was enough to cast criminal liability, the section would have said so. Instead of 'every person' the section would have said 'every director, manager or secretary in a company is liable' . . . etc. The Legislature is aware that it is a case of criminal liability which means serious consequences so far as the person sought to be made liable is concerned. Therefore, only persons who can be said to be connected with the commission of a crime at the relevant time have been subjected to action . . .

The conclusion is inevitable that the liability arises on account of conduct, act or omission on the part of a person and not merely on account of holding an office or a position in a company. Therefore, in order to bring a case within section 141 of the Act the complaint must disclose the necessary facts which make a person liable."

31 The ratio of the above judgment has been reiterated by this court in *N. K. Wahi* v. *Shekhar Singh* [2007] 9 SCC 481[1], *National Small Industries Corp. Ltd.* v. *Harmeet Singh Paintal* [2010] 3 SCC 330[2] and *Pooja Ravinder Devidasani* v. *State of Maharashtra* [2014] 16 SCC 1[3].

32 The learned Additional Solicitor General placed reliance on the judgment of this court reported in *N. Rangachari* v. *Bharat Sanchar Nigam Ltd.* [2007] 5 SCC 108[4]. This court in *N. Rangachari* v. *Bharat Sanchar Nigam Ltd.* [2007] 5 SCC 108[4] was again considering the provisions of section 141 of the Negotiable Instruments Act, 1881. The learned Additional Solicitor General relied on paragraphs 17 to 22. In *N. Rangachari* v. *Bharat Sanchar Nigam Ltd.* [2007] 5 SCC 108[4] this court has noticed the earlier three-Judge judgment in *S. M. S. Pharmaceuticals Ltd.* v. *Neeta Bhalla* [2005] 8 SCC 89[5] and clearly held that the said judgment is binding. In paragraph 20 of *N. Rangachari* v. *Bharat Sanchar Nigam Ltd.* [2007] 5 SCC 108[4], this court laid down following[6] :

1. See [2007] 137 Comp Cas 939 (SC).
2. See [2010] 154 Comp Cas 313 (SC).
3. See [2015] 190 Comp Cas 106 (SC).
4. See [2007] 137 Comp Cas 198 (SC).
5. See [2005] 127 Comp Cas 563 (SC).
6. See page 117 of 190 Comp Cas.

"In other words, the law laid down by this court is that for making a director of a company liable for the offences committed by the company under section 141 of the N. I. Act, there must be specific averments against the director showing as to how and in what manner the director was responsible for the conduct of the business of the company."

33 Thus, what was held in *S. M. S. Pharmaceuticals Ltd.* v. *Neeta Bhalla* [2005] 8 SCC 89[1] has been reiterated by *N. Rangachari* v. *Bharat Sanchar Nigam Ltd.* [2007] 5 SCC 108[2]. We may also refer to paragraph 23 of the *N. Rangachari* v. *Bharat Sanchar Nigam Ltd.* [2007] 5 SCC 108[2] judgment where following has been laid down[3] :

"In the light of the ratio in *S. M. S. Pharmaceuticals Ltd.* v. *Neeta Bhalla* [2005] 8 SCC 89[1], what is to be looked into is whether in the complaint, in addition to asserting that the appellant and another are the directors of the company, it is further alleged that they are in charge of and responsible to the company for the conduct of the business of the company. We find that such an allegation is clearly made in the complaint which we have quoted above. Learned senior counsel for the appellant argued that in *Saroj Kumar Poddar* case [2007] 3 SCC 693[4], this court had found the complaint unsustainable only for the reason that there was no specific averment that at the time of issuance of the cheque that was dishonoured, the persons named in the complaint were in charge of the affairs of the company. With great respect, we see no warrant for assuming such a position in the context of the binding ratio in *S. M. S. Pharmaceuticals Ltd.* v. *Neeta Bhalla* [2005] 8 SCC 89[1] and in view of the position of the directors in a company as explained above."

34 In the facts of the above case this court held that allegations were clearly made out in the complaint. Judgment of this court in *N. Rangachari* v. *Bharat Sanchar Nigam Ltd.* [2007] 5 SCC 108[2], thus, does not help the respondent nor it, in any manner, dilute the ratio of three-Bench judgment in *S. M. S. Pharmaceuticals Ltd.* v. *Neeta Bhalla* [2005] 8 SCC 89[1].

1. See [2005] 127 Comp Cas 563 (SC).
2. See [2007] 137 Comp Cas 198 (SC).
3. See page 209 of 137 Comp Cas.
4. See *Saroj Kumar Poddar* v. *State (NCT of Delhi)* [2007] 137 Comp Cas 837 (SC).

35 We may notice one more judgment of this court, *National Small Industries Corp. Ltd.* v. *Harmeet Singh Paintal* [2010] 3 SCC 330[1], interpreting section 141 of the Negotiable Instruments Act, 1881. After extracting section 141 of the Negotiable Instruments Act dealing with offences by companies, this court in paragraphs 12 and 13 laid down[2] :

> "It is very clear from the above provision that what is required is that the persons who are sought to be made vicariously liable for a criminal offence under section 141 should be, at the time the offence was committed, was in charge of, and was responsible to the company for the conduct of the business of the company. Every person connected with the company shall not fall within the ambit of the provision. Only those persons who were in charge of and responsible for the conduct of the business of the company at the time of commission of an offence will be liable for criminal action. It follows from the fact that if a director of a company who was not in charge of and was not responsible for the conduct of the business of the company at the relevant time, will not be liable for a criminal offence under the provisions. The liability arises from being in charge of and responsible for the conduct of the business of the company at the relevant time when the offence was committed and not on the basis of merely holding a designation or office in a company.
>
> Section 141 is a penal provision creating vicarious liability, and which, as per settled law, must be strictly construed. It is therefore, not sufficient to make a bald cursory statement in a complaint that the director (arrayed as an accused) is in charge of and responsible to the company for the conduct of the business of the company without anything more as to the role of the director. But the complaint should spell out as to how and in what manner respondent No. 1 was in charge of or was responsible to the accused company for the conduct of its business. This is in consonance with strict interpretation of penal statutes, especially, where such statutes create vicarious liability."

36 In the above case, this court held that directors can be prosecuted only if they were in charge and responsible for the conduct of the business of the company. In paragraph 36, following has been laid down (page 344 of [2010] 3 SCC) :

1. See [2010] 154 Comp Cas 313 (SC).
2. See page 320 of 154 Comp Cas.

"Section 291 of the Companies Act provides that :

'291. *General powers of Board.*—(1) Subject to the provisions of that Act, the board of directors of a company shall be entitled to exercise all such powers, and to do all such acts and things, as the company is authorized to exercise and do.

A company, though a legal entity, can act only through its board of directors. The settled position is that a managing director is prima facie in charge of and responsible for the company's business and affairs and can be prosecuted for offences by the company. But in so far as other directors are concerned, they can be prosecuted only if they were in charge of and responsible for the conduct of the business of the company'."

37 Section 68 of the FERA, 1973 deals with "Offences by companies". Section 68(1) provides that ". . . every person who, at the time of the contravention was committed, was in charge of, and was responsible to, the company for the conduct of business of the company as well as the company, shall be deemed to be guilty of the contravention . . ." section 68(1) creates a legal fiction, i. e., "shall be deemed to be guilty". The legal fiction triggers on fulfilment of conditions as contained in the section. The words "every person who, at the time of the contravention was committed, was in charge of, and was responsible to, the company for the conduct of business" has to be given some meaning and purpose. The provision cannot be read to mean that whosoever was a director of a company at the relevant time when contravention took place, shall be deemed to be guilty of the contravention. Had the Legislature intended that all the directors irrespective of their role and responsibilities shall be deemed to be guilty of contravention, the section could have been worded in different manner. When a person is proceeded with for committing an offence and is to be punished, necessary ingredients of the offence as required by section 68 should be present.

38 We may notice that section 141 of the Negotiable Instruments Act, which was inserted in the Negotiable Instruments Act by amendment in the year 1988 contains the same conditions for a person to be proceeded with and punished for offence as contained in section 68 of the FERA, 1973. Section 141(1) of the Negotiable Instruments Act uses the same expression "every person, who, at the time the offence was committed, was in charge of and was responsible to the company for the conduct of the business of the company, as well as the company, shall be deemed to be guilty of the offence". Section 68 of the FERA, 1973 as well as section

141 of the Negotiable Instruments Act deals with the offences by the companies in the same manner. The ratio of the judgments of this court on section 141 of Negotiable Instruments Act as noted above are also clearly relevant while interpreting section 68 of the FERA. We, thus, hold that for proceeding against a director of a company for contravention of provisions of the FERA, 1973, the necessary ingredient for proceeding shall be that at the time offence was committed, the director was in charge of and was responsible to the company for the conduct of the business of the company. The liability to be proceeded with for offence under section 68 of the FERA, 1973 depends on the role one plays in the affairs of the company and not on mere designation or status. This court in *S. M. S. Pharmaceuticals Ltd.* v. *Neeta Bhalla* [2005] 8 SCC 89[1] while elaborating the ambit and scope of section 141 of the Negotiable Instruments Act has already laid down above in paragraph 10 of the judgment as extracted above.

39 It is true that with regard to any offence punishable under section 138 of the Negotiable Instruments Act with respect to offences by companies, a complaint in writing has to be filed as required by section 142 of the Negotiable Instruments Act. A complaint as contemplated for offence under section 138 needs to be necessarily contain all allegations constituting offence. In FERA, 1973 for imposing a penalty under section 50, the adjudicating officer is required to hold an enquiry after giving the person a reasonable opportunity for making a representation in the matter. Even though, FERA, 1973 does not contemplate filing of a written complaint but in proceedings as contemplated by section 51, the person, who has to be proceeded with has to be informed of the contravention for which penalty proceedings are initiated. The expression "after giving that person a reasonable opportunity for making a representation in the matter" as occurring in section 51 itself contemplate due communication of the allegations of contravention and unless allegations contains complete ingredients of offence within the meaning of section 68, it cannot be said that a reasonable opportunity for making a representation in the matter has been given to the person, who is to be proceeded with.

40 Learned ASG is right in his submission that the FERA, 1973 does not contemplate any complaint but the scheme of the Act indicate that a person, who is to be proceeded with has to be made aware of the necessary allegations, which may constitute an offence on his part. This court in

1. See [2005] 127 Comp Cas 563 (SC).

N. Rangachari v. *Bharat Sanchar Nigam Ltd.* [2007] 5 SCC 108[1] has observed that a person in the commercial world having a transaction with company is entitled to presume that the directors of the company are in charge of the affairs of the company. The presumption of a person in the commercial world is a rebuttable presumption and when adjudicating authority proceeds to impose a penalty for a contravention of the FERA, 1973, essential ingredients constituting an offence under the FERA read with section 68 has to be communicated to the person proceeded with to enable him to make effective representation in the matter.

Learned Additional Solicitor General also submitted that all the three courts have held and found contravention proved by the appellant, this court may not interfere with such conclusion. We have already noticed above that the plea of the appellant that he was a part-time, non-executive director not in charge of the conduct of business of the company at the relevant time was erroneously discarded by the authorities and the High Court and there is no finding by any of the authorities after considering the material that it was the appellant who was responsible for the conduct of business of the company at the relevant time. Thus, present is a case where the liability has been fastened on the appellant without there being necessary basis for any such conclusion. **41**

It is also relevant to notice that an order which was passed on February 13, 2004 by the Deputy Director in the adjudication proceedings although with regard to different period, the plea of the appellant that he was only a part-time, non-executive director and not responsible of the conduct of business of the company was accepted and notice was discharged against the appellant. The order dated February 13, 2004 although related to different period but has categorically noticed the status of the appellant as part-time non-executive director. There being decision of adjudicating authority, in the recent past, passed on February 13, 2004 that the appellant was only a part-time non-executive director of MXL, there has to be some reasons for taking a contrary view by the adjudicating officer in order dated March 31, 2004 with regard to affairs of the same company, i. e., MXL. **42**

In view of the foregoing discussions, we are of the view that the adjudicating officer has erroneously imposed penalty on the appellant for the alleged offence under section 8(3), (4) and 68 of the FERA, 1973 which order was erroneously affirmed both by the Appellate Tribunal and the High Court. **43**

1. See [2007] 137 Comp Cas 198 (SC).

44 In view of the aforesaid, this appeal deserves to be allowed, the judgments of the High Court as well as those of the adjudicating officer and the Appellate Tribunal are set aside. The appeal is allowed and the penalty imposed on the appellant is set aside.

End of Volume 221

(IV) in Schedule C,

(i) clause 10 shall be substituted with the following, namely—

"Without prejudice to the power of the Board under the Act, the code of conduct shall stipulate the sanctions and disciplinary actions, including wage freeze, suspension, recovery, etc., that may be imposed, by the intermediary or fiduciary required to formulate a code of conduct under sub-regulation (1) and sub-regulation (2) of regulation 9, for the contravention of the code of conduct. Any amount collected under this clause shall be remitted to the Board for credit to the Investor Protection and Education Fund administered by the Board under the Act."

(ii) in clause 11, the words "inform the Board promptly" shall be replaced by the words

"promptly inform the stock exchange(s) where the concerned securities are traded, in such form and such manner as may be specified by the Board from time to time".

[ADVT.-III/4/Exty./118/2020-21]

Securities Contracts (Regulation) (Second Amendment) Rules, 2020

Notification No. G. S. R. 485(E), dated 31st July, 2020[1].

In exercise of the powers conferred by section 30 of the Securities Contracts (Regulation) Act, 1956 (42 of 1956), the Central Government hereby makes the following rules further to amend the Securities Contracts (Regulation) Rules, 1957, namely :—

1. Short title and commencement.—(1) These rules may be called as **Securities Contracts (Regulation) (Second Amendment) Rules, 2020.**

(2) They shall come into force on the date of their publication in the Official Gazette.

2. In the Securities Contracts (Regulation) Rules, 1957, in rule 19A, in sub-rule (1), in the proviso, for the words "two years" the words "three years" shall be substituted.

[F. No. 5/35/CM/2006 Volume-III]

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1. Gaz. of India, Extry. No. 380, dt. 31-7-2020, Pt. II, sec. 3(i).

Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) (Second Amendment) Regulations, 2020

Notification No. SEBI/LAD-NRO/GN/2020/25, dated 5th August, 2020[1].

In exercise of the powers conferred by section 11, sub-section (2) of section 11A and section 30 of the Securities and Exchange Board of India Act, 1992 (15 of 1992) read with section 31 of the Securities Contracts (Regulation) Act, 1956 (42 of 1956), the Board hereby makes the following regulations to further amend the Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015[2], namely :—

1. These regulations may be called the **Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) (Second Amendment) Regulations, 2020.**

2. They shall come into force on the date of their publication in the Official Gazette.

3. In the Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015,—

(I) In regulation 42,—

(a) in sub-regulation (1), the words and symbols "to all the stock exchange(s) where it is listed for the following purposes :", shall be substituted with the words and symbols "for the following events to all the stock exchange(s) where it is listed or where stock derivatives are available on the stock of the listed entity or where listed entity's stock form part of an index on which derivatives are available :"

(b) in sub-regulation (1), the existing clause (e), shall be substituted with the following, namely,—

"(e) corporate actions like mergers, demergers, splits, etc. ;"

[ADVT.-III/4/Exty./163/2020-21]

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1. Gaz. of India, Extry. No. 309, dt. 5-8-2020, Pt. III, sec. 4.
2. See [2015] 193 Comp Cas (St.) 5.

SEBI Circulars

I

Ref. SEBI/HO/CFD/DIL2/CIR/P/2020/78,
dated 6th May, 2020.

To

All Registered Merchant Bankers

All Recognized Stock Exchanges

All Registered Registrars to an Issue

All Self Certified Syndicate Banks

All listed entities

All entities who propose to list specified securities

Dear Sir/Madam,

Subject: **Relaxations relating to procedural matters—Issues and listing**

1. In view of the impact of the COVID-19 pandemic and the lockdown measures undertaken by Central and State Governments, based on representations, SEBI has decided to grant the following one time relaxations from strict enforcement of certain regulations of the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2018[1] (hereafter "ICDR Regulations"), pertaining to rights issue opening up to July 31, 2020 :

(i) Service of the abridged letter of offer, application form and other issue material to shareholders may be undertaken by electronic transmission as already provided under regulation 77(2) of the ICDR Regulation. Failure to adhere to modes of dispatch through registered post or speed post or courier services due to prevailing Covid-19 related conditions will not be treated as non-compliance during the said period.

However, the issuers shall publish the letter of offer, abridged letter of offer and application forms on the websites of the company, Registrar, stock exchanges and the lead manager(s) to the rights issue. Further, the issuer company along with lead manager(s) shall undertake all adequate steps to reach out its shareholders through other means such as ordinary post or SMS or audio-visual advertisement on television or digital advertisement, etc.

(ii) The issue related advertisement as mandated by regulation 84(1), shall contain additional details as regards the manner in which the shareholders who have not been served notice electronically may apply. The

1. See [2019] 213 Comp Cas (St.) 2.

issuer may have the flexibility to publish the dispatch advertisement in additional newspapers, over and above those required in regulation 84. The advertisement should also be made available on the website of the Issuer, Registrar, Lead Managers, and Stock Exchanges. The Issuer shall make use of advertisements in television channels, radio, internet, etc., to disseminate information relating to the application process. Such advertisements can be in the form of crawlers/tickers as well.

(iii) In terms of SEBI circular dated January 22, 2020, SEBI introduced dematerialized rights entitlements (REs). Further, physical shareholders are required to provide their demat account details to Issuer/Registrar to the Issue for credit of REs. In view of COVID-19 pandemic and the lockdown measures undertaken by Central and State Governments, in case the physical shareholders who have not been able to open a demat account or are unable to communicate their demat details, in terms of clause 1.3.4 of SEBI circular dated January 22, 2020 to the issuer/registrar for credit of REs within specified time, such physical shareholders may be allowed to submit their application subject to following conditions :

(a) Issuer along with lead manager(s) and other recognized intermediary shall institute a mechanism to allow physical shareholders to apply in the rights issue. Issuer along with lead manager(s) shall ensure to take adequate steps to communicate such a mechanism to physical shareholders before the opening of the issue.

(b) Such shareholder shall not be eligible to renounce their rights entitlements.

(c) Such physical shareholders shall receive shares, in respect of their application, only in demat mode. The lead managers may also be guided by paragraph 10 of the Form A Schedule V of the ICDR Regulations.

(iv) In terms of regulation 76 of the ICDR Regulations, an application for a rights issue shall be made only through ASBA facility. In view of the difficulties faced due to COVID-19 pandemic and the lockdown measures, and in order to ensure that all eligible shareholders are able to apply to rights issue during such times, the issuer shall along with lead manager(s) to the issue, the registrar, and other recognized intermediaries (as deemed fit by issuer and lead manager(s)) institute an optional mechanism (non-cash mode only) to accept the applications of the shareholders subject to ensuring that no third party payments shall be allowed in respect of any application.

(v) In respect of mechanisms at point (iii) and (iv) above, the issuer along with lead manager(s) shall ensure the following :

(a) The mechanism(s) shall only be an additional option and not a replacement of the existing process. As far as possible, attempts will be made to adhere to the existing prescribed framework.

(b) The mechanism(s) shall be transparent, robust and have adequate checks and balances. It should aim at facilitating subscription in an efficient manner without imposing any additional costs on investors. The issuer along with lead manager(s), and registrar shall satisfy themselves about the transparency, fairness and integrity of such mechanism.

(c) An FAQ, online dedicated investor helpdesk, and helpline shall be created by the issuer company along with lead manager(s) to guide investors in gaining familiarity with the application process and resolve difficulties faced by investors on priority basis.

(d) The issuer along with lead manager(s), registrar, and other recognized intermediaries (as incorporated in the mechanism) shall be responsible for all investor complaints.

2. In respect of all offer documents filed until July 31, 2020 it has been decided to grant the following relaxations :

(i) Authentication/certification/undertaking(s) in respect of offer documents, may be done using digital signature certifications.

(ii) The issuer along with lead manager(s) shall provide procedure for inspection of material documents electronically.

3. This Circular shall come into force with immediate effect.

4. This Circular is issued in exercise of the powers conferred by section 11(1) of the Securities and Exchange Board of India Act, 1992.

5. A copy of this Circular is available on SEBI website at *www.sebi.gov.in* under the categories "Legal Framework/Circulars".

Yours faithfully,
Jeevan Sonparote,
Chief General Manager.

II

Ref. SEBI/HO/CFD/DIL1/CIR/P/2020/136,
dated 24th July, 2020.

To

All Registered Merchant Bankers

All Recognized Stock Exchanges

All Registered Registrars to an Issue

All Self Certified Syndicate Banks

All listed entities

All entities who propose to list the specified securities

Dear Sir/Madam,

Subject: **Relaxations relating to procedural matters—Issues and listing**

1. SEBI vide Circular No. SEBI/HO/CFD/DIL2/CIR/P/2020/78, dated May 6, 2020[1] granted one time relaxations from strict enforcement of certain regulations of the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2018[2], pertaining to rights issue opening up to July 31, 2020.

2. Based on the representations received from the market participants, the validity of relaxations, as provided by Circular No. SEBI/HO/CFD/DIL2/CIR/P/2020/78, dated May 6, 2020 is further extended and shall be applicable for rights issue opening up to December 31, 2020.

3. This Circular is issued in exercise of the powers conferred by section 11(1) of the Securities and Exchange Board of India Act, 1992.

4. A copy of this Circular is available at *www.sebi.gov.in* under the categories "Legal→Circulars."

Yours faithfully,
Jeevan Sonparote,
Chief General Manager.

General Circulars

I

Circular No. 27/2020, dated 3rd August, 2020.

To

All Regional Directors,

All Registrar of Companies,

The Stakeholders

Subject: **Clarification on dispatch of notice under section 62(2) of the Companies Act, 2013 by listed companies for rights issues opening up to 31st December, 2020**

1. See [2020] 221 Comp Cas (St.) 67.
2. See [2019] 213 Comp Cas (St.) 2.

Sir/Madam,

Reference is drawn to this Ministry's General Circular No. 21/2020, dated 11th May, 2020[1] regarding clarification on dispatch of notice under section 62(2) of the Companies Act, 2013 by listed companies for rights issue opening up to 31st July, 2020. Representations have been received for extending the validity of such clarification. The Circular (Number SEBI/HO/CFD/DIL1/CIR/P/2020/136) issued by SEBI on 24th July, 2020[2] has also been considered. In view of this it has been decided that clarification given under paragraph 2 of General Circular No. 21/2020, dated 11th May, 2020, would continue to be applicable for rights issues, in case of listed companies, opening up to 31st December, 2020. Accordingly, in case of listed companies, which comply with relevant circulars issued by SEBI, inability to dispatch the relevant notice to shareholders through registered post or speed post or courier would not be viewed as violation of section 62(2) of the Act for rights issues opening up to 31st December, 2020. Other requirements provided in the said General Circular remain unchanged.

2. This issues with the approval of the competent authority.

Yours faithfully,
K. M. S. Narayanan,
Assistant Director (Policy).

[*Source : Issued by the Ministry of Corporate Affairs, New Delhi, dated 3rd August, 2020.*]

II

Circular No. 28/2020, dated 17th August, 2020.

To

All Regional Directors

All Registrar of Companies

All Stakeholders

Subject: **Clarification on extension of annual general meeting (AGM) for the financial year ended as at 31st March, 2020—Companies Act, 2013—Regarding**

Sir/Madam,

Several representations have been received in the Ministry for providing relaxations in the provisions of the Companies Act, 2013 (the Act) or rules

1. See [2020] 220 Comp Cas (St.) 215.
2. See [2020] 221 Comp Cas (St.) 69.

made thereunder to allow companies to hold their annual general meeting (AGM) for the financial year ended on March 31, 2020 beyond the statutory period provided in section 96 of the Act.

2. The matter has been examined in this Ministry and it is stated that this Ministry had, inter alia, clarified vide General Circular No. 20/2020, dated 5th May, 2020[1] (G. C. No. 20/2020) regarding holding of AGM through video conferencing (VC) or other audio visual means (OAVM) for the calendar year 2020. In addition, the companies which are unable to hold their AGMs were advised to prefer applications for extension of AGM at a suitable point of time before the concerned Registrar of Companies under section 96 of the Act.

3. In view of the above, it is once again reiterated that the companies which are unable to hold their AGM for the financial year ended on 31st March, 2020 despite availing the relaxations provided in the G. C. No. 20/2020 ought to file their applications in Form No. GNL-1 for seeking extension of time in holding of AGM for the financial year ended on 31st March, 2020 with the concerned Registrar of Companies on or before 29th September, 2020.

4. The Registrar of Companies are hereby advised to consider all such applications (filed in Form No. GNL-1) liberally in view of the hardships faced by the stakeholders and to grant extension for the period as applied for (up to three months) in such applications.

5. This issues with the approval of the competent authority.

Yours faithfully,

K. M. S. Narayanan,

Assistant Director (Policy).

[*Source : Issued by the Ministry of Corporate Affairs, New Delhi, dated 17th August, 2020.*]

End of Volume 221

1. See [2020] 220 Comp Cas (St.) 211.