IN THE NATIONAL COMPANY LAW APPELLATE TRIBUNAL
COMPANY APPELLATE JURISDICTION

Company Appeal (AT) (Insolvency) No. 5 of 2017

(arising out of Order dated 17th February, 2017 passed by National Company Law Tribunal, Mumbai Bench, in C.P. No. 12/I&B/NCLT/MAH/2017)

IN THE MATTER OF:

M/s. Starlog Enterprises Limited ... Appellant

Vs

ICICI Bank Limited ... Respondent

Present:

For Appellant :- Mr R.S. Majumdar, Senior Advocate alongwith Mr Darshan Mehta, Mr Raghav Dwivedi, Ms Nirali Sanghavi and Mr Vaibhav Modi, Advocates

For Respondents:- Mr Ramji Srinivasan, Senior Advocate with Mr Aslam Ahmed, Mr Sharad Kharra, Ms Srivardhani and Mr Babit Singh Jamwal, Advocates.

J U D G M E N T

SUDHANSU JYOTI MUKHOPADHAYA, J.

This application under Section 61 of Insolvency & Bankruptcy Code, 2016 (hereinafter referred to as I&B Code) has been preferred by Appellant/Corporate Debtor against *ex-parte*

order dated 17th February 2017 passed by 'adjudicating authority', Mumbai Bench, under Section 7 of the I&B Code whereby the 'adjudicating authority' was pleased to admit the petition preferred by Respondent/Financial Creditor.

2. The Appellant has challenged the impugned order on one of the ground that in absence of notice given to the Appellant before admitting the case under Section 7 of the I&B Code, the impugned order is violative of rules of natural justice.

3. The other ground taken by the Appellant is that the application preferred by Respondent/Financial Creditor under Section 7 is incomplete, misleading and being not bonafide was fit to be rejected.

4. Ld. Counsel for the Appellant submitted that the Appellant could have brought the aforesaid facts to the notice of the 'adjudicating authority' had it been given notice prior to admission. Detailed argument has been made by Ld. Senior Counsel for the Appellant on the question of issuance of notice prior to admission, in adherence to principle of rules of natural justice,

5. The aforesaid issue now stands decided by decision of the Appellate Tribunal in "M/s. Innoventive Industries Limited vs ICICI Bank & Anr. in CA (AT) (Insolvency) No. 1 & 2 of 2017" wherein the Appellate Tribunal observed and held :-

> *" 43. There is no specific provision under the I&B Code, 2016 to provide hearing to Corporate debtor in a petition under Section 7 or 9 of the I&B Code, 2016."*

> *"53. In view of the discussion above, we are of the view and hold that the Adjudicating Authority is bound to issue a limited notice to the corporate debtor before admitting a case for ascertainment of existence of default based on material submitted by the corporate debtor and to find out whether*

the application is complete and or there is any other defect required to be removed. Adherence to Principles of natural justice would not mean that in every situation the adjudicating authority is required to afford reasonable opportunity of hearing to the Corporate debtor before passing its order."

In this connection we may state that the vires of Section 7 of I&B Code was considered by Hon'ble Calcutta High Court in " Sree Metaliks Limited & Anr." in writ petition 7144 (W) of 2017, wherein Hon'ble High Court by its judgment dated 7th April, 2017 held as follows:-

> *".....However, it is to apply the principles of natural justice in the proceedings before it. It can regulate it own procedure, however, subject to the other provisions of the Act of 2013 or the Insolvency and Bankruptcy Code of 2016 and any Rules made thereunder. The Code of 2016 read with the Rules 2016 is silent on the procedure to be adopted at the hearing of an application under section 7 presented before the NCLT, that is to say, it is silent whether a party respondent has a right of hearing before the adjudicating authority or not.*
>
> *Section 424 of the Companies Act, 2013 requires the NCLT and NCLAT to adhere to the principles of the natural justice above anything else. It also allows the NCLT and NCLAT the power to regulate their own procedure. Fetters of the Code of Civil Procedure, 1908 does not bind it. However, it is required to apply its principles. Principles of natural justice require an authority to hear the other party. In an application under Section 7 of the Code of 2016, the financial creditor is the applicant while the corporate debtor is the respondent. A proceeding for declaration of insolvency of a company has drastic consequences for a company. Such proceeding may end up in its liquidation. A person cannot be condemned unheard. Where a statute is silent on the right of hearing and it does not in express terms, oust the principles of natural justice, the same can and should be read into in. When the NCLT receives an application under Section 7 of the Code of 2016, therefore, it must afford a reasonable opportunity of hearing to the corporate debtor as Section 424 of the Companies Act, 2013 mandates it to ascertain the existence of default as claimed by the financial creditor in the application. The NCLT is, therefore, obliged to afford a reasonable opportunity to the financial debtor to contest such claim of default by filing a written objection or any other written document as the NCLT may direct and provide a reasonable opportunity of hearing to the corporate debtor prior to admitting the petition filed under Section 7 of the Code of 2016. Section*

7(4) of the Code of 2016 requires the NCLT to ascertain the default of the corporate debtor. Such ascertainment of default must necessarily involve the consideration of the documentary claim of the financial creditor. This statutory requirement of ascertainment of default brings within its wake the extension of a reasonable opportunity to the corporate debtor to substantiate by document or otherwise, that there does not exist a default as claimed against it. The proceedings before the NCLT are adversarial in nature. Both the sides are, therefore, entitled to a reasonable opportunity of hearing.

The requirement of NCLT and NCLAT to adhere to the principles of natural justice and the fact that, the principles of natural justice are not ousted by the Code of 2016 can be found from Section 7(4) of the Code of 2016 and Rule 4 of the Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016. Rule 4 deals with an application made by a financial creditor under Section 7 of the Code of 2016. Sub- rule (3) of Rule 4 requires such financial creditor to despatch a copy of the application filed with the adjudicating authority, by registered post or speed post to the registered office of the corporate debtor. Rule 10 of the Rules of 2016 states that, till such time the Rules of procedure for conduct of proceedings under the Code of 2016 are notified, an application made under Sub-section (1) of Section 7 of the Code of 2017 is required to be filed before the adjudicating authority in accordance with Rules 20, 21, 22, 23, 24 and 26 or Part-III of the National Company Law Tribunal Rules, 2016.

Adherence to the principles of natural justice by NCLT or NCLAT would not mean that in every situation, NCLT or NCLAT is required to afford a reasonable opportunity of hearing to the respondent before passing its order.

In a given case, a situation may arise which may require NCLT to pass an ex-parte ad interim order against a respondent. Therefore, in such situation NCLT, it may proceed to pass an ex-parte ad interim order, however, after recording the reasons for grant of such an order and why it has chosen not to adhere to the principles of natural justice at that stage. It must, thereafter proceed to afford the party respondent an opportunity of hearing before confirming such ex-parte ad interim order.

In the facts of the present case, the learned senior advocate for the petitioner submits that, orders have been passed by the NCLT without adherence to the principles of natural justice. The respondent was not heard by the NCLT before passing the order.

It would be open to the parties to agitate their respective grievances with regard to any order of NCLT or NCLAT as the case may be in accordance with law. It is also open to the parties to point out that the NCLT and the NCLAT are bound to follow the principles of natural justice while disposing of proceedings before them.

In such circumstances, the challenge to the vires to Section 7 of the Code of 2016 fails."

6. Therefore, it is clear that before admitting an application under Section 9 of the I&B Code it is mandatory duty of the 'adjudicating authority' to issue notice.

7. In the present case admittedly no notice was issues by the 'adjudicating authority' to the corporate debtor, before admitting the application filed under Section 9 of the I&B Code. For the said reason the judgement order cannot be upheld having passed in violation of principle of natural justice.

8. Next contention of Ld. Senior Counsel for the Appellant was that the Financial Creditor misrepresented material facts before the 'adjudicating authority' in order to obtain order of admission of the application. He highlighted the conduct of the Financial Creditor by highlighting the following facts.

9. On 6th February, 2017, the Financial Creditor addressed a notice to the Appellant calling upon to pay a sum of Rs.10,02,28,271.60 (Rupees ten crore two lac twenty eight thousand two hundred seventy one and paise sixty only) which was overdue as on 6th February, 2017. The notice dated 6th February, 2017 was received by the Appellant only on 8th February 2017.

10. Before the Appellant could have replied or taken any necessary action in respect of the said notice on 8th February 2017

the Appellant received a letter from the Counsel for the Financial Creditor serving a copy of the present application, relevant portion of which reads as follows:-

> *'We send herewith a copy of the captioned Company Application on behalf of our client under Section 7 of the I&B Code, as and by way of service upon you,'*

without directly or indirectly specifying whether the said application has been filed or clarifying whether the said application would be mentioned or heard on any particular date/time, as is the prevalent practice.

11. Ld. Senior Counsel for the Appellant also submitted that the application filed by the Financial Creditor before the 'adjudicating authority' they inflated the default amount to be Rs.29,81,02,395.62 (Rupees twenty nine crore eighty one lac two thousand three hundred ninety five and paise sixty two only). Even Annexure 2 to the said application reflected 'Principal Unmatured' arrived in the computing the 'Default Amount'.

12. Ld. Senior Counsel for the Appellant further submits that as per the repayment schedule under the loan agreements, the entire aforementioned amount had not become due and payable as on 6th February, 2017. Neither the Financial Creditor, by his own admission, recalled the entire loan amount.

13. In view of the same, it was submitted that the computation of the default amount of Rs.29,81,02,395.62 (Rupees twenty nine crore eighty one lac two thousand three hundred ninety five and paise sixty two only) is grossly incorrect and contrary to the provisions of law.

14. It was further submitted that for the said misstatement, the Financial Creditor ought to be adequately penalised under the provisions of the I&B Code,2016 particularly under Section 75.

15. The Ld. Counsel also highlighted the conduct of the Respondent – ICICI Bank – and pleaded as follows:

a. The Respondent herein is a part of the Joint Lenders' Forum (hereinafter referred to as JLF) constituted by the Appellant pursuant to the guidelines of the Reserve Bank of India (hereinafter referred to as RBI). The JLF for the Appellant was formed at the instance of the Respondent vide the meeting held on 14th June, 2014. Thereafter, from 14th June 2014till 2nd February, 2017, the Respondent along with the other lenders of the Appellant and the Appellant itself, have been participating in the periodically held meetings of the JLF, in all of which meetings the JLF had unanimously agreed to adopt 'rectification' as the corrective action plan (CAP) for the Appellant. It is pertinent to note that the Respondent itself had requested the lead lender of the Appellant (L&T Infrastructure Finance Company) to convene the JLF meetings as the lead lender from February 2016 onwards.

b. As per the minutes of the meeting held on 2nd February 2017 circulated by the Lead Lender, the effect of the JLF meeting is that the JLF has decided to continue with rectification as CAP for the Appellant and members of JLF have been requested *'not to proceed with any individual asset level action'*. The Respondent however, chose to dispute these minutes vide their email dated 16th February 2017as circulated by Respondent No. 33.

As per the purported minutes of the meeting, the JLF lenders had resolved that rectification as the CAP has failed and the JLF members have decided to explore their options for regularising the account.

c. By the time the correct minutes of the meeting dated 2.2.2017 were circulated by the Lead lender on 16.2.2017, the Respondent had already filed its application on 8th February 2017 itself with the 'adjudicating authority' against the Appellant without the knowledge/consent of the other members of the JLF. It is pertinent to note that the Respondent while disputing the said minutes does not even mention about the said application filed by the Respondent against the Appellant before the 'adjudicating authority' and their reliance on the purported minutes of meeting in the said application.

d. *Arguendo* the purported minutes of the meeting are correct, that still does not justify the filing of the said application by the Respondent before the 'adjudicating authority' *de hors* the structure of JLF. The JLF members as per Respondent's own version had agreed to *'explore their action for resolving....'* And not to resort to filing of application under Section 7 of the I&B Code. Possibly the notice of demand served by the Respondent to the Appellant on 6th February 2017 was in furtherance of 'exploration of its action for resolving....' However, the filing of the application under Section 7 of the I&B Code independently by the Respondent, totally disregarding the other members of the Forum was a mischief played by the Respondent upon the Appellant

for reasons best known to them, which mischief is apparent from the aforesaid conduct of the Respondent.

e. The Respondent has acted contrary to the guidelines of the RBI in relating to JLF, particularly the guideline issued on 24.9.2015 which at para 5.2 of the guidelines stipulates that in case of disagreement between the members of the JLF on deciding the CAP for borrower, the dissenting lender shall have an option to exit their exposure by completely selling their exposure to a new or existing lender. Therefore, clearly the object of the RBI is clearly that the lenders act through the JLF structure and do not go beyond the JLF structure or in other words lenders do not act independent of JLF especially when an exit option exists for an individual lender. In this regard, it is pertinent to refer to the recent judgment of the Hon'ble Bombay High Court in the caser of IDFC Bank Limited v M/s. Ruchi Soya Industries Limited, *inter alia*, laying down two propositions – firstly, circulars issued by the RBI pertaining to JLF are statutory in nature and binding upon the banks and secondly, that member of JLF cannot independently resort to/adopt any proceedings during the on-going process of rectification through the JLF.

16. Similar argument was raised in M/s. Innoventive Industries Ltd v ICICI Bank & Anr. Having noticed such argument, the Appellate Tribunal in "M/s. Innoventive Industries Ltd v ICICI Bank & Anr." held that:-

> *"82. As discussed in the previous paragraphs, for initiation of corporate resolution process by financial creditor under sub-section*

(4) of Section 7 of the Code, 2016, the 'adjudicating authority' on receipt of application under sub-section (2) is required to ascertain existence of default from the records of Information Utility or on the basis of other evidence furnished by the financial creditor under sub-section (3). Under Section 5 of Section 7, the 'adjudicating authority' is required to satisfy –

(a) Whether a default has occurred;
(b) Whether an application is complete; and
(c) Whether any disciplinary proceeding is against the proposed Insolvency Resolution Professional.

83. Once it is satisfied it is required to admit the case but in case the application is incomplete application, the financial creditor is to be granted seven days' time to complete the application. However, in a case where there is no default or defects cannot be rectified, or the record enclosed is misleading, the application has to be rejected.

84. Beyond the aforesaid practice, the 'adjudicating authority' is not required to look into any other factor, including the question whether permission or consent has been obtained from one or other authority, including the JLF. Therefore, the contention of the petition that the Respondent has not obtained permission or consent of JLF to the present proceeding which will be adversely affect loan of other members cannot be accepted and fit to be rejected."

17. The impact of the Insolvency Resolution Professional on the business and management of the Appellant, alleged to be as follows:

The Interim Insolvency Resolution Professional (hereinafter referred to as IRP) has been appointed by the 'adjudicating authority' by the impugned order. On 1st March 2017 the IRP issued a public notice in Economic Times therein calling upon the creditors of the company to submit their claims. From 2nd March 2017 onwards the IRP has been attending office from the Appellant's premises and has taken over the management of affairs of the Appellant.

18. Ld. Counsel highlighted the events that occurred pursuant to IRP taking over the management of the affairs of the Appellant.

18.1 M/s. G.E Industrial India Pvt Ltd (hereinafter referred to as GE) has been a crucial and important client of the Appellant. GE had placed several orders in October 2016 and January 2017 for commission of the Appellant's cranes at its project sites at Lalpur, Kadapa, Jamnagar etc. The nature of Appellant's contracts with its clients are such that the Appellant is required to regularly and in a very prompt, timely manner, meet the requirements raised by its clients such as release of funds for the day to day functioning of the cranes as well as management of the staff handling the cranes, hiring and dispatching the necessary contractors, engineers to the project sites as may be required etc.

18.2 M/s. G.E addressed several e-mails dated 6th march and 7th March 2017 and so on to the Appellant in respect of the Appellant's cranes commissioned at G.E's Kadappa site. GE, inter-alia, required the Appellant to urgently release funds for the crane's diesel, send a safety engineer at the project site and take necessary action in respect of replacement of cotter pin in one of the ancillary equipments.

18.3 The appellant's Project Manager forwarded each of these e-mails to the IRP along with an explanation regarding the nature of the service and the time lines for the same, wherever required.

18.4 Despite the lengthy trail of correspondence and constant service requests, IRP failed to do much as satisfactorily reply to GE's concerns, much less release the necessary funds and take actions. As a result of IRP's failure to release necessary funds and act on the service requests in a timely manner, the Appellant was unable to perform its contractual obligations qua G.E.

18.5 Ultimately vide an email dated 18th march 2017, G.E has terminated the contract with the Appellant resulting in a financial loss of at least Rs.2,70,00,000/- as well as loss of goodwill that the Appellant has painstakingly built in this business over the last 30 years.

18.6 It came to the knowledge of one of Appellant's Director Mr Saket Agarwal that the IRP had contrary to the powers granted to him under the I&B Code, instruct some of the employees of the Respondent to disclose the bank account details of the following companies which are subsidiaries of the Appellant – (i) Starport Logistics Ltd; (ii) ABG Turnkey Pvt Ltd; (iii) Kandla Container Terminal Pvt Ltd and (iv) ABG Projects & Services Ltd., UK.

18.7 It appears that the IRP had directed employees of the Appellant to change the mandate of authorised signatories in the bank accounts of the aforesaid subsidiaries and had also addressed correspondence to the banks requesting a change in the authorised signatories.

18.8 The I&B Code does not in any manner empower an IRP to interfere with the affairs of the subsidiaries of the corporate debtor. In fact, the Explanation to Section 18 of the I&B Code, 2016 explicitly provides that the assets of the corporate debtor shall not include the assets of its Indian or foreign subsidiaries. In that view of the matter, the aforesaid act of the IRP is ex-facie illegal and unsustainable in law.

18.9 As a result of the absolute mismanagement and dis interest in the management of the affairs of the Appellant, the Appellant has suffered loss of several valuable human resources namely, Mr R.C Swamy, Project Manager who has been with the employment of the Appellant since 26 years, submitted his resignation therein citing "the working

atmosphere" at the Appellant's office as "severe stress" as the reasons for his resignation. Mr Meet Shay, Deputy Manager e-mailed his resignation on 28th March, 2017. Mr Arup Kumar Ghosh, who was directed by the IRP to take charge of the head office activities of the Appellant e-mailed his resignation on 29th March 2017 citing inability to "bear the stress to do so". Mr Varun Kaka, Legal Associate of the Appellant also resigned on 29th March, 2017.

19. Sub-section (12) of Section 3 of I&B Code defined "default" to mean "*a liability or obligation in respect of claim which is due from an person...*" The principal (unmatured) amount, never having become due and payable to the Financial Creditor could not have been claimed as the default amount.

20. Impugned order herein suffers from the vice of non-application of mind by the 'adjudicating authority' on the following counts:-

20.1 The ascertainment of existence of default by the 'adjudicating authority' which under the provisions of Sub-Section (4) of Section 7 of the I&B Code has to be based on the application/other evidence submitted by the financial creditor, suffers from non-application of mind given the apparent and conspicuous mismatch between the amount demanded by the Respondent from the Appellant in its demand notice dated 6th February 2017 and the amount stated to be in default in the said application.

20.2 Secondly, the 'adjudicating authority' in paragraph 8 of the impugned order has recorded that proof of service showing service of notice upon the corporate debtor before filing the

petition has been filed by the Financial Creditor, without considering the true nature and purport of the so called notice dated 8th February 2017 which did not even mention the essential details which were to be mentioned, such as:-

a. Whether the application has been filed;
b. if the application is filed, what is the filing number; and
c. date of listing, if notified.

20.3 The notice has been given without considering the provisions of sub-rule (3) of Rule 4 of Insolvency & Bankruptcy (Application to Adjudicating Authority) Rules, 2016 which mandates that an application shall "dispatch forthwith", a copy of the application "**filed with the Adjudicating Authority**". Thereby meaning a post-filing notice and not 'before filing", the obvious purpose for the same being to put the corporate debtor to adequate and informed notice. The 'adjudicating authority' ought to have realised these deviations from the prescribed procedure and either rejected the application or directed the Respondent to follow the provisions of sub-Rule (3) of Rule 4 of Insolvency & Bankruptcy (Application to Adjudicating Authority) Rules, 2016 and Rule 21 of the National Company Law Tribunal Rules.

20.4 Lastly, the 'adjudicating authority' has reached a conclusion at paragraph 9 of the impugned order that it is satisfied that the Appellant has committed a default of Rs.27.77 crores, which finding is not only perverse, but also is contrary to the very application of the Financial Creditor itself in complete disregard to the apparent and conspicuous mismatch between the amount demanded by the Financial Creditor from the Appellant-Corporate Debtor in its demand notice dated 6th

February 2017 and the amount stated to be in default in the said application.

21. Showing an incorrect claim, moving the application in a hasty manner and obtaining an ex-parte order from the 'adjudicating authority' which admitted such an incorrect claim, the Financial Creditor cannot disprove its mala fide intention by stating that the claim submitted is correct amount. The I&B Code does not provide for any such mechanism where post-admission, the applicant financial creditor can modify their claim amount.

22. In some of the cases, an insolvency resolution process can and may have adverse consequences on the welfare of the company. This makes it imperative for the 'adjudicating authority' to adopt a cautious approach in admitting insolvency applications and also ensuring adherence to the principles of natural justice.

23. Admittedly the impugned order is ex-facie illegal and ought to be set aside by the Appellate Tribunal. For the reasons aforesaid, we set aside the ex-parte impugned order dated 17th February 2017 passed by 'adjudicating authority', Mumbai Bench in C.P. No. 12/I&BP/NCLT/MAH/2017 and allow the appeal.

24. In effect the appointment of Interim Resolution Professional, order declaring moratorium, freezing of account and all other order passed by 'adjudicating authority' pursuant to impugned order and action taken by the Interim Resolution Professional, including the advertisement published in the newspaper calling for applications are declared illegal. The 'adjudicating authority' is directed to close the proceeding. The appellant company is released from the rigour

of law and allow the appellant company to function independently through its Board of Directors from immediate effect.

25. In the facts and circumstances, we impose a cost of Rs. 50,000/- (Rupees fifty thousand only) on Respondent - Financial Creditor, ICICI Bank – to be paid in favour of Registrar, National Company Law Appellate Tribunal, New Delhi by demand draft within one month towards development of its Library. The appeal is allowed with aforesaid observations and directions.

(Mr. Balvinder Singh)
Member (Technical)

(Justice S.J.Mukhopadhaya)
Chairperson

NEW DELHI
24th May, 2017

RC