

**NATIONAL COMPANY LAW APPELLATE TRIBUNAL, NEW DELHI**

**Company Appeal (AT) (Insolvency) No. 494 of 2018**

[Arising out of Order dated 23<sup>rd</sup> July, 2018 passed by the Adjudicating Authority (National Company Law Tribunal), Single Bench, Chennai in Company Petition No. CP/769/(IB)/2018]

**IN THE MATTER OF:**

**G. Sreevidhya**

26, Third Cross Street,  
R. A. Puram,  
Chennai – 600 028.

**...Appellant**

**Vs**

**M/s. Karismaa Foundations Pvt. Ltd.**

No. 340, First South Main Road,  
Kapaleeswarar Nagar,  
Neelangerai, Kancheepuram,  
Chennai – 600 115.

**....Respondent**

**Present:**

**For Appellant:** Mr. A. Muraleedharan and Mr. Kamal Kishore,  
Advocates.

**For Respondent:** Mr. Krishnendu Datta and Ms. Aakanksha Kaul,  
Advocates.

**J U D G M E N T**

**BANSI LAL BHAT, J.**

The Appellant - ‘G. Sreevidhya’, claiming to be a ‘financial creditor’, sought initiation of Corporate Insolvency Resolution Process qua the Respondent - ‘M/s Karismaa Foundations Pvt. Ltd.’ (Corporate Debtor) for default in discharging the financial debt by filing an application under

Section 7 of the Insolvency and Bankruptcy Code, 2016 (hereinafter referred to as 'I&B Code') before the Adjudicating Authority (National Company Law Tribunal), Single Bench, Chennai. However, tables were turned on the Appellant when in terms of the impugned order dated 23<sup>rd</sup> July, 2018 the Adjudicating Authority rejected the prayer of Appellant after recording a finding that the Appellant was an 'Operational Creditor' and there being an existence of dispute on account of civil suits pending between the parties initiation of Corporate Insolvency Resolution Process was not warranted. Aggrieved thereof the Appellant has preferred the instant appeal assailing the impugned order as being legally unsustainable.

2. The only question arising for consideration in this appeal relates to the status of Appellant and initiation of Corporate Insolvency Resolution Process at her instance.

3. A brief resume of the factual matrix for comprehending the real controversy inter-se the parties is inevitable. The Appellant and the Respondent entered into an agreement for construction of a residential building on a turnkey basis at a cost of Rs.4 Crore. The Appellant transferred a sum of Rs.1.5 Crore to the Respondent pursuant to the aforesaid agreement executed on 10<sup>th</sup> November, 2014. This happened on 5<sup>th</sup> December, 2014. However, the Agreement could not be implemented. The Respondent retained the money received from the Appellant as loan and started paying interest thereon w.e.f. 5<sup>th</sup> December, 2014. Respondent is stated to have issued balance confirmation on 1<sup>st</sup> April, 2015 in regard to

Principal Amount together with interest accrued thereon for the financial year 2014-15 after deducting tax at source though the same was not remitted to Income Tax Department. According to Appellant, the Respondent issued three cheques dated 13<sup>th</sup> March, 2015, 18<sup>th</sup> March, 2015 and 30<sup>th</sup> April, 2015 each valuing Rs.5 Lakhs, thereby repaying a sum of Rs.15 Lakhs out of Rs.1.5 Crores and further issued a cheque dated 30<sup>th</sup> June, 2015 for the balance loan amount of Rs.1.35 Crores. However, the cheque bounced when presented on 22<sup>nd</sup> September, 2015 for encashment at State Bank of Travancore, Taramani Branch, Chennai with endorsement “exceeds arrangement” as reflected vide Memo dated 22<sup>nd</sup> September, 2015. Subsequently, Respondent issued three cheques for Rs.25 Lakh each and one cheque for Rs.50 Lakh favouring the Appellant, some of which were antedated and others post dated. On presentation at the State Bank of Travancore, Taramani Branch, Chennai these cheques were dishonored due to “insufficient funds”. According to Appellant, Respondent confirmed the details of repayment of Principal Amount together with interest in confirmation of accounts dated 6<sup>th</sup> July, 2016 covering the period ending March, 2016. Respondent is stated to have paid interest on the outstanding amount. However, subsequently Respondent committed default prompting the Appellant to lodge a criminal complaint against Respondent for cheating and breach of trust which led to registration of case under FIR No. 180/2016 with City Crime Branch, Chennai. However, the FIR was quashed by the Hon’ble High Court of Madras on the petition of Respondent filed under Section 482 of CrPC. This was followed by issuance of a demand

notice by the Appellant to Respondent under wrong legal advice tendered by her counsel wrongly treating the debt as 'operational debt'. Same was replied to by the Respondent stating that it had filed a Civil Suit No. 3007 of 2018 pending adjudication before the Hon'ble High Court of Madras which came to be returned to the Respondent for failure to pay court fee. Subsequently, the Appellant filed Civil Suit No. 46 of 2018 against the Respondent for recovery of money which is still pending before the Hon'ble High Court of Madras. Since the Respondent had committed default in discharge of financial debt in a sum of Rs.1.25 Crores, the Appellant was within her rights to initiate Corporate Insolvency Resolution Process.

4. At the very outset, we may observe that the Adjudicating Authority has given a short shrift to the matter and virtually failed to apply its mind to determine that the nature of transaction inter-se the parties would embrace the definition of 'Financial Debt'. The Adjudicating Authority, briefly referred to the agreement dated 10<sup>th</sup> November, 2014 executed inter-se the parties but without deliberating upon the facts and circumstances leading to termination of the agreement and issuance of balance confirmation on 1<sup>st</sup> April, 2015 by the Respondent as also the issuance of cheques to discharge the liability, proceeded to hold that the claim of Appellant essentially falls under the category of 'Operational Creditor' under Section 9 of I&B Code with regard to which there was an existence of dispute. In arriving upon such conclusion the Adjudicating Authority appears to have been influenced by the observations of Hon'ble High Court of Madras which quashed the FIR

filed by the Appellant alleging cheating and criminal breach of trust on the part of Respondent, after holding that the dispute between the parties was civil in nature and facts were required to be proved at the trial. The Adjudicating Authority also appears to have been influenced by pendency of cross civil suits between the parties before Hon'ble High Court of Madras. This despite the fact that the Respondent had admitted the factum of interest having been paid on the amount disbursed by Appellant to it to implement the agreement.

5. We have heard the learned counsel for the parties and fathomed through the depths of material on record.

6. Section 3(11) of I&B Code defines 'debt' as a liability or obligation in respect of a claim which is due from any person and includes a 'financial debt' and 'operational debt'. The term 'claim' defined under Section 3(6) of the same Code means a right to payment in any of its manifestations including right to remedy for breach of contract giving rise to a right to payment. Section 5(7) of I&B Code defines the legal expression 'financial creditor' as a person to whom a financial debt is owed which also includes an assignee or a transferee. Section 5(8) of I&B Code defines the term 'financial debt' as a debt along with interest, if any, which is disbursed against the consideration for the time value of money and includes the money borrowed against the payment of interest, amounts raised under credit facility, purchase facility, issue of bonds, notes, debentures, loan stock or similar instrument, amount of liability in respect of any lease or

hire purchase contract, receivables other than on non-recourse basis, amount raised under any other transaction including forward sale or purchase agreement having commercial effect of a borrowing, derivative transactions in connection with protection against fluctuation in price, counter indemnity obligations in respect of guarantee, indemnity, bond, letter of credit or any instrument issued by a bank or financial institution and the amount of any liability in respect of any guarantee or indemnity with reference to the aforesaid transactions. This Appellate Tribunal, while dealing with the interpretation of 'financial debt' in '**Shailesh Sangani Vs. Joel Cardoso, Company Appeal (AT) (Insolvency) No. 616 of 2018 decided on 30<sup>th</sup> January, 2019**' observed as under:-

*6. A plain look at the definition of 'financial debt' brings it to fore that the debt alongwith interest, if any, should have been disbursed against the consideration for the time value of money. Use of expression 'if any' as suffix to 'interest' leaves no room for doubt that the component of interest is not a sine qua non for bringing the debt within the fold of 'financial debt'. The amount disbursed as debt against the consideration for time value of money may or may not be interest bearing. What is material is that the disbursement of debt should be against consideration for the time value of money. Clauses (a) to (i) of Section 5(8) embody the nature of transactions which are included in*

*the definition of 'financial debt'. It includes money borrowed against the payment of interest. Clause (f) of Section 5(8) specifically deals with amount raised under any other transaction having the commercial effect of a borrowing which also includes a forward sale or purchase agreement. It is manifestly clear that money advanced by a Promoter, Director or a Shareholder of the Corporate Debtor as a stakeholder to improve financial health of the Company and boost its economic prospects, would have the commercial effect of borrowing on the part of Corporate Debtor notwithstanding the fact that no provision is made for interest thereon. Due to fluctuations in market and the risks to which it is exposed, a Company may at times feel the heat of resource crunch and the stakeholders like Promoter, Director or a Shareholder may, in order to protect their legitimate interests be called upon to respond to the crisis and in order to save the company they may infuse funds without claiming interest. In such situation such funds may be treated as long term borrowings. Once it is so, it cannot be said that the debt has not been disbursed against the consideration for the time value of the money. The interests of such stakeholders cannot be said to be in conflict with the interests of the Company. Enhancement of assets, increase in production and the growth in profits,*

*share value or equity enures to the benefit of such stakeholders and that is the time value of the money constituting the consideration for disbursement of such amount raised as debt with obligation on the part of Company to discharge the same. Viewed thus, it can be said without any amount of contradiction that in such cases the amount taken by the Company is in the nature of a 'financial debt'.*

7. Dwelling on the scope of provisions of Section 7 of I&B Code dealing with triggering of Corporate Insolvency Resolution Process at the instance of 'Financial Creditors' and converging on the procedure regulating initiation of such process, the Hon'ble Apex Court held in **'Swiss Ribbons Pvt. Ltd. & Anr. Vs. Union of India & Ors.'**, **Writ Petition (Civil) No. 99/2018 (2019 SCC OnLine SC 73)** as follows:-

*"36. 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.*

**37.** *A financial creditor may trigger the Code either by itself or jointly with other financial creditors or such persons as may be notified by the Central Government when a “default” occurs. The Explanation to Section 7(1) also makes it clear that the Code may be triggered by such persons in respect of a default made to any other financial creditor of the corporate debtor, making it clear that once triggered, the resolution process under the Code is a collective proceeding in rem which seeks, in the first instance, to rehabilitate the corporate debtor. Under Section 7(4), the Adjudicating Authority shall, within the prescribed period, ascertain the existence of a default on the basis of evidence furnished by the financial creditor; and under Section 7(5), the Adjudicating Authority has to be satisfied that a default has occurred, when it may, by order, admit the application, or dismiss the application if such default has not occurred. On the other hand, under Sections 8 and 9, an operational creditor may, on the occurrence of a default, deliver a demand notice which must then be replied to within the specified period. What is important is that at this stage, if an application is filed*

*before the Adjudicating Authority for initiating the corporate insolvency resolution process, the corporate debtor can prove that the debt is disputed. When the debt is so disputed, such application would be rejected.”*

8. Adverting to the facts of the case in hand be it seen that initially parties entered into an agreement of construction on 10<sup>th</sup> November, 2014 in terms whereof the Respondent was to raise construction of a residential building as per design provided by the Appellant for a turnkey price of Rs.4 Crore. The Appellant was required to pay an advance of Rs.1.5 Crore within a month with stipulation that the balance payment will be made in equal instalments over the construction period, the agreed time frame for completing the construction being 18 months from the date of approval. What emerges from the stipulations in the agreement is that the construction was to be raised at the site of Appellant at Koturpuram. The factum of Appellant having paid the advance amount of Rs.1.5 Crore to the account of Respondent on 4<sup>th</sup> December, 2014 has not been controverted by the Respondent. It emerges from the material on record that the project had been abandoned by the Appellant as the market conditions did not favour going ahead with the proposed construction. She sought repayment in regard to balance amount of Rs.1.35 Crores as according to her an amount of Rs.15 Lakhs had been repaid in three instalments in March and April, 2015. It is further borne out from record that the Respondent initially issued a cheque worth Rs.1.35 Crores dated 30<sup>th</sup> June, 2015 favouring the

Appellant. Upon presentation of the Cheque at State Bank of Travancore the same bounced due to lack of funds in the account of Respondent. This happened twice. The Appellant felt cheated and served a legal notice dated 1<sup>st</sup> October, 2015 upon the Respondent before lodging an FIR alleging cheating and criminal breach of trust, which ultimately came to be quashed at the instance of Respondent by Hon'ble High Court of Madras in terms of its order dated 20<sup>th</sup> November, 2017. It is further borne out by record that the Respondent filed a Civil Suit before the Madras High Court wherein, inter-alia the relief of declaration adjudging the bounced cheque as null and void was sought by the Respondent. Appeal preferred by the Appellant against order of Madras High Court came to be dismissed by Hon'ble Supreme Court in terms of order dated 22<sup>nd</sup> January, 2018. Admittedly, Appellant too has filed a civil suit in regard to the same subject matter which is pending adjudication before the Madras High Court. The nature of transaction and debt has to be determined in the aforesaid context.

9. Agreement executed inter-se the parties on 10<sup>th</sup> November, 2014 envisaged construction of a residential building at the site of Appellant at Koturpuram. The construction was to be raised by Respondent on the design provided by the Appellant for a turnkey price of Rs.4 Crore. The Appellant was under obligation to pay an advance of Rs.1.5 Crore within 30 days of the execution of the Agreement which admittedly she paid to Respondent. Balance payment was to be made in equal instalments over the construction period spread over 18 months from the date of approval.

Admittedly, the project was abandoned by the Appellant due to market considerations. This is clearly borne out from the statutory notice dated 1<sup>st</sup> October, 2015 served by Appellant on the Respondent. The Appellant has admitted receipt of Rs.15 Lakhs from Respondent while alleging that the cheque issued by Respondent towards refund of the balance amount of Rs.1.35 Crore was dishonoured when presented for encashment twice at the State Bank of Travancore, Taramani Branch for lack of funds. Respondent, while responding to the notice stated that an amount of Rs.25 Lakhs was paid towards the interest @ 15% per annum while the debt was discharged by issuing a cheque worth Rs.25 Lakhs and further three cheques totalling to Rs.37,50,000/- in the name of one Mr. Ashok, styled as Appellant's 'stooge'. It further emanates from the reply of respondent to the notice of Appellant that the Appellant was advised to hold back the cheque for Rs.1.35 Crore being no longer valid on account of discharge of debt. It is manifestly clear that the Respondent has not denied the transaction which initially related to execution of a construction project for which the Appellant had disbursed amount of Rs.1.5 Crores as advance money but on the project becoming commercially unviable got transformed into a 'financial debt' and was treated so. Payment of interest thereon, as admitted by the Respondent is compatible with this proposition and speaks of no exception. The money disbursed by the Appellant cannot be said to have been bestowed upon the Respondent as largesse nor as alms. It was disbursed in pursuance of an agreement in the nature of a financial transaction against consideration of time value of money as the building raised in pursuance of such agreement

would fetch fortunes for the Appellant. The project however fell through on account of market considerations. If there were any doubt in the nature of transaction, same got cleared as even according to Respondent interest was paid on the advance money. Thus viewed, we find no impediment in holding that the debt in question fell within the purview of 'financial debt' and the Appellant's status was that of a 'financial creditor' and not an 'operational creditor' as erroneously held by the Adjudicating Authority.

10. Once we hold that the Appellant was a 'financial creditor' qua the Respondent – Corporate Debtor and the application under Section 7 being in the prescribed format and not being defective was required to be admitted on proof of default, we find that the Respondent has failed to discharge onus of proof of discharge of debt. The plea raised that some cheques were delivered to one Mr. Ashok, the so called 'stooge' of the Appellant in his name, when she allegedly resorted to arm twisting using coercive methods for recovery of outstanding dues is neither plausible nor has the same been substantiated by record. That apart, the Respondent, subsequent to termination of agreement, issued balance confirmation on 1<sup>st</sup> April, 2015 in regard to Principal Amount and interest accrued thereon for the financial year, 2014-15 after deducting tax at source which stares in its face. There is no explanation for issuance of cheque worth Rs.1.35 Crore favouring the Appellant which was dishonoured and led to lodging of FIR and filing of cross suits. The dispute raised is neither relevant for triggering of Corporate Insolvency Resolution Process under Section 7 of I&B Code nor does the same relate to the issue of insolvency resolution. Given the mandate of

Section 238 of I&B Code, pendency of cross suits inter-se the parties regarding the claim and the bounced cheque is no bar to initiation of Corporate Insolvency Resolution Process at the instance of Appellant – ‘Financial Creditor’.

11. In view of the foregoing discussion, the impugned order holding the Appellant as ‘operational creditor’ and declining to initiate Insolvency Resolution Process on account of pre-existence of dispute is unsustainable. The findings recorded by the Adjudicating Authority are erroneous and cannot be supported. We accordingly allow the appeal and set aside the impugned order. The Adjudicating Authority is directed to admit the application of Appellant - ‘Financial Creditor’ under Section 7 of I&B Code after a limited notice to Respondent to enable it to settle the claim of the Appellant, if it so chooses. There shall be no orders as to costs.

[Justice S. J. Mukhopadhaya]  
Chairperson

[Justice Bansi Lal Bhat]  
Member (Judicial)

**NEW DELHI**

**19<sup>th</sup> March, 2019**

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