

ACUITY **LAW**

**INSOLVENCY LAW**  
**NEWSLETTER**

**May 2022**

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## ABOUT ACUITY LAW

Acuity Law was founded in November 2011. Acuity Law comprises of a team of young and energetic lawyers/ professionals led by Souvik Ganguly, Gautam Narayan, Deni Shah and Renjith Nair who have deep and diverse experiences in their chosen areas of practice. We advise Indian and multinational companies, funds, banks and financial institutions, founders of companies, management teams, international law firms, domestic and international investment banks, financial advisors, and government agencies in various transactions in and outside India.

Acuity Law takes pride in rendering incisive legal advice taking into consideration commercial realities. Our areas of practice are divided into three departments. The Corporate practice is led by Souvik Ganguly, the Global Trade and Tax practice is led by Deni Shah and the Disputes practice is led by Gautam Narayan with assistance from Renjith Nair.

As part of the Corporate practice, Acuity Law advises on:

- Mergers and acquisitions;
- Distressed mergers and acquisitions;
- Insolvency Law;
- Private Equity and Venture Funding;
- Employment and labour laws;
- Commercial and trading arrangements; and
- Corporate Advisory

As part of the Global Trade and Tax practice, Acuity Law advises on:

- Cross-border tax planning and jurisdiction analysis
- Strategies for acquisitions, mergers, divestitures, diversification or consolidation of businesses
- Inbound and outbound investment structuring
- Endowment planning / wealth management strategies
- Global Trade & Customs laws, including foreign trade policy
- International supply chain optimization
- Goods & Services Tax and other Indirect taxes

As part of the Disputes practice, Acuity Law advises and represents clients on domestic and cross - border:

- Civil disputes;
- Criminal law matters; and
- Arbitration matters

Acuity Law actively follows legislative and policy developments in its chosen areas of practice and shares such developments with clients and friends on a regular basis.

If you want to know more about Acuity Law, please visit our website [acuitylaw.co.in](http://acuitylaw.co.in) or write to us at [al@acuitylaw.co.in](mailto:al@acuitylaw.co.in).

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## INTRODUCTION

This newsletter covers key updates about developments in insolvency law during the month of May 2022.

We have summarized the key judgments passed by the Supreme Court (**SC**) and the National Company Law Appellate Tribunals (**NCLAT**). Please see the summary of the relevant regulatory developments below.

### 1) A PERFORMANCE BANK GUARANTEE CAN BE INVOKED OR ENCASHED AFTER MORATORIUM HAS BEEN IMPOSED

**Matter:** Engineering Projects (India) Ltd. v. Mr. Ram Ratan Kanoongo, RP of D. Thakkar Construction Pvt. Ltd.

**Order dated:** 06 May 2022

#### **Summary:**

In the present case, Engineering Projects (India) Ltd. (**Engineering Projects**) sanctioned certain construction work to D. Thakkar Construction Pvt. Ltd. (**Thakkar Construction**), which was to be completed within a period of fifteen months. As per the terms of the contract, Thakkar Construction submitted a performance bank guarantee and a mobilization advance bank guarantee (collectively **Bank Guarantees**). Thakkar Construction failed to complete the awarded work and Engineering Projects invoked the Bank Guarantees and issued directions to the banks who had given the guarantees. Before the banks could remit the guarantee amount, corporate insolvency resolution process (**CIRP**) of Thakkar Construction was initiated and a moratorium was imposed under the Insolvency and Bankruptcy Code, 2016 (**Code**).

After the initiation of CIRP, the Bank Guarantees were encashed, and the resolution professional of Thakkar Construction approached the NCLT seeking refund of the amounts encashed. This application was allowed by the NCLT, and Engineering Projects was directed to refund the amounts. The NCLT's order was challenged before the NCLAT.

NCLAT ruled that the amount given as an advance under the mobilization advance bank guarantee is not a debt or an obligation in respect of a claim; it is only on completion of the project or execution of the contract in its totality, that the liability kicks in. Similarly, the NCLAT ruled that a debtor can invoke the performance bank guarantee in the event of any shortcoming in the performance of the contract. Therefore, the amount given under the Bank Guarantees does not belong to the corporate debtor, i.e., Thakkar Construction and it cannot be said as an asset of Thakkar Construction either. Therefore, the provisions of the moratorium won't apply to such assets. Accordingly, NCLAT held that the resolution profession has no jurisdiction to take over a third-party asset which does not belong to Thakkar Construction and the NCLT order was dismissed.

### 2) INSOLVENCY CANNOT BE INITIATED ON THE BASIS OF UNPAID LEAVE TRAVEL CONCESSION AND LEAVE ENCASHMENT DUES

**Matter:** Kishore K. Lonkar v. Hindustan Antibiotics Ltd.

**Order dated:** 10 May 2022

#### **Summary:**

Kishore K. Lonkar, an employee of Hindustan Antibiotics Ltd. (**Hindustan Antibiotics**) had attained superannuation. As an amount of INR 1.6 million which includes gratuity, earned leave encashment, unpaid leave travel concession, etc. was not paid by Hindustan Antibiotics, the employee filed an application before the NCLT for initiating CIRP of Hindustan Antibiotics. NCLT's order rejecting the application was challenged before the NCLAT.

The issue under consideration before the NCLAT was whether service benefits such as gratuity, earned leave encashment, unpaid leave travel concession, etc., would fall under the definition of 'operational debt' under the Code. NCLAT noted that for a claim to be considered as 'operational debt' under the Code, it must be in respect of goods or services including employment. NCLAT observed that in the present case, the amount claimed by Kishore K. Lonkar is not towards any services rendered by him during his employment but rather 'welfare claims' that arise after cessation of employment, which depends on the tenure of the employment. NCLAT, observing that the intention and object of code is not recovery and only resolution, held that CIRP cannot be initiated for dues which are welfare benefits.

### 3) JOINT SALE OF ASSETS OF A CORPORATE DEBTOR UNDER LIQUIDATION AND THE GUARANTOR UNDER SARFAESI ACT IS PERMITTED

**Matter:** Ayan Mallick v. Pratim Bayal, Liquidator & Ors.

**Order dated:** 13 May 2022

**Summary:**

In the present case, a joint auction under the Code and Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (**SARFAESI Act**) was carried out as part of the land on which factory of the corporate debtor was built was owned by the guarantor. Without such a joint auction, the liquidator was unable to sell the assets of the corporate debtor. The guarantor challenged the joint auction notice before the NCLT which refused to stay the joint auction. The order of the NCLT was challenged before the NCLAT.

NCLAT observed that a joint auction shall result in maximization of assets of the corporate debtor and in the present case, both land and factory were needed to be sold together to maximize the value of the assets. Further, as the possession of the properties of the guarantor had already been taken under SARFAESI Act, NCLAT ruled that a mere joint auction of the assets will not cause any harm to the guarantor. Accordingly, the appeal was dismissed, and the joint auction was permitted.

### 4) HOLDER OF A RECOVERY CERTIFICATE ISSUED UNDER RECOVERY OF DEBTS AND BANKRUPTCY ACT, 1993 IS A 'FINANCIAL CREDITOR' UNDER THE CODE

**Matter:** Kotak Mahindra Bank Ltd. vs. A. Balakrishnan & Anr.

**Order dated:** 30 May 2022

**Summary:**

Kotak Mahindra Bank Limited (**Kotak Mahindra**) was an assignee of certain loans in respect of which Prasad Properties and Investments Private Limited (**Prasad Properties**) stood as a guarantor. As Prasad Properties defaulted in payment to Kotak Mahindra as per the terms of a compromise settlement entered between the two, Kotak Mahindra approached the Debt Recovery Tribunal (**DRT**) under the Recovery of Debts and Bankruptcy Act, 1993 (**RDB Act**). The DRT decided in favour of Kotak Mahindra and issued recovery certificates in its favour.

On the basis of the recovery certificates, Kotak Mahindra filed an application before the NCLT seeking initiation of CIRP of Prasad Properties. Though CIRP was initiated by the NCLT, the NCLAT set aside the order by stating that the issuance of recovery certificates by the DRT would not give a right to initiate CIRP. The NCLAT's order was challenged before the SC.

The issue before the SC was whether a liability in respect of a claim arising out of a recovery certificate under the RDB Act would be a 'financial debt' under the Code. The SC noted that for filing an application for initiation of CIRP, there must be a debt and default. The Code defines 'debt' as a liability in respect of a claim. Claim is further defined as a right to payment, whether or not such right has been reduced to judgment. Looking at the framework of the Code, the SC opined that it could not have been the legislative intent of the Code to exclude from the definition of 'financial debt' a liability of a claim that is due and payable in terms of a recovery certificate. The SC held that any person holding such a recovery certificate is well within the scope of a financial creditor under the Code and therefore can file an application for initiating CIRP of the debtor.

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