

Insolvency and Bankruptcy Hotline

February 15, 2018

HAS BOMBAY HIGH COURT SETTLED THE BANKRUPTCY LAW SUPREMACY DEBATE?

- Corporate Debtor itself or any other creditor may file fresh proceedings under the Bankruptcy Code regardless of admitted and pending winding up petitions before Company Courts
- The Bankruptcy Code has primacy over Company Law and gives special powers to the NCLT in implementing provisions in a strict time bound manner
- Company Courts have no authority to injunct proceedings initiated under the Bankruptcy Code

INTRODUCTION

The Ministry of Corporate affairs had on December 07, 2016 notified the Companies (Transfer of Pending Proceedings) Rules, 2016 (“**Transfer Rules**”) which provides for the transition of proceedings from the High Court to the National Company Law Tribunal (“**NCLT**”) based on certain criterion. In accordance with Rule 5 of the said Rules, where the petition for winding up has been served on the company and is pending before the relevant High Court, such a petition shall be adjudged by the High Court.

Ever since the notification of the Transfer Rules and the direction to banks by the Reserve Bank of India (“**RBI**”) to commence insolvency proceedings against the 12 big ticket corporate defaulters, concerns have been raised over the ability of the NCLT to initiate the Corporate Insolvency Resolution Process (“**CIRP**”) in light of the existing winding up petitions against the said defaulters. The issue first came to light after Union Bank of India’s application under Section 7 of the Insolvency and Bankruptcy Code, 2016 (“**IBC**”) against Era Infra Engineering, one of the chosen 12, while around 18 winding up petitions against it remained pending in the Delhi High Court. This matter has been escalated to a special bench of NCLT, Delhi which has considered the issue of proceedings pending before the High Court and initiated in the NCLT against the same company, and has reserved its judgment on the same¹.

In the meanwhile, the High Court of Bombay (“**Court**”) in the matter of *Jotun India Private Limited (“Jotun”) Vs. PSL Limited (“PSL”)*² while hearing an application against an order of the Company Court staying proceedings initiated by the Corporate Debtor before the NCLT in light of a pending winding up petition against the Corporate Debtor in the said Company Court, had occasion to rule on (i) whether an application under the IBC can be made even in cases where a winding up petition has been admitted and is pending before a Company Court; and (ii) whether such an admission of a winding petition allows the Company Court to injunct proceedings before the NCLT.

FACTUAL MATRIX

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| March 10, 2015 | Jotun filed a petition under Sections 433 and 434 of the Companies Act, 1956 (“ Companies Act ”), seeking winding up of PSL in respect of unpaid invoices for goods supplied. |
| June 19, 2015 | During pendency of the petition, PSL made a reference to the Board of Industrial and Financial Reconstruction (“ BIFR ”) under the Sick Industrial Companies (Special Provisions) Act, 1985 (“ SICA ”). |
| December 01, 2016 | Sick Industrial Companies (Special Provisions) Repeal Act, 2003 (“ Repeal Act ”) was notified and hence SICA was repealed. The IBC was simultaneously brought into force and Section 252 of the IBC (as specified in the Eighth Schedule) amended Section 4(b) of the Repeal Act to allow companies whose reference was pending before the BIFR to file cases afresh under Section 10 of the IBC within 180 days from the date of the repeal. |
| March 09, 2017 | The winding up petition against PSL was admitted by the Court. |
| March 29, 2017 | PSL i.e. the Corporate Debtor filed an application under Section 10 before NCLT, Ahmedabad (“ IBC Application ”) for the commencement of the CIRP within the prescribed window of 180 days. |
| July 18, 2017 | The NCLT heard the IBC application filed by PSL on July 18, 2017 and reserved the matter for orders. On the same date, Jotun filed an application before the Court seeking appointment of a provisional liquidator. |
| July 19, 2017 | The Court passed an order dated July 19, 2017 (“ Impugned Order ”) restraining the NCLT, Ahmedabad from continuing with the IBC Application while the application before it remained pending. |

Hence the application filed by PSL seeking to recall the Impugned Order which had stayed the proceedings initiated by PSL under Section 10 of the IBC.

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Relying on the decision the Supreme Court of India in *Innovative Industries Limited V/s ICICI Bank & Anr*³, the Court considered the views of the Bankruptcy Law Reforms Committee ("Reforms Committee") which inter alia concluded that where a default occurs, it is best for one forum, such as a creditors committee, to evaluate a debt restructuring and/or liquidation and make a decision on whether the entity was facing financial or business failure and whether it was capable of being revived. It further observed that the IBC has been enacted to set up the Insolvency and Bankruptcy resolution process in a strict time bound manner, powers which can only be exercised by the NCLT. In light of the above, the Court recognized that, under IBC, there is a paradigm shift from the erstwhile regime in as much as it displaces the management of the company, an IRP is appointed, and the committee of creditors is left to decide the fate of the company.

Primacy of the IBC

Placing reliance on the Supreme Court case of *Madura Coats Ltd. vs. Modi Rubber Ltd. & Anr*⁴ the Court observed that even during the regime of SICA, SICA was held to have primacy over the provisions of the Companies Act. Hence, the Court held that since SICA is repealed and replaced by the IBC, the provisions of IBC should prevail over the provisions of the Companies Act insofar as IBC is admittedly a successor statute to SICA.

No Carving out of existing winding up proceedings

The Court took due note of the fact that the effect of the amended Section 4(b) of the Repeal Act conferred an express power upon a company to make a reference under the IBC to the NCLT within 180 days of the commencement of the IBC. It further observed that there was no express and implied saving of any substantive provisions of the Companies Act to warrant the interpretation that a reference made by a company under section 252, in a situation where a post notice winding up petition remains pending against the same company, cannot be entertained by the NCLT.

Legislative Intent

The Court observed that the legislature while enacting the IBC was well aware that company petitions may have already been filed, admitted and pending before Company Courts under the Companies Act. It observed that the Transfer Rules only mention that winding up petitions in respect of which notice has been issued to the respondent company or which have been admitted would remain with the jurisdictional high court whereas all other winding up petitions get transferred to the NCLT. If the legislature had intended that the saved winding up petitions would have primacy over the NCLT proceedings which may be filed in respect of the same company by another creditor, the legislature would have said so, either in the IBC or in the Transfer Rules, which it hasn't.

The Court noted that what is saved are only the proceedings of winding up pending before the jurisdictional High Court and not the company itself in relation to which such proceedings are saved. The Court therefore held that such a corporate debtor company is still subject to the provisions of the IBC whereby the corporate debtor itself (such as PSL in this case) or any other creditor may file fresh proceedings before the NCLT, regardless of whether the winding up petition in relation to the said corporate debtor are admitted and pending. The Court further noted that by virtue of Section 64(2) of the IBC, the Company Court does not have the power to injunct proceedings initiated before the NCLT.

JUDGMENT & ANALYSIS

In light of the above considerations, the Court went on to hold that there was no bar on NCLT, Ahmedabad from proceeding with the IBC Application filed by PSL i.e. the Corporate Debtor even though a winding up petition against it remained pending against it in the High Court of Bombay.

This ruling re-affirms and forwards the legislative intent of giving supremacy to the IBC where the Court has recognized the primacy of the IBC and the special powers of the NCLT in implementing the provisions of the IBC in a strict time bound manner, powers which are not available to company courts. However, in allowing proceedings before the NCLT to be proceeded with while a winding up petition remains admitted and pending before the Company Court (until a moratorium is imposed under Section 14 of the IBC), the Bombay High Court has created a situation where the ultimate fate of the company and the creditors might depend on a race between admission of an Insolvency Application before the NCLT and an order of final winding-up under Section 481 of the Companies Act. Further, Creditors who may have filed a winding up petition before a Company Court and may be close to obtaining a final order, may be forced to re-assert and re-prove all their claims before the Insolvency Resolution Professional and the committee of creditors.

Interestingly, in a petition moved by Nissan Motor India and Renault Nissan Automotive in the Madras High Court praying for a stay on proceedings initiated before the NCLT due to the transfer of winding up petitions filed against them, the Madras High Court granted an interim order staying the proceedings before the said NCLT. The Petitioners therein had averred that the Transfer Rules have been misconstrued and erroneously applied to the winding up petition in which the entire pleadings were already over. They have also sought to declare the provisions of the Transfer Rules as ultra vires of the Constitution. While the Madras High Court, contrary to the view of the Bombay High Court, went on to stay the proceedings before the NCLT, it will be interesting to see what it finally holds regarding the constitutionality of the Transfer Rules. Such issues however, are mere teething problems associated with the transition from the old to the new regime. These ought to iron out as and when such petitions achieve completion either before the Company Courts or the NCLTs and the transition phase comes to an end.

– Siddharth Ratho & Vyapak Desai

You can direct your queries or comments to the authors

¹ (IB) – 190 (PB) / 2017

² CA No. 572 of 2017 in C.P. No. 434 of 2015

³ (2017) SCC Online 1025

⁴ (2016) 7 SCC 603

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