NATIONAL COMPANY LAW APPELLATE TRIBUNAL
PRINCIPAL BENCH, NEW DELHI

Company Appeal (AT) (Insolvency) No. 258 of 2021

[Arising out of order dated 2nd February 2021, passed by the Adjudicating Authority/National Company Law Tribunal, Kolkata Bench, Kolkata in CP (IB) No. 2192/KB/2019]

IN THE MATTER OF:

Hytone Merchants Private Limited
A company within the meaning of the Companies Act, 2013, having its registered Office at:
87, Diamond Harbour Road,
Kolkata – 700038, West Bengal **Appellant**

Versus

Satabadi Investment Consultants Private Limited
A company within the meaning of the Companies Act, 2013, having its registered Office at:
235/2Ac AJC Bose Road,
Kolkata – 700020, West Bengal **Respondent**

Present:

For Appellant : Mr Shaunak Mitra and Mr Sarad Singhania, Advocates

For Respondent : Ms Swati Sood, Advocate

J U D G M E N T

[Per; V. P. Singh, Member (T)]

This Appeal emanates from the order dated 2nd February, 2021, passed by the Adjudicating Authority/National Company Law Tribunal, Kolkata Bench, Kolkata in CP (IB) No. 2192/KB/2019, whereby the Adjudicating

Authority has rejected the Application filed under Section 7 of the Insolvency and Bankruptcy Code, 2016 (in short '**I&B Code**'). The original status of the Parties in the Company Petition represents them in this Appeal for the sake of convenience.

2. The brief facts of the case are as follows:

(a) The Appellant had given an unsecured loan of Rs.3 lakhs to the Respondent / Corporate Debtor for six months carrying interest @ 15% per annum, on 15th February 2019. This was under request for financial assistance by the Respondent / Corporate Debtor.

(b) The Appellant is a Financial Creditor of the Respondent viz. Satabadi Investment Consultants Private Limited. As stated above, the Appellant had filed the Section 7 Application against the Respondent on account of default committed by the Respondent / Corporate Debtor in repaying loan amount advanced by the Appellant.

(c) The Respondent / Corporate Debtor acknowledged receipt of the unsecured loan amount and also issued a demand promissory note. However, the Respondent Corporate Debtor defaulted to repay the dues.

(d) The Appellant had issued a demand notice dated 16th October 2019 recalling the unsecured loan, but the Respondent Corporate Debtor failed to clear the outstanding dues despite the same.

(e) The existence of debt and default are admitted. In fact, in the Reply Affidavit filed by the Respondent / Corporate Debtor, there is a definite admission of default.

(f) The Section 7 Application was complete in all respects and met all requirements under IBC and Regulations thereunder. However, in the impugned order dated 2nd February 2021, despite finding and ascertaining that there was indeed the existence of default and that the Section 7 Application was complete in all respects, the Adjudicating Authority proceeded to dismiss the Section 7 Application.

(g) The Adjudicating Authority has observed that:

> "*on perusal of the master debt of the corporate debtor it is seen that the corporate debtor has given a corporate guarantee of ₹ 482,42,00,000. On further enquiry and on perusal of the financial statements for the financial year 2018-19 of the corporate debtor, it has come to light that the networks of the corporate debtor is ₹ 15,36,39,015. It is hard to convince oneself that the Company having a network of ₹ 15,36,39,015 is not able to make a payment of ₹ 3 lakhs. It appears that the petition at hand has been filed in collusion with the corporate debtor.*"
>
> *(verbatim copy)*

(h) Based on the above finding, the Adjudicating Authority rejected the Application filed U/S 7 of the Code. Accordingly, being aggrieved by the said order, this Appeal is filed.

Appellants Submission

3. The learned Counsel for the Appellant submits that by the impugned order dated 2nd February 2021, the Adjudicating Authority has dismissed the Appellant/Financial Creditor's Section 7 Application against the Corporate Debtor despite holding that; the Application was complete in all respects as required by law, and the Application clearly showed that the Corporate Debtor was in default of a debt due and payable. The default amount was more than the minimum threshold stipulated in Section 4 (1) of the Code.

4. The Adjudicating Authority has overreached and exceeded its authority and jurisdiction in passing the impugned order. Accordingly, the impugned order is liable to be set aside. Accordingly, the Section 7 Application should be admitted by commencing the Corporate Insolvency Resolution Process (CIRP) regarding the Respondent Corporate Debtor.

5. In paragraph 9 of the impugned order, there is a definite finding by the Adjudicating Authority that the Section 7 Application was complete in all respects. Consequently, there was existing default, also meeting the minimum threshold under IBC. In the circumstances, under Section 7(5) of IBC, the Adjudicating Authority had no further discretion to exercise in the matter and ought to have admitted the Section 7 Application. However, the Adjudicating Authority, instead of following the mandate of Section 7(5) of IBC, has proceeded with an unjustified and roving enquiry of its own (without even affording any opportunity to the Appellant to make any submissions in such

regard) to hold that the Section 7 Application was filed in collusion with the Respondent / Corporate Debtor.

6. There is no basis for the finding in the impugned order that the Section 7 Application is a product of collusion between the parties. The Adjudicating Authority has referred to the master data of the Corporate Debtor and the financial statements for 2018-19 to come to the finding of collusion. However, in doing so, the Adjudicating Authority has grossly exceeded its jurisdiction and authority and/or has acted without authority or jurisdiction. Neither the Master Data nor the financial statements of the Corporate Debtor, as referred to in paragraph 9 of the impugned order, were even part of the records in the Section 7 Application. It is to be noted that master data appearing on page 11 of the Section 7 Application did not show the corporate guarantee amount as in paragraph 9 of the impugned order.

7. Anyhow, the Adjudicating Authority cannot embark on a roving enquiry of its own to adjudicate an Application under Section 7.

8. The Adjudicating Authority has misdirected itself in ignoring the materials on record, categorically showing the existence of default. Instead, the Adjudicating Authority has proceeded to refer to and rely on purported documents that were not on record to arrive at a finding of purported collusion without giving any opportunity to the Appellant to make submissions in this regard.

9. The impugned order has been passed in contravention of law, the provisions of IBC and Regulations thereunder. The Adjudicating Authority has acted in excess and/or without jurisdiction in passing the impugned order without appreciating the facts and records of the case.

10. The impugned order has been passed without Application of mind and without taking into consideration the aforesaid facts and the materials on record, and without appreciating the submissions made on behalf of the Appellant.

11. Under Section 7 (5), it is submitted that there is no discretion vested to the Adjudicating Authority to reject a Section 7 Application if the default has occurred and the Application is complete.

12. The Appellant further contends that Hon'ble Supreme Court in Innoventive Industries Limited vs ICICI Bank held that "the moment the Adjudicating Authority is satisfied that the default has occurred, the Application must be admitted unless it is complete." Relying on the observations of the Hon'ble Supreme Court, which leaves no room for doubt that there is no discretion to reject if there is default and the Application is complete.

13. However, in passing the impugned order, the Adjudicating Authority has acted in derogation of the settled principles of law. Therefore, Ex-facie, the impugned order deserves to be set aside on this ground alone, especially after the Adjudicating Authority has arrived at the factual finding that debt

was due, default by the Corporate Debtor, and the Application was complete in all respects. Furthermore, there were no facts on record to warrant the exercise of discretion to reject the Application.

14. Section 7 (4) of the Code is also relevant since the same categorically provides that the Adjudicating Authority is required to "ascertain the existence of a default from the records of an information utility or on the basis of other evidence furnished by the Financial Creditor under Sub-section (3)". This evidences the scope of an adjudication of the Adjudicating Authority, i.e. adjudication is to be made on the evidence disclosed and on record. The Adjudicating Authority is not empowered to initiate a roving enquiry dehors the records.

15. The only sole reason given in the impugned order to reject the Section 7 Application is based on an erroneous assumption regarding the financial position of the Corporate Debtor, which is arrived based on the Corporate Debtor's financial statement for 2018-2019 (which were anyway not on record before the Adjudicating Authority) and the Corporate Debtor's Master Data available on the MCA portal.

16. It is further submitted that the Corporate Debtor's financial statement for 2018-19 was not part of the records. Still, the Appellant/Financial Creditor also was not given any opportunity to address such issues at all. This amounts to a violation of principles of natural justice since the Adjudicating Authority has arrived at an erroneous inference based on the irrelevant

records, and that too, without allowing the Appellant/Financial Creditor to make submissions regarding the same.

17. Furthermore, the financial statements of the Corporate Debtor for the year ending 31st March 2019 are not at all relevant because; the Section 7 Application was filed in December 2019, i.e. more than eight months after 31st March 2019; the impugned order rejecting the Section 7 Application was passed on 2nd February 2021, almost two years after the 31st March 2019; the Adjudicating Authority has ignored the possibility that the financial position reflected on 31st March 2019 may have undergone a sea change in the intervening two years.

18. Significantly, the Corporate Debtor's submission that it was unable to make payment to Appellant/Financial Creditor due to "economic recession and losses in its business" and due to Corporate Debtor "being a victim of circumstances" and "by reason of the duration of the business", though recorded in para 7 of the impugned order, the Adjudicating Authority has failed to appreciate the meaning of the same.

19. Now the Corporate Debtor has disclosed its financial statement for 2018-19 in this Appeal in their reply affidavit, and the Corporate Debtor has categorically stated on oath (at paragraph 7, page 3 of reply affidavit) that the financial condition of Corporate Debtor has starkly deteriorated after 31st March 2019**. Because the major portion of its investment into companies, namely, Kohinoor Newsprint and Papers Private Limited & Kohinoor Pulp**

and Paper Private Limited, are sunk investments, where the Corporate Debtor has no chance of getting its money back, and the amounts are reflected in the accounts as per the accounting standard since the same cannot be immediately written off. The Corporate Debtor has disclosed that the said two companies are under CIRP and in liquidation, respectively, under the provisions of the Code. The Appellant/Financial Creditor has also enquired ascertained that even in respect of Kohinoor Newsprint, Application for liquidation is already filed. In short, the net worth of the Corporate Debtor stands substantially eroded after 31st March 2019.

20. Further, it is pertinent to mention that the Appellant/Financial Creditor has no relation or connection with the Corporate Debtor. Even the Adjudicating Authority has not found any relationship or connection. Thus the conclusion drawn by the Adjudicating Authority of collusion existing between Financial Creditor and the Corporate Debtor is unwarranted, unfounded and bereft of any basis. There are no particulars to support the finding of collusion. A finding of collusion cannot be the outcome of guesswork, which is exactly the case in the impugned order and that too, without even giving the Appellant/Financial Creditor opportunity to make any submissions on such issue, and thus, the impugned order of rejection is in violation of natural justice.

21. Without prejudice, Section 65 of the Code also does not and cannot apply to the facts of the case, firstly because there is no connection between

the parties. Secondly, the Appellant/Financial Creditor has demonstrated the existence of default recognised by the Adjudicating Authority. Consequently, the scheme of the Code has been ignored by the Adjudicating Authority.

22. The Adjudicating Authority has also totally failed to appreciate that the Appellant/Financial Creditor has no control over the stand taken by the Corporate Debtor to defend the Application. Therefore, merely because the Corporate Debtor has admitted the default due to its hopeless financial condition and the Corporate Debtor has refused to pay, it is not and cannot be a ground to reject the Section 7 Application on an unsubstantiated guess, as has been done in the instant case.

23. The net effect of the impugned order is that the Appellant/Financial Creditor, which has a genuine and established claim against Corporate Debtor, has been made to suffer for the Corporate Debtor's failure to make payment of the defaulted amount.

24. **The reference by the Adjudicating Authority to the corporate guarantee mentioned in the Corporate Debtor's master data (page 40 of the Appeal) is also totally irrelevant. Assuming that any such guarantee exists, the same is a liability of the Corporate Debtor**. Therefore, it is not even mentioned in the impugned order as to the relevance of the same.

Respondent/Corporate Debtor's submission

25. The Corporate Debtor submits that an unsecured loan of ₹ three lakhs was sought from the Appellant/Financial Creditor for six months carrying

interest at the rate of 15% per annum on 15th February 2019. But due to business losses and economic recession, the Company was not able to recover and thus was unable to pay back such loan.

26. The impugned order alleges of existing collusion, mentioned in the impugned order, is vehemently disagreed disputed as there has been proper disbursement of a sum of ₹ three lakhs. It was taken as a loan, and by a demand notice dated 16th October 2019, the Appellant had recalled the unsecured loan, which is explained herein. However, due to staggering economic and business exigencies, the same could not be fulfilled, and the amount was not returned timely. Moreover, the Corporate Debtor Company had made several other commitments and investments, and it was in no current position to pay back the recalled amount.

27. As per the order dated 4th April 2021, necessary clarifications were sought regarding the balance-sheet with regards to its mention in the Order of National Company Law Tribunal, dated 4th January 2021, where it is mentioned that the net worth of the Company's ₹ 15,36,39,015 as per the financial statements of 2018-2019. The Respondent contends that the Application was filed during the said period 2019-2020. But at the present situation, when the Hon'ble Tribunal passed the order, and that is on or about 4th January 2021, the condition of the Company had starkly deteriorated, and the Respondent Company was not in a condition to pay back the same. **Additionally, it will be evident from the entries in the balance sheet of the Respondent herein that the Corporate Debtor has made substantial**

investments in M/S Kohinoor Pulp and Paper Private Limited and M/S Kohinoor Paper and Newsprint Private Limited. M/S Kohinoor Pulp and Paper Private Limited are under liquidation, and M/S Kohinoor Paper and Newsprint Private Limited are under the Corporate Insolvency Resolution Process. In the said matter, an Application has already been filed for initiation of the liquidation process; the Corporate Debtor herein being an unsecured Financial Creditor, there is no chance of getting said money back. As per standard accounting practices, the Respondent herein is bound to show said receivable in its accounts and cannot write it off.

28. **Statutory provisions**

CORPORATE INSOLVENCY RESOLUTION PROCESS

6. Persons who may initiate corporate insolvency resolution process.—Where any corporate debtor commits a default, a financial creditor, an operational creditor or the corporate debtor itself may initiate corporate insolvency resolution process in respect of such corporate debtor in the manner as provided under this Chapter.

7. Initiation of Corporate Insolvency Resolution Process by Financial Creditor.—(1) A financial creditor either by itself or jointly with [other Financial Creditors, or any other person on behalf of the financial creditor, as may be notified by the Central Government] may file an application for initiating corporate insolvency resolution process

against a corporate debtor before the Adjudicating Authority when a default has occurred.

[Provided that for the financial creditors, referred to in clauses (*a*) and (*b*) of sub-section (6-A) of Section 21, an application for initiating corporate insolvency resolution process against the corporate debtor shall be filed jointly by not less than one hundred of such creditors in the same class or not less than ten per cent. of the total number of such creditors in the same class, whichever is less:

Provided further that for financial creditors who are allottees under a real estate project, an application for initiating corporate insolvency resolution process against the corporate debtor shall be filed jointly by not less than one hundred of such allottees under the same real estate project or not less than ten per cent. of the total number of such allottees under the same real estate project, whichever is less:

Provided also that where an application for initiating the corporate insolvency resolution process against a corporate debtor has been filed by a financial creditor referred to in the first and second provisos and has not been admitted by the Adjudicating Authority before the commencement of the Insolvency and Bankruptcy Code (Amendment) Act, 2020, such Application shall be modified to comply with the requirements of the first or second proviso within thirty days of the

commencement of the said Act, failing which the Application shall be deemed to be withdrawn before its admission.]

Explanation.—For the purposes of this sub-section, a default includes a default in respect of a financial debt owed not only to the applicant financial creditor but to any other financial creditor of the corporate debtor.

(2) The financial creditor shall make an application under sub-section (1) in such form and manner and accompanied with such fee as may be prescribed.

(3) The financial creditor shall, along with the application furnish—

(*a*) record of the default recorded with the information utility or such other record or evidence of default as may be specified;

(*b*) the name of the resolution professional proposed to act as an interim resolution professional; and

(*c*) any other information as may be specified by the Board.

(4) The Adjudicating Authority shall, within fourteen days of the receipt of the Application under sub-section (2), ascertain the existence of a default from the records of an information utility or on the basis of other evidence furnished by the financial creditor under sub-section (3):

[Provided that if the Adjudicating Authority has not ascertained the existence of default and passed an order under sub-section (5) within such time, it shall record its reasons in writing for the same.]

(5) Where the Adjudicating Authority is satisfied that—

(*a*) a default has occurred and the Application under sub-section (2) is complete, and there is no disciplinary proceedings pending against the proposed resolution professional, it may, by order, admit such Application; or

(*b*) default has not occurred or the Application under sub-section (2) is incomplete or any disciplinary proceeding is pending against the proposed resolution professional, it may, by order, reject such Application:

Provided that the Adjudicating Authority shall, before rejecting the Application under clause (*b*) of sub-section (5), give a notice to the applicant to rectify the defect in his Application within seven days of receipt of such notice from the Adjudicating Authority.

(6) The corporate insolvency resolution process shall commence from the date of admission of the Application under sub-section (5).

(7) The Adjudicating Authority shall communicate—

(*a*) the order under clause (*a*) of sub-section (5) to the financial creditor and the corporate debtor;

(*b*) the order under clause (*b*) of sub-section (5) to the financial creditor, within seven days of admission or rejection of such Application, as the case may be.

65. <u>Fraudulent or malicious initiation of proceedings</u>.—

(1) If, any person initiates the insolvency resolution process or liquidation proceedings fraudulently or with malicious intent for any purpose other than for the resolution of Insolvency, or liquidation, as the case may be, the Adjudicating Authority may impose upon such person a penalty which shall not be less than one lakh rupees, but may extend to one crore rupees.

(2) <u>If, any person initiates voluntary liquidation proceedings with the intent to defraud any person, the Adjudicating Authority may impose upon such person a penalty which shall not be less than one lakh rupees but may extend to one crore rupees.</u>

Judgements Referred

29. Hon'ble Supreme Court in case of *Innoventive Industries Ltd. v. ICICI Bank*, (2018) 1 SCC 407 : 2017 SCC OnLine SC 1025 : (2018) 1 SCC (Civ) 356 at page 438 held:

> *"**28.** When it comes to a financial creditor triggering the process, Section 7 becomes relevant. Under the Explanation to Section 7(1), a default is in respect of a financial debt owed to any financial creditor of the corporate debtor — it need not be a debt owed to the applicant financial creditor. Under Section*

7(2), an application is to be made under sub-section (1) in such form and manner as is prescribed, which takes us to the Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016. Under Rule 4, the Application is made by a financial creditor in Form 1 accompanied by documents and records required therein. Form 1 is a detailed form in 5 parts, which requires particulars of the applicant in Part I, particulars of the corporate debtor in Part II, particulars of the proposed interim resolution professional in Part III, particulars of the financial debt in Part IV and documents, records and evidence of default in Part V. Under Rule 4(3), the applicant is to dispatch a copy of the Application filed with the adjudicating authority by registered post or speed post to the registered office of the corporate debtor. The speed, within which the adjudicating authority is to ascertain the existence of a default from the records of the information utility or on the basis of evidence furnished by the financial creditor, is important. This it must do within 14 days of the receipt of the Application. It is at the stage of Section 7(5), where the adjudicating authority is to be satisfied that a default has occurred, that the corporate debtor is entitled to point out that a default has not occurred in the sense that the "debt", which may also include a disputed claim, is not due. A debt may not be due if it is not payable in law or in fact. The moment the adjudicating authority is satisfied that a default has occurred, the Application must be admitted unless it is incomplete, in which case it may give notice to the applicant to rectify the defect within 7 days of receipt of a notice from the adjudicating authority. Under sub-section (7), the adjudicating authority shall then communicate the order passed to the financial creditor and corporate debtor

within 7 days of admission or rejection of such Application, as the case may be.

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30. *On the other hand, as we have seen, in the case of a corporate debtor who commits a default of a financial debt, the adjudicating authority has merely to see the records of the information utility or other evidence produced by the financial creditor to satisfy itself that a default has occurred. It is of no matter that the debt is disputed so long as the debt is "due" i.e. payable unless interdicted by some law or has not yet become due in the sense that it is payable at some future date. It is only when this is proved to the satisfaction of the adjudicating authority that the adjudicating authority may reject an application and not otherwise."*

30. **Hon'ble Supreme Court in *Swiss Ribbons (P) Ltd. v. Union of India*, (2019) 4 SCC 17 : 2019 SCC OnLine SC 73 at page 71has held:**

"***55. Apart from the record maintained by such utility, Form I appended to the Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016, makes it clear that the following are other sources which evidence a financial debt****:*

(a) Particulars of security held, if any, the date of its creation, its estimated value as per the creditor;

(b) Certificate of registration of charge issued by the Registrar of Companies (if the corporate debtor is a company);

(c) Order of a court, Tribunal or arbitral panel adjudicating on the default;

(d) Record of default with the information utility;

(e) Details of succession certificate, or probate of a will, or letter of administration, or court decree (as may be applicable), under the Indian Succession Act, 1925;

(f) The latest and complete copy of the financial contract reflecting all amendments and waivers to date;

(g) A record of default as available with any credit information company;

(h) Copies of entries in a bankers book in accordance with the Bankers Books Evidence Act, 1891.

54. It is clear from these sections that information in respect of debts incurred by financial debtors is easily available through information utilities which, under the Insolvency and Bankruptcy Board of India (Information Utilities) Regulations, 2017 (Information Utilities Regulations), are to satisfy themselves that information provided as to the debt is accurate. This is done by giving notice to the corporate debtor who then has an opportunity to correct such information.

58. *Rules 11, 34 and 37 of the National Company Law Tribunal Rules, 2016 (NCLT Rules) state as follows:*

*"**11. Inherent powers**.—**Nothing in these Rules shall be deemed to limit or otherwise affect the inherent powers of the Tribunal to make such orders as may be necessary for meeting the ends of justice or to prevent abuse of the process of the Tribunal.***

21. ***

34. General procedure*.—(1)* ***In a situation not provided for in these Rules, the Tribunal may, for reasons to be recorded in writing, determine the procedure in a particular case in accordance with the principles of natural justice.***

(2) The general heading in all proceedings before the Tribunal, in all advertisements and notices shall be in Form No. NCLT 4.

(3) Every petition or Application or reference shall be filed in form as provided in Form No. NCLT 1 with attachments thereto accompanied by Form No. NCLT 2 and in case of an interlocutory application, the same shall be filed in Form No. NCLT 1 accompanied by such attachments thereto along with Form No. NCLT 3.

(4) Every petition or Application including interlocutory Application shall be verified by an affidavit in Form No. NCLT 6. Notice to be issued by the Tribunal to the opposite party shall be in Form NCLT 5.

37. Notice to Opposite Party*.—(1) The Tribunal shall issue notice to the Respondent to show cause against the Application or petition on a date of hearing to be specified in the notice. Such notice in Form No. NCLT 5 shall be accompanied by a copy of the Application with supporting documents.*

(2) If the Respondent does not appear on the date specified in the notice in Form No. NCLT 5, the Tribunal, after according reasonable opportunity to the

Respondent, shall forthwith proceed ex parte to dispose of the Application.

(3) If the respondent contests to the notice received under sub-rule (1), it may, either in person or through an authorised representative, file a reply accompanied with an affidavit and along with copies of such documents on which it relies, with an advance service to the petitioner or applicant, to the Registry before the date of hearing and such reply and copies of documents shall form part of the record."

A conjoint reading of all these Rules makes it clear that at the stage of the adjudicating authority's satisfaction under Section 7(5) of the Code, the corporate debtor is served with a copy of the Application filed with the adjudicating authority and has the opportunity to file a reply before the said authority and be heard by the said authority before an order is made admitting the said Application*.*

59. What is also of relevance is that in order to protect the corporate debtor from being dragged into the corporate insolvency resolution process mala fide, the Code prescribes penalties. Thus, Section 65 of the Code reads as follows:

*"**65. Fraudulent or malicious initiation of proceedings**.—*

*(1) **If, any person initiates the insolvency resolution process or liquidation proceedings fraudulently or with malicious intent for any***

purpose other than for the resolution of Insolvency, or liquidation, as the case may be*, the adjudicating authority may impose upon such person a penalty which shall not be less than one lakh rupees, but may extend to one crore rupees.*

(2) ***If, any person initiates voluntary liquidation proceedings with the intent to defraud any person, the adjudicating authority may impose upon such person a penalty which shall not be less than one lakh rupees but may extend to one crore rupees."***

60. *Also, punishment is prescribed under Section 75 for furnishing false information in an application made by a financial creditor which further deters a financial creditor from wrongly invoking the provisions of Section 7. Section 75 reads as under:*

*"****75. Punishment for false information furnished in Application****.—Where any person furnishes information in the Application made under Section 7, which is false in material particulars, knowing it to be false or omits any material fact, knowing it to be material, such person shall be punishable with fine which shall not be less than one lakh rupees, but may extend to one crore rupees."*

56. *Rule 4(3) of the aforesaid Rules states as follows:*

> *"****4. Application by financial creditor****.—(1)-*
> *(2) * * **
> *(3) The applicant shall dispatch forthwith, a copy of the Application filed with the adjudicating*

authority, by registered post or speed post to the registered office of the corporate debtor."

Discussion and findings

31. We have heard argument of the Learned Counsel for the parties and perused the record. Based on the pleadings of the parties, the question that arises for our consideration is as under;

> **Whether the petition complying with all requirements of Section 7(5) of the Insolvency and Bankruptcy Code, 2016, but if it appears that the Application is filed collusively, not with the intention of Resolution of Insolvency, and so with malicious intent, or malafides, then whether the Application can be rejected relying on Section 65 of the Code?**

32. Undisputedly the petition filed under Section 7 of the Code meets all the requirements under the Insolvency and Bankruptcy Code, 2016. The Adjudicating Authority has also observed that "the Application is complete in all respects as required by law and the Application clearly showed that the Corporate Debtor is in default of a debt due and payable and that the default amount is more than the minimum threshold stipulated in Section 4 (1) of the Code".

33. Based on the above findings, the Learned Counsel for the Appellant submits that the Adjudicating Authority had no discretion except to admit the Application filed under Section 7 of the Code. It is emphasised that Section 7

(5) of the Code leaves no discretion to the Court where other ingredients of Section 7 are fulfilled. Section 7 (5) of the Code provides that "*where the Adjudicating Authority is satisfied that in default has occurred and the Application under Sub-section (2) is complete, and there is no disciplinary proceedings pending against the proposed Resolution Professional**, it may**, by order, admit such Application."*

34. The use of the phrase '**it may**' under Sub-section (5) of section 7 itself leaves the scope of discretion exercised by the Adjudicating Authority in admitting or rejecting the Application. Section 7 (5) (a) lays down parameters about general conditions to admit an Application. However, in the given situation where it appears that Application is filed collusively not with the purpose of Insolvency Resolution but otherwise, then despite fulfilling all the conditions of Section 7(5) of the Code, the Adjudicating Authority can exercise its discretion in rejecting the Application relying on Section 65 of the Code.

35. Hon'ble Supreme Court in Swiss ribbons (P) Ltd v Union of India, (2019) 4 SCC 17 held;

> ***Para 55.*** *****
> ***"A conjoint reading of all these Rules makes it clear that at the stage of the adjudicating authority's satisfaction under Section 7(5) of the Code, the corporate debtor is served with a copy of the Application filed with the adjudicating authority and has the opportunity to file a reply before the said authority and be heard by the said authority before an order is made admitting the said Application***.

59. What is also of relevance is that in order to protect the corporate debtor from being dragged into the corporate insolvency resolution process mala fide, the Code prescribes penalties. Thus, Section 65 of the Code reads as follows:

"65. Fraudulent or malicious initiation of proceedings.—

(1) ***If, any person initiates the insolvency resolution process or liquidation proceedings fraudulently or with malicious intent for any purpose other than for the resolution of Insolvency, or liquidation, as the case may be****, the adjudicating authority may impose upon such person a penalty which shall not be less than one lakh rupees, but may extend to one crore rupees.*

(2) ***If, any person initiates voluntary liquidation proceedings with the intent to defraud any person, the adjudicating authority may impose upon such person a penalty which shall not be less than one lakh rupees but may extend to one crore rupees."***

60. *Also, punishment is prescribed under Section 75 for furnishing false information in an application made by a financial creditor which further deters a financial creditor from wrongly invoking the provisions of Section 7. Section 75 reads as under:*

*"**75. Punishment for false information furnished in Application**.—Where any person furnishes information in the Application made under Section 7, which is false in material particulars, knowing it to be false or omits any material fact, knowing it to be material, such person shall be punishable with*

fine which shall not be less than one lakh rupees, but may extend to one crore rupees."

36. In the above mentioned case Hon'ble Supreme Court in Para 59 has very clearly observed that "***What is also of relevance is that in order to protect the Corporate Debtor from being dragged into the Corporate Insolvency Resolution Process mala fide, the Code prescribes penalties. Thus, Section 65 of the Code."***

37. Based on the law laid down by Hon'ble Supreme Court in the above-mentioned case, it is clear that even if the Application filed under Section 7 meets all the requirements, then also the Adjudicating Authority has exercise discretion carefully to prevent and protect the Corporate Debtor from being dragged into the Corporate Insolvency Resolution Process mala fide.

38. Therefore, the Code prescribes penalties under Section 65 and 75. Furthermore, Section 65 explicitly says that if any person initiates the insolvency resolution process or liquidation proceedings fraudulently or with malicious intent **for any purpose other than for resolution of Insolvency or liquidation, as the case may,** the Adjudicating Authority may impose a penalty.

39. Thus, it is clear that the Adjudicating Authority should be very cautious in admitting the Application so that Corporate Debtor cannot be dragged into Corporate Insolvency Resolution Process with mala fide for any purpose other than the resolution of the Insolvency. Therefore, to protect the Corporate

Debtor from the mala fide Initiation of CIRP, the law has provided a penalty under sections 65 and 75 of the Code. Before admitting the Application, every precaution is necessary to be exercised so that the insolvency process is not misused for any other purposes other than the resolution of Insolvency.

40. It is pertinent to mention that Hon'ble Supreme Court in Arcelor Mittal India Private Limited (supra) while interpreting the statutory provision of Section 29 A of the Insolvency and Bankruptcy Code 2016, has held that **the corporate veil may be lifted when a statute itself contemplates lifting the veil**, **or improper conduct is intended to be prevented**, or a taxing statute or beneficial statute is sought to be evaded or where associated companies are inextricably connected as to be, in reality, part of one concern.

41. The doctrine of "piercing the corporate veil" stands as an exception to the principle that the Company is a legal entity separate and distinct from a shareholder with its own legal rights and obligations. It seems to disregard the separate personality of Company and attribute the acts of the Company to those who are allegedly in direct control of its operation.

42. The concept of the corporate entity was evolved to encourage and promote trade and commerce but not to commit illegalities or to defraud people**. Where, therefore, the corporate character is employed for the purpose of committing illegality or for defrauding others, the Court would ignore the corporate character and will look at the reality behind**

the corporate veil so as to enable it to pass appropriate orders to do justice between the parties concerned.

43. The expression "acting jointly" in the opening sentence of Section 29-A cannot be confused with "joint venture agreements". All that is to be seen by the expression "acting jointly" is whether certain persons have got together and are acting "jointly" in the sense of acting together. If this is made out on the facts, no superadded element of "joint venture" as is understood in law is to be seen. The other important phrase is "in concert". Section 3 (37) of the Code, words and expressions used but not defined in the Code but defined, inter alia, by the SEBI Act, 1992, and the Companies Act 2013, shall have the meanings respectively assigned to them under those Acts.

44. Thus it is clear that Hon'ble Supreme Court in Arcelor Mittal India Private Limited (supra) while interpreting the statutory provision of Section 29 A of the Insolvency and Bankruptcy Code 2016, has recognised the principle of lifting the corporate veil in matters relating to Insolvency under the Code. Section 65 of the Insolvency and Bankruptcy Code, 2016 provides for punishment or fraudulent or malicious initiation of proceedings. It does not mean that Section 65 will not be applicable to prevent such fraudulent or malicious initiation of proceedings. When a statute makes a provision for punishment for any wrong, it also contains deemed power to prevent it. Therefore it cannot be said that section 65 will be applicable only after initiation of the Corporate Insolvency Resolution Process fraudulently or with malicious intent.

45. Based on the above discussion, we believe that even if the petition complies with all requirements of Section 7 of the Insolvency and Bankruptcy Code, 2016, it is filed collusively, not with the intention of Resolution of Insolvency but otherwise. Therefore, it is not mandatory to admit the Application to save the Corporate Debtor from being dragged into Corporate Insolvency Resolution Process with mala fide.

46. In the instant case, the Adjudicating Authority has observed that "*on perusal of the master debt of the Corporate Debtor it is seen that the Corporate Debtor has given a corporate guarantee of ₹ 482,42,00,000. On further enquiry and perusal of the financial statements for the Financial Year 2018-19 of the Corporate Debtor, it has come to light that the networth of the Corporate Debtor is ₹ 15,36,39,015. It is hard to convince oneself that the Company having a net worth of ₹ 15,36,39,015 is not able to make a payment of ₹ 3 lakhs. It appears that the petition at hand has been filed in collusion with the Corporate Debtor.*"

47. In its reply to the Appeal, the Corporate Debtor stated that by order dated 4th April 2021, necessary clarification/sought regarding the balance-sheet, while it is mentioned that the Company's net worth is ₹ 15,36,39,015 as per the financial statement of 2018 -19. The Corporate Debtor/Respondent contends that the Application was filed during the year 2019-20. Still, in the present situation when the order was passed, the Company's position is starkly deteriorated and is not able to pay back the loan amount.

48. The Corporate Debtor further admitted that it had made a substantial investment in M/s' Kohinoor Pulp and Paper Private Limited' and 'Kohinoor Paper and Newsprint Private Limited'. Kohinoor Pulp and Paper Private Limited are under liquidation, and Kohinoor Paper and Newsprint Private Limited is under this Corporate Insolvency Resolution Process wherein an Application has already been filed to initiate the liquidation process. Master data of the Corporate Debtor further reflects that the Corporate Debtor had extended the corporate guarantee of ₹ 482,42,00,000, and the Company's net worth is ₹ 15,36,39,015.

49. In the circumstances, the Adjudicating Authority decided that the petition is filed in collusion with the Corporate Debtor and thereby rejected the Petition filed U/S 7 of the Code. There is a plausible contention to form such an opinion of collusion with the Financial Creditor that a company with a net worth of ₹ 15,36,39,015 has already given a corporate guarantee worth ₹ 4,82,42,000,00 is unable to repay a loan of ₹ 3 lakhs only. The Corporate Debtor, in its reply, has not disputed that it has extended the corporate guarantee worth ₹ 482,42,00,000. Since the master data of the Corporate Debtor reflects that the Corporate Debtor is also a Corporate Guarantor and has extended the Corporate Guarantee of a considerable amount worth ₹482,42,00,000, therefore, such plausible contention cannot be ruled out that the Corporate Debtor colluded with the Financial Creditor to escape its liability as a corporate guarantor.

50. In the circumstances stated above, we believe that the Appeals sans merit and deserve to be dismissed.

ORDER

The Appeal is dismissed- no order as to costs.

[Justice A.I.S. Cheema]
The Officiating Chairperson

[V. P. Singh]
Member (Technical)

NEW DELHI
30TH JUNE, 2021

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