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GRC Bulletin

February 2022

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About

ricago is a dynamic next generation company focusing on Enterprise Governance, Risk Management and Compliance Management (GRC) solutions.

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CORPORATE LAWS

RBI'S MASTER CIRCULAR ON BANK FINANCE TO NBFCs DATED 05.01.2022

The Reserve Bank of India has been regulating the financial activities of the Non-Banking Financial Companies under the provisions of Chapter III B of the Reserve Bank of India Act, 1934.

Bank Finance to NBFCs Registered With RBI

The ceiling on bank credit linked to Net Owned Fund (NOF) of NBFCs has been withdrawn in respect of all NBFCs which are statutorily registered with RBI and are engaged in principal business of asset financing, loan, factoring and investment activities.

- Banks may extend need based working capital facilities as well as term loans to all NBFCs registered with RBI.
- Banks may also extend finance to NBFCs against second hand assets financed by them.
- Banks may formulate suitable loan policy with the approval of their Boards of Directors within the prudential guidelines and exposure norms prescribed by the Reserve Bank to extend various kinds of credit facilities to NBFCs subject to the condition that the activities indicated in paragraphs 4 and 6 are not financed by them.

For NBFCs not needing registration with the Reserve Bank, banks may take their credit decisions on the basis of usual factors like the purpose of credit, nature and quality of underlying assets, repayment capacity of borrowers as also risk perception, etc.

Activities Not Eligible For Bank Credit

The following activities undertaken by NBFCs, are not eligible for bank credit:

(i) Bills discounted / rediscounted by NBFCs, except for rediscounting of bills discounted by NBFCs arising from sale of -

(a) commercial vehicles (including light commercial vehicles), and

(b) two wheeler and three wheeler vehicles, subject to the following conditions:

- the bills should have been drawn by the manufacturer on dealers only;
- the bills should represent genuine sale transactions as may be ascertained from the chassis / engine number; and
- before rediscounting the bills, banks should satisfy themselves about the bona fides and track record of NBFCs which have discounted the bills.

CORPORATE LAWS

(ii) Investments of NBFCs both of current and long-term nature, in any company / entity by way of shares, debentures, etc. However, Stock Broking Companies may be provided need-based credit against shares and debentures held by them as stock-in-trade.

(iii) Unsecured loans / inter-corporate deposits by NBFCs to / in any company.

(iv) All types of loans and advances by NBFCs to their subsidiaries, group companies / entities.

(v) Finance to NBFCs for further lending to individuals for subscribing to Initial Public Offerings (IPOs) and for purchase of shares from secondary market.

Leased and Sub-Leased Assets

As banks can extend financial assistance to equipment leasing companies, they should not enter into lease agreements departmentally with such companies as well as other Non-Banking Financial Companies engaged in equipment leasing.

Bank Finance to Factoring Companies

Banks can extend financial assistance to support the factoring business of Factoring Companies, which comply with the following criteria:

- The companies qualify as factoring companies and carry out their business under the provisions of the Factoring Regulation Act, 2011 and Notifications issued by the Reserve Bank in this regard from time to time.
- They derive at least 50 per cent of their income from factoring activity.
- The receivables purchased / financed, irrespective of whether on 'with recourse' or 'without recourse' basis, form at least 50 per cent of the assets of the Factoring Company.
- The assets / income referred to above would not include the assets / income relating to any bill discounting facility extended by the Factoring Company.
- The financial assistance extended by the Factoring Companies is secured by hypothecation or assignment of receivables in their favour.

Other Prohibitions on Bank Finance To NBFCs

- Banks should not grant bridge loans of any nature, or interim finance against capital / debenture issues and / or in the form of loans of a bridging nature pending raising of long-term funds from the market by way of capital, deposits, etc. to all categories of Non-Banking Financial Companies.
- Shares and debentures cannot be accepted as collateral securities for secured loans granted to NBFC borrowers for any purpose.

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- Banks should not execute guarantees covering inter-company deposits / loans thereby guaranteeing refund of deposits / loans accepted by NBFCs / firms from other NBFCs / firms.

Prudential Ceilings For Exposure Of Banks To NBFCs

- Banks' exposures to a single NBFC (excluding gold loan companies) will be restricted to 20 percent of their eligible capital base (Tier I capital). However, based on the risk perception, more stringent exposure limits in respect of certain categories of NBFCs may be considered by banks.
- The exposure of a bank to a single NBFC which is predominantly engaged in lending against collateral of gold jewellery (i.e. such loans comprising 50 per cent or more of their financial assets), shall not exceed 7.5 per cent of the bank's capital funds (Tier I plus Tier II Capital).

Restrictions Regarding Investments Made By Banks In Securities / Instruments Issued By NBFCs

- Banks should not invest in Zero Coupon Bonds (ZCBs) issued by NBFCs unless the issuer NBFC builds up sinking fund for all accrued interest and keeps it invested in liquid investments / securities (Government bonds).
- Banks are permitted to also invest in Non-Convertible Debentures (NCDs) with original or initial maturity up to one year issued by NBFCs

#Source: Click here for more details

CORPORATE LAWS

SEBI ISSUED CIRCULAR ON ISSUANCE OF SECURITIES IN DEMATERIALIZED FORM IN CASE OF INVESTOR SERVICE REQUESTS

The SEBI has issued a circular dated 25th January, 2022 in exercise of powers conferred under section 11 (1) of SEBI Act 1992 to protect the interests of the investors and to regulate the securities market read with Regulation 101 of SEBI (LODR) Regulations, 2015.

As an ongoing measure to ease of dealing in securities markets by investors, it has been decided that listed companies shall hence forth issue the securities in dematerialized form only while processing the following service request:

i. Issue of duplicate securities certificate;
ii. Claim from Unclaimed Suspense Account;
iii. Renewal / Exchange of securities certificate;
iv. Endorsement;
v. Sub-division / Splitting of securities certificate;
vi. Consolidation of securities certificates/folios;
vii. Transmission;
viii. Transposition;

The securities holder/claimant shall submit duly filled up Form ISR-4 (to be hosted on the website of the Issuer Companies and the RTAs) as per the format attached to this circular along with the documents / details specified therein. For item nos. iii to viii in paragraph 1 above, the RTA / Issuer Companies shall obtain the original securities certificate(s) for processing of service requests.

The RTA / Issuer Companies shall verify and process the service requests and thereafter issue a 'Letter of confirmation' in lieu of physical securities certificate(s), to the securities holder/claimant within 30 days of its receipt of such request after removing objections, if any.

a. The 'Letter of Confirmation' shall be valid for a period of 120 days from the date of its issuance, within which the securities holder/claimant shall make a request to the Depository Participant for dematerializing the said securities.
b. The RTA / Issuer Companies shall issue a reminder after the end of 45 days and 90 days from the date of issuance of Letter of Confirmation, informing the securities holder/claimant to submit the demat request as above, in case no such request has been received by the RTA / Issuer Company.

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c. In case the securities holder/claimant fails to submit the demat request within the aforesaid period, RTA / Issuer Companies shall credit the securities to the Suspense Escrow Demat Account of the Company.
d. The operational guidelines are detailed in the Annexure – A to this circular.

The Stock Exchanges and Depositories are advised to make necessary amendments to the relevant bye-laws, rules and regulations, operational instructions, as the case may be, for the implementation of the above circular and bring the provisions of this circular to the notice of their constituents and also disseminate the same on the website.

The Circular shall come into force with immediate effect.

#Source: Click here for more details

TAX LAWS

CBDT EXTENDS DUE DATES FOR FILING OF INCOME TAX RETURNS AND VARIOUS REPORTS OF AUDIT FOR THE ASSESSMENT YEAR 2021-22

On consideration of difficulties reported by the taxpayers and other stakeholders due to COVID and in electronic filing of various reports of audit under the provisions of the Income-tax Act, 1961 (the Act), the Central Board of Direct Taxes (CBDT) has decided to further extend the due dates for filing of Income Tax Returns and various reports of audit for the Assessment Year 2021-22.

The further details are as under:

1. The due date of furnishing of Report of Audit under any provision of the Act for the Previous Year 2020-21, which was 30th September, 2021, in the case of assessees referred in clause (a) of Explanation 2 to sub-section (1) of section 139 of the Act, as extended to 31st October, 2021 and 15th January, 2022 by Circular No.9/2021 dated 20.05.2021 and Circular No.17/2021 dated 09.09.2021 respectively, is further extended to 15th February, 2022;
2. The due date of furnishing of Report of Audit under any provision of the Act for the Previous Year 2020-21, which was 31st October, 2021, in the case of assessees referred in clause (aa) of Explanation 2 to sub-section (1) of section 139 of the Act, is extended to 15th February, 2022;
3. The due date of furnishing of Report from an Accountant by persons entering into international transaction or specified domestic transaction under section 92E of the Act for the Previous Year 2020-21, which was 31st October 2021, as extended to 30th November, 2021 and 31st January, 2022 by Circular No.9/2021 dated 20.05.2021 and Circular No.17/2021 dated 09.09.2021 respectively, is further extended to 15th February, 2022;
4. The due date of furnishing of Return of Income for the Assessment Year 2021-22, which was 31st October, 2021 under sub-section (1) of section 139 of the Act, as extended to 30th November, 2021 and 15th February, 2022 by Circular No.9/2021 dated 20.05.2021 and Circular No.17/2021 dated 09.09.2021 respectively, is further extended to 15th March, 2022;
5. The due date of furnishing of Return of Income for the Assessment Year 2021-22, which was 30th November, 2021 under sub-section (1) of section 139 of the Act, as extended to 31st December, 2021 and 28th February, 2022 by Circular No.9/2021 dated 20.05.2021 and Circular No.17/2021 dated 09.09.2021 respectively, is further extended to 15th March, 2022.

It is also clarified that the extension of the dates as referred to in clauses (12) and (13) of Circular No.9/2021 dated 20.05.2021, clauses (4) and (5) of Circular No.17/2021 dated 09.09.2021 and in clauses (4) and (5) above shall not apply to

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Explanation 1 to section 234A of the Act, in cases where the amount of tax on the total income as reduced by the amount as specified in clauses (i) to (vi) of subsection (1) of that section exceeds rupees one lakh. Further, in case of an individual resident in India referred to in sub-section (2) of section 207 of the Act, the tax paid by him under section 140A of the Act within the due date (without extension under Circular No.9/2021 dated 20.05.202, Circular No. 17/2021 dated 09.09.2021 and as above) provided in that Act, shall be deemed to be the advance tax.

#Source: Click here for more details

TAX LAWS

CBDT NOTIFIES THE E-ADVANCE RULING SCHEME, 2022

The Central Government makes the following Scheme named as "e-advance ruling Scheme, 2022" with the powers conferred under the provisions of the Income Tax Act 1961.

This Scheme is applicable to applications of advance rulings where it is–

a. Made to the Board for Advance Rulings under sub-section (1) of section 245Q of the Act.
b. Transferred to Board for Advance Ruling under sub-section (4) of section 245Q of the Act.

E-advance rulings by board for Advance Rulings

- The Board for Advance Rulings shall pronounce e-advance rulings of applications allocated or transferred to it.
- The Board for Advance Rulings shall have such other income-tax Authority, ministerial staff, executive or consultant to assist the members of the Board for Advance Rulings.

Procedure for filing applications:

- an application, referred to in clause (a) of paragraph 3, shall be made, in Form Nos, 34C, 34D,34DA,34E,34EA mentioned in under Rule 44E of the Rules, by the applicant, to the Secretary or any other officer authorised in writing by the Secretary of Board for Advance Rulings, by electronic mail.
- if the applicant is not hitherto assessed in India, he shall indicate in Annexure I as provided in the relevant Forms to the application:
  (a) his head office in any country,
  (b) the place where his office and residence is located or is likely to be located in India, and
  (c) the name and address of his representatives in India, if any, authorised to receive notices and papers and act on his behalf.

Order of Advance Ruling: where an application for advance rulings has been allowed by an order, as referred to in sub-clause (vii) or item (a) of sub-clause (viii) or sub-clause (x) or sub-clause (xi) of clause B, the Board for Advance Rulings may send a notice to the applicant and the authority to whom the reference has been made, to submit such further material, information or evidence, as may be

TAX LAWS

relevant to the proceedings, within such time or extended time, as may be allowed by the Board for Advance Rulings.

Powers of the Board for Advance Rulings:

(1) The Board for Advance Rulings shall, for the purpose of exercising its powers, have all the powers of a civil court under the Code of Civil Procedure, 1908 (5 of 1908) as are referred to in section 131 of the Act.

(2) The Board for Advance Rulings shall be deemed to be a civil court for the purposes of section 195, but not for the purposes of Chapter XXVI of the Code of Criminal Procedure, 1973 (2 of 1974) and every proceeding before the Board for Advance Rulings shall be deemed to be a judicial proceeding within the meaning of sections 193 and 228, and for the purpose of section 196, of the Indian Penal Code (45 of 1860).

(3) If any difficulty arises in giving effect to any order of the Board for Advance Rulings, it may, on its own motion or on an application made by the applicant or the Principal Commissioner of Income-tax or the Commissioner of Income-tax, as the case may be, remove the difficulty in so far as it is not inconsistent with the provisions of the Act.

Powers and functions of the Secretary

The Secretary shall also have the following powers and duties, namely:

(i) to receive all applications filed before the Board for Advance Rulings.

(ii) to scrutinise the applications to find out whether they are in conformity with the Act, the rules and the procedure.

(iii) to point out defects in such application to the parties and require them to remove the defects by affording them a reasonable opportunity to do so and, where, within the time granted, the defects are not removed, to obtain necessary orders of the Board for Advance Rulings.

(iv) to fix the date of hearing for the applications in consultation with the members of the Board for Advance Rulings and direct the issue of notices therefore.

(v) to issue the service of notices or other processes and to ensure that the parties are properly served.

(vi) to requisition records from the custody of any person including a Commissioner of Income-tax or any other authority.

(vii) to allow inspection of records of the Board for Advance Rulings.

(viii) to direct any formal amendment of the records of the Board for Advance Rulings.

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(ix) to grant certified copies of the orders of the Board for Advance Rulings to the parties.

(x) to grant certified copies of documents filed in the proceedings to the parties in accordance with the rules.

(xi) to bring on record legal representatives, in case of death or retirement of any party to the proceedings and to make such appropriate amendments in the cause title as may become necessary in the other situations.

(xii) to discharge any other function as may be assigned by the Board for Advance Rulings by special or general order.

#Source: Click here for more details

OTHER LAWS

CENTRAL KYC RECORDS REGISTRY ON CYBER SECURITY ADVISORY – PRECAUTIONARY MEASURES

Due to the outbreak of COVID-19, many employees are currently working from home. This has resulted in an increased dependency on digital communications manifold and many operations may be under remote monitoring mode. This is the time when cyber-attacks generally peak as the attackers try to utilize the paranoia around such pandemics and hence, we request all of you to be very wary and careful. The most common scams and possible attacks are as follows:

Social Engineering Attacks - You may receive bogus emails that appear to be from legitimate sources containing malicious links. These links, if clicked may lead to your devices being infected with malware.

Ransomware Attacks – Applications from unknown sources that claim to provide a much-needed utility. Once installed, the app asks for various permissions which it claims are needed to be able to deliver notifications and then installs ransomware due to which you cannot access your phone as it forces a change in the phone's lock screen password.

Phishing Attacks - Phishing emails which claim to be from legitimate sources and generally contain a malicious link. Once clicked, it requests the victim for their financial and tax information, bank details and PII.

Protection Measures

1. Do not click on links or download attachments from unknown sources.
2. Always verify the security of a website – Check the site has been secured using HTTPS /Check for a website privacy policy / Use a website safety check tool such as Google Safe Browsing / Do a WHOIS lookup to see who owns the website.
3. Pay close attention to the spelling of an email or web address, if there are any inconsistencies, delete immediately.
4. Ignore and delete emails with poor grammar and formatting.
5. Question the validity of any email that asks you to submit personal or financial information.
6. Do not download apps from untrusted and unfamiliar sites.
7. Pay close attention to the permissions requested by an app and think twice before you grant access to sensitive information such as your address book or access to your photo library.
8. Use a Secure Wi-Fi connection while connecting to office environment. Avoid the use of public Wi-Fi. With an insecure connection, people in the

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near vicinity can snoop your traffic. Place the Router in the Center of Your Home. Change default passwords on you home Wi-Fi router.

9. Use strong passwords/passphrases to login to your personal desktops/laptops.
10. Ensure your laptops/systems are updated with latest anti-virus versions and patches.
11. Remember to back up all important files regularly. Disk encryption is an option available in most operating systems. In many cases it is optional that can be enabled as and when required.
12. Don't click on COVID-19 related messages with attachments. Don't forward them to family or friends.
13. Be wary of websites that start "Coronavirus" or "Covid." E.g. Do not install or click on apps like "coronavirusapp.site." which supposedly tracks virus outbreaks. Downloading such applications will infect your systems/phones with ransomware.
14. Seek legitimate information from authentic government, university, hospital and news sites with names you know.
15. Think carefully about letting family and friends use a computer that's also now used for work.

#Source: Click here for more details

JUDICIAL INSIGHT

WRIT JURISDICTION OF HIGH COURT CANNOT BE INVOKED WHEN THERE IS AN ALTERNATE REMEDY AVAILABLE UNDER SARFAESI ACT

FACTS OF THE CASE

The respondent, Vishwa Bharati Vidya Mandir and St. Ann's Education Society are running educational institutions and is a Society which had availed credit facilities to the tune of Rs.105,60,84,000/- (Rupees One Hundred Five Crores Sixty Lacs and Eighty-Four Thousand Only) and Rs.20,05,00,000/- (Rupees Twenty Crores and Five Lacs Only) from Saraswat Co-operative Bank Limited. The respondents also created an equitable mortgage by way of deposit of title deeds over the immovable properties with respect to the mortgaged properties. The respondents then committed defaults in repayment of the outstanding dues, in the month of April, 2013 and was classified as a "Nonperforming Asset" (NPA) by the Bank. The Bank issued a notice dated 01.06.2013 under Section 13(2) of the Securitization and Reconstruction of Financial Assets and Enforcement of Securities Interest Act, 2002 (hereinafter referred to as "SARFAESI Act"). In the month of March, 2014, the NPA account of the respondents with respect to the credit facilities availed by them was assigned by the Bank in favour of the appellant – Phoenix ARC Private Limited vide registered Assignment Agreement dated 28.03.2014.

Pursuant to the assignment of the NPA account in favour of the appellant, the borrowers approached the appellant with a request for restructuring the repayment of outstanding dues. However, the borrowers failed to repay the dues as per the Letter of Acceptance. Since the borrowers again committed defaults in payment of the outstanding dues, the appellant – Phoenix ARC Private Limited issued a letter dated 13.08.2015 intimating the borrowers that since despite issuance of 13(2) notice dated 01.06.2013 and the subsequent execution of the Letter of Acceptance dated 27.02.2015, the borrowers had failed to repay the outstanding dues, therefore, the appellant would be proceeding to take possession of the mortgaged properties after expiry of 15 days from the date of the said letter. Against the aforesaid communication/letter dated 13.08.2015, the respondents herein filed the writ petitions before the High Court on the ground that the communication/letter dated 13.08.2015 is a possession notice under Section 13(4) of the SARFAESI Act, which is against the Security Interest (Enforcement) Rules, 2002. The High Court passed an ex-parte ad-interim order dated 26.08.2015 directing status quo to be maintained with regard to possession of the mortgaged properties subject to the borrowers making a payment of Rs. 1 crore with the appellant – Phoenix. The petition was opposed by the appellant by

filing statement of objections to the writ petitions contending, inter alia, that the letter dated 13.08.2015 as such cannot be said to be taking a measure under Section 13(4) of the SARFAESI Act and that it was only a proposed action/measure to be taken by the appellant. It was also submitted that the writ petitions are not maintainable.

SUBMISSIONS BY THE APPELLANT

Shri V. Giri, learned Senior Advocate appearing on behalf of the appellant(s) has vehemently submitted that in the present case the borrowers are liable to pay to the appellant – ARC / secured creditor an amount of Rs.117,31,68,487/-. Despite the Letter of Acceptance dated 27.02.2015 admitting the dues and agreeing to make the payment due and payable, the borrowers failed to repay the amount due and payable, the appellant proposed to proceed further with the proceedings under the SARFAESI Act and therefore vide communication dated 13.08.2015, the borrowers were called upon to make the payment within 15 days failing which it was proposed to take further steps under the provisions of the SARFAESI Act. At that stage communication dated 13.08.2015 cannot be said to be notice under Section 13(4) of the SARFAESI Act. Despite the above and treating and/or considering the communication dated 13.08.2015 as possession notice under Section 13(4) of the SARFAESI Act, the borrowers filed the writ petitions before the High Court against communication dated 13.08.2015. It is submitted that unfortunately the High Court has entertained the aforesaid writ petitions though not maintainable against a private party like the appellant – ARC and has granted an ex-parte ad- interim order, which has been extended from time to time directing to maintain status quo with respect to the possession of the mortgaged properties on payment of meager amount of Rs. 1 crore (in all Rs. 3 crores only) against the total dues of Rs.117 crores approximately.

SUBMISSIONS BY THE RESPONDENT

Shri Basavaprabhu S. Patil, learned Senior Advocate appearing on behalf of the original borrowers has vehemently submitted that the present appeals are against the ad interim order/interim order passed by the High Court and the main writ petitions are pending before the High Court. It is submitted that pursuant to the earlier order passed by this Court dated 06.08.2018, the impugned interim order passed by the High Court has been stayed. It is therefore submitted that when the main writ petitions are pending before the High Court, the present appeals may not be further entertained. It is submitted that despite the fact that there is a stay of operation of the impugned order passed by the High Court since 06.08.2018, thereafter no further steps have been taken by the appellant against the borrowers under the provisions of the SARFAESI Act. Now, so far as the maintainability of the writ petition against the Assets Reconstruction Company

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(ARC) is concerned, it is submitted that the writ petition is filed against the ARC complaining of infraction of Rule. It is submitted that the said rule imposes a statutory duty on the secured creditor - the ARC to act fairly while dealing with the security so as to secure the interest of the borrower as well as public at large (depositors).

HELD

The Supreme Court held that while considering the issue regarding the maintainability of the writ petitions by the High Court in the instant case, the Court is conscious that the powers conferred upon the High Court under Article 226 of the Constitution to issue to any person or authority, including in appropriate cases, any Government, directions, orders or writs including the five prerogative writs for the enforcement of any of the rights conferred by Part III or for any other purpose are very wide and there is no express limitation on exercise of that power but, at the same time, we cannot be oblivious of the rules of self-imposed restraint evolved by this Court, which every High Court is bound to keep in view while exercising power under Article 226 of the Constitution. It is true that the rule of exhaustion of alternative remedy is a rule of discretion and not one of compulsion, but it is difficult to fathom any reason why the High Court should entertain a petition filed under Article 226 of the Constitution and pass interim order ignoring the fact that the petitioner can avail effective alternative remedy by filing application, appeal, revision, etc. and the particular legislation contains a detailed mechanism for redressal of his grievance. It must be remembered that stay of an action initiated by the State or its agencies/instrumentalities for recovery of taxes, cess, fees, etc. seriously impedes execution of projects of public importance and disables them from discharging their constitutional and legal obligations towards the citizens. In cases relating to recovery of the dues of banks, financial institutions and secured creditors, stay granted by the High Court would have serious adverse impact on the financial health of such bodies/institutions, which (sic will) ultimately prove detrimental to the economy of the nation. Therefore, the High Court should be extremely careful and circumspect in exercising its discretion to grant stay in such matters.

Assuming that the communication dated 13.08.2015 can be said to be a notice under Section 13(4) of the SARFAESI Act, in that case also, in view of the statutory remedy available under Section 17 of the SARFAESI Act and in view of the law laid down by this Court in the cases referred to hereinabove, the writ petitions against the notice under Section 13(4) of the SARFAESI Act was not required to be entertained by the High Court. Therefore, the High Court has erred in entertaining the writ petitions against the communication dated 13.08.2015 and also passing the ex-parte ad-interim orders directing to maintain the status quo with respect

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to possession of secured properties on the condition directing the borrowers to pay Rs. 1 crore only (in all Rs.3 crores in view of the subsequent orders passed by the High Court extending the ex- parte ad-interim order dated 26.08.2015) against the total dues of approximate Rs.117 crores. Even the High Court ought to have considered and disposed of the application for vacating the ex-parte ad- interim relief, which was filed in the year 2016 at the earliest considering the fact that a large sum of Rs.117 crores was involved.

In view of the above and for the reasons stated above, present appeals succeed. The Writ Petition Nos. 35564 to 35566 of 2015 before the High Court are dismissed.

#Source:** Phoenix Arc Private Limited **v. Vishwa Bharati Vidya Mandir [Civ. Appl. No. 257 - 259 of 2022] dated 12th January 2022

JUDICIAL INSIGHT

WHEN A COMPANY IS UNABLE TO PAY ITS DEBTS U/S 434 OF THE COMPANIES ACT 1956, IT IS SUBJECTED TO WINDING UP U/S 433(E)

Facts of the Case

The respondent which is a private Sector Airline had availed of the services of a Company named SR Technics, Switzerland, for maintenance, repair and overhauling of Air Craft Engines, modules, components, assemblies and parts which are mandatory for its operations. An agreement for performance of such services for a period of 10 years was entered into between the respondent and S.R. Technics on 24.11.2011. The terms of payments were also agreed. On 24.08.2012 a supplemental agreement was entered into to change certain terms of the agreement. The amendments included extension of time for payment of monies due under various invoices raised by SR Technics and also a deferred payment scheme. Since there was a general increase in the cost, the supplemental agreement dated 24.08.2012 included adjustment of flight hour rates and provisions for escalation were also made.

Upon provision of the services under the agreement, SR Technics had raised invoices and the respondent had issued seven bills of exchange for the monies due under the invoices. The respondent also acknowledges the debts from time to time by issuing certificate of acceptance in relation to the bills of exchange which would imply that the respondent had not disputed the correctness of the claim made in the invoices. Credit Suisse AG, entered into a financing agreement on 26.09.2012 with SR Technics and under a transaction agreement dated 26.09.2012, SR Technics assigned all its present and future rights to receive payments under the agreement to the petitioner. The assignment included the Bills of exchange issued by the respondent pursuant to the agreement dated 24.11.2011 and the supplementary agreement dated 24.08.2012. In view of the assignments made by SR Technics, the petitioner is entitled to receive payments of the monies due under the seven Invoices from the respondent.

Submission by the Petitioner

Mr. Rahul Balaji, learned counsel appearing for the petitioner would vehemently contend that Section 433(e) of the Companies Act 1956, provides for winding up of a Company, if it is found that the Company is unable to pay its debts. Relying upon Section 434, the learned counsel would contend that once a notice under Section 434(1)(a) of the Companies Act 1956, had been issued and the Company fails to pay the debt demanded under said notice within the three weeks' period

or to secure or compound for it to the reasonable satisfaction of the creditor, a company is deemed to be unable to pay its debts. In view of the presumption of inability to pay created under Section 434 of the Companies Act, an order for winding up should automatically follow, unless the debtor Company is able to show that the debt itself is unenforceable or that there is a bona fide dispute. In the absence of any dispute regarding the fact that the Debtor Company had availed the services of the SR Technics, it is not open to the respondent to contend that the debts are unenforceable or that the enforcement of the debt would be against the public policy. Despite knowledge of the fact that SR Technics, had not obtained a license from the DGCA, the Debtor Company had availed of the engine maintenance services by SR Technics. Therefore, it is not open to the respondent to contend that the enforcement of the debt will be opposed to public policy.

Submissions by the Respondent

Mr. V. Ramakrishnan, learned Senior Counsel appearing for the respondent would submit that a mere existence of a debt and its non-payment would not attract an order of winding up under Section 433 of the Companies Act 2013. He would submit that it is open to the respondent resisting a winding up petition to show that there is a bona fide dispute regarding the debt, enforcement of such debt would be against the public policy in India, the documents relied upon in support of the debt or the documents relied upon to prove the debt are not properly stamped in accordance with the law relating to stamping in India and if the Court finds that the debt is not legally enforceable or the enforcement of the debt would be against the law in India, the Company Court shall reject an application seeking winding up.

Held

The Court while examining the question, as to whether, a winding up proceeding is to be admitted or not must, upon the existence of a debt being proved, consider whether:

i. The defence of the Company is in good faith and one of substance.
ii. The defence is likely to succeed on point of law.
iii. The company adduces prima facie proof of the facts on which the defence depends.

Therefore, even after the Court comes to the conclusion that there is a debt existing, the Company Court sitting in winding up proceedings need not automatically issue an order for winding up. It is well open to the Company Court to see or to examine by applying the three pronged test suggested by the Hon'ble Supreme Court, as to whether, the defence of the Company is in good faith and is

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one of substance, the defence is likely to succeed on a point of law and the company adduces prima facie proof of the facts on which the defence depends.

The three pronged test suggested by the Hon'ble Supreme Court which I have already extracted would show that the Company Court need not render a conclusive finding on the enforceability of the debt, while examining the issuance of notice of winding up or while examining the admission of a winding up petition. The question whether the documents require stamping or the question whether the bills of exchange are payable on demand or otherwise than on demand or questions which, as rightly pointed out by Mr. Rahul Balaji, learned counsel appearing for the petitioner, will have to be examined at the time when the actual enforcement or examination of the claim of the petitioner by the Official Liquidator takes place. I must point out, even ignoring the agreements and the bills of exchange, the certificates of acceptance that had been issued by the respondent would show that there is a categorical admission of liability.

I thus find that the respondent Company has miserably failed to satisfy the three pronged test suggested by the Hon'ble Supreme Court in Mathusudan Gordhandas & Co. v. Madhu Woollen Industries (P) Ltd., supra, and hence had rendered itself liable to be wound up for its inability to pay its debts under Section 433 (e) of the Companies Act 1956. I am therefore of the opinion that this Company Petition should be allowed and the respondent Company directed to be wound up. The Official Liquidator is directed to take over the assets of the respondent Company.

#Source: Credit Suisse AG vs Spice Jet Limited, [2021] 229 Comp Cas 758 (Mad), High Court of Madras, on 6th December 2021.

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