

**Insolvency and Bankruptcy Board of India**  
**7<sup>th</sup> Floor, Mayur Bhawan, Connaught Place, New Delhi - 110001**

14<sup>th</sup> July, 2022

***Subject: Judgment<sup>1</sup> dated 12<sup>th</sup> July, 2022 of the Hon'ble SC in the matter Vidarbha Industries Power Limited Vs. Axis Bank Limited [Civil appeal No. 4633 of 2021].***

The Hon'ble Supreme Court vide its order dated 12<sup>th</sup> July, 2022 held that section 7(5)(a) of Insolvency and Bankruptcy Code, 2016 (the Code), confers discretionary power on the Adjudicating Authority (AA) to admit an application of a Financial Creditor (FC) under section 7 of the Code for initiation of Corporate Insolvency Resolution Process (CIRP). The Hon'ble SC made some important findings and observations as under:

<b>Sl. No.</b>	<b>Subject / Issue</b>	<b>Ruling</b>	<b>Para / Page No.</b>
1	Objectives of the Code	(a) The framework that had existed prior to the Code, for insolvency and bankruptcy was inadequate, ineffective and resulted in undue delay.  (b) The new Insolvency and Bankruptcy framework has been designed, inter alia, to facilitate the assessment of viability of an enterprise at a very early stage, and to ensure a time bound Insolvency Resolution Process to preserve the economic value of the enterprise.	47/16  49/19
2	Whether section 7(5)(a) is a mandatory or a discretionary provision?	(a) AA is required to ascertain the existence of a default from the records of the information utility or any other evidence furnished by the FC under section 7(3) of the Code, within 14 days of the date of receipt of the application.  (b) Both, the AA and the NCLAT proceeded on the premises that an application must necessarily be entertained under section 7(5)(a) of the Code if a debt existed and the CD was in default of payment of debt. AA found section 7(5) (a) of the Code to be mandatory.  (c) There can be no doubt that a CD who is in the red should be resolved expeditiously, following the timelines in the Code. No extraneous matter should come in the way. However, the	54/20  56/21  59/22

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		<p>viability and overall financial health of the CD are not extraneous matters.</p> <p>(d) The NCLAT erred in holding that the AA was only required to see whether there had been a debt and the CD had defaulted in making repayment of the debt, and that these two aspects, if satisfied, would trigger the CIRP. The existence of a financial debt and default in payment thereof only gave the financial creditor the right to apply for initiation of CIRP.</p> <p>(e) Legislature has, in its wisdom, chosen to use the expression “<i>may</i>” in section 7(5)(a) of the Code. When AA is satisfied that a default has occurred and the application of a FC is complete and there are no disciplinary proceedings against proposed IRP, it may by order admit the application.</p> <p>(f) Ordinarily the word “<i>may</i>” is directory. The expression ‘<i>may admit</i>’ confers discretion to admit. The use of the word “<i>shall</i>” postulates a mandatory requirement. The use of the word “<i>shall</i>” raises a presumption that a provision is imperative. However, it is well settled that the <i>prima facie</i> presumption about the provision being imperative may be rebutted by other considerations such as the scope of the enactment and the consequences flowing from the construction.</p> <p>(g) Had it been the legislative intent that section 7(5)(a) of the Code should be a mandatory provision, Legislature would have used the word ‘<i>shall</i>’ and not the word ‘<i>may</i>’. There is no ambiguity in section 7(5)(a).</p>	<p>61/23</p> <p>62/23</p> <p>64/24</p> <p>69/25</p>
3	Distinction between section 7(5) & section 9(5) of the Code	<p>(a) Section 9 prescribes the mode and manner by which an Operational Creditor (OC) can make an application for initiation of CIRP. After expiry of ten days from the date of delivery of the notice or invoice demanding payment, if the OC does not receive payment from the CD or notice of dispute, the OC may file an application before the AA for initiation of CIRP.</p> <p>(b) Section 9(5) provides that the AA shall, within 14 days of the receipt of an application of an OC under section 9(2), admit the application and communicate the decision to the OC and the CD, provided, the conditions stipulated in section 9(5)(i) (a) to (e) are satisfied. AA must reject the application in the circumstances specified in section 9(5)(ii) (a) to (e).</p> <p>(c) Legislature has in its wisdom used the word ‘<i>may</i>’ in section 7(5)(a) of the Code in respect of an application for CIRP initiated by a FC against a CD but has used the expression ‘<i>shall</i>’ in the otherwise almost identical provision of section 9(5) of the Code relating to the initiation of CIRP by an OC.</p>	<p>72/26</p> <p>74/28</p> <p>75/28</p>

	<p>(d) Legislature intended section 9(5)(a) to be mandatory and section 7(5)(a) of the Code to be discretionary. An application of an OC for initiation of CIRP under section 9(2) of the Code is mandatorily required to be admitted if the application is complete in all respects and in compliance of the requisites of the Code.</p>	76/28
	<p>(e) On the other hand, in the case of an application by a FC who might even initiate proceedings in a representative capacity on behalf of all FCs, the AA might examine the expedience of initiation of CIRP, taking into account all relevant facts and circumstances, including the overall financial health and viability of the CD. The AA may in its discretion not admit the application of a FC.</p>	77/29
	<p>(f) The Legislature has consciously differentiated between FCs and OCs, as there is an innate difference between FCs, in the business of investment and financing, and OCs in the business of supply of goods and services. The impact of the non-payment of admitted dues could be far more serious on an OC than on a FC.</p>	78/29
	<p>(g) The financial strength and nature of business of FCs and OCs being different, as also the tenor and terms of agreements/contracts with FCs and OCs, the provisions in the Code relating to commencement of CIRP at the behest of an OC, whose dues are undisputed, are rigid and inflexible.</p>	79/30
	<p>(h) AA has been conferred the discretion to admit the application of the FC. If facts and circumstances so warrant, the AA can keep the admission in abeyance or even reject the application.</p>	79/30
	<p>(i) It is certainly not the object of the Code to penalize solvent companies, temporarily defaulting in repayment of its financial debts, by initiation of CIRP.</p>	81/31
	<p>(j) Section 7(5)(a) of the IBC, therefore, confers discretionary power on the AA to admit an application of a FC under section 7 of the Code for initiation of CIRP.</p>	81/31
	<p>(k) AA failed to appreciate that the question of time bound initiation and completion of CIRP could only arise if the companies were bankrupt or insolvent and not otherwise. The timeline starts ticking only from the date of admission of the application for initiation of CIRP and not from the date of filing the same.</p>	82/31
	<p>(l) The judgment of the SC in the matter of <i>Swiss Ribbons Private Limited and Anr. v. Union of</i></p>	84/32

		<p><i>India and Ors</i>, which was rendered in the context of a challenge to the vires of the Code, does not consider the question of whether section 7(5)(a) of the Code is mandatory or discretionary. It is well settled that a judgment is a precedent for the question of law that is raised and decided. The language used in a judgment cannot be read like a statute. In any case, words and phrases in the judgment cannot be construed in a truncated manner out of context.</p> <p>(m) Legislature has, in its wisdom made a distinction between the date of filing an application under Section 7 of the Code and, the date of admission of such application for the purpose of computation of timelines.</p> <p>(n) CIRP commences on the date of admission of the application for initiation of CIRP and not the date of filing thereof. There is no fixed time limit within which an application under Section 7 of the IBC has to be admitted.</p>	85/32
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4	Conclusion	<p>(a) Even though section 7 (5)(a) may confer discretionary power on the AA, such discretionary power cannot be exercised arbitrarily or capriciously.</p> <p>(b) AA would have to exercise its discretion to admit an application under section 7 and initiate CIRP on satisfaction of the existence of a financial debt and default on the part of the CD in payment of the debt, unless there are good reasons not to admit the petition.</p> <p>(c) AA has to consider the grounds made out by the CD against admission, on its own merits. For example, when admission is opposed on the ground of existence of an award or a decree in favour of the CD, and the Awarded/decree amount exceeds the amount of the debt, the AA would have to exercise its discretion under section 7(5)(a) to keep the admission of the application of the FC in abeyance, unless there is good reason not to do so. The AA may, for example, admit the application of the FC, notwithstanding any award or decree, if the Award/Decree amount is incapable of realisation. The example is only illustrative.</p> <p>(d) AA and the NCLAT fell in error in holding that once it was found that a debt existed, and a CD was in default in payment of the debt there would be no option to the AA but to admit the petition under section 7.</p> <p>(e) The appeal was allowed.</p>	86/32
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