NATIONAL COMPANY LAW APPELLATE TRIBUNAL
PRINCIPAL BENCH, NEW DELHI

Company Appeal (AT) (Insolvency) No. 1427 of 2023

[Arising out of the Impugned Order dated 11.10.2023 passed by the Adjudicating Authority, National Company Law Tribunal, Kolkata Bench in C.P.(IB) No. 323/KB/2021 and I.A. No. 778/KB/2022 in C.P.(IB) No. 323/KB/2021]

In the matter of:

Adhunik Corporation Limited,
Registered office at:
14, Netaji Subhas Road,
2nd Floor, Kolkata,
West Bengal- 700001

...Appellant

Versus

Shivam India Limited,
Registered Office at:
Govind Mahal, 2nd Floor,
Wood Street, Flat No.1,
Kolkata- 700016

...Respondent

Present:

For Appellant : Mr. Ramji Srinivasan, Sr. Advocate with Mr. Anup Kumar, Ms. Pragya Choudhary, Ms. Neha Jaiswal, Ms. Nisha Adhikari, Mr. Arjun Bhatia and Ms. Shefali Munde, Advocates.

For Respondent : Mr. Rishav Banerjee, Advocate.

J U D G M E N T
(Hybrid Mode)

Per: Barun Mitra, Member (Technical)

The present appeal filed under Section 61 of Insolvency and Bankruptcy Code 2016 ('**IBC**' in short) by the Appellant arises out of the Order dated 11.10.2023 (hereinafter referred to as '**Impugned Order**') passed by the

Adjudicating Authority (National Company Law Tribunal, Kolkata Bench) in C.P.(IB) No. 323/KB/2021 and I.A. No. 778/KB/2022 in C.P.(IB) No. 323/KB/2021. By the impugned order, the Adjudicating Authority has dismissed the Section 7 application filed by the Appellant seeking initiation of Corporate Insolvency Resolution Proceedings (**'CIRP'** in short) of the Respondent-Corporate Debtor. Aggrieved by the impugned order, the present appeal has been preferred by the Appellant.

2. Coming to the brief facts of the case, the Appellant-Adhunik Corporation Limited was approached by Shivam India Limited-Respondent for financial assistance towards operationalization of their factory which had been shut down for financial constraints and want of working capital. The Appellant and the Respondent entered into an agreement dated 18.05.2015 by which the Appellant through one of its sister concerns-Adhunik Industries Limited provided financial assistance. Later a fresh Memorandum of Agreement (**'MoA'** in short) was executed on 23.06.2020 for a further period of five years which was entered into between Adhunik Corporation Limited, Shivam India Limited and promoters of Shivam India Limited. In terms of the MoA, the Appellant provided a sum of Rs. 27.85 crore to the Respondent out of which Rs.23.49 crore was direct financial assistance and another sum of Rs.4.36 crore was towards raw material. The financial assistance was also secured by depositing 69.42% equity shares of the Respondent with Trans Scan Securities Pvt. Ltd., a depository participant on behalf of the Appellant. The Appellant in return of the financial assistance was to also receive sales commission. However, since the Appellant did not receive back the financial assistance given to the Respondent and there was an

outstanding amount due in respect of sales commission due from the Respondent, the financial creditor issued a notice dated 11.10.2021 to the Corporate Debtor demanding the return of an amount of Rs. 27.85 crore along with interest @18% per annum effective from 01.03.2021. Subsequently, on 30.10.2021, the Appellant filed Section 7 application and the total amount claimed to be in default in the Section 7 application was Rs.42,47,32,067/- (as on 30.09.2021) with the date of default shown as 11.10.2021. In the interim, the Respondent had given a notice under Section 21 of the Arbitration and Conciliation Act, 1996 on 09.12.2021 and subsequently filed an arbitration petition No. 360 of 2022 under Section 11 of the Arbitration and Conciliation Act, 1996 before the Hon'ble High Court of Calcutta on 20.05.2022. The Respondent also filed a Reply to the Section 7 application on 04.06.2022. The Section 7 application was dismissed by the Adjudicating Authority on 11.10.2023 by holding that the purported debt claimed by the Appellant was not a financial debt and that the Appellant was not a financial creditor. Aggrieved by the impugned order, the Appellant has come up in appeal.

3. Making his submissions, the Ld. Senior Counsel for the Appellant, Shri Ramji Srinivasan submitted that the Adjudicating Authority had erroneously failed to appreciate that the credit facility provided by the Appellant to the Respondent was in the nature of a financial debt falling within the meaning of Section 5(8) of the IBC. The MoA executed between the parties had clearly provided for infusion of funds by the Appellant to the Respondent which amount was fully refundable and in pursuance of the MoA, a direct fund transfer/infusion of Rs.23.49 crore had been made by the Appellant to the

account of the Respondent which is corroborated by the statement of account of the two parties. It was also contended that the Appellant having provided financial assistance/credit to the Respondent which was required to be repaid by the Respondent and this outstanding financial debt was not paid back and which sum was beyond the threshold limit of Rs.1 crore stipulated by the Section 4 of the IBC, this was a fit case for attracting Section 7. Further since the MoA provided for collection of sales commission from the sale of finished products, there was a clear element of commercial effect of borrowing which constituted time value for money. Hence in the present case, the basic ingredients of financial debt of disbursal of money against consideration of time value of money stood met. The Appellant clearly fell in the category of Financial Creditor under Section 5(7) of IBC and therefore been wrongly non-suited by the Adjudicating Authority. Assailing the impugned order, it was submitted that the Adjudicating Authority had wrongly held that the financial assistance advanced to the Respondent was in the nature of business arrangement and not a financial debt.

4. Submission was also pressed that the time value of money covers any other form of benefit/value accruing in return of providing financial assistance. In support of their contention, it was asserted that the Hon'ble Supreme Court has clearly held that provision of credit facility without charging of any interest can be considered to be a financial debt in ***Orator Marketing Pvt. Ltd. Versus Samtex Desinz Pvt. Ltd. 2021 SCC Online SC 513.*** Similarly, this Tribunal in the matter of ***Sanjay D. Kakade Vs. HDFC Ventures Trustee Co. Ltd. in CA (AT)(Ins) No. 481/2023*** has also held that interest free loans advanced to finance the business operations of a corporate body can as well be construed to be

treated as financial debt. Thus, even if the credit advanced was not interest bearing, it does not deprive the transaction to be treated as financial debt. Hence the rival contention that since no interest was purportedly chargeable on the funds infused by the Appellant, the amount in question did not have the character of financial debt was a misplaced contention. It was also vehemently contended that merely because the Respondent had invoked clause 21 of the MoA on 23.09.2021 for resolution of their *interse* disputes and invoked the provisions contained in Section 11 of the Arbitration and Conciliation Act, 1996 it cannot become a ground for rejection for Section 7 application. It was also contended that reference to arbitration is immaterial in a Section 7 proceeding.

5. Refuting the contentions made by the Appellant, Shri Rishav Banerjee, Ld. Counsel for the Respondent-Corporate Debtor submitted that in terms of the MoA, it was the responsibility of the Appellant to infuse funds, bring in raw material and convert the same into finished products and sell the same to recover the costs. The Appellant was required to supply raw material at the prevailing market price as per production schedule mutually agreed between the Appellant and the Respondent. Furthermore, the removal and disposal by way of sale of the finished products under the MoA was also the obligation of the Appellant. Therefore, the Appellant was in fact in control of the said unit and the Respondent was to only get any surplus out of the sales proceeds of the finished product after meeting all costs provided and infused by the Appellant. Moreover, to keep control over the funds infused and to monitor the realisation and utilisation of funds, the Appellant had also prevailed upon the Respondent to allow operation of the bank account exclusively by them. Thus, the Appellant

had control both over the finances of the Respondent-Corporate Debtor and also the sale of finished products as well as for recovery of the funds infused from the sale proceeds of the finished goods. It was also emphatically asserted that the MoA nowhere depicts the fund infusion by the Appellant to be a loan. Moreover, the Appellant had been collecting sales commission on sale proceeds in return for the sum infused. Hence the sum infused was not in the nature of financial debt. It was therefore contended that it was purely a business arrangement between the Appellant and the Respondent and the funds infused was not in the form of a debt or loan since the Appellant was entitled to recover the same from the sale proceeds of the finished goods. The infusion of funds was therefore not in the nature of financial debts. The MoA therefore could not be termed as a loan agreement. There was no consideration of time value for money. Since the proceedings under IBC are not supposed to be recovery proceedings, Section 7 could not have been initiated in the absence of debt. Reliance was placed on the judgment of this Tribunal in ***Mukesh N. Desai Vs. Piyush Patel in CA (AT)(Ins) No.780 of 2020*** to assert that a Section 7 application is not maintainable when the MoU entered between parties contains reciprocal rights and obligation in which the parties are involved profit sharing. In the present case too, the Appellant was the owner of the finished products as per terms of the MoA, hence, the investment was not a financial debt.

6. Submission was made that the alleged dues claimed by the Appellant was barred by Section 10A of the IBC. The alleged demand of the Appellant was w.e.f. 01.03.2021 which period clearly fell during the Section 10A period. The Appellant has shown date of default as 11.10.2021 to merely overcome the

Section 10A hurdle. It was also contended that the Appellant had realised more money through sale of goods and commission than the aggregate funds infused by them. Section 7 of the IBC necessitates that evidence of default has to be furnished which the Appellant has failed to provide. Since there was no proof of default, the Appellant did not enjoy the locus to file the Section 7 application. Furthermore, when the Respondent protested against the Appellant for having drawn more money than funds infused and initiated arbitration proceeding that the Appellant filed the Section 7 application. The Section 7 application was therefore a counter blast to the initiation of dispute resolution sought by the Respondent through arbitration.

7. We have duly considered the arguments advanced by the Learned Counsel for both the parties and perused the records carefully.

8. Having heard the submissions advanced by the Ld. Counsels for both the parties and examining the materials on record, the following two interconnected issues arise for our consideration:

(a) Whether the infusion of funds by the Appellant in the Corporate Debtor was in the nature of financial debt and, if so, whether the Appellant, being a financial creditor, was entitled to file the Section 7 application.

(b) Whether in dismissing the Section 7 application of the Appellant, the Adjudicating Authority had committed an error in passing the impugned order.

9. Before we proceed further it would be relevant to take notice of the statutory construct of the IBC. We may now go through some of the relevant definition clauses which finds place in Section 3 and Section 5 of the IBC in the

context of “Claim”, “Debt”, “Transactions”, “Financial Creditor” and “Financial Debt”.

*3(6) "**claim**" means—*

(a) a right to payment, whether or not such right is reduced to judgment, fixed, disputed, undisputed, legal, equitable, secured or unsecured;

(b) right to remedy for breach of contract under any law for the time being in force, if such breach gives rise to a right to payment, whether or not such right is reduced to judgment, fixed, matured, unmatured, disputed, undisputed, secured or unsecured;

*3(11) **“debt”** means a liability or obligation in respect of a claim which is due from any person and includes a financial debt and operational debt;*

*3(33) **“transaction”** includes a agreement or arrangement in writing for the transfer of assets, or funds, goods or services, from or to the corporate debtor;*

*5(7) **“financial creditor**” means any person to whom a financial debt is owed and includes a person to whom such debt has been legally assigned or transferred to;*

*5(8) **“financial debt”** means a debt alongwith interest, if any, which is disbursed against the consideration for the time value of money and includes—*

(a) money borrowed against the payment of interest;

(b) any amount raised by acceptance under any acceptance credit facility or its de-materialised equivalent;

(c) any amount raised pursuant to any note purchase facility or the issue of bonds, notes, debentures, loan stock or any similar instrument;

(d) the amount of any liability in respect of any lease or hire purchase contract which is deemed as a finance or capital lease under the Indian Accounting Standards or such other accounting standards as may be prescribed;

(e) receivables sold or discounted other than any receivables sold on nonrecourse basis;

(f) any amount raised under any other transaction, including any forward sale or purchase agreement, having the commercial effect of a borrowing;

[Explanation. -For the purposes of this sub-clause,-

(i) any amount raised from an allottee under a real estate project shall be deemed to be an amount having the commercial effect of a borrowing; and
(ii) the expressions, "allottee" and "real estate project" shall have the meanings respectively assigned to them in clauses (d) and (zn) of section 2 of the Real Estate (Regulation and Development) Act, 2016 (16 of 2016);]

(g) any derivative transaction entered into in connection with protection against or benefit from fluctuation in any rate or price and for calculating the value of any derivative transaction, only the market value of such transaction shall be taken into account;

(h) any counter-indemnity obligation in respect of a guarantee, indemnity, bond, documentary letter of credit or any other instrument issued by a bank or financial institution;

(i) the amount of any liability in respect of any of the guarantee or indemnity for any of the items referred to in sub-clauses (a) to (h) of this clause;

10. Having run our eyes through the salient statutory provisions, for a proper appreciation of the issue at hand, it will be relevant to take cognisance of four landmark judgments of the Hon'ble Supreme Court dealing with the definition of "Financial Debt" and "Financial Creditor" in the IBC framework and find out its applicability in the facts of the present matter at hand.

11. We would like to begin by taking note of the observations made by the Hon'ble Supreme Court in ***Pioneer Urban Land & Infrastructure Ltd. v. Union of India (2019) 8 SCC 416*** where the concept of 'Financial Debt' in the IBC

framework has been expansively discussed which is extracted below for easy reference:

"70. The definition of "financial debt" in Section 5(8) then goes on to state that a "debt" must be "disbursed" against the consideration for time value of money. "Disbursement" is defined in Black's Law Dictionary (10th Edn.) to mean:

> *"1. The act of paying out money, commonly from a fund or in settlement of a debt or account payable. 2. The money so paid; an amount of money given for a particular purpose."*

71. In the present context, it is clear that the expression "disburse" would refer to the payment of instalments by the allottee to the real estate developer for the particular purpose of funding the real estate project in which the allottee is to be allotted a flat/apartment. The expression "disbursed" refers to money which has been paid against consideration for the "time value of money". In short, the "disbursal" must be money and must be against consideration for the "time value of money", meaning thereby, the fact that such money is now no longer with the lender, but is with the borrower, who then utilises the money. Thus far, it is clear that an allottee "disburses" money in the form of advance payments made towards construction of the real estate project. We were shown the Dictionary of Banking Terms (2nd Edn.) by Thomas P. Fitch in which "time value for money" was defined thus:

> *"present value : today's value of a payment or a stream of payment amount due and payable at some specified future date, discounted by a compound interest rate of DISCOUNT RATE. Also called the time value of money. Today's value of a stream of cash flows is worth less than the sum of the cash flows to be received or saved over time. Present value accounting is widely used in DISCOUNTED CASH FLOW analysis."*

That this is against consideration for the time value of money is also clear as the money that is "disbursed" is no longer with the allottee, but, as has just been stated, is with the real estate developer who is legally obliged to give money's equivalent back to the allottee, having used it in the construction of the project, and being at a discounted value so far as the allottee is concerned (in the sense of the allottee having to pay less by way of instalments than he would if he were to pay for the ultimate price of the flat/apartment).

75. And now to the precise language of Section 5(8)(f). First and foremost, the sub-clause does appear to be a residuary provision which is "catch all" in

nature. This is clear from the words "any amount" and "any other transaction" which means that amounts that are "raised" under "transactions" not covered by any of the other clauses, would amount to a financial debt if they had the commercial effect of a borrowing. The expression "transaction" is defined by Section 3(33) of the Code as follows:

> *3. (33) "transaction" includes an agreement or arrangement in writing for the transfer of assets, or funds, goods or services, from or to the corporate debtor;*

As correctly argued by the learned Additional Solicitor General, the expression "any other transaction" would include an arrangement in writing for the transfer of funds to the corporate debtor and would thus clearly include the kind of financing arrangement by allottees to real estate developers when they pay instalments at various stages of construction, so that they themselves then fund the project either partially or completely.

"76. Sub-clause (f) of Section 5(8) thus read would subsume within it amounts raised under transactions which are not necessarily loan transactions, so long as they have the commercial effect of a borrowing. We were referred to Collins English Dictionary & Thesaurus (2nd Edn., 2000) for the meaning of the expression "borrow" and the meaning of the expression "commercial". They are set out hereinbelow:

> *"borrow- vb 1. to obtain or receive (something, such as money) on loan for temporary use, intending to give it, or something equivalent back to the lender. 2. to adopt (ideas, words, etc.) from another source; appropriate. 3. Not standard. To lend. 4. (intr) Golf. To put the ball uphill of the direct path to the hole : make sure you borrow enough."*

> *"commercial.- adj. 1. of or engaged in commerce. 2. Sponsored or paid for by an advertiser: commercial television. 3. Having profit as the main aim: commercial music. 4. (of chemicals, etc.) unrefined and produced in bulk for use in industry. 5. A commercially sponsored advertisement on radio or television."*

77. A perusal of these definitions would show that even though the petitioners may be right in stating that a "borrowing" is a loan of money for temporary use, they are not necessarily right in stating that the transaction must culminate in money being given back to the lender. The expression "borrow" is wide enough to include an advance given by the homebuyers to a real estate developer for "temporary use" i.e. for use in the construction project so long as it is intended by the agreement to give "something equivalent" to money back to the homebuyers. The "something equivalent" in these matters

is obviously the flat/apartment. Also of importance is the expression "commercial effect". "Commercial" would generally involve transactions having profit as their main aim.....”

(Emphasis supplied)

12. Another seminal judgment made by the Hon’ble Supreme Court delineating the essential ingredients and characteristic of financial debt and financial creditor is the judgment of ***Jaypee Infratech Ltd. (Interim Resolution Professional) Vs Axis Bank Ltd. (2020) 8 SCC 401,*** the relevant paras of which are reproduced as below:

"The essentials for financial debt and financial creditor

46. Applying the aforementioned fundamental principles to the definition occurring in Section 5(8) of the Code, we have not an iota of doubt that for a debt to become a “financial debt” for the purpose of Part II of the Code, the basic elements are that it ought to be a disbursal against the consideration for time value of money. It may include any of the methods for raising money or incurring liability by the modes prescribed in sub-clauses (a) to (f) of Section 5(8); it may also include any derivative transaction or counter-indemnity obligation as per sub-clauses (g) and (h) of Section 5(8); and it may also be the amount of any liability in respect of any of the guarantee or indemnity for any of the items referred to in sub-clauses (a) to (h). The requirement of existence of a debt, which is disbursed against the consideration for the time value of money, in our view, remains an essential part even in respect of any of the transactions/dealings stated in sub-clauses (a) to (i) of Section 5 (8), even if it is not necessarily stated therein. In any case, the definition, by its very frame, cannot be read so expansive, rather infinitely wide, that the root requirements of "disbursement" against "the consideration for the time value of money" could be forsaken in the manner that any transaction could stand alone to become a financial debt. In other words, any of the transactions stated in the said sub- clauses (a) to (i) of Section 5(8) would be falling within the ambit of "financial debt" only if it carries the essential elements stated in the principal clause or at least has the features which could be traced to such essential elements in the principal clause. In yet other words, the essential element of disbursal, and that too against the consideration for time value of money, needs to be found in the genesis of any debt before it

may be treated as "financial debt" within the meaning of Section 5(8) of the Code. This debt may be of any nature but a part of it is always required to be carrying, or corresponding to, or at least having some traces of disbursal against consideration for the time value of money.

47. As noticed, the root requirement for a creditor to become financial creditor for the purpose of Part II of the Code, there must be a financial debt which is owed to that person. He may be the principal creditor to whom the financial debt is owed or he may be an assignee in terms of extended meaning of this definition but, and nevertheless, the requirement of existence of a debt being owed is not forsaken.

48. It is also evident that what is being dealt with and described in Section 5(7) and in Section 5(8) is the transaction vis-a-vis the corporate debtor. Therefore, for a person to be designated as a financial creditor of the corporate debtor, it has to be shown that the corporate debtor owes a financial debt to such person. Understood this way, it becomes clear that a third party to whom the corporate debtor does not owe a financial debt cannot become its financial creditor for the purpose of Part II of the Code.

49. Expounding yet further, in our view, the peculiar elements of these expressions "financial creditor" and "financial debt", as occurring in Sections 5(7) and 5(8), when visualised and compared with the generic expressions "creditor" and "debt", respectively, as occurring in Sections 3(10) and 3(11) of the Code, the scheme of things envisaged by the Code becomes clearer. The generic term "creditor" is defined to mean any person to whom the debt is owed and then, it has also been made clear that it includes a "financial creditor", a "secured creditor", an "unsecured creditor", an "operational creditor", and a "decree-holder". Similarly, a "debt" means a liability or obligation in respect of a claim which is due from any person and this expression has also been given an extended meaning to include a "financial debt" and an "operational debt".

49.1. The use of the expression "means and includes" in these clauses, on the very same principles of interpretation as indicated above, makes it clear that for a person to become a creditor, there has to be a debt i.e. a liability or obligation in respect of a claim which may be due from any person. A "secured creditor" in terms of Section 3(30) means a creditor in whose favour a security interest is created; and "security interest", in terms of Section 3(31), means a right, title or interest or claim of property created in favour of or provided for a secured creditor by a transaction which secures payment for the purpose of an obligation and it includes, amongst others, a mortgage. Thus, any mortgage created in favour of a creditor leads to a

security interest being created and thereby, the creditor becomes a secured creditor. However, when all the defining clauses are read together and harmoniously, it is clear that the legislature has maintained a distinction amongst the expressions "financial creditor", "operational creditor", "secured creditor" and "unsecured creditor". Every secured creditor would be a creditor; and every financial creditor would also be a creditor but every secured creditor may not be a financial creditor. As noticed, the expressions "financial debt" and financial creditor", having their specific and distinct connotations and roles in insolvency and liquidation process of corporate persons, have only been defined in Part II whereas the expressions "secured creditor" and "security interest" are defined in Part I.

50. A conjoint reading of the statutory provisions with the enunciation of this Court in Swiss Ribbons, leaves nothing to doubt that in the scheme of IBC, what is intended by the expression "financial creditor" is a person who has direct engagement in the functioning of the corporate debtor; who is involved right from the beginning while assessing the viability of the corporate debtor; who would engage in restructuring of the loan as well as in reorganization of the corporate debtor's business when there is financial stress. In other words, the financial creditor, by its own direct involvement in a functional existence of corporate debtor, acquires unique position, who could be entrusted with the task of ensuring the sustenance and growth of the corporate debtor, akin to that of a guardian. In the context of insolvency resolution process, this class of stakeholders, namely, financial creditors, is entrusted by the legislature with such a role that it would look forward to ensure that the corporate debtor is rejuvenated and gets back to its wheels with reasonable capacity of repaying its debts and to attend on its other obligations. Protection of the rights of all other stakeholders, including other creditors, would obviously be concomitant of such resurgence of the corporate debtor.

(Emphasis supplied)

13. We also notice the findings of the Hon'ble Apex Court in the matter of ***Phoenix ARC Pvt. Ltd. Vs Spade Financial Services Ltd. (2021) 3 SCC 475*** in which the terms Financial Creditor and Financial Debt in the context of IBC has been elucidated upon which is as extracted below:

"44. Section 5(8) IBC provides a definition of "financial debt" in the following terms:

G.3.2. Financial creditor and financial debt

45. Under Section 5(7) IBC, a person can be categorised as a financial creditor if a financial debt is owed to it. Section 5(8) IBC stipulates that the essential ingredient of a financial debt is disbursal against consideration for the time value of money. This Court, speaking through Rohinton F. Nariman, J., in Swiss Ribbons (P) Ltd. v. Union of India has held: (SCC p. 64, para 42)

> *"42. A perusal of the definition of "financial creditor" and "financial debt" makes it clear that a financial debt is a debt together with interest, if any, which is disbursed against the consideration for time value of money. It may further be money that is borrowed or raised in any of the manners prescribed in Section 5(8) or otherwise, as Section 5(8) is an inclusive definition. On the other hand, an "operational debt" would include a claim in respect of the provision of goods or services, including employment or a debt in respect of payment of dues arising under any law and payable to the Government or any local authority."*

(Emphasis supplied)

14. Yet another judgment of the Hon'ble Apex Court which has looked into the ambit and scope of Financial Debt is the judgment contained in ***Orator Marketing (P) Ltd. Vs Samtex Desinz (P) Ltd. (2023) 3 SCC 753*** which is reproduced as below:

"21. The definition of "financial debt" in Section 5(8) IBC has been quoted above. Section 5(8) defines "financial debt" to mean "a debt along with interest if any which is disbursed against the consideration of the time value of money and includes money borrowed against the payment of interest, as per Section 5(8)(a) IBC. The definition of "financial debt" in Section 5(8) includes the components of sub-clauses (a) to (i) of the said Section.

22. NCLT and NCLAT have overlooked the words "if any" which could not have been intended to be otiose. "Financial debt" means outstanding principal due in respect of a loan and would also include interest thereon,

if any interest were payable thereon. If there is no interest payable on the loan, only the outstanding principal would qualify as a financial debt. Both NCLAT and NCLT have failed to notice clause (f) of Section 5(8), in terms whereof "financial debt" includes any amount raised under any other transaction, having the commercial effect of borrowing.

23. Furthermore, sub-clauses (a) to (i) of sub-section (8) of Section 5 IBC are apparently illustrative and not exhaustive. Legislature has the power to define a word in a statute. Such definition may either be restrictive or be extensive. Where the word is defined to include something, the definition is prima facie extensive.

29. In Jaypee Infratech Ltd., the debts in question were in the form of third-party security, given by the corporate debtor to secure loans and advances obtained by a third party from the respondent lender and, therefore, held not to be a financial debt within the meaning of Section 5(8) IBC. There was no occasion for this Court to consider the status of a term loan advanced to meet the working capital requirements of the corporate debtor, which did not carry interest. Having regard to the Aims, Objects and Scheme of the IBC, there is no discernible reason, why a term loan to meet the financial requirements of a corporate debtor for its operation, which obviously has the commercial effect of borrowing, should be excluded from the purview of a financial debt.

31. At the cost of repetition, it is reiterated that the trigger for initiation of the corporate insolvency resolution process by a financial creditor under Section 7 IBC is the occurrence of a default by the corporate debtor. "Default" means non-payment of debt in whole or part when the debt has become due and payable and debt means a liability or obligation in respect of a claim which is due from any person and includes financial debt and operational debt. The definition of "debt" is also expansive and the same includes, inter alia, financial debt. The definition of "financial debt" in Section 5(8) IBC does not expressly exclude an interest free loan. "Financial debt" would have to be construed to include interest free loans advanced to finance the business operations of a corporate body."

(Emphasis supplied)

15. From a reading of the above judgments, broadly speaking, for a debt to be treated as financial debt there has to be an element of disbursal of money and

the disbursal must be against the consideration for time value of money. The concept of time value of money has been further explained to also include a transaction which does not necessarily culminate into interest being paid in respect of money that has been borrowed.

16. The nature of underlying transaction is therefore a determinative factor in deciding whether infusion of funds can be classified as financial debt or not. To find out whether any element of commercial borrowing for time value of money is noticeable in the transactions which have taken place in the present facts of the case, we have to study the various relevant clauses of the MoA since it is the MoA which constitutes the underlying edifice of the transactions.

17. The significant clauses of the MoA which needs to be noticed to find out the real nature of transaction are as under:

> *And Whereas the management of Shivam, represented by the Promoters herein, is not in a position to operate the said Unit due to financial constraints and the said Unit is now closed for over 6 (six) months.*
>
> *And Whereas the said management of Shivam has in deference to the desire expressed by Adhunik agreed to recommence the operations of the said Unit with funds in the Interim to be provided by Adhunik since Shivam does not have the ability to infuse any further amount of funds mandatorily required to make the said Unit operative.*
>
> *And Whereas Shivam has suggested that some amount of funding would be immediately required to recommence the operations of the said Unit.*
>
> *And Whereas Adhunik has, on an Interim basis, agreed to infuse the said funds and to facilitate operations of the said Unit by effecting supply of the raw materials during the period of this MoA, all on the clear understanding of the Parties that the entire funds so infused by Adhunik is fully refundable.*
>
> *And Whereas the Parties are now desirous of recording their understanding in this regard.*

NOW, THEREFORE, THIS MEMORANDUM OF AGREEMENT WITNESSETH and it is hereby agreed by and amongst the Parties hereto as follows:

1. Shivam shall forthwith, upon receipt of the first instalment of fund as mutually decided from Adhunik take immediate steps to recommence the operations of the said Unit and shall make the said Unit fully operative as soon as possible but not beyond 15 days from the date of such first infusion of fund. In case Shivam is unable to make the said Unit fully operative within the said period, the Parties shall jointly discuss the way forward failing which the total amount infused by Adhunik into Shivam shall become refundable forthwith.

4. The said Unit shall be run and operated in terms of this MoA by Shivam for such period(s) as may be decided by Adhunik subject to the maximum period of 5 (five) years envisaged under this MoA. It is hereby clarified and agreed between the Parties hereto that during the term of this MoA, the said Unit shall be run and operated by Shivam in accordance with the recommendations made by Adhunik.

5. To enable Shivam to carry out operations of the said Unit, Adhunik shall supply raw-materials as per the production schedule of the said Unit, which shall be agreed at the beginning of each month by and between Shivam and Adhunik

6. Shivam shall utilize the raw-materials supplied by Adhunik and operated the said Unit for a period of 5 (five) years and shall allow the authorized representatives of Adhunik to observe the operations of the said Unit so as to ascertain the quantity and quality of production. Shivam shall at all reasonable times allow all authorized personnel of Adhunik to visit and stay in the plant whenever deemed so necessary by Adhunik. It is hereby also agreed that the representatives of Adhunik shall be entitled to, if necessary, (i) monitor the receiving of the raw materials, (ii) observe production and processing of the materials at the said Unit; (iii) observe both quantity and quality of the finished products; and (iv) oversee the dispatch and delivery of the finished goods. No material shall be removed from the said unit without prior permission of the authorized representative of Adhunik.

7. Adhunik shall supply raw materials to Shivam for its said Unit at the prevailing market prices for manufacturing Hot Rolled Finished Products as well as for Billets through Induction furnace route to be subsequently charged in rolling mill in hot charging process and the left-out billet not charged, will be sold. During the term of this MOA, Adhunik shåll remove the entire finished products, coils and billets made out of the raw materials supplied by Adhunik,

for disposal at the prevailing market prices and Adhunik shall be entitled to the following charges/commission out of the sale proceeds:-

(I) For Hot-rolled finished products and coils- Rs. 600/- per ton; and

(II) For Induction Furnace sale-able Billets – Rs. 300/- per ton.

(III) Adhunik shall also be fully entitled to remove By-products like Mis-rolls and end-cutting etc.

9. Subject to the above, the raw-materials supplied by Adhunik and the finished products as stated in paragraphs 6 and 7 above made out of such materials shall at all times be the property of Adhunik, and Adhunik shall be entitled to take all decisions over the raw-materials, any others materials and the finished products.

11. Till such sums are fully repaid by Shivam to Adhunik, Adhunik shall be entitled to exercise lien over all raw-materials supplied by Adhunik to Shivam and also on all finished products manufactured at the said factory of Shivam including stores, and accordingly the parties do hereby agree and undertake that during the term of this MoA all goods, materials and inventory at all the factory of Shivam shall remain hypothecated to Adhunik and Shivam shall be under an obligation not to effect sale of any finished goods made at the factory of Shivam durlng the term of this MoA without specific written permission of Adhunik. The shares in Shivam held in separate Demat Account in terms of this MoA shall also be continued to be held as collateral by Adhunik till sum sums are fully repaid by Shivam to Adhunik.

19. This MoA shall remain valid for a period of 5(five) years from the date the said until operative. This period may, however, be extended on mutually agreed terms. Till such time Adhunik agrees to continue the MoA, Shivam shall not be entitled to terminate the MoA during its validity period.

(Emphasis supplied)

18. Before we weigh the rival contentions made by both parties, it would be appropriate to first look into the findings returned by the Adjudicating Authority on how it has treated the infusion of funds by the Appellant. The impugned order has held that the infusion of fund was not in the nature of financial debt since

the infusion was not against any consideration for time value of money. The relevant portions of the impugned order is reproduced below:

"57. After having accorded consideration to the aforementioned conditions of the MoA, we are of the view, the MoA was a business agreement wherein admittedly, the Financial Creditor infused the funds. However, this infusion was not against any consideration for the time value of money. In Swiss Ribbons Pvt Ltd & Anr. v. Union of India & Ors., the Supreme Court held as follows:

> *"23. A perusal of the definition of financial creditor and financial debt makes it clear that a financial debt is a debt together with interest, if any, which is disbursed against the consideration for time value of money. It may further be money that is borrowed or raised in any of the manners prescribed in Section 5(8) or otherwise, as Section 5(8) is an inclusive definition. On the other hand, an operational debt would include a claim in respect of the provision of goods or services, including employment, or a debt in respect of payment of dues arising under any law and payable to the Government or any local authority."*

58. In the present case, it was a business arrangement and somehow, this business arrangement could not fructify.

59. We are not inclined to accept the contention of the Financial Creditor with regard to debt or default within the meaning of Section 7 of the Insolvency and Bankruptcy Code, 2016 in view of the above position based on the terms of the agreement and the law."

19. Coming to our analysis and findings, we would like to examine whether money disbursed by the Appellant to the Corporate Debtor to operationalize its business can be treated as a financial debt.

20. In the present facts of the case, there is sufficient material on record to prove that there was disbursal of funds by the Appellant to the Corporate Debtor in their account. The bank transaction details have been placed at page 248-284 of Appeal Paper Book (**"APB"** in short) to substantiate their contention that

money was actually disbursed to the Corporate Debtor, which was in dire financial straits, towards working capital to make the Corporate Debtor operational. Receipt of this amount has also not been denied by the Corporate Debtor. Further, invoices have been placed on record from pages 287 to 365 of APB to prove that Rs 4.35 Cr was paid towards direct supply of raw material by the Appellant to the Corporate Debtor. Details have also been furnished at page 376 of APB for an amount of Rs 11.78 Cr. towards outstanding amount to be paid by Corporate Debtor to third party vendor for supply of raw material. Besides this, an abstract of commission on sales received by the Appellant from the Corporate Debtor for Rs 2.95 Cr. along with tax invoices have been placed from pages 366 to 375 of APB. It has also been indicated that an amount of Rs 11.54 lakhs was still due from the Corporate Debtor towards commission. This leaves no doubts in our mind that there was fund infusion into the Corporate Debtor by the Appellant.

21. This now brings us to the issue whether this disbursal was made by the Appellant against consideration for time value of money.

22. It is the case of the Respondent that the MoA is not a loan agreement as it did not provide for payment of any amount on account of interest on the funds infused by the Appellant. The Appellant for the first time had demanded interest although there was no interest clause in the MoA. Simply because the funds to be infused by the Appellant was fully refundable in terms of Clause 1 of the MoA, it does not establish a case of financial debt. It was strongly canvassed that the MoA is required to be read as a whole and not in isolation. Attention was adverted

to Clause 7 of MoA which stipulated that the Appellant was entitled to sell the products and get commission thereon which clearly proves that the Appellant was running the business of the Corporate Debtor and the case of financial debt was put up by the Appellant as an after-thought. When the funds infused by the Appellant and the costs of raw material supplied by them was to be recovered by selling the products of the Corporate Debtor and only the surplus thereafter was to be used by the promoters of the Corporate Debtor to operate the said entity, the infusion of funds/raw material costs was not a loan in the nature of financial debt but a business arrangement. This was a profit-sharing business arrangement with the Appellant having full control over the Corporate Debtor. Much emphasis was laid by the Respondent that the Appellant in their own reply to the notice dated 23.09.2021 have admitted that the amount of Rs.27.85 crore was an 'undisputed invested amount' at page 193 of APB. Thus, when it is an admission made by the Appellant that it was an investment, this amount was clearly not in the nature of financial debt but was an investment. The real nature of transactions entered between the two parties would show that it was not in the nature of financial debt. It was contended that the MoA did not provide for any consideration as time value for money.

23. Per contra, it is the contention of the Appellant that it is settled law that for any debt to be treated as financial debt, the pre-requisite is disbursal of money to the borrower for utilization by the borrower and that such disbursal is in the nature of financial debt as long as it is disbursed against consideration for time value of money even if it is not interest-bearing. It is the case of the

Appellant that the commercial effect of the borrowing against disbursal of funds can be noticed from the charges/commissions which was to be received by the Appellant from the sale proceeds of the finished product from the Corporate Debtor which find mention at Clause 7 of the MoA at page 143 of APB. Moreover, the funds were infused in a manner that they were to be fully refundable as may be seen at Clause 1 of the MoA at page 142 of the APB. Since the MoA was for a period of five years, the Appellant was entitled to demand the payment of the outstanding debt from the Corporate Debtor at any point of time within the period of five years. Further Clause 9 and 11 of the MoA provided an enabling framework for the Appellant to exercise lien besides placing the shares of the Corporate Debtor held by their promoters as collateral and specific security till the amount infused was fully repaid. The right to exercise lien and pledging of shares of the Corporate Debtor as collateral was contended by the Appellant to be akin to security provided in standard forms of loans and credit facility extended by the banks. It was vehemently contended that the substance of commercial effect of borrowing is quite evident from the underlying nature of transaction which the Adjudicating Authority wrongly ignored by holding the agreement to be merely a business agreement.

24. When we peruse the clauses of the MoA, it is an undisputed fact that payment of interest against disbursal was not specifically mentioned in the clauses. Be that as it may, we are of the considered opinion that the IBC does not provide for any prescriptive requirement for the Financial Creditor to place on record formal written agreements/documents between the parties to establish

that the disbursal made was in the form of loan with interest. It would be misconceived to hold that the fund infusion did not qualify to be a financial debt merely because loan component was not explicitly mentioned in the MoA. It is a well settled proposition of law that interest on loan is not the only binding criterion for determining time value of money. The question whether a credit facility without charging interest can be considered to be a financial debt in terms of Section 5(8) of the IBC is no longer *res integra* and has already been decided by the Hon'ble Supreme Court in ***Orator judgment supra*** to hold that the definition of "financial debt" in Section 5(8) IBC does not expressly exclude an interest free loan. Viewed against this backdrop, the contention of the Respondent that the disbursal of the fund was bereft of loan component and hence not in the nature of a financial debt does not have legs to stand on.

25. The issue to be seen next is whether the disbursal made by the Appellant in the present context reflected consideration for time value of money. As per the Insolvency Law Report, 2018, time value of money means compensation or the price paid for the length of time for which money has been disbursed. Time value of money is not only a regular or timely return received for the duration for which the amount is disbursed as an amount in addition to the principal but also covers any other form of benefit or value accruing to the creditor as a return for providing money for a long duration. We need to see if the Appellant had envisioned enhancement of economic prospect in return for the funds disbursed and if so then the sum advanced would qualify to entail time value of money and acquire the colour and character of commercial borrowing.

26. The MoA is a matter of record. When we look at the MoA, it clearly provides for the Appellant to supply raw material and also the disposal of finished products. Merely because the MoA allowed the Appellant to monitor the production of the unit does not in any manner show that they were in control of the unit and were not entitled to receive back the funds infused by them. This in way diminished the obligation of the Corporate Debtor to discharge their debt liability. It is further clear from the terms of the MoA that the Appellant was required to infuse funds to the Corporate Debtor to render the Corporate Debtor operational from its dysfunctional state. Moreover, the credit so provided was in the form of working capital and the entire amount was fully refundable. Even the funds provided for purchase of raw material at prevailing market prices was towards operationalization of the Corporate Debtor. The right of the Appellant to enjoy sales commission was also a form of return for the amount financed. From the judgment of the Hon'ble Supreme Court in ***Pioneer judgment supra*** the ratio is clear that even if transactions are not necessarily loan transactions, they still attract Section 5(8) of the IBC as long as the transactions have the commercial effect of a borrowing. The essential condition which needs to be fulfilled is disbursement against the consideration for time value of money. Since in the present case, the infusion of funds was a transaction which has direct bearing on the business carried out by the Corporate Debtor, raising of the amount through the above agreement has the commercial effect of borrowing. The clauses of the MoA contain clear indication that the infusion of funds was being done with the intent of earning profits and the investments was therefore for consideration for the time value of money. Therefore, this transaction has the

contours of a borrowing as contemplated under Section 5(8) of IBC. The investments made by the Appellant-Financial Creditor was with an eye for consideration for time value of money and therefore the transaction had commercial effect of borrowing.

27. Therefore, seen in totality, the disbursals clearly display commercial effect of borrowing. In our considered opinion the Adjudicating Authority committed an error in holding the transaction to be a business arrangement and non-suiting of the Appellant on the ground of not being a financial creditor. The Appellant has been wrongfully ousted by the Adjudicating Authority on the ground that the Appellant was not a financial creditor and the infusion of fund was not in the nature of financial debt. We have no hesitation to observe that this is a case of financial debt and the Appellant is clearly a financial creditor in terms of statutory provisions of IBC.

28. Having been convinced that the disbursal made by the Appellant has all the trappings of a 'financial debt' which falls within the purview of Section 5(8) of IBC and the Appellant is squarely covered by the definition of 'Financial Creditor', on the issue of default, we, however, notice from the pleadings and submissions made by the Respondent that the Appellant had already realised and recovered the funds infused and as such there is no default. Capturing some of their other related submissions, it is their case that the Appellant also made wrongful gains by their illegal act of supply of raw materials through their own chosen suppliers at price higher than the prevailing market price. The Appellant had allegedly benefitted themselves by clandestinely making profits while

increasing the liability of the Corporate Debtor. Moreover, the invoices relied upon by the Appellant show that they fell due for payment within the period excluded by Section 10A of the IBC. The Appellant had also acted in complete breach of their obligations having stopped the supply of raw materials and infusion of funds though the agreement was for a period of five years. All this had led to the erratic functioning of the Corporate Debtor causing damages to the Respondent which became the subject matter of arbitration proceedings. It has been pointed out by the Respondent that they had invoked clause 21 of the MoA on 23.09.2021 for resolution of their *interse* disputes which eventually led to the filing of Arbitration Petition No. 360 of 2022 under Section 11 of the Arbitration and Conciliation Act before the Hon'ble High Court of Calcutta. It is also the case of the Respondent that the Appellant had filed the application under Section 7 as a counterpoise. Further, as the Appellant was supplying raw material under Clause 5 of the MoA, the amount involved was an operational debt and not a financial debt and clubbing of operational and financial debt in a single application is not permissible under IBC. Hence the application of the Appellant is defective and not maintainable.

29. On the other hand, we also notice that the Appellant has brought on record the Section 7 application filed by them. In Part-IV of the Section 7 application, the amount claimed to be in default as well as date of default has been clearly depicted therein. Part-IV also contains the pleadings and submissions made pertaining to debt and default. In Form-1 filed by the Appellant under Section 7 of IBC read with Rule 4 of the Insolvency and

Bankruptcy (Application to Adjudicating Authority) Rules, 2016, we find that the principal amount of loan advanced as 'Financial Assistance' by the Appellant is shown as Rs.39,84,72,111/- and the amount claimed in default to be Rs.42,47,32,067/- including interest. The Appellant along with the Section 7 application has also submitted schedule of payment along with supporting bank statement; schedule of raw materials along with invoices; statement along with commission bills; statement regarding TDS and schedule of outstanding claims of different suppliers of raw materials as well as a chart showing calculation of outstanding dues. It has also been contended that the financial debt which is above the threshold limits has not been repaid by the Corporate Debtor despite a demand notice.

30. The Adjudicating Authority is obliged to determine whether default has occurred and whether the debt which was due and payable has remained unpaid. Clearly enough, the rival contentions of the two parties with respect to default in repayment of debt has not been considered and adjudicated upon by the Adjudicating Authority. We also do not wish to express our opinion on this aspect at this stage.

31. Given this backdrop, we set aside the impugned order and allow the Appeal. Having arrived at our finding that the present is a case where the financial assistance given by the Appellant has a clear element of commercial effect of borrowing and therefore qualifies to be treated as financial debt and the Appellant is a financial creditor in terms of the statutory provisions of IBC, we remand the matter to the Adjudicating Authority to exercise its satisfaction as to

whether financial debt has crossed the threshold limits and has become due and payable and basis these findings decide to accept or refuse admission of the Section 7 application of the Appellant.

[Justice Ashok Bhushan]
Chairperson

[Barun Mitra]
Member (Technical)

Place: New Delhi
Date: 19.02.2025

Harleen/Abdul