

**IN THE NATIONAL COMPANY LAW TRIBUNAL
DIVISION BENCH – I, CHENNAI**

IBA/312/2019 filed under Section 7 of the Insolvency and Bankruptcy Code, 2016 r/w Rule 4 of the Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016

In the matter of ***M/s. Wellknit Apparels Private Limited***

M/s. Eight Capital India (M) Ltd.

.. *Financial Creditor*

-Vs-

M/s. Wellknit Apparels Private Limited

.. *Corporate Debtor*

Order Pronounced on 11th December 2019

CORAM:

**R. VARADHARAJAN, MEMBER (JUDICIAL)
ANIL KUMAR B, MEMBER (TECHNICAL)**

For Financial Creditor : Manoj Kumar Mishra, *Advocate*
For Corporate Debtor : R. Sivaraman, *Advocate*

ORDER

Per: ANIL KUMAR B, MEMBER (TECHNICAL)

1. This Application has been filed invoking the provisions of Section 7 of the Insolvency and Bankruptcy Code, 2016 ("I&B Code-2016") in the format as prescribed under Rule 4 of the Insolvency & Bankruptcy (Application to Adjudicating Authority) Rules, 2016 (hereinafter referred to as "AAA Rules") by the



Applicant in the capacity of Financial Creditor viz. Eight Capital India (M) Ltd. against the Respondent viz. Welknit Apparels Pvt. Ltd. (hereinafter referred to as "Corporate Debtor")

2. Part I of the application, sets out the details of the Financial Creditor from which, it is evident that the Financial Creditor is Private Limited Company, with identification number 069375 c1/GBL and having registered office at GFin Corporate Services Ltd., Level 6, GFin Tower, 42 Hotel Street, Cybercity, Ebene 72201, Mauritius.

3. As per Part II of the application, the Corporate Debtor is a Private Limited Company with Corporate Identification Number U18101TN1988PTC015427 and having registered office at Phase II, Plot No.A11 to A14, MEPZ SEZ, Chennai 600 045. As per Part III of the application, the Financial Creditor has nominated Interim Resolution Professional with the following particulars:

A R Ramasubramania Raja
No.3, Sundaram Brothers Layout,
Opp. to All India Radio,
Trichy Road,
Ramanathapuram,
Coimbatore 641 045
Regn.No. IBBI/IPA-002/IP/N00635/2018-19/11982

4. Part IV of the application signifies the amount of remittance in foreign exchange (US\$ dollar) to the tune of US\$

37,15,000 equivalent amount of ₹15 Crores for the purpose of Project Finance by way of issuance of fully convertible debentures by the Corporate Debtor; 40 debentures of ₹25 lakhs each, for an amount of ₹10 Crore on 20th August 2007 and 20 debentures of ₹25 lakhs each, totalling ₹5 Crores on 20th November, 2007 ; total value of the debenture being ₹15 Crores.

5. Part V of the application describes the particulars of Financial Debt, documents, records and evidence of default as described below:

Mortgage Deed: (Annexure I)

All that piece of land known as Plot Nos. A11, A12, A13 and A14 in Phase II in MEPZ-Special Economic Zone area forming part of Survey No.164/1(Part) within the village limits of Kadaperi, Tambaram Taluk, Kancheepuram District containing by admeasurements 9,940 sq.meter.

Mortgage Deed: (Annexure 2)

Superstructure consisting of main building, security building and connected facilities constructed on the land comprising a total built up area of 133,610 Square feet (Approx.) together with borewell, roads and amenities and situated at Plot Nos.A11, A12, A13 and A14, Phase-II, MEPZ Special Economic Zone, NH-45, Tambaram, Chennai 600 045 within the Sub-Registration District of Tambaram and Registration District of Chennai South.



Charge created in favour of M/s.IDBI Trusteeship Services Ltd., Mumbai for the benefit of debenture holders (i.e. Eight Capital India (M) Ltd.)

6. The Corporate Debtor incorporated on 3rd March 1988 was engaged in the business of Manufacture of wearing apparel, except fur apparel and during the year 2007, they approached the Financial Creditor seeking Financial support of around ₹15 Crore. Accordingly, Financial Creditor and Corporate Debtor had entered into Debenture Subscription Agreement dated 21st May, 2007 and Master Facility Agreement dated 21st May, 2007.

7. As per the terms of the Agreement the subscription to the debenture was done for a period of 84 months. Interest was to be paid at the rate of 12% per annum and for default an additional interest of 6% per annum.

8. Financial Creditor has represented that the Corporate Debtor made a repayment only once during the period of quarter ended 30th September, 2007 for an amount of ₹39,86,371/- (Rupees Thirty Nine Lacs Eight Six Thousand Three Hundred and Seventy One only). It was further represented that the Corporate Debtor defaulted on all the payment of interest till the time stipulated in the agreement till 20th May, 2014. Further, it



has been alleged that the Corporate Debtor failed to convert the debenture into equity Share Capital after the specified period.

9. Article 8 of the Debenture subscription agreement lays down certain stipulations on events of default, such as on default of payment, **the Financial Creditor can initiate the proceeding against the Corporate Debtor for the appointment of receiver, liquidator or make an application for winding up.** Therefore in exercise of the right, Financial Creditor seeks to appoint Insolvency Professional for the company and start of Corporate Insolvency Resolution Process.

10. It is further stated that on the failure of Corporate Debtor, the Financial Creditor had moved Madras High Court for the recovery of interest and restraining corporate debtor from alienating the assets of the Corporate Debtor. Application filed by Corporate Debtor for opposing the suit had been dismissed by Madras High Court on the ground that suit is continuing breach of tort and every act of breach giving rise to fresh cause of action. [Appeal No. 5071 of 2011 in C.S. No. 405 of 2011]

11. On 18th April 2017 a Memorandum of Agreement was executed by and between the Financial Creditors and Corporate Debtor, which is stated to have been confirmed and made



binding by Madras High Court on 14th July, 2017, to which Corporate Debtor did not cooperate with Financial Creditor to monetize the assets and to make the payments to Financial Creditor as was agreed in the MOA.

12. Total amount claimed as due as on 20th May, 2014 was ₹49,13,76,941/- (Rupees Forty Nine Crore Thirteen Lacs Seventy Six Thousands Nine Hundred Forty one only) to be broken up as a Principal sum of ₹15,00,00,000/- (Rupees Fifteen Crores only) and an interest of ₹34,13,76,941/- (Rupees Thirty Four Crore Thirteen Lacs Seventy Six Thousands Nine Hundred and Forty One only)

13. In the counter statement filed by the Respondent/ Corporate Debtor, it has been stated that:

- a) the Respondent Company was engaged in the business of manufacture of knitted garments who had entered into a Master Facility Agreement with the Applicant whereby the Applicant subscribed to fully convertible debentures of the Respondent Company to the extent of ₹15,00,00,000/- (Rupees Fifteen Crores only). After detailed discussion and having considered various options including optional convertible debentures, the Applicant agreed to extend the facility of Fully Convertible Debentures to the Respondent Company and did so in two tranches totaling ₹15 Crores. It is stated that owing to unforeseen developments in the



international market and in particular the totally unexpected appreciation of the Indian Rupee at the relevant point of time, the respondent company's business operations suffered a heavy jolt and the operations became increasingly unviable and the respondent company with the full knowledge and concurrence of the Applicant had to scale down the operations and eventually close down the operations in the interest of the company as well as the applicant.

- b) The Corporate Debtor has stated that as per the arrangement contemplated by the said Master Facility Agreement, the applicant was entitled to convert the debentures at the maturity of the debentures or even earlier to equity to an extent of 37.5% of the total equity of the company which had been predetermined. The Corporate Debtor has claimed that it was not contemplated that this money will be returned or repaid which would have been the case if it was a loan and it would follow that the respondent company therefore is not a debtor.
- c) Despite the fact that the Applicant knew full well the circumstances that to the downturn in the business of the Respondent Company and the decision to close down the operations was taken with the knowledge and concurrence of the Applicant, the Applicant filed C.S. No.424 of 2009 on the file of the Hon'ble High Court of Judicature at Madras for recovery of a sum of ₹4,04,26,095 (Rupees Four Crore Four Lakh Twenty Six Thousand and ninety five) together with interest and also filed C.S.No.405 of 2011 on the file of the Hon'ble High Court of Judicature at Madras for



recovery of a sum of ₹5,40,00,000 (Rupees Five Crore and Forty Lakhs) together with interest.

14. The Corporate Debtor admitted that Memorandum of Agreement on 18.04.2017 was entered into for a compromise which provided for resolving the disputes amicably but not to admit or determine the quantum of liability by the Respondent Company to the Applicant. The Corporate Debtor stated that it was done in a spirit of goodwill and compromise and to put a quietus to the litigation the Respondent Company entered into the Memorandum of Agreement, agreeing to share 50% of the net assets after deducting/adjusting certain statutory dues etc. which was higher than the maximum of 37.5% equity entitlement of the Applicant. The Corporate Debtor stated that the claims were sought to be settled on the basis of assets available and not on the basis of any liability admitted or otherwise.

15. The Corporate Debtor stated to have approached the MEPZ-SEZ Authorities after obtaining the High Court Order which was given in November 2017 with a view to accomplish the surrender and sale of the assets as contemplated by the said MOA through the office of the MEPZ-SEZ. The Corporate Debtor also submitted that the property in question namely the factory



building belonging to the MEPZ-SEZ (Government of India). The Corporate Debtor further submitted that company being a 100% export oriented company had various obligations concerning debonding of machinery etc. and elucidated various procedural prescriptions.

16. The Corporate Debtor has also claimed that the Memorandum of Agreement constituted a separate Contract distinguishable from the Master Facility Agreement and it supersedes the earlier contract and the contract clearly explains the mode and the time of performance of the respective obligations. The contract is conditional upon the sale of the property by the authorized officer of MEPZ.

17. The Ld. Counsel for the Corporate Debtor contended that the Applicant claims himself to be a Financial Creditor and for reasons stated earlier about the character of the facility extended namely that of Fully Convertible Debentures which does not contemplate any repayment of the amount and instead only conversion into equity shares of a maximum of 37.5% of the shareholding in favour of the Applicant and the subsequent action of the Applicant in entering into the Memorandum of Agreement which contemplates sale of the assets and dividing the surplus in an agreed manner only reinforces the proposition



that the Applicant is a stakeholder in equity and is not a financial creditor as there is no debt involved.

18. In the rejoinder filed by the Financial Creditor, it has been submitted that the applicant is a debenture holder by virtue of Master Facility Agreement and Debenture Subscription Agreement dated 21.05.2007 that was entered into between the Applicant and the Respondent Company based on which a sum of ₹15,00,00,000/- (Rupees Fifteen Crores only) was disbursed to the Respondent Company and the Applicant subscribed to two series of convertible debentures with each of it for a period of 84 months. As per clause 1 of Schedule 5 of Debenture Subscription Agreement, during the subsistence of the agreement and until the date on which Fully Convertible Debentures are converted into Equity Shares, the Fully Convertible Debentures shall earn interest quarterly at a rate of 12% p.a. and in event of delay in the payment of amounts due, a penal interest of 6% per annum would be levied in addition to the interest payable on such due amounts. The Applicant has all along been a debenture holder and the debentures were never converted into equity shares at any point of time and reproduced the definition of "Financial Debt" as defined under Section 5(8) of IBC, 2016 is herewith reproduced:



"Section 5(8): 'financial debt' means a debt along with interest, if any, which is disbursed against the consideration for the time value of money. It includes:

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

A mere perusal of the aforesaid definition makes it very clear that any amount raised pursuant to issuance of debentures falls within the ambit of "Financial Debt" and therefore the principal and interest amount that is liable to be paid by the Respondent to the Applicant in pursuance to the Master Facility Agreement is a "Financial Debt". It is also stated in the Rejoinder that the Respondent Company has acknowledged the Applicant as a "Debenture Holder" in its Balance Sheet for the year ending 2016-2017, further establishing that a "Financial Debt" is due to the Financial Creditor.

19. This Tribunal has examined the averments and statements as per the application of the Financial Creditor, the affidavit by the Corporate Debtor, the Rejoinder filed by the Financial Creditor and various documents such as Master Facility Agreement, Debenture Subscription Agreement, Simple Mortgage Deed, etc. which form part of the application.



20. On evaluation of the aforementioned documents and after hearing both the parties, this Tribunal hereby is of the opinion that the intention of both the parties is manifested in the Master Facility Agreement and the Debenture Subscription Agreement. The parties have made arrangement for an investment in the business of the Corporate Debtor in order to scale up their business operations. The investment was sought to be made by the Financial Creditor by way of subscribing to the Debentures in consideration of the money brought in by the Financial Creditor into the coffers of the Corporate Debtor. Fully convertible debentures are a financial instrument within the meaning of Section 5(8) of the Insolvency and Bankruptcy Code, 2016 as mentioned above. Convertible Debenture is in the nature of financial debt; though it is hybrid in nature, it cannot be treated as equity unless converted into equity; it cannot partake the characteristics of equity until the conversion is done.

21. Had the Investor/Financial Creditor intended to subscribe to equity in the Corporate Debtor Company it could have been done at the inception itself. The concept behind subscribing to the Convertible Debenture by an Investor is to safeguard his interest since he doesn't have confidence and belief in the executing and managing capability of the investee company management during the initial stage. Once the confidence is built



up in terms of timely Project execution and scaling up of business as per the business plan they will convert their stake into equity's which is the standard practice in this type of arrangement.

22. In this context, the Financial Creditor has taken all precautions to safeguard his interest so long as the Convertible Debenture remains as debenture. It is also seen from the documents that a Simple Mortgage is seen to have been created in favour of the Financial Creditor which shows that there is debt which is a financial debt based on the principle that "**once a mortgage; always mortgage**". It postulates that unless and until a mortgage is discharged it remains as a mortgage and as such the financial debt.

23. On a perusal of Clause 8.1.2 of the Master Facility agreement, a "default" is said to have occurred when there is non-payment in full, any of the interest amount that becomes due within a period of 30 days on which such amounts become payable. Therefore, it cannot be contented by the Respondent that no sum was liable to be returned or repaid. Apart from payment of a sum of ₹39,86,371.36 for the quarter ending September, 2007, interest amount was not paid for the



remaining period by the Respondent and there is a clear default on part of the Respondent.

24. The Applicant being a debenture holder and further in order to secure the amounts due and payable under the Master Facility Agreement and Debenture Subscription Agreement dated 21.05.2007, a Simple Mortgage Deed dated 25.02.2010 was executed by the Respondent Company.

25. Thus taking into consideration the facts and circumstances of the case as well as the position of Law, we are of the view that this Application as filed by the Applicant – Financial Creditor is required to be admitted under Section 7 (5) of the I&B Code, 2016.

26. The Financial Creditor has proposed the name of **Mr. A.R. Ramasubramania Raja** having Registration Number [IBBI/IPA-002/IP-N00635/2018-19/11982] (e-mail:- arrsraja@yahoo.com) (Mobile No: +91-9843043576) as Interim Resolution Professional (IRP) and a written communication in the format prescribed under Form 2 of the Insolvency and Bankruptcy Board of India (Application to Adjudicating Authority) Rules, 2016 has been filed by the proposed IRP who is appointed as the IRP to take forward the process of Corporate insolvency



Resolution of the Corporate Debtor. The IRP appointed shall take in this regard such other and further steps as are required under the Statute, more specifically in terms of Section 15,17,18 of the Code and file his report within 20 days before this Bench. The powers of the Board of Directors of the Corporate Debtor shall stand superseded as a consequence of the initiation of the CIR Process in relation to the Corporate Debtor in terms of the provisions of I&B Code, 2016.

27. As a consequence of the Application being admitted in terms of Section 7 of the Code, moratorium as envisaged under provisions of Section 14(1) and as extracted hereunder shall follow in relation to the Corporate Debtor;

- (a) the institution of suits or continuation of pending suits or proceedings against the Corporate Debtor including execution of any judgment, decree or order in any court of law, tribunal, arbitration panel or other authority;
- (b) transferring, encumbering, alienating or disposing of by the Corporate Debtor any of its assets or any legal right or beneficial interest therein;
- (c) any action to foreclose, recover or enforce any security interest created by the Corporate Debtor in respect of its property including any action under the



Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002;

- (d) the recovery of any property by an owner or lessor where such property is occupied by or in the possession of the Corporate Debtor.”

28. However during the pendency of moratorium period in terms of Section 14(2) and 14(3) as extracted hereunder;

- (2) The supply of essential goods or services to the Corporate Debtor as may be specified shall not be terminated or suspended or interrupted during moratorium period.
- (3) The provisions of sub – section (1) shall not apply to such transactions as may be notified by the Central Government in consultation with any financial sector regulator.”

29. The duration of period of moratorium shall be as provided in Section 14(4) of the Code which is reproduced below for ready reference;

- (4) The order of moratorium shall have effect from the date of such order till the completion of the Corporate Insolvency Resolution Process

Provided that where at any time during the Corporate Insolvency Resolution Process period, if



the Adjudicating Authority approves the Resolution Plan under sub – section (1) of Section 31 or passes an order for liquidation of Corporate Debtor under Section 33, the moratorium shall cease to have effect from the date of such approval or liquidation order, as the case may be.”

30. Based on the above terms, the Petition stands **admitted** in terms of Section 7 of the Code and the Moratorium shall come into effect as of this date. A copy of the order shall be communicated to the Petitioner as well as to the Respondent above named by the Registry. In addition, a copy of the order shall also be forwarded to IBBI for its records. Further, the IRP above named be also furnished with copy of this order forthwith by the Registry.

-SD-
(ANIL KUMAR B)
MEMBER (TECHNICAL)

-SD-
(R.VARADHARAJAN)
MEMBER (JUDICIAL)

Elz / Raymond