

NATIONAL COMPANY LAW APPELLATE TRIBUNAL, NEW DELHI

Company Appeal (AT) (Insolvency) No. 616 of 2018

[Arising out of order dated 31st August, 2018 passed by the Adjudicating Authority (National Company Law Tribunal), Mumbai Bench in Company Petition No. (1732/I&BP/2018)]

IN THE MATTER OF:

Shailesh Sangani

D/10, Ananta Building,
Dr. Rajjabali Ali Pater Road,
Breach Candy,
Mumbai – 400 026.

...Appellant

Vs

1. Joel Cardoso

601, 6th Floor, Colden Ferns,
Opp. Supari Talao Rebello Road,
Bandra (West),
Mumbai – 400 050.

2. Priority Marketing Private Limited

Having its registered office at
Gala No. 423-B, 4th Floor,
Shah & Nahar Industrial Premises,
Dhanraj Mills Compound,
S. J. Marg, Lower Parel (W),
Mumbai – 400 013.
Represented through its
Resolution Professional Mr. Pranav Damania.

....Respondents

Present:

For Appellant:

Dr. U. K. Chaudhary, Senior Advocate assisted by
Mr. Srisabri, Mr. Mahesh Agarwal, Mr. Rajeev Kumar
and Ms. Swati Sinha, Advocates.

For Respondents:

Mr. Gaurav Mitra and Mr. Rohan Ganpathy,
Advocates.

J U D G M E N T

BANSI LAL BHAT, J.

Appellant is Promoter/Shareholder/Director of Respondent No.2 Company 'Priority Marketing Private Limited' (Corporate Debtor). Being aggrieved of the impugned order dated 31st August, 2018 passed by the Adjudicating Authority (National Company Law Tribunal) Mumbai Bench in Company Petition No. 1732/I&BP/2018 by virtue whereof petition filed by Respondent No. 1 - 'Mr. Joel Cardoso' as a 'Financial Creditor' under Section 7 of the Insolvency and Bankruptcy Code, 2016 (hereinafter referred to as 'I&B Code') has been admitted, moratorium slapped and Interim Resolution Professional appointed with certain directions, has assailed the impugned order primarily on the ground that the amount claimed by Respondent No. 1 is not a 'Financial Debt' within the meaning of Section 5(8) and Respondent No. 1 cannot be treated as a 'Financial Creditor' for the purposes of I&B Code.

2. For better understanding of the controversy involved in this appeal it would be apposite to refer to the factual matrix of the case. Respondent No.1, claiming to be a Shareholder of Respondent No. 2 (hereinafter referred to as Corporate Debtor), filed an application under Section 7 of I&B Code

before the Adjudicating Authority (National Company Law Tribunal) Mumbai Bench, seeking initiation of Corporate Insolvency Resolution Process against the Corporate Debtor on the ground that the Respondent No. 1 had granted unsecured loan repayable on demand from time to time to the Corporate Debtor which stood at Rs.3,23,46,475/- as on 31st March, 2008, major portion whereof was repaid by the Corporate Debtor from year 2008 to 2010 leaving an amount of Rs.1,45,36,475/- as outstanding which was duly reflected in the financial statements of Corporate Debtor and in respect whereof the Corporate Debtor issued balance confirmation as on 1st April, 2016 which was confirmed by the statutory auditor in terms of email dated 5th October, 2017 and since the Corporate Debtor did not repay the aforesaid loan amount, Respondent No. 1 served a notice of demand upon the Corporate Debtor, which was not complied. Corporate Debtor raised the plea before the learned Adjudicating Authority that there were cross holdings inter-se the respondents in various companies and the amounts so arrived at was a settlement amount which had not ended in compliance of mutual obligations between the parties. The Corporate Debtor further stated that the unsecured loan of Rs.1,45,36,475/- was a part of overall settlement and it was ready to settle the cross holding of shares and loans inter-se the Respondents. Respondent further contended that none of the loans under the quasi partnership arrangement inter-se the Respondents had any term for repayment or interest. The learned Adjudicating Authority found that the contention raised on behalf of Corporate Debtor was not plausible as the factum of amount advanced as loan by Respondent no.1 to

Corporate Debtor was admitted and reflected in the accounts and confirmed by the Corporate Debtor. Learned Adjudicating Authority was of the view that the said amount was arrived at after the parties mutually agreed and the same was reflected in the books of the Corporate Debtor under the head 'long term borrowings', the amount of debt fell within the purview of 'financial debt' notwithstanding the fact that no interest was payable. The contention raised by the Corporate Debtor was accordingly repelled.

3. Learned counsel for the Appellant submits that the learned Adjudicating Authority landed in error in holding that the amount claimed by Respondent No.1 for triggering Corporate Insolvency Resolution Process, in respect whereof default on the part of Corporate Debtor was alleged, was not a 'Financial Debt' as defined under Section 5(8) of the I&B Code despite the admitted position that there was no consideration for the time value of money in the transaction. It is further submitted that learned Adjudicating Authority failed to notice that no interest was ever claimed by the Respondent No.1 or paid by the Corporate Debtor to Respondent No.1, that no TDS amount was ever deducted in respect of the part payments made, that there was no tenure for the repayment of amounts granted by Respondent No.1 to Corporate Debtor and that there was no time value of money in the transaction and no consideration for the time value of the money was agreed between the parties at the time of disbursement of moneys by Respondent No.1.

4. Per contra it has been argued on behalf of Respondent No.1 that he had provided moneys to the Corporate Debtor by way of interest free unsecured loans between the period starting on 1st April, 2002 and ending on 29th November, 2007, totalling to Rs.3,23,46,475/-, portion whereof to the tune of Rs.1,78,10,100/- stands repaid by the Corporate Debtor leaving a balance amount of Rs.1,45,36,475/- as outstanding, which is reflected in the balance sheet of the Corporate Debtor as unsecured loan. It is further submitted that by way of confirmation of accounts dated 1st April, 2016, the Corporate Debtor has admitted the outstanding loan amount being due to Respondent No. 1 which is further clarified by the statutory auditor of the Corporate Debtor vide its email dated 5th December, 2017. It is further submitted that there was no partnership or quasi-partnership between the Appellant and Respondent No. 1 and moneys advanced by the Appellant himself to the Corporate Debtor by way of unsecured loans in similar fashion have been repaid by the Corporate Debtor. It is further submitted that the ledger account maintained by the Corporate Debtor clearly reflects the loan amounts provided by Respondent No.1 at different intervals and repayments made to him by the Corporate Debtor. It is further submitted that interest is not the mandatory factor to determine the nature of debt and in the instant case loan provided by Respondent No. 1 to Corporate Debtor being against the consideration for time value of money falls within the purview of 'Financial Debt'. It is submitted that the Corporate Debtor owes a 'financial debt' since the borrowing by the Corporate Debtor from Respondent No.1 is '*an amount raised under any other transaction....xxx...*

having the commercial effect of a borrowing, covered under Section 5(8)(f) of the I&B Code.'

5. We have gone through the record and given our anxious consideration to the submissions made at the Bar. For determination of the issue whether the amount claimed by Respondent No. 1 from the Corporate Debtor, default in payment whereof culminated in initiation of Corporate Insolvency Resolution Process, falls within the purview of 'financial debt' as defined under Section 5(8) of the I&B Code, be it seen that the legal expression 'debt', defined under Section 3 (11) means a liability or obligation in respect of a claim which is due from any person and includes a financial debt and operational debt. It is manifestly clear that the liability or obligation to pay must arise out of a claim due from a debtor/ borrower. The nature of obligation and from where it springs is immaterial. The obligation may be contractual or otherwise. Since, the legal expression 'debt' includes a 'financial debt' across the ambit of I&B Code, it would be appropriate to refer to the definition of legal expression 'financial debt' as engrafted in Section 5(8) of I&B Code, which is reproduced hereinbelow:

"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 non-recourse basis;

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

(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;”

6. A plain look at the definition of ‘financial debt’ brings it to fore that the debt alongwith interest, if any, should have been disbursed against the consideration for the time value of money. Use of expression ‘if any’ as suffix to ‘interest’ leaves no room for doubt that the component of interest is not a sine qua non for bringing the debt within the fold of ‘financial debt’. The amount disbursed as debt against the consideration for time value of money may or may not be interest bearing. What is material is that the disbursement of debt should be against consideration for the time value of money. Clauses (a) to (i) of Section 5(8) embody the nature of transactions which are included in the definition of ‘financial debt’. It includes money borrowed against the payment of interest. Clause (f) of Section 5(8) specifically deals with amount raised under any other transaction having the commercial effect of a borrowing which also includes a forward sale or purchase agreement. It is manifestly clear that money advanced by a Promoter, Director or a Shareholder of the Corporate Debtor as a stakeholder to improve financial health of the Company and boost its economic prospects, would have the commercial effect of borrowing on the

part of Corporate Debtor notwithstanding the fact that no provision is made for interest thereon. Due to fluctuations in market and the risks to which it is exposed, a Company may at times feel the heat of resource crunch and the stakeholders like Promoter, Director or a Shareholder may, in order to protect their legitimate interests be called upon to respond to the crisis and in order to save the company they may infuse funds without claiming interest. In such situation such funds may be treated as long term borrowings. Once it is so, it cannot be said that the debt has not been disbursed against the consideration for the time value of the money. The interests of such stakeholders cannot be said to be in conflict with the interests of the Company. Enhancement of assets, increase in production and the growth in profits, share value or equity enures to the benefit of such stakeholders and that is the time value of the money constituting the consideration for disbursement of such amount raised as debt with obligation on the part of Company to discharge the same. Viewed thus, it can be said without any amount of contradiction that in such cases the amount taken by the Company is in the nature of a 'financial debt'.

7. Adverting to the facts of the instant case be it seen that in the balance sheet of 2009 forming Annexure B of the reply affidavit filed by Respondent No. 1 under the heading 'unsecured loans' name of Respondent no. 1 figures with particulars of loan. Same is extracted as under:-

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| PRIORITY MARKETING PRIVATE LIMITED. Schedules forming part of Balance sheet as at 31st March 2009 | | | |
|--|----------|-------------------|---------------------|
| | Schedule | Amt in Rs. | Amt in Rs. |
| SHARE CAPITAL | | | SCHEDULE : A |
| PARTICULARS | | 31.03.2009 | 31.03.2008 |
| SHARE CAPITAL | | | |
| AUTHORISED : (100,000)100,000 Equity Shares of Rs.10/- each | | 1,000,000 | 1,000,000 |
| ISSUED, SUBSCRIBED AND PAID UP : (100,000)100,000 Equity Shares of Rs.10/- each fully paid | | 1,000,000 | 1,000,000 |
| Total | | 1,000,000 | 1,000,000 |
| RESERVES AND SURPLUS | | | SCHEDULE : B |
| PARTICULARS | | 31.03.2009 | 31.03.2008 |
| Profit & Loss A/c | | | |
| Opening Balance | | 28,234,310 | 21,968,381 |
| Add: Profit for the Year | | 6,732,156 | 6,265,929 |
| Total | | 34,966,465 | 28,234,310 |
| SECURED LOANS | | | SCHEDULE : C |
| PARTICULARS | | 31.03.2009 | 31.03.2008 |
| SECURED LOANS : | | | |
| Yes Bank Limited Cash Credit | | 163,687 | 10,702,528 |
| Citi Bank N.A. Cash Credit | | 16,384,038 | - |
| Citi Bank N.A. W.C.D.L. | | 30,000,000 | - |
| Provision for Interest on OD A/c (Secured against hypothecation of Stock & Debtors) | | 439,315 | - |
| Vehicle Loan | | 1,724,811 | - |
| Total | | 48,711,852 | 10,702,528 |
| UNSECURED LOANS | | | SCHEDULE : D |
| PARTICULARS | | 31.03.2009 | 31.03.2008 |
| UNSECURED LOANS : | | | |
| From Directors / Shareholders | | | |
| Manisha Sangani | | 4,395,720 | 7,145,720 |
| Joel Cardoso | | 14,846,475 | 32,346,475 |
| | | 19,242,195 | 39,492,195 |
| From Others | | | |
| M. Square Silver Pvt. Ltd. | | 3,391,200 | 3,381,200 |
| | | 3,391,200 | 3,381,200 |
| Total | | 22,633,395 | 42,873,395 |



For PRIORITY MARKETING PRIVATE LIMITED

S.H. Sangani
Shailesh Sangani
Director

Manisha Sangani
Manisha Sangani
Director



8. The confirmation of accounts for the period between 1st April, 2015 to 31st March, 2016 forming 'Annexure C' to the reply affidavit reflects an amount of Rs.1,45,36,475/- as balance in the book of accounts in the name of Respondent No. 1. Same is extracted hereinbelow:-

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To : Joel Cardoso - Loan
401, FRANCEDEL,
DR. PETER DIAS ROAD,
BARNDR - WEST
MUMBAI

From: Priority Marketing Pvt Ltd
Unit No. 302, 3rd Floor,
Kamla Executive Park,
J.B. Nagar, Andheri Kuria Road,
Andheri East, Mumbai

Dear Sir/Madam,

Sub: Confirmation of Accounts
1-Apr-2015 to 31-Mar-2016

Dated: 1-Apr-2016

Given below is the details of your Accounts as standing in my/our Books of Accounts for the above mentioned period.
Kindly return 3 copies stating your I.T. Permanent A/c No., duly signed and sealed, in confirmation of the same. Please note that if no reply is received from you within a fortnight, it will be assumed that you have accepted the balance shown below.

| Date | Particulars | Debit Amount | Date | Particulars | Credit Amount |
|------|-------------|--------------|------------|-----------------|----------------|
| | | | 1-Apr-2015 | Opening Balance | 1,45,36,475.00 |

Closing Balance 1,45,36,475.00

I/We hereby confirm the above

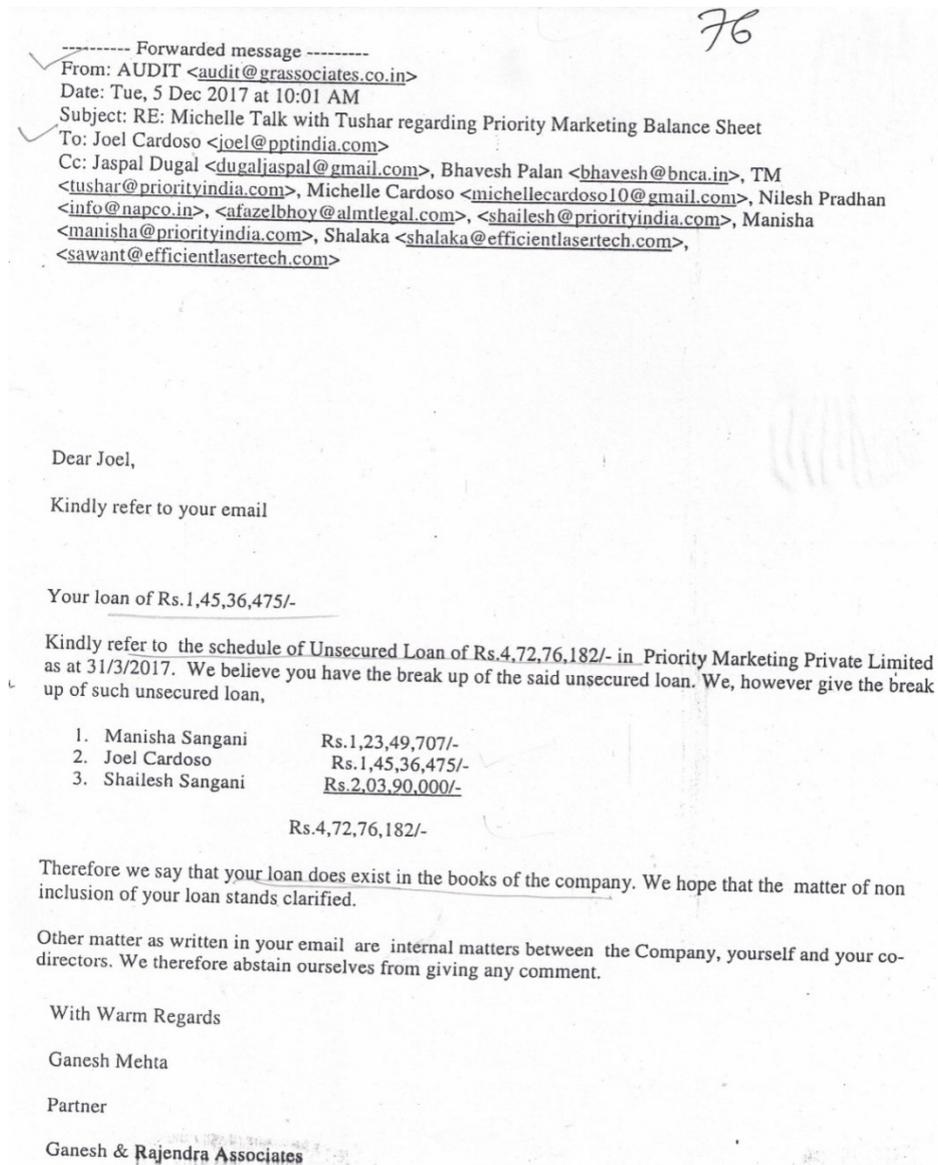
I.T. PAN No. : ABUPC5468P

Yours faithfully,
Authorised Signatory

NOTARY
S. M. H. ZAHEDI
Member of Thane Dist.
Reg. No. 2649
GOVT. OF INDIA

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9. The balance sheet as on 31st March, 2017 at page 83 of the reply affidavit filed by Respondent No.1, inter alia, reflects a non-current liability of Rs.4,72,76,182/- treated as 'long term borrowings' and not treated as shareholder's funds. Same factual position is reflected in the communication made by the Company Auditor 'Ganesh Mehta', Partner 'Ganesh and Rajendra Associates' addressed to Respondent No.1 in his communication dated 5th December, 2017 forming Annexure D to the reply affidavit of Respondent no.1 which is reproduced hereinbelow:-



This communication reflects total unsecured loan of Rs.4,72,76,182/- against the Corporate Debtor in the books of the Company as on 31st March, 2017, the breakup showing the loan amount of Rs.1,45,36,475/- in the name of Respondent No.1.

In the face of this documentary evidence it is abundantly clear that the amount disbursed by Respondent No.1 to the Corporate Debtor was in the nature of debt treated as long term loan and not as an investment in the nature of share capital or equity. Such disbursement cannot either be treated as largesse. We are convinced that the aforesaid amount outstanding as against Corporate Debtor, default whereof is not in issue, has all the trappings of a 'financial debt' and falls within the purview of Section 5(8)(f) of the I&B Code and Respondent No.1 is covered by the definition of 'Financial Creditor'.

10. Learned counsel for the Appellant relied upon judgments of this Appellate Tribunal rendered in '*Dr. B. V. S. Laxmi Vs. Geometrics Laser Solutions Pvt. Ltd.*', Company Appeal (AT) (Insolvency) No. 38 of 2017 decided on 22nd December, 2017 and '*Macksoft Tech Pvt. Ltd. & Ors. Vs. Quinn Logistics India Ltd.*', Company Appeal (AT) (Insolvency) No. 143,175 & 176 of 2017 decided on 21st May, 2018 to buttress his point that the Respondent No.1 is not a 'Financial Creditor'. We have carefully gone through the aforesaid judgments in '*Dr. B. V. S. Laxmi (Supra)*', wherein this Appellate Tribunal noticed that there was nothing on record to suggest that

the Corporate Debtor borrowed the money and the creditor failed to establish that the Corporate Debtor had raised the amount under any other transaction having commercial effect of borrowing. The judgment relied upon, on facts, is distinguishable and is not attracted to the facts of instant case. In *'Macksoft Tech Pvt. Ltd. & Ors. (Supra)'*, this Appellate Tribunal held as under:-

"37. Grant of loan and to get benefit of development is object of the Respondent - ('Financial Creditor'), as apparent from their 'Memorandum of Association'. Thus, we find that there is a 'disbursement' made by the Respondent - ('Financial Creditor') against the 'consideration for the value of money'. The investment was made to derive benefit of development of 'Q-City', which is the consideration for time value of money. Thus, we find that the Respondent - ('Financial Creditor') come within the meaning of 'Financial Creditor' and is eligible to file an application under Section 7, there being a 'debt' and 'default' on the part of the 'Corporate Debtor'."

This judgment also does not support the Appellant's case in as much as it holds that the amount disbursed as loan by a shareholder to derive benefit of development of assets of the Corporate Debtor would be in the nature of a loan disbursed against the consideration for time value of

money. Appellant, therefore, does not gain anything by placing reliance on this judgment.

11. For the foregoing reasons we find no merit in this appeal. There being no infirmity in the impugned order, this appeal is dismissed. There shall be no orders as to costs.

[Justice S. J. Mukhopadhaya]
Chairperson

[Justice Bansi Lal Bhat]
Member (Judicial)

NEW DELHI

30th January, 2019

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