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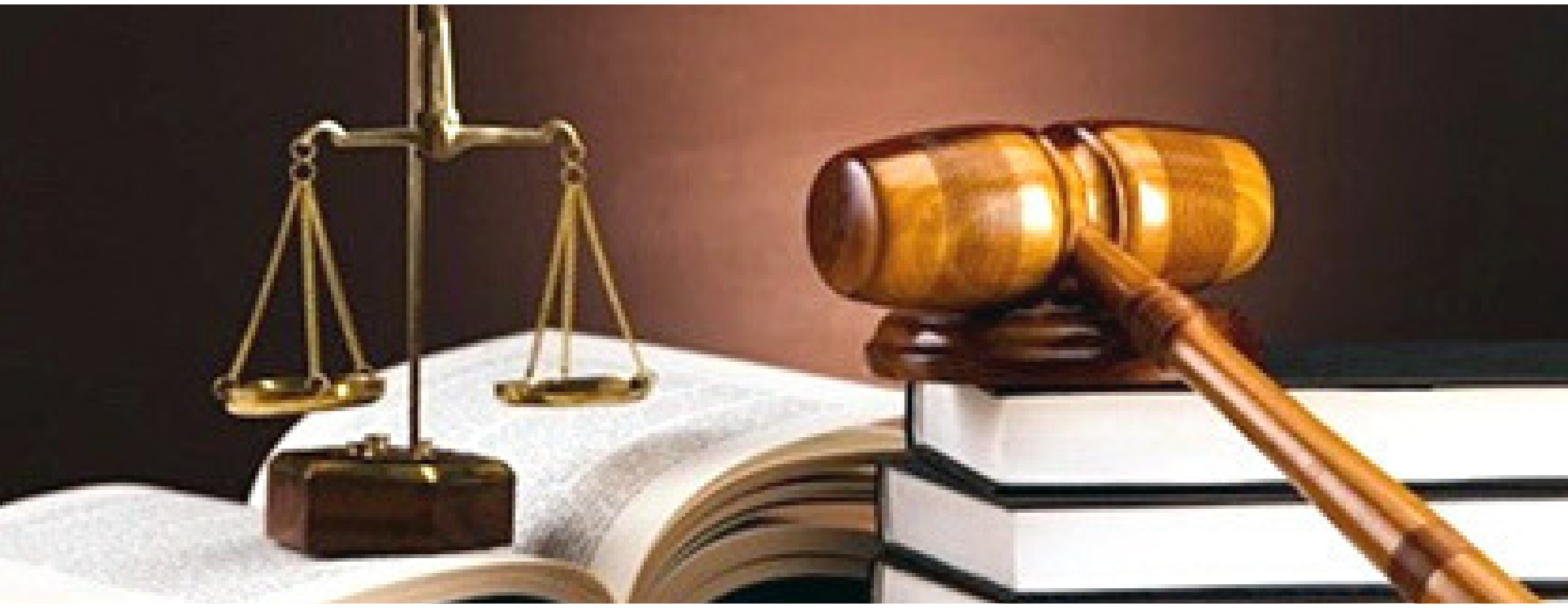

ANUJ JAIN INTERIM RESOLUTION PROFESSIONAL FOR JAYPEE INFRATECH LIMITED VS. AXIS BANK LIMITED ETC. ETC. (CIVIL APPEAL NOS. 8512-8527 OF 2019)

Brief Facts

- Jaiprakash Associates Limited ("JAL") is a Public Listed Company and Jaypee Infratech Limited ("JIL") is its subsidiary.IDBI Bank Limited filed a petition under Section 7 of the Insolvency and Bankruptcy Code, 2016 ("Code") before the National Company Law Tribunal, Allahabad Bench for seeking initiation of CIRP against JIL on default of payment of Rs. 526.11 Crores, which got admitted on 9th August 2017.
- NCLT on 9th May 2018 and 15th May 2018 approved the decision of the IRP of JIL rejecting the claims of the JAL Lenders to be recognized as financial creditors of the Corporate Debtor JIL on the strength of the mortgages created by Corporate Debtor JIL as collateral security of the debt of its holding company JAL.
- NCLT on 16th May 2018 held certain transactions in which JIL had mortgaged its properties as collateral securities for loans and advances made by the JAL Lenders, as being preferential, undervalued and fraudulent under Section 43, 45 and 66 of the Code.
- National Company Law Appellate Tribunal ("NCLAT") on 1st August 2019 by a common order set aside the NCLT order dated 16th May 2018 and also allowed the appeals by the Lenders of JAL to be financial creditors of Corporate Debtor JIL.
- However, the entire NCLAT judgement had only been in relation to the order dated 16th May 2018 passed by NCLT on the application for avoidance filed by the IRP and no reasons were given for reversing the NCLT judgments of 9th May 2018 and 15th May 2018.
- The appeal was preferred against NCLAT order before Hon'ble Supreme Court ("SC")and two major issues that arose before SC are as follows:

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Whether the transactions made by JIL by mortgaging its properties as collateral securities for the loans and advances made by the lender banks and financial institutions to JAL are preferential, undervalued and fraudulent transactions in terms of Sections 43, 45 and 66 of the Code respectively.

Whether the respondents who are the lender of JAL could be recognized as financial creditors of JIL on the strength of the mortgage created by the JIL, as collateral security of the debt of its holding company JAL.

Decision

- SC held that since sub-sections (4) and (2) of Section 44 of the code are deeming provisions, upon existence of the ingredients stated therein, the legal fiction would come into play and such transaction entered into by a corporate debtor would be regarded as preferential transaction, irrespective whether the transaction was in fact intended or even anticipated to be so.
- Clause (a) of sub-section (3) of Section 43 of the Code call for purposive interpretation so as to ensure that the provision operates in sync with the intention of legislature and achieves the avowed objectives. Therefore, the expression "or", appearing as disjunctive between the expressions "corporate debtor" and "transferee", ought to be read as "and"; so as to be conjunctive of the two expressions i.e., "corporate debtor" and "transferee". Thus read, clause (a) of sub-section (3) of Section 43 of the Code shall mean that, for the purposes of sub-section (2), a preference shall not include the transfer made in the ordinary course of the business or financial affairs of the corporate debtor and the transferee. Only by way of such reading of "or" as "and", it could be ensured that the principal focus of the enquiry on dealings and affairs of the corporate debtor is not distracted and remains on its trajectory, so as to reach to the final answer of the core question as to whether corporate debtor has done anything which falls foul of its corporate responsibilities.
- Lenders of JAL on the strength of the mortgages in question, may fall in the category of secured creditors, but such mortgages being neither towards any loan, facility or advance to the corporate debtor nor towards protecting any facility or security of the corporate debtor, it cannot be said that the corporate debtor owes them any 'financial debt' within the meaning of Section 5(8) of the Code and hence such lenders of JAL do not fall in the category of the 'financial creditors' of the corporate debtor JIL.
- SC also clarified that for any debt to be 'financial debt' under the Code, it ought to satisfy the condition of being disbursed against the consideration for time value of money and by any mode of disbursal prescribed for a financial debt under the Code. Since mortgages are not expressly covered under the said definition, the same cannot be viewed as financial debt.
- The Court highlighted an interesting distinction between a person having 'security interest' and a 'financial creditor'. The Court held that for a person to be a 'financial creditor' it needs to be shown that the corporate debtor owes a financial debt to such person. The Court further held that while every 'secured creditor' and every 'financial creditor' is a 'creditor', every 'secured creditor' may not be a 'financial creditor' for the purposes of the Code.
- SC also analysed the unique position that is enjoyed by financial creditors whose stakes are intrinsically inter-woven with the well-being of the corporate debtor and held that in view of the objective of the Code, a person having only a security interest in the corporate debtor, or as in the present case mortgagees, can easily be contrasted with a financial creditor as the former shall only have interest in realising the value of its security rather than simultaneously looking for revival of the corporate debtor.
- Thus, the SC held that persons who are mortgagees securing debts of third parties would not be 'financial creditors' under the Code. In light of this discussion, the Supreme Court held that though the lenders of JAL are secured creditors, they are not financial creditors of JIL.

Link to the Order
https://ibbi.gov.in//uploads/order/907727a75205927c2d2d7689c4ece444.pdf

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