

Supreme Court: Can A Recovery Certificate Holder Initiate The Corporate Insolvency Resolution Process (CIRP)?

written by Juhi Chandel | June 30, 2022



Recovery Certificate Holder

The Supreme Court, vide a judgment dated May 30th 2022, has held that any liability concerning a claim arising out of a Recovery Certificate would be treated as “financial debt” vis-à-vis clause (8) of Section 5 of the Insolvency and Bankruptcy Code (IBC). Consequently, the holder of the Recovery Certificate would be a financial creditor vis-à-vis clause (7) of Section 5 of the IBC. As such, the holder of such a certificate would be entitled to initiate the Corporate Insolvency Resolution Process (CIRP) – *if initiated within a period of three years from the date of issuance of the Recovery Certificate.*

The Brief Facts

The dispute stemmed from the sanction of credit facilities by Ind Bank Housing Limited (hereinafter referred to as ‘IBHL’) to three borrower entities namely, M/s. Green Gardens Pvt. Ltd., M/s. Gemini Arts Pvt. Ltd., M/s. Mahalakshmi Properties & Investments Pvt. Ltd. (hereinafter collectively referred to as ‘borrower entities’) in the year 1993-1994. M/s. Prasad Properties and Investments Pvt. Ltd. (‘the Corporate Debtor’) stood as guarantor/mortgagor by mortgaging its immovable property to secure the credit facilities.

Later, the borrower entities defaulted on the repayment of dues, in response to which IBHL declared them to be Non-performing Assets (NPA) in 1997. Following this, IBHL filed three recovery suits before the High Court of Madras against the borrower entities and the Corporate Debtor. While the suits were pending, IBHL entered into a Deed of Assignment with Kotak Mahindra Bank Limited (‘KMBL’) in 2006, assigning all its title, rights, interests, claims and demands to KMBL.

KMBL and borrower entities subsequently entered into a compromise agreement in 2006. However, borrower entities allegedly failed to make payments as per the compromise agreement. Owing to the said default, KMBL issued a demand notice followed by a possession notice under Section 13(2) and Section 13(4) of the SARFAESI Act, 2002. Subsequently, KMBL issued a Winding Up notice under Section 433 and 434 of the Companies Act, 1956. KMBL also filed applications under Section 31(A) of the RDDBFI Act, 1993 and the same was allowed by a Debts Recovery Tribunal (DRT) vide subsequent orders in 2016.

The DRT also issued separate recovery certificates against each of the borrower entities and Corporate Debtor.

On the basis of the aforesaid Recovery Certificates, KBML, under the capacity of a financial creditor, filed an application under Section 7 of IBC to initiate Corporate Insolvency Resolution Process (CIRP). The National Company Law Tribunal (NCLT), Chennai admitted the application vide order dated September 20th 2019. However, the Corporate Debtor – being aggrieved by the admission order dated September 20th 2019 – filed an appeal before the National Company Law Appellate Tribunal (NCLAT) on the grounds of limitation and the same was allowed vide order dated November 24th 2020. The present appeal was then filed against the impugned order dated November 24th 2020.

Questions of Law

- Whether the petition under Section 7 of the IBC was barred by limitation, on the sole ground that it had been filed beyond a period of 3 years from the date of declaration of the loan account of the Corporate Debtor as a Non-Performing Asset (NPA).
- Whether liability concerning a claim arising out of a Recovery Certificate would be included within the meaning of the term “financial debt” as defined under clause (8) of Section 5 of the IBC.
- Whether KBML is under the capacity to initiate CIRP on account of being a financial creditor.

Ruling

The Hon’ble Court upheld the contentions of the precedent in the *Dena Bank (Now Bank of Baroda) vs C. Shivakumar Reddy and another* where it was held that once a claim fructifies into a final judgment and order/decreed, upon adjudication, and a certificate of recovery is also issued authorizing the creditor to realize its decretal dues, a fresh right allows the creditor to recover the amount specified in the Recovery Certificate.

The Hon’ble Court also held that a liability concerning a claim arising out of a Recovery Certificate would be a “financial debt” within the meaning of clause (8) of Section 5 of the IBC. Thus, the holder of the Recovery Certificate would be a financial creditor within the meaning of clause (7) of Section 5 of the IBC. Therefore, such a “person” would be a “person” as provided under Section 6 of the IBC who would be entitled to initiate the CIRP.

Finally, the Hon’ble Court held that, as per the facts of the present case, the application under Section 7 of the IBC was filed within a period of three years from the date on which the Recovery Certificate was issued. And further, that the application under Section 7 of the IBC was within limitation and NCLAT had erred in holding that it is barred by limitation.

Remarks

In view of the aforesaid discussions and rationale considered by the Hon’ble Court, the question of capacity to file an application under Section 7 of IBC was explored. The pivotal question regarding the admissibility of the application is whether KBML was entitled to be a financial creditor based on the recovery certificates issued by the DRT. It was understood that the Recovery Certificates issued under Section 19(22) of the Debt Recovery Act will be deemed to be a decree or order of the court for the initiation of winding up proceedings.

In light of the pronouncements by the Hon’ble Court, it can be noted that the issuance of recovery certificates by the Debt Recovery Tribunal constitutes

financial debt. Besides, even if there has been a delay in initiating the suit under IBC, a fresh limitation period shall be computed from the date on which the recovery certificate is issued. Thus, based on these views and circumstances, KBML was well within its rights to initiate an application under Section 7 of the Code.

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