

L E X

WITNESS

Volume 11 Issue 1 | August 2019

₹65 US \$6 UK £4



the pondering pill



Krishna Venkat
Co-founding Partner,
Anoma Legal

P46

let's arbitrate



S. Ravi Shankar
Sr. Partner,
Law Senate

P42

in conversation with



Dr. Manoj Kumar
Founder,
Hammurabi & Solomon

P26

expert speak



Prithiviraj Senthil Nathan
Partner,
King Stubb & Kasiva

P28

Your Witness Please!

expert speak



Niraj Singh
Partner, RNS Associates
Rajshree Chaudhary
Associate, RNS Associates

P35

expert speak



Ravneet Kaur
Associate,
Singh & Singh

P22

expert speak

Varsha Banerjee
Partner, Dhir & Dhir Associates
Kunal Godhwani
Associate, Dhir & Dhir Associates

P16



Contractual Rights of Guarantors – Treatment Under The Insolvency & Bankruptcy Code, 2016

■ Varsha Banerjee & Kunal Godhwani

W

ith the coming into force of the Insolvency and Bankruptcy Code, 2016 ('IBC') various issues pertaining to the Guarantors also appeared in the forefront. Since the inception of IBC in December 2016 certain aspects pertaining to the rights and liabilities of the Guarantors have been settled by the Judiciary and necessary amendments have also been carried out by the Parliament to plug loopholes as and when the same emerged to the surface. In case of a company undergoing insolvency proceedings under the IBC, there are two sets of guarantors i.e. Corporate Guarantor and Personal Guarantor.

The first and foremost issue which came up before the Court was whether the moratorium under IBC would extend to personal guarantors of Corporate Debtor. In *Sanjeev Shriya v State Bank of India & Ors*, Allahabad High Court held that a moratorium under section 14 of the IBC would extend to personal guarantors as well, whereas, the Bombay High Court in the matter of *Sicom Investments and Finance Limited vs. Rajesh*

Kumar Drolia & Ors. held that moratorium would not extend to personal guarantors. There was difference of opinion between the Courts which was elevated to the Hon'ble Supreme Court. In the matter of *State Bank of India V. Ramakrishna & Anr*, wherein the Hon'ble Supreme Court finally settled the issue held that no such moratorium is applicable as regards a personal guarantee. Further, the Parliament also simultaneously brought an amendment to the IBC, whereby it clarified that moratorium shall not apply to a surety in a contract of guarantee to a Corporate Debtor.

Subsequently, at the stage of invitation of claim, whether a guarantor who has not invoked his Corporate Guarantee can still file its claim before the Resolution Professional of Corporate Debtor came in light, when the Adjudicating Authority, in the matter of *Axis Bank V. Edu Smart Services Pvt. Ltd.*, held that only the claims which are matured at the stage of initiation of Corporate Insolvency Resolution Process (CIRP) can be filed before the Resolution Professional and as Axis Bank failed to invoke Corporate Guarantee before the initiation of CIRP, their claim being 'un-



D-55, Defence Colony,
New Delhi-110 024.
Tel: 91(11) 42410000,
Fax: 91 (11) 42410091
E:expertspeak@dhirassociates.com



matured' cannot be filed before the Resolution Professional. However, in the appeal, the said view was overturned by Hon'ble NCLAT and it was held that maturity of a claim has no nexus with filing of claim and accordingly, a claim whether matured or not can be filed before the Resolution Professional.

Initially, the Hon'ble NCLAT held that proceedings against Guarantors are legally tenable under the IBC without taking recourse against the Principal Borrower. Thereafter, an issue of simultaneous initiation of CIRP against the

Guarantor(s) for the same very claim emerged, wherein, the Hon'ble Appellate Tribunal in the matter of Dr. Vishnu Kumar Agarwal V. Piramal Enterprises Ltd., held that simultaneous proceedings cannot be filed against the Guarantor(s) for the same amount of claim. However, the said order is now pending before the Hon'ble Supreme Court, wherein, the Hon'ble Supreme Court has passed a status quo order but the final outcome is still awaited.

It is interesting to note that apart from simultaneous initiation of proceedings

against the principal borrower and guarantor, the terms of the Resolution Plan approved in the case of a Corporate Debtor also plays vital role in determining the rights and liabilities of the Guarantors. One might say that such rights of guarantors are protected under the India Contract Act, 1872 and anything in violation to the provisions of Indian Contract Act, 1872 cannot pass a muster under Section 30(2)(e) of the IBC but the judicial approach is divergent as in the matter of State Bank of India vs. V. Ramakrishnan & Anr., the Hon'ble Supreme Court has categorically held that



guarantors cannot take benefit of Section 133 of Contract Act, 1872, and such scaling down of debt of the principal borrower in terms of the Resolution Plan would not relieve the Guarantor for the remainder debt as the guarantor in terms of Section 31 of the IBC is bound by the terms of the Resolution Plan and hence, the Resolution Plan may provide for payments which can be recovered from the guarantor.

Similarly, in case of Sharon-Biomedicine, wherein terms of Resolution Plan, the Committee of Creditors had written-off certain debt qua the principal borrower, the said debt was not written-off qua the guarantors of Sharon bio-medicine which was also approved by the Adjudicating Authority. The guarantors being aggrieved by the said order preferred an appeal on the ground that the guarantor is not liable for any variance between the creditor and principal borrower without his consent in terms of Section 133 of Contract Act and its liability is co-extensive to the

corporate debtor by virtue of Section 128 of Companies Act and hence, any scaling down of debt under resolution plan would result in scaling down of debt qua the guarantor as well, therefore, such resolution plan which provides for waiving off of debt qua principal borrower and not qua guarantor is in contravention to the provisions of the Indian Contract Act and is liable to be set aside. However, the said appeal was dismissed by Hon'ble NCLAT by virtue of Section 31 of the IBC that the guarantors are bound by the terms of the Resolution Plan and even the Hon'ble Supreme Court decided not to interfere with the said order.

CONCLUSION

The provisions of IBC are silent on the aspect of the rights and liabilities of guarantors and on initiation of simultaneous proceedings against the guarantors, it appears that the Resolution of Corporate Debtor will not in any manner absolve the guarantors from discharging their obligations under the Deed of Guarantee.¹⁴



Varsha Banerjee is a Partner and has been in practice for the last 7 years and represents corporate entities, institutional creditors, shareholders etc. She focuses her litigation practice on corporate restructuring and insolvency matters with expertise in the rehabilitation of distressed entities, issues pertaining to recovery of debt, securitization-related matters and commercial disputes arising out of other contractual matters, civil suits and arbitration law arising in cases of distressed entities.



Kunal Godhwani is an Associate and has nearly 4 years of experience in Litigation. He has been handling commercial disputes and regularly appears before Hon'ble High Court of Delhi, various Courts, Tribunals and Forums. He also has extensive experience of appearing in insolvency matters before NCLT and NCLAT.