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SUPREME COURT: TIME-BARRED CLAIMS CANNOT BE BROUGHT UNDER IBC

29 October 2018

On 11 October 2018, the Supreme Court (Court) *vide* its judgment in *B.K. Educational Services Private Limited v Parag Gupta and Associates* (Civil Appeal No. 23988 of 2017) clarified the applicability of Limitation Act, 1963 (Limitation Act) to the Insolvency and Bankruptcy Code, 2016 (Code).

Background

Parag Gupta and Associates, a financial creditor (Respondent) had filed an appeal before the National Company Law Appellate Tribunal (NCLAT) against an order of the National Company Law Tribunal (NCLT) whereby the Respondent's application for initiation of insolvency proceedings under Section 7 of the Code was rejected because it was barred by limitation. *Vide* its judgment dated 07 November .2017, the NCLAT held that the Limitation Act would not be applicable to the initiation of Corporate Insolvency Resolution Process (CIRP), and in cases where the financial and operational creditors are able to reasonably justify their delays in filing applications, the same can be entertained. The decision of NCLAT was challenged by B.K. Educational Services Private Limited, the corporate debtor (Appellant) before the Court.

In the meantime, with effect from 06 June 2018, Section 238A was inserted in the Code *vide* the Insolvency and Bankruptcy Code (Second Amendment) Act, 2018 (Amendment), which provided that the provisions the Limitation Act shall, as far as may be, apply to the proceedings or appeals before the Adjudicating Authority under the Code i.e. NCLT, NCLAT, the Debt Recovery Tribunal; and the Debt Recovery Appellate Tribunal, as the case may be.

In light of this background, the Court was faced with the issue of whether the Limitation Act would apply to applications filed by financial and operational creditors for initiation of CIRP before the Amendment.

Contentions of Parties

The Appellant contended that Limitation Act would apply to applications by creditors under the Code as a time barred debt cannot be held to be 'debt due' so as to trigger the Code. The Appellant further contended that the 'Adjudicating Authority' under the Code is the NCLT, as established under the Companies Act, 2013 (Companies Act), and Limitation Act is applicable to proceedings before NCLT as per Section 433 of Companies Act. Therefore, Limitation Act would be applicable to proceedings under the Code before NCLT as well.

On the contrary, the Respondent contended that applying Section 433 of the Companies Act to proceedings under the Code before the NCLT would lead to incongruous results, as NCLAT is a common appellate forum under three statutes namely, Competition Act, 2002, Companies Act, 2013 and the Code, and Limitation Act cannot be sweepingly applied to proceedings before the NCLAT under all these statutes. The Respondent further contended that Limitation Act only applies to courts and not tribunals, and accordingly, it would not apply to proceedings before the NCLT under the Code. Another contention that was raised by the Respondent was that the Code is a complete Code dealing with insolvency and not debt recovery. It was submitted that while the definition of 'debt' under Section 3(11) of the Code refers to claims that are 'due', 'default' under Section 3(12) of the Code means non-payment of debt that is 'due and payable', which is different from debts 'due and recoverable'. Therefore, even a time barred debt, which is due and payable but not due and recoverable can trigger proceedings under the Code.

Findings of the Court

While rejecting the contentions of the Respondents, the Court made the following observations:

- The Court relied on the Report of the Insolvency Law Committee (Committee) of March 2018 (Report) to cull out the intention of the Code and held that the intention of the Code could not have been to give a new lease of life to stale and time-barred claims, but was solely to clarify that Limitation Act is been applicable to the Code.
- The NCLT, which was established under the Companies Act is the 'Adjudicating Authority' under the Code, and Section 433 of the Companies Act makes Limitation Act applicable to the NCLT. Therefore, Limitation Act would be applicable to proceedings under the Code before the NCLT as well.
- Section 238A of the Code is a clarification of the law and is procedural in nature, and therefore, it is retrospective. The Court observed that the amendment of Section 238A would not serve its object unless it is construed as being retrospective. Otherwise, applications seeking to resurrect time-barred claims would have to be allowed, not being governed by the law of limitation.
- The Court noticed that the expressions 'due' and 'due and payable' under Sections 3(11) and 3(12) refer to a default which is a non-payment of a debt that is due in law, i.e., such debt is not barred by limitation, and even Sections 7 and 8 of the Code make it clear that CIRP can be initiated by a financial or operational creditor in relation to debts which have not become time-barred.
- Rejecting the argument that applying Limitation Act may lead to an anomalous situation, the Court held that even though there is one appellate forum under three statutes, each appeal would be decided keeping in mind the provisions of the particular Act in question.
- The Court also held that Section 60(6) of the Code, which provides for exclusion of period of moratorium in computing the period of limitation for a suit or application against a corporate debtor, would have been wholly unnecessary if the intention of the Legislature was to exclude the application of Limitation Act from the Code.
- While examining section 433 of the Companies Act and Section 238A of the Code, the Court observed that both these provisions make the Limitation Act applicable 'as far as may be', and thus, in the event the Code specifically provides for certain limitation periods, the same would override the Limitation Act.

In view of the above-mentioned reasons, the Court held that Limitation Act is applicable to applications filed by financial and operational creditors under Section 7 and 9 of the Code, from the inception of the Code. The right to sue accrues when a default occurs and if the default occurs over three years prior to the date of filing of the application, the application would be barred by limitation, except in those cases where delay can be condoned by showing sufficient cause under section 5 of the Limitation Act.

Comment

The judgment has laid to rest the uncertainty regarding the time frame within which claims could be brought by financial creditors and operational creditors. Further, the judgment will restrict the number of stale claims made under the Code, especially by operational creditors, where their ability to approach civil courts is restricted by the law of limitation.

The judgment further clarifies that where periods of limitation have been laid down in the Code, the same would apply notwithstanding anything to the contrary contained in the Limitation Act. Accordingly, Section 5 of the Limitation Act, may be invoked to condone delays in filing applications under Section 7 and/or Section 9 of the Code, by showing sufficient cause for the delay. However, Section 5 of the Limitation Act cannot be relied upon to condone delays in filing of appeals under Section 61 of the Code, as a specific period of 30 days (extendable to 45 days) has been provided in the Code for filing of appeals.

Therefore, this judgment is likely to ease the burden on the already overloaded NCLTs and the NCLAT as it would filter the time barred claims.

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