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Insolvency Law Update-Proceedings Against Guarantors

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Insolvency Law Update

Supreme Court upholds NCLAT's (*defined below*) ruling permitting creditors to proceed against a guarantor *de hors* pendency of any Corporate Insolvency Resolution Process ("CIRP") or liquidation proceedings against principal borrower/ Corporate Debtor.

On October 5, 2021 the National Company Law Tribunal Kolkata Bench ("NCLT") had rejected an application filed by State Bank of India ("Financial Creditor") under Section 95(1) of the Insolvency and Bankruptcy Code, 2016 ("IBC") against a personal guarantor.¹ The NCLT observed that as per Section 60(2) of the IBC, an Insolvency Resolution Process can be initiated against a guarantor only when CIRP or liquidation process is pending against the principal borrower/Corporate Debtor and since, that requirement was not satisfied, the application was held to be premature and was dismissed.

On appeal, the National Company Law Appellate Tribunal, Principal Bench at New Delhi ("NCLAT") set aside the NCLT's order.² The NCLAT observed that Section 60(2) of the IBC is without prejudice to Section 60(1) *thereof*. Accordingly, as per Section 60(1) of IBC, even when no CIRP or liquidation proceedings are pending against a principal borrower/ Corporate Debtor, an application against its guarantor can still be filed in the NCLT which has territorial jurisdiction over the place where the registered office of principal borrower/ Corporate Debtor is situated. The NCLAT further clarified that the purpose and object of Section 60(2) of IBC is that when CIRP or liquidation proceedings are pending in a particular NCLT against a Corporate Debtor, any proceeding against its guarantor should also be filed before the same NCLT (*idea being both proceedings are tried by same NCLT*), and this does not in any way prohibit filing of proceedings under Section 95 of the Code even if no proceedings are pending before NCLT against the Corporate Debtor.

The above judgment of the NCLAT was carried in appeal to the Supreme Court. While initially *vide* order dated March 21, 2022³, the Supreme Court had stayed the operation of the NCLAT's order by relying on the decision of *Lalit Kumar Jain vs. Union of India & Ors.* [2021 (9) SCC 231], subsequently the

¹ https://nclt.gov.in/gen_pdf.php?filepath=/Efile_Document/ncltdoc/casedoc/1908134028762021/04/Order-Challenge/04_order-Challenge_004_1635744092928579657617f795c73710.pdf

² <https://ibbi.gov.in/uploads/order/2022-01-28-124013-g0wpl-26414f3846632f4c82d397e67e510d1f.pdf>

³ https://main.sci.gov.in/supremecourt/2022/6511/6511_2022_37_18_34352_Order_21-Mar-2022.pdf

Supreme Court on May 6, 2022⁴ dismissed the appeal filed by the guarantor and held that the NCLAT judgment does not warrant any interference.

While the Supreme Court in a previous judgment⁵ had held that a moratorium declared under Section 14 of the IBC against a Corporate Debtor would not apply to a guarantor by relying on Insolvency Law Committee's report dated March 26, 2018 which concluded that Section 14 does not intend to bar actions against assets of guarantors to the debts of the corporate debtor in view of the principle of co-extensive liability enshrined in Section 128 of the Contract Act, 1872; the recent order of the Supreme Court refusing to interfere with the NCLAT judgment also removes any confusion which may have existed on the approach to be adopted by Creditors to either first proceed against the principal borrower/ Corporate Debtor or the guarantor.

⁴ https://main.sci.gov.in/supremecourt/2022/6511/6511_2022_7_48_35604_Order_06-May-2022.pdf

⁵ https://ibbi.gov.in/webadmin/pdf/order/2018/Aug/11958_2018_Judgement_14-Aug-2018_2018-08-14%2022:04:34.pdf