Insolvency and Bankruptcy Board of India
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27th February, 2020

Subject: Judgment[1] dated 26th February, 2020 of the Hon'ble Supreme Court of India in the matter of *Anuj Jain Interim Resolution Professional for Jaypee Infratech Limited Vs Axis Bank Limited Etc. Etc.* [Civil Appeal Nos. 8512-8527 of 2019 and other petitions]

While setting aside the judgment dated 1st August, 2019 of the NCLAT on avoidance of certain transactions under section 43, 45 and 66 of the Code whereby CD had mortgaged its properties for the financial assistance to JAL (holding company), the Hon'ble Supreme Court settled several issues and made important rulings as under:

Sl. No.	Issue/ Theme	Rulings	Para / Page No.
1.	Analysis of sections 43 and 44.	a. Provisions of sections 43 and 44 need to be strictly construed towards achieving the object of these provisons.	18/65
		b. For a transaction to fall within the mischief sought to be remedied by sections 43 and 44 of the Code, it ought to be a preferential one answering to the requirements of sub-section (2) of section 43; and the preference ought to have been given at the relevabnt time, as specified in sub-section (4) of section 43.	18.2/67
		c. A CD shall be deemed to have given preference at a relevant time if the twin requirements of clauses (a) and (b) of sub-section (2) coupled with either clause (a) or clause (b) of sub-section (4), as the case may be, are satisfied.	19/68
		d. Since sub-sections (2) and (4) of section 43 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 with the attendant consequences as per Section 44 of the Code, irrespective whether the transaction was in fact intended or even anticipated to be so.	19.3/72
		e. In order to find as to whether a transaction, of transfer of property or an interest thereof of the corporate debtor, falls squarely within the ambit of Section 43 of the Code, ordinarily, the following questions shall have to be examined in a given case: (i). As to whether such transfer is for the benefit of a creditor or a surety or a guarantor? (ii). As to whether such transfer is for or on account of an antecedent financial debt or operational debt or other liabilities owed by the corporate debtor? (iii). As to whether such transfer has the effect of putting such creditor or surety or guarantor in a beneficial position than it would have	20/73

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			been in the event of distribution of assets being made in accordance with Section 53? (iv). If such transfer had been for the benefit of a related party (other than an employee), as to whether the same was made during the period of two years preceding the insolvency commencement date; and if such transfer had been for the benefit of an unrelated party, as to whether the same was made during the period of one year preceding the insolvency commencement date? (v) As to whether such transfer is not an excluded transaction in terms of sub-section (3) of Section 43?	
2.	Whether impugned transactions are preferential, falling within section 43(2)	a. b. c.	It is true that there had not been any creditor-debtor relationship between the lender banks and corporate debtor JIL but that will not be decisive of the question of the ultimate beneficiary of these transactions. The mortgage deeds in question, entered by the CD JIL to secure the debts of JAL, obviously, amount to creation of security interest to the benefit of JAL. JAL as holding company of CD, is a creditor and also surety of CD. It is a related party to CD. The CD owed antecedent financial debts as also operational debts and other liabilities towards JAL. The impugned transactions had been of transfers for the benefit of JAL, who is a related party of the corporate debtor JIL and is its creditor and surety by virtue of antecedent operational debts as also other facilities extended by it; and the impugned transactions have the effect of putting JAL in a beneficial position than it would have been in the event of distribution of assets being made in accordance with Section 53 of the Code. Thus, the corporate debtor JIL has given a preference in the manner laid down in sub-section (2) of Section 43 of the Code.	22.2.1/77 22.2.2/78 22.5/80
3.	Look back period in terms of section 43(4)	a. b. c. d.	By virtue of proviso to sub-section (3) of Section 1 of the Code, different dates can be provided for enforcement of different provisions of the Code; and in fact, different provisions have been brought into effect on different dates. However, after coming into force of the provisions, if a look-back period is provided for the purpose of any particular enquiry, it cannot be said that the operation of the provision itself would remain in hibernation until such look-back period from the date of commencement of the provision comes to an end. There is nothing in the Code to indicate that any provision in Chapter II or Chapter III be taken out and put in operation at a later date than the date notified. Such contentions being totally devoid of substance, deserve to be, and are, rejected. As noticed, the preference is given to JAL who is related party of JIL. Hence, the look-back period is two years preceding insolvency commencement date i.e., 09.08.2017 as per section 43(4)(a). Therefore, the transaction commencing from 10.08.2015 until the date of insolvency commencemnet shall fall under the scanner. The contention of respondents that most of the mortgages were not creation of new encumbrance by JIL as the properties were already mortgaged and during that period they were only re-mortgaged. Such contention was not accpeted as so called re-mortagage is only as a fresh mortgage The transaction in question had been of deemed preference to related party JAL by the coporate debtor JIL during the look back period of two years and covered under section 43(4).	23.1.2/84 24/84 24.3.1/86 24.5/89

	Ordinary Course of Business or financial affairs	a. "*we have no hesitation in accepting the submissions made on behalf of the appellants that the said contents of clause (a) of sub-section (3) of Section 43 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 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."* b. It remains trite that an activity could be regarded as 'business' if there is a course of dealings, which are either actually continued or contemplated to be continued with a profit motive. c. Even when furnishing a security may be one of normal business practices, it would become a part of 'ordinary course of business' of a particular corporate entity only if it falls in place as part of 'the undistinguished common flow of business done'; and is not arising out of 'any special or particular situation'. d. The ordinary course of business or financial affairs of the corporate debtor JIL cannot be taken to be that of providing mortgages to secure the loans and facilities obtained by its holding company and that too at the cost of its own financial health. As noticed, JIL was already reeling under debts with its accounts with some of the lenders having been declared NPA; and it was also under heavy pressure to honour its commitment to the home buyers. In the given circumstances, we have no hesitation in concluding that the transfers in questions were not made in ordinary course of business or financial affairs of the corporate debtor JIL. e. The transactions are hit by section 43 of the Code and AA rightly held so.	25.5/94-95 25.6.1/95-96 25.6.2/96 25.6.2/97-98 27/100
4.	Duties and responsibilities of RP in CIRP as per section 25 w.r.t. section 43	a. The RP is ordinarily required to do as illustrated, step wise: 1. In first place, shifting through the entire cargo of transactions relating to the property or an interest of CD backwords from the date of commencement of CIRP and upto the preceding two years.The other step shall be identifying the persons involved in such transactions and of putting them in two categories; one being of the persons who fall within the definition of 'related party' in terms of section 5(24) and another of the remaining persons; 2. Then, the RP ought to identify as to in which of the said transactions of preceding two years, the beneficiary is related party of the CD and in which the beneficiary is not a related party, with each sub-	28.1/101-104

		set requiring different analysis. The sub-set concering unrelated party/ parties shall further be trimmed to include only the transactions of preceding one year from the date of commencement of insolvency; 3. After having two sub-set, the further steps would be to examine every transaction in each of these sub-sets to find :(i) as to whether the transaction is of transfer of property or an interest thereof of the CD; and (ii) as to whether the beneficiary involved in the transaction stands in the capacity of creditor or surety or guarantor qua the CD. These steps shall lead to shortlisting of such transactions which carry the potential of being preferential; 4. The said shortlisted transactions would be scrutinised to find if the transfer in question is made for or on account of an antecedent financial debt or operational debt or other liability owed by the CD. The transactions which are so found would be answering to secetion 43(2)(a); 5. Such of the scanned and scrutinised transactions that are found covered by section 43(2)(a) shall have to be examined on another touchstone as to whether the transfer in question has the effect of putting such creditor or surety or guarantor in a beneficial position than it would have been in the event of distribution of assets per Section 53 of the Code. If answer to this question is in the affirmative, the transaction under examination shall be deemed to be of preference within a relevant time, provided it does not fall within the exclusion provided by sub-section (3) of Section 43; 6. Then, the transaction which otherwise is to be of deemed preference, will have to pass through another filtration to find if it does not answer to either of the clauses (a) and (b) of sub-section (3) of Section 43; 7. After the resolution professional has carried out the aforesaid volumetric as also gravimetric analysis of the transactions on the defined coordinates, he shall be required to apply to the AA for necessary order/s in relation to the transaction/s that had passed through all the positive tests of sub-section (4) and sub-section (2) as also negative test of sub-section (3) of section 43. b. AA after steps taken by RP and application to it, shall have to examine if the referred transactions answers to all the descriptions noted above and shall then decide to what order is required to be passed for aviodance of such transactions.	28.2/104
5.	Undervalued and fraudulent transactions	a. As the transactions are held as preferential, the other aspects such as undervalued and fraudulent are not considred to be examined. The said questions are open in appropriate case; b. However, the combined application under section 43, 45 and 66 should not have filed as the degree of examination in preferential and undervalued & fraudulent are different. In preferential transaction, the intent is not involved by virute of legal fiction of deeming provision, whereas for undervalued transaction requires a different enquiry under section 45 and 46 in which AA to require to examine the intent if such undervalued transactions was to defraud the creditors. c. Specific material facts are required to be pleaded if a transaction is sought to be brought under the mischief sought to be remedied by Sections 45/46/47 or Section 66. The AA would have examined the aspect of preferential , undervalued and fraudulent separately and distintively.	29/104 29.1/105 29.1/106

6.	Whether lenders of JAL could be categorised as FCs of JIL	a. It is the FC who lends finance on a term loan or for working capital that enables the CD to set up and/or operate its business; and who has specified repayment schedules with default consequences. The most important feature, as this Court has said, is that an FC is, from the very beginning, involved in assessing the viability of the CD who can, and indeed, engage in restructuring of the loan as well as reorganisation of the CD's business when there is financial stress. Hence, an FC is not only about in terrorem clauses for repayment of dues; it has the unique parental and nursing roles too. In short, the FC is the one whose stakes are intrinsically inter-woven with the well-being of the CD.	39.3/133
		b. The expressions "means and includes" in the definition clauses of section 5(7) and 5(8) of Financial creditor and financial debt respectively-As noticed, in the case of *Pioneer Urban*, a suggestion made on behalf of the respondents with reference to the decision in *Krishi Utapadan Mandi Samiti*, that when the words 'means and includes' are used in a definition, they are to be given a wider meaning and are not exhaustive or restricted to the items contained therein, was not accepted by this Court; and the statement of law in *Krishi Utapadan Mandi Samiti* was held to be not that of good law for it ignored the earlier precedents of larger and coordinate Benches and was also out of sync with the later decisions on the same point. However, the other extreme of interpretation, as canvassed by the petitioners, that a financial debt could only be a debt which is disbursed against the consideration for the time value of money, and such requirement pervades all sub-clauses (a) to (i) of section 5(8), was also not accepted as a matter of statutory interpretation by this Court while observing that the expression 'and includes' speaks of subject matters which may not necessarily be reflected in the main part of the definition. Thus, it is evident that this Court did not accept either of the extremities suggested by the parties in *Pioneer Urban* for interpretation and implication of the expressions 'means and includes' in a definition clause of the statute. Significantly, in *Pioneer Urban*, none of the extremities had any bearing on the conclusion because, eventually, the amendment in question was held to be only clarificatory in nature; and this Court held that the Explanation added to Section 5(8)(f) of the Code by the Amendment Act did not enlarge the scope of the original Section.	42.1/148
		c. Essentials for financial debt and financial creditor-the definition, by its very frame, cannot be read so expansive, rather infinitely wide, that the root requirements of 'disbursement' against 'the consideration for the time value of money' could be forsaken in the manner that any transaction could stand alone to become a financial debt. In other words, any of the transactions stated in the said subclauses (a) to (i) of Section 5(8) would be falling within the ambit of 'financial debt' only if it carries the essential elements stated in the principal clause or at least has the features which could be traced to such essential elements in the principal clause.	43/153
		d. A person having only security interest over the assets of corporate debtor (like the instant third party securities), even if falling within the description of 'secured creditor' by virtue of collateral security	47.2/157

			extended by the corporate debtor, would nevertheless stand outside the sect of 'financial creditors' as per the definitions contained in subsections (7) and (8) of Section 5 of the Code. Differently put, if a corporate debtor has given its property in mortgage to secure the debts of a third party, it may lead to a mortgage debt and, therefore, it may fall within the definition of 'debt' under Section 3(10) of the Code. However, it would remain a debt alone and cannot partake the character of a 'financial debt' within the meaning of Section 5(8) of the Code. e. Such 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.	54/171