NATIONAL COMPANY LAW APPELLATE TRIBUNAL,
PRINCIPAL BENCH, NEW DELHI

Company Appeal (AT) (Insolvency) No. 1614 of 2023

[Arising out of Order dated 17.10.2023 passed by the Adjudicating Authority (National Company Law Tribunal), Mumbai Bench-I in IA No.2909 of 2023 in CP (IB) No. 162/MB/2023]

In the matter of:

Sainik Industries Private Limited **....Appellant**

Vs.
Ritesh Raghunath Mahajan, RP, **...Respondent**
Indian Sugar Manufacturing Company Limited

For Appellant: Mr. Krishnendu Datta, Sr. Advocate with Mr. Anand Varma, Ms. Apoorva Pandey, Advocates.
For Respondent: Mr. Rohit Gupta, Mr. Ramchandra Madan, Advocates for RP

JUDGMENT
(11th January, 2024)

Ashok Bhushan, J.

This Appeal has been filed challenging the order dated 17.10.2023 passed by the Adjudicating Authority (National Company Law Tribunal), Mumbai Bench-I in IA No. 2909 of 2023 filed by the Appellant claiming admission of claim as Financial Creditor which has been rejected by the Adjudicating Authority by the impugned order.

2. Brief facts of the case necessary to be noticed for deciding this Appeal are:-

2.1. Appellant engaged in the business of purchasing sugar from various sugar factories, corporate companies and selling said sugar to sugar brokers,

consumers, confectioneries etc. The Respondent- 'M/s. Indian Sugar Manufacturing Company Limited' (Corporate Debtor) is engaged in the business of manufacturing and sale of sugar. An Agreement dated 28.07.2016 was entered between the Appellant and the Corporate Debtor for supply of 5200 M.T of sugar produced in the crop year 2016-2017. Agreement contained certain other clauses providing for penalty in event the second party refuses or fail to deliver the entire/part quantity of sugar. Agreement also contemplated giving of security cheques by the Corporate Debtor towards refund of advance amount. Appellant advanced an amount of Rs.10 Crores in the year 2016 to the Corporate Debtor. Upon failure of the Corporate Debtor to meet its obligations, Appellant issued a legal notice dated 31.01.2017 calling upon the Corporate Debtor to pay applicable interest and damages. Corporate Debtor having failed to deliver sugar as well as making payment of applicable interest, Appellant deposited the security cheques which were dishonoured. Consequently, Appellant initiated proceedings under Section 138 of the Negotiable Instruments Act, 1881 against the Corporate Debtor. Appellant filed a Company Petition No. 469 of 2020 against the Corporate Debtor under Section 9 of the Code seeking initiation of the CIRP of the Corporate Debtor. In Company Petition No. 469 of 2020, notices were issued on 06.02.2020 by the Adjudicating Authority. Appellant also filed Commercial Suit No.474 of 2019 against the Corporate Debtor seeking grant of money decree of an admitted amount of Rs.19,55,30,723/-. A summary judgment was awarded on 12.01.2023 for an amount of Rs.3,75,35,765/-. On an application filed under Section 7 by 'Saisidha Sugar Equipments and Engineering Company Pvt. Ltd.', CIRP against the Corporate Debtor was

initiated by the order dated 23.03.2023 of the Adjudicating Authority. Appellant on 01.06.2023 submitted claim in Form C to the IRP classifying its debt of Rs.34,65,36,490/- as a Financial Debt. Resolution Professional on 05.06.2023 by e-mail rejected the claim of the Appellant as Financial Creditor and categorised the claim of the Appellant as Operational Debt. Aggrieved by the refusal of the IRP to admit the claim as Financial Debt, Appellant filed an IA No.2909 of 2023 before the Adjudicating Authority seeking direction to the IRP to claim as Financial Debt.

2.2. Company Petition No. 469 of 2020 filed by the Appellant under Section 9 was dismissed as infructuous by order dated 28.08.2023. CIRP against the Corporate Debtor having already commenced by order dated 23.03.2023, the Adjudicating Authority heard IA No. 2909 of 2023 and by impugned order has dismissed the said application. Appellant aggrieved by the said order has come up in this Appeal.

3. Shri Krishnendu Datta, Learned Senior Counsel appearing for the Appellant submits that the Adjudicating Authority committed error in appreciating the real nature of transaction between the parties and has erroneously held that the claim of the Appellant is an operational debt whereas terms and conditions of the Agreement between the parties made it clear that it was financial debt. It is submitted that the Clauses 2, 4, 5, 6, 7 and 11 in the Agreement dated 28.07.2016 clearly indicate that the Corporate Debtor owed a financial debt to the Appellant. It is submitted that the Adjudicating Authority has relied on the judgment of the Hon'ble Supreme Court in ***"Consolidated Construction Consortium Limited vs. Hitro***

Energy Solutions Private Limited- (2022) 7 SCC 164" which judgment was not applicable in the facts of the case. Since in the above case there was only advance given and clauses which are contained in the Agreement between the parties was absent in the said case, hence, the judgment of the Hon'ble Supreme Court in the above case was not applicable. It is submitted that the test laid down by the Hon'ble Supreme Court in ***"Pioneer Urban Land and Infrastructure Limited and Anr. vs. Union of India and Ors.- (2019) 8 SCC 416"*** regarding establishment of financial debt were fully proved in the facts of the present case and the Adjudicating Authority committed error in holding otherwise. Counsel for the Appellant has also referred to the judgment of this Tribunal in Company Appeal (AT) (Insolvency) No. 19 of 2019- ***"N.S. Rangachari vs. Consolidated Construction Consortium Ltd."*** which gave rise to the judgment of the Hon'ble Supreme Court in *'Consolidated Construction Consortium Limited' (supra).*

4. Learned Counsel appearing for the Resolution Professional refuting the submissions of the Counsel for the Appellant contends that the transaction between the parties was a transaction for supply of sugar and the debt arising out of such transaction is clearly as operational debt within the definition of 'operational debt' under Section 2(21) of the Code. It is submitted that the Appellant himself has filed Section 9 application claiming its operational debt which application being CP No.469 of 2020 was dismissed on 28.08.2023 as infructuous. It is submitted that the Appellant cannot be allowed to change his stand and contend that the debt is a financial debt. It is submitted that the terms and conditions of the Agreement between the parties clearly indicate

that the nature of transaction was transaction for supply of goods and services. The provision in the Agreement to give security is not uncommon even in cases of supply of goods and services, merely because security has been given by the Corporate Debtor it does not lead the transaction to a financial transaction.

5. We have considered the submissions of the Counsel for the parties and perused the record.

6. 'Financial Debt' is defined in Section 5(8) of the Code, which is as follows:-

> *"**5. Definitions. –(8)** "financial debt" means a debt alongwith interest, if any, which is disbursed against the consideration for the time value of money and includes–*
> *(a) money borrowed against the payment of interest;*
> *(b) any amount raised by acceptance under any acceptance credit facility or its dematerialised equivalent;*
> *(c) any amount raised pursuant to any note purchase facility or the issue of bonds, notes, debentures, loan stock or any similar instrument;*
> *(d) the amount of any liability in respect of any lease or hire purchase contract which is deemed as a finance or capital lease under the Indian Accounting Standards or such other accounting standards as may be prescribed;*
> *(e) receivables sold or discounted other than any receivables sold on non-recourse basis;*

(f) any amount raised under any other transaction, including any forward sale or purchase agreement, having the commercial effect of a borrowing;

*[**Explanation.** -For the purposes of this sub-clause, -*

(i) any amount raised from an allottee under a real estate project shall be deemed to be an amount having the commercial effect of a borrowing; and

(ii) the expressions, "allottee" and "real estate project" shall have the meanings respectively assigned to them in clauses (d) and (zn) of section 2 of the Real Estate (Regulation and Development) Act, 2016 (16 of 2016);]

(g) any derivative transaction entered into in connection with protection against or benefit from fluctuation in any rate or price and for calculating the value of any derivative transaction, only the market value of such transaction shall be taken into account;

(h) any counter-indemnity obligation in respect of a guarantee, indemnity, bond, documentary letter of credit or any other instrument issued by a bank or financial institution;

(i) the amount of any liability in respect of any of the guarantee or indemnity for any of the items referred to in sub-clauses (a) to (h) of this clause;"

7. 'Operational Debt' has been defined in Section 5(21) of the Code in following words:-

> *"**5. Definitions. –(21)** "operational debt" means a claim in respect of the provision of goods or services including employment or a debt in respect of the [payment] of dues arising under any law for the time being in force and payable to the Central Government, any State Government or any local authority;"*

8. The definition of 'operational debt' as contained above indicates that a claim ***in respect of the provision of goods or services*** is operational debt. Thus, any claim in respect of the provision of goods or services falls within the definition of operational debt.

9. The moot question to be answered in this Appeal is the nature of transaction between the parties as is reflected in the Agreement dated 28.07.2016. The Agreement contained a heading "Supply Agreement/Loan Agreement-1". The Agreement mentions that in the Agreement, the Appellant is first party and the Corporate Debtor is second party. We may notice following statement in the Agreement describing both the parties which is at Page 69 of the Appeal:-

> *"Whereas the Party of the First Part is engaged in the business of purchasing sugar from various sugar factories, corporate companies and sale said sugar to sugar brokers, consumers, confectioneries, retail market, domestic market, Government supplies, export through Road transport as well as Railway wagons/Rakes as per the requirement of the clients.*

> ***AND WHERAS*** *the Party of Second Part is engaged in the business of Manufacturing and sale of sugar in the domestic market as well as for exports.*
>
> *And WHEREAS the Party of second part has approached to the party of first part and requested for supply of 5200 MT's of sugar against the advance amount of RS 10,00,00,000/- (ten Crore) by way of this agreement"*

10. Nature of Agreement entered between the parties has also been described in Agreement in following words:-

> *"Whereas parties of the first part as well as party of the second part have entered into an agreement (White Sugar Supply Agreement) as per which the party of the second part confirms and agrees to sell and deliver to the party of the first part 5200 M.T's of white crystal sugar S-30 grade packed in P.P. bags of 50 KG's net weight at a fixed price of 3215/- per quintal inclusive of excise duty and cess (i.e. 3020 + 195) by and before 20.11.2016 (hereinafter referred as due date).*
>
> *Now, the second party has issued a sale order no. Ref No- ISMCL/Acct/Sugar sale / 2016-17/0198 dated 27.7.2016 and attached as annexure-1 to this agreement."*

11. The above statement in the Agreement clearly indicates that the parties have entered into an Agreement for sale and delivering of 5200 M.T of white crystal sugar.

12. Learned Counsel for the Appellant has relied on various conditions in the Agreement in support of the submission which we noticed as follows:-

> *"2. That it is specifically agreed between the parties that in case the party of the second part refuses or fails to deliver the entire / part quantity of sugar by and before 28.02.2016 as agreed between the parties in terms of this agreement i.e. 5200 M.T's or less then the party of the first part shall be entitled to obtain a penalty @6000 Per MT for 5200 Mts which equals to an amount of Rs. 3,12,00,000/- (Three Crores Tweleve lacs only) from the party of the second part, fully or proportionately as the case may be.*
>
> *4. That it is also agreed and confirmed by the second party that besides the above mentioned amount, the party of the first part shall be entitled to receive and recover the difference in price (i.e. market price of sugar minus the agreed price of this contract), if any applicable, in case the price of sugar increases from the present agreed price and the party of the second part refuses/fails to supply the sugar at such increased rates on or before the due date, on the quantity not delivered and supplied by the second party.*
>
> *5. That it is also agreed between the parties that in case of default by the second party in adjustment of advance, the second party of the second part shall also pay the above mentioned amount along with interest at the rate of Rs. 30/-PMT per day till refund of the advance amount from the date of this agreement up to 28.02.2017. The payment of interest remains independent and in addition of the second party*

commitment to supply agreed quantities of sugar at the agreed prices as mentioned above.

7. That it is further agreed between the parties that the party of the second part have issued towards security, the undated two cheques for Rs.5 each towards the refund of advance amount along with 3.12 cores discount as security for the supply of 5200 MT of sugar. Further second part has issued the cheque of Rs 17835480.00 as delay/interest @ Rs 33.33 per MT per day from 15.11.2016 to 28.02.2017. The cheques details are more specifically described in annexure -2 of this agreement.

11. That as a collateral security, the second party shall also pledge 10% of its equity share capital with the first party vide a separate agreement and in case the second party defaults on any provisions of this agreement, the first shall automatically be entitled for a right to sell the pledged shares to such person at such price and such terms and condition as it may deem fit without any obligation for prior information to the second party. This clause will be applicable only after 1.3.2017 onwards."

13. At this stage, we may notice the judgment of the Hon'ble Supreme Court in ***'Consolidated Construction Consortium Limited' (supra)*** where the Hon'ble Supreme Court had occasion to consider the provision of Section 5(21) i.e. operational debt. The undisputed facts of the said case have been captured by the Hon'ble Supreme Court in paragraph 47, which is as follows:-

"47. In the present case, there are few undisputed facts:

47.1. The appellant and the proprietary concern entered into a contract for supply of light fittings, since the appellant had been engaged for a project by CMRL.

47.2. CMRL, on the appellant's behalf, paid a sum of Rs 50 lakhs to the proprietary concern as an advance on its order with the appellant.

47.3. CMRL cancelled its project with the appellant.

47.4. The proprietary concern encashed the cheque for Rs 50 lakhs anyways.

47.5. The appellant paid the sum of Rs 50 lakhs to CMRL."

14. One of the questions was as to whether the advance payment made to the proprietary concern would fall within the definition of operational debt. This Appellate Tribunal has rejected the claim of operational debt holding that the IBC only includes those who supply goods or services to the Corporate Debtor. The view of the Appellate Tribunal was reversed and the Hon'ble Supreme Court held that the operational debt is a claim in respect of the provision of goods or services. In paragraphs 49, 50, 50.1, 50.2 and 50.3 are as follows:-

"49. We have to now consider the "debt" in the present appeal. According to the appellant, it is the advance payment CMRL made on their behalf to the

proprietary concern, which was encashed even though the project between a CMRL and the appellant was terminated. On the other hand, the respondent has attempted to urge that there was no privity of contract between the appellant and the respondent, and that CMRL had not transferred the debt to the appellant. We reject both these submissions. It is amply clear from the facts that the debt arises from purchase orders between the appellant and the proprietary concern (which is the underlying contract), regardless of whether CMRL may have made the b payment on behalf of the appellant. Thus, the ultimate dispute still remains between the appellant and the proprietary concern, and the debt arises from that.

50. It is then that we come to the core of the dispute while the appellant has argued that the debt is in the nature of an operational debt which makes them an operational creditor, the respondent has opposed this submission. The respondent's submission, which was accepted by NCLAT, seeks to narrowly define "operational debt" and "operational creditors" under the IBC to only include those who supply goods or services to a corporate debtor and exclude those who receive goods or services from the corporate debtor. For reasons which shall follow, we reject this argument:

50.1. First, Section 5(21) defines "operational debt" as a "claim in respect of the provision of goods or services". The operative requirement is that the claim must bear some nexus with a provision of goods or services, without specifying who is to be the supplier

or receiver. Such an interpretation is also supported by the observations in the BLRC Report, which specifies that operational debt is in relation to operational requirements of an entity.

50.2. Second, Section 8(1) IBC read with Rule 5(1) and Form 3 of the 2016 Application Rules makes it abundantly clear that an operational creditor can issue a notice in relation to an operational debt either through a demand notice or an invoice. As such, the presence of an invoice (for having supplied goods or services) is not a sine qua non, since a demand notice can also be issued on the basis of other documents which prove the existence of the debt. This is made even more clear by Regulations 7(2)(b)(i) and (ii) of the 2016 CIRP Regulations which provide an operational creditor, seeking to claim an operational debt in a CIRP, an option between relying on a contract for the supply of goods and services with the corporate debtor or an invoice demanding payment for the goods and services supplied to the corporate debtor. While the latter indicates that the operational creditor should have supplied goods or services to the corporate debtor, the former is broad enough to include all forms of contracts for the supply of goods and services between the operational creditor and corporate debtor, including ones where the operational creditor may have been the receiver of goods or services from the corporate debtor.

50.3. Finally, the judgment of this Court in Pioneer Urban", in comparing a allottees in real estate projects to operational creditors, has noted that the latter do not receive any time value for their money

as consideration but only provide it in exchange for goods or services. Indeed, the decision notes that "[e]xamples given of advance payments being made for turnkey projects and capital goods. where customisation and uniqueness of such goods are important by reason of which advance payments are made, are wholly inapposite as examples vis-à-vis b advance payments made by allottees". Hence, this leaves no doubt that a debt which arises out of advance payment made to a corporate debtor for supply of goods or services would be considered as an operational debt."

15. It was further held that the expression "in respect of" in Section 5(21) has to be interpreted in a broad and purposive manner. Paragraph 52 of the judgment is as follows:-

"52. Similarly, in the present case, the phrase "in respect of" in Section 5(21) has to be interpreted in a broad and purposive manner in order to include all those who provide or receive operational services from the corporate debtor. which ultimately lead to an operational debt. In the present case, the appellant clearly sought an operational service from the proprietary concern when it contracted with them for the supply of light fittings. Further, when the contract a was terminated but the proprietary concern nonetheless encashed the cheque for advance payment, it gave rise to an operational debt in favour of the appellant, which now remains unpaid. Hence, the appellant is an operational creditor under Section 5(20) IBC."

16. We may also notice the judgment of the Hon'ble Supreme Court in ***"Pioneer Urban Land and Infrastructure Limited and Anr."*** (supra) where the definition of financial debt has been considered and explained. Reliance has been placed by the Appellant on paragraphs 75 and 77 which are as follows:-

> *"5. And now to the precise language of Section 5(8)(f). First and foremost, the sub-clause does appear to be a residuary provision which is "catch all" in nature. This is clear from the words "any amount" and "any other transaction" which means that amounts that are "raised" under "transactions" not covered by any of the other clauses, would amount to a financial debt if they had the commercial effect of a borrowing. The expression "transaction" is defined by Section 3(33) of the Code as follows:*
>
> > ***3. (33) "transaction"*** *includes an agreement or arrangement in writing for the transfer of assets, or funds, goods or services, from or to the corporate debtor;*
>
> *As correctly argued by the learned Additional Solicitor General, the expression "any other transaction" would include an arrangement in writing for the transfer of funds to the corporate debtor and would thus clearly include the kind of financing arrangement by allottees to real estate developers when they pay instalments at various stages of construction, so that they themselves then fund the project either partially or completely.*

77. A perusal of these definitions would show that even though the petitioners may be right in stating that a "borrowing" is a loan of money for temporary use, they are not necessarily right in stating that the transaction must culminate in money being given back to the lender. The expression "borrow" is wide enough to include an advance given by the homebuyers to a real estate developer for "temporary use" i.e. for use in the construction project so long as it is intended by the agreement to give "something equivalent" to money back to the homebuyers. The "something equivalent" in these matters is obviously the flat/apartment. Also of importance is the expression "commercial effect". "Commercial" would generally involve transactions having profit as their main aim. Piecing the threads together, therefore, so long as an amount is "raised" under a real estate agreement, which is done with profit as the main aim. such amount would be subsumed within Section 5(8)(1) as the sale agreement between developer and home buyer would have the "commercial effect" of a borrowing, in that, money is paid in advance for temporary use so that a flat/ apartment is given back to the lender. Both parties have "commercial" interests in the same the real estate developer seeking to make a profit on the sale of the apartment, and the flat/apartment purchaser profiting by the sale of the apartment. Thus construed, there can be no difficulty in stating that the amounts raised from allottees under real estate projects would, in fact, be subsumed within Section 5(8)(1) even without adverting to the Explanation introduced by the Amendment Act."

17. The Hon'ble Supreme Court in the said judgment has held that the expression any other transaction would include an arrangement in writing for the transfer of fund to the Corporate Debtor and would thus, clearly include the kind of financing arrangement by allottees to real estate developers. It is to be noted that the challenge in the above case was challenge to various provisions including Section 5(8)(f) expression as inserted by IBC Second Amendment Act, 2018 and the said observation was made in the above context. The above judgment does not help the Appellant in the present case.

18. Counsel for the Appellant has further submitted that the judgment of the Hon'ble Supreme Court in ***'Consolidated Construction Consortium Limited'*** (supra) arose out of proceedings where conditions as are now contained in the Agreement in question were not present and the said case was only case for advance. Hon'ble Supreme Court in ***'Consolidated Construction Consortium Limited'*** (supra) had occasion to interpret Section 5(21) of the Code which interpretation is fully attracted in the facts of the present case. The case of ***'Consolidated Construction Consortium Limited'*** (supra) was also a case of advance given for carrying out for supply of goods which project was subsequently cancelled and claim for return of advance was laid in the said context and question arose as to whether advance is operational debt or not. Hon'ble Supreme Court ruled that the advance is operational debt.

19. Now reverting to the terms and conditions of the Agreement dated 28.07.2016. It is clear that the opening part of the Agreement clearly stated

that *"Whereas parties of the first part as well as party of the second part have entered into an agreement (White Sugar Supply Agreement) as per which the party of the second part confirms and agrees to sell and deliver to the party of the first part 5200 M.T's of white crystal sugar S-30 grade packed in P.P. bags of 50 KG's net weight at a fixed price of 3215/- per quintal inclusive of excise duty and cess (i.e. 3020 + 195) by and before 20.11.2016 (hereinafter referred as due date).".* Thus, the transaction between the parties emanates from the White Sugar Supply Agreement.

20. Now we need to look into clauses which have been relied by Counsel for the Appellant. Clause 2 of the Agreement provides that in case the party of the second part refuses or fails to deliver the entire / part quantity of sugar by and before 28.02.2016 as agreed between the parties in terms of this agreement i.e. 5200 M.T's or less then the party of the first part shall be entitled to obtain a penalty @6000 Per MT for 5200 Mts. The penalty is envisaged in event the second party refuses or fails to deliver the entire/ part quantity. Provision providing for penalty is not uncommon in Agreement of supply and the said clause has no bearing on the claim of the Appellant that it is financial debt. Clause 4 relates to entitlement of first party to receive and recover the difference in price in event sugar is sold on the higher price. Recovery in difference of price is natural consequence of Agreement between the parties for supply of white sugar on fixed price of 6000 per MT as has been mentioned in the Agreement. Clause 5 provide that in case of default by the second party in adjustment of advance, the second party of the second part shall also pay the above mentioned amount along with interest at the rate of

Rs. 30/-PMT per day till refund of the advance amount. The said clause also in the nature of penalty on account of failure of performance by the second party. Clause 7 deals with security under which the second party has given security cheque of Rs.5 Crore each towards the refund of advance amount. Security of refund of advance amount cannot change the nature of transaction for supply of sugar into financial debt. Security for advance in supply of goods is also an accepted mode and manner for protecting the advance but the said clause has no bearing on nature of transaction. Clause 11 deal with the collateral security where the second party shall also pledge 10% of its equity share capital with the first party vide a separate agreement and in case the second party defaults on any provisions of this agreement, the first shall automatically be entitled for a right to sell the pledged shares to such person at such price and such terms and condition as it may deem fit without any obligation for prior information to the second party. It is not shown any separate agreement for pledging of share was entered. Furthermore, the pledge of share is at best the security measures to protect the advance and to ensure that the obligation of second party is performed.

21. All the above clauses in no manner reflect that transaction between the parties was a financial transaction and the debt due is a financial debt. Adjudicating Authority has rightly come to the conclusion that the claim which was filed by the Appellant was a claim of operational debt and the Resolution Professional has rightly treated the claim as operational debt. It is further to be noticed that the Appellant itself has filed Section 9 Application being CP No.469 of 2020 on 29.01.2020 by which time CIRP was not even

commenced against the Corporate Debtor. Learned Counsel for the Appellant submits that there is no estopple against law. The factum of filing Section 9 application by the Appellant itself indicate that the Appellant itself considered it as Operational Creditor since it filed Section 9 application which got dismissed due to initiation of the CIRP against the Corporate Debtor by order dated 23.03.2023. The said conduct of the Appellant fully supports the stand taken by the Resolution Professional that the claim of the Appellant is operational debt.

22. In view of the foregoing discussions, we are of the view that no error has been committed by the Adjudicating Authority in rejecting IA No.2909 of 2023 filed by the Appellant. Appellant's claim has rightly been held to be operational debt. We do not find any error in the impugned order. The Appeal is dismissed.

[Justice Ashok Bhushan]
Chairperson

[Barun Mitra]
Member (Technical)

[Arun Baroka]
Member (Technical)

New Delhi
Anjali