

Business Standard

SBI's plan to invoke guarantees on companies under NCLT unlikely to succeed

Lawyers say SBI's credit recovery team will have to wait for a while

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A proposed plan of the State Bank of India (SBI) to invoke personal and corporate guarantees of defaulting companies is unlikely to pass legal scrutiny, having been barred from doing so in previous cases. The country's largest bank is likely to issue about 200 notices invoking personal guarantees, even in cases where insolvency proceedings were underway.

Apart from numerous smaller companies, at least 40 large accounts are facing insolvency. The Reserve Bank of India (RBI) had in June last year come up with 12 names for immediate bankruptcy referrals. Later, it brought another list of 26 large accounts.

Such promoters might have personal guarantees running into tens of billions, but may not be in a position to pay. And, in case, the SBI plans to invoke these personal guarantees, the bank will be sued by these promoters.

The promoter of a company on the RBI's first list said he was aware that a plan of invoking personal guarantees was in the works, but added it was

completely against the spirit of the Insolvency and Bankruptcy Code (IBC).

Another promoter on the second list said that it won't stand on grounds of law. "Invoking guarantees is effective of liquidation, and we have not reached that stage yet. Once you go to the National Company Law Tribunal (NCLT), there is a moratorium."

IBC provides 180 days for a resolution, which can be extended by 90 more days. If a resolution is not achieved within this timeframe, the company is liquidated.

"In case the SBI does go ahead with its plan, it will be legally challenged," said the promoter.

So far, promoters on the first and second list have refrained from challenging the ordinance that barred them from bidding. However, any such move would be challenged, they say. It is likely that the promoters would prevail in such cases, say senior lawyers. In fact, any ambiguity on the matter has been cleared in two earlier cases, with SBI asked to back off when insolvency proceedings were on. A legal expert said the situation would unlikely to change, irrespective of what SBI's interpretation of the law was.

In one such case, Veasons Energy Systems versus SBI, the Chennai bench of the NCLT stopped the bank from invoking the personal guarantee of V Ramakrishnan, director of the company. SBI notified Veasons and Ramakrishnan on November 12, 2016, that the personal assets would be sold. The firm challenged it, stating it had applied to the Board for Industrial and Financial Reconstruction (BIFR) and till its application was decided, dues could not be recovered.

The IBC became operational in December 2016. The NCLT bench ruled that in case a guarantor's personal property is sold to realise a portion of debt dues against a company in default, it would create a charge on assets of the company, "which shall amount to 'encumbering' the properties of the corporate debtor". Meaning, if the bank tried to sell off the assets, the promoter would be deemed a creditor to the company, since his assets had been sold to pay off debt. The IBC says when a firm is going through insolvency proceedings, "transferring, encumbering, alienating or disposing of by the corporate debtor any of its assets or any legal right or beneficial interest therein" is prohibited.

Beside, there are several cases that spurned the banks' claim whenever the lenders went to invoke personal guarantees of the promoter, simultaneously with insolvency proceedings going on. In the case of Sanjeev Shriya verses SBI & others, the Allahabad High Court turned down SBI's move.

"The argument advanced by Shri Navin Sinah is also fortified on the ground that once the liability is still in a fluid situation and the same has not been crystallised, then in such a situation, two parallel/split proceedings in a different jurisdiction should be avoided, if possible," the court ruled in early September 2017.

Similarly, in the case of Axis Bank versus Edu Smart Services, the Delhi NCLT ruled against the bank. Stating it could not invoke such guarantees when there was an insolvency proceeding on and the mandatory limit of 270 days had to be honoured.

The Insolvency and Bankruptcy Board of India was trying to change these through tweaks in the law to help banks invoke such guarantees. It is unclear if the recommendations on favouring of creditors have been accepted by the board or not.

Even if accepted, it is highly unlikely that the law would be changed in favour of bankers as far as guarantees are concerned in a relatively short span. Therefore, lawyers say, SBI's credit recovery team will have to wait for a while.

