

Acknowledgment of debt will not extend the time for triggering an action under the Code (Babulal v. Veer Gurjar Aluminium Industries Pvt. Ltd.)

INTRODUCTION

The Supreme Court in a recent ruling, *Babulal Vardharji Gurjar v. Veer Gurjar Aluminium Industries Pvt. Ltd. & Anr, Civil Appeal No. 6347/2019*, has held that Section 18 of the Limitation Act, 1963 (**'Limitation Act'**), which provides for a fresh period of limitation to be computed from the time when an acknowledgment of liability has been made in writing and signed, is not applicable to proceedings under Section 7 of the Insolvency and Bankruptcy Code, 2016 (**'Code'**).

Quite often, to overcome the bar of limitation and maintain a claim, a creditor relies upon the acknowledgement of liability in the financial records of the debtor to contend that the debt having been acknowledged, the claim is saved by Section 18 of the Limitation Act.

In light of this ruling, an operational creditor or a financial creditor will have to be vigilant while initiating proceedings under the Code and ensure that application is within 3 years from the date of default. The creditor will be unable to take the benefit of the provisions of the Limitation Act, which provide for a fresh period of limitation to run/exclusion of time in computing limitation.

BACKGROUND FACTS

On or about 21.03.2018, JM Financial Assets Reconstruction Company Pvt. Ltd. (**'Financial Creditor'**), the assignee of loans extended by Corporation Bank, filed an application under Section 7 of the Code before the National Company Law Tribunal (**'NCLT'**) seeking initiation of Corporate Insolvency Resolution Process (**'CIRP'**) in respect of the Veer Gurjar Aluminium Industries Pvt. Ltd (**'Corporate Debtor'**). In the application, the date of default was stated as 08.07.2011, when Corporation Bank classified the Corporate Debtor's account as a Non-Performing Asset. By order dated 09.08.2018, the NCLT admitted the application and appointed an Interim Resolution

Professional. It may be noted that Section 238-A, which provides for Limitation Act to be applicable to proceedings under the Code, was introduced with retrospective effect from 06.06.2018. The order of NCLT was challenged all the way up to the Supreme Court¹, which *vide* order dated 26.02.2019, remanded the matter to the National Company Law Appellate Tribunal (**'NCLAT'**) to decide on the issue of limitation.

Before the NCLAT, it was contended that the claim of the Financial Creditor was barred by limitation since the default was committed on 08.07.2011, whereas the application was filed on 21.03.2018. By the impugned order dated 14.05.2019, the NCLAT, rejected this argument, on two principal grounds, that:

- The right to apply under Section 7 of the Code accrued only on 01.12.2016 when the Code came into force and hence, the application filed by the Financial Creditor in the year 2018 is not barred by limitation.
- In order to secure the loan, the Corporate Debtor had executed equitable mortgage. The limitation period under Article 61 (b) of the Limitation Act, 1963 is 12 years to recover possession of mortgaged property. As such, the claim was not barred by limitation.

This order was challenged before the Supreme Court, by Mr. Babulal Gurjar, the erstwhile director of the Corporate Debtor. The Corporate Debtor, arrayed as Respondent No.1, was represented by the Interim Resolution Professional. The Financial Creditor was arrayed as Respondent No.2.

The main issue before the Supreme Court was whether the application made by the Financial Creditor under Section 7 of the Code was within limitation.

The Appellant argued that limitation period for an application under Section 7 of the Code is three years as per Article 137 of the Limitation Act and Article 61 (b) is not attracted. That the limitation is triggered from the date of alleged "default". That in the present case the date of

¹ In *Babulal Vardharji Gurjar v. Veer Gurjar Aluminium Industries Pvt. Ltd. & Anr, Civil Appeal No. 10710 of 2018*

default was 08.07.2011, as such the application filed on 21.03.2018, was barred by limitation.

The gravamen of the Respondents' case was that the debt had been admitted in the balance sheet of the Corporate Debtor since the year 2011 until 2017 and as such, Section 18 of the Limitation Act, which provides for a fresh period of limitation to be computed in case of written acknowledgment of debt during the original period of limitation, would save the application from the bar of limitation.

This argument was countered by the Appellant, who argued that Section 18 of the Limitation Act cannot revive the "default" relevant for the Code. Drawing a distinction between 'default' and 'cause of action,' it was argued that Section 18 of the Limitation Act cannot revive the 'default' relevant for proceedings under section 7 of the Code and could only revive limitation with respect to the cause of action available *qua* other remedies. The limitation period for proceedings under Section 7 of the Code starts from the date of default. Any acknowledgment of the debt in the balance sheet will not give rise to any fresh date of default. Default occurs only once and cannot be continuing.

FINDING

The Court rejected both the findings of the NCLAT, being in teeth of the decision in *B.K. Educational Services Pvt. Ltd. v. Paras Gupta & Associates*², which has been consistently followed in *K. Sashidhar v. Indian Overseas Bank*³, *Jignesh Shah and Anr. v. Union of India and Anr*⁴, *Vashdeo R. Bhojwani v. Abhyudaya Co-operative Bank Ltd. & Anr*⁵, *Gaurav Hargovindbhai Dave v. Asset Reconstruction Company (India) Ltd. & Anr*⁶ and *Sagar Sharma & Anr. v. Phoenix Arc Pvt. Ltd. & Anr*⁷. Analyzing all these decisions, the Court summarized the law as:

- The period of limitation for an application under Section 7 of the Code is governed by Article 137 of the Limitation Act and is, therefore, three years from the date of default;
- The right to apply under the Code accrues on the date when the default occurs and the date of

commencement of the Code is not the trigger point of limitation;

- If the default had occurred over three years prior to the date of filing of the application, the application would be time-barred save and except in those cases where, on facts, the delay in filing may be condoned; and
- An application under Section 7 of the Code is not for enforcement of mortgage liability and thus Article 62 of the Limitation Act is not applicable. The NCLAT has mistakenly mentioned Article 61 (b) in the impugned judgment but was in fact relying on Article 62.

While the aforesaid principles remain clear with the consistent decisions of the Supreme Court, the only gray area was whether Section 18 of the Limitation Act can be made applicable to the present case.

In support of this argument, Respondent strongly relied upon the observation made in *Jignesh Shah*. In *Jignesh Shah*, it was contended, placing reliance on Section 238-A of the Code, that the winding up proceeding - which was transferred to NCLT and treated as a Section 7 application - was barred by limitation. The Supreme Court following *BK Educational* upheld this contention. However, the Respondent placed reliance on paragraph 21 of *Jignesh Shah*, wherein the Court observed that:

"21. [...]. In law, when time begins to run, it can only be extended in the manner provided in the Limitation Act. For example, an acknowledgment of liability under Section 18 of the Limitation Act would certainly extend the limitation period, but a suit for recovery, which is a separate and independent proceeding distinct from the remedy of winding up would, in no manner, impact the limitation within which the winding-up proceeding is to be filed, by somehow keeping the debt alive for the purpose of the winding-up proceeding."

The Court rejected such reliance of the Respondent and held the reference to Section 18, in paragraph 21 of *Jignesh Shah*, had only been in relation to the suit or other proceedings, wherever it could apply. It was further held that it was difficult to read the above observation of

² AIR 2018 SC 5601

³ 2019 SCC Online SC 257;

⁴ 2019 SCC Online 1254

⁵ (2019) 9 SCC 158

⁶ (2019) 10 SCC 572

⁷ (2019) 10 SCC 353

Jignesh Shah to mean that the ratio of *B.K. Educational Services* had, in any manner, been altered by the Court. The Court further noted that in *Vashdeo R. Bhojwani*, the Supreme Court had rejected the contention suggesting continuing cause of action for the purpose of extending the limitation for application under Section 7 of the Code.

Even on facts, the Court found that Section 18 of the Limitation Act would not be attracted since the Section 7 application was bereft of pleadings in this respect. All that was pleaded was that the date of default was 08.07.2011 with no mention of any other date of default and/or date of acknowledgment of debt.

ANALYSIS

The ruling of the Supreme Court is another step in the direction that the Code is not a mere money recovery legislation for creditors. That the scheme of the Code is such that it is triggered on the determination of default and not on an inability to pay. As such, an acknowledgment of

debt will extend the time to sue for recovery of money, but does not extend the time for triggering an action under the Code.

On an analysis of this decision and considering the decision in *Vashdeo R Bhojwani*, it appears that the date of default is sacrosanct for computing the period of limitation and no subsequent action would extend the period of limitation available for instituting proceedings under the Code. While in this case the Supreme Court was only considering Section 18 of the Limitation Act, the logical sequitur of this ruling and the decision in *Vashdeo R Bhojwani* is that all provisions of Limitation Act which grant additional time for computing limitation such as Section 16 and 17, would not be applicable to proceedings under the Code. Though for bona fide cases, a silver lining remains, which is recognized by the Court, that under Section 5 of the Limitation Act, the NCLT has the power to condone delay in filing the application, in appropriate facts and circumstances.

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