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TREATMENT OF INTEREST IN OPERATIONAL DEBTS

Introduction

1. Section 3(11) of the Insolvency and Bankruptcy Code, 2016 (IBC) defines a “debt” as a liability or obligation that is due from one person to another and it may include a financial debt as well as operational debt.
2. Under Section 5(8) of the IBC, a financial debt means a debt along with interest which is disbursed against the consideration for time value of money, whereas Section 5(21) defines an operational debt as a claim in respect of goods or services including employment or debt in respect of payment of dues.
3. Thus, in case of a financial debt, default in payment of interest may also become the subject matter of insolvency proceedings.
4. In view of the difference between these definitions and different procedures being provided for dealing with claims in respect of financial and operational debt, the question that has arisen before multiple fora is whether interest may be included in the debt amount claimed in an application filed by the operational creditor under Section 9 of the IBC.

Section 4 of the IBC

1. Section 4 of the IBC is applicable to Part-II (Insolvency Resolution and Liquidation for Corporate Persons).
2. It states that Part-II shall apply to “*matters relating to insolvency and liquidation of corporate debtors where the minimum amount of default is one lakh rupees.*” The proviso to Section 4 allows the Central Government to raise such amount of default to a higher value which shall not be more than one crore rupees.
3. By a Notification dated 24th March, 2020, the minimum amount of default was raised to one crore rupees for the purposes of Section 4 of IBC.
4. As an effect of such Notification, a financial or an operational creditor may only approach the Adjudicating Authority, National Company Law Tribunal (“NCLT”) in insolvency proceeding cases where the

claim amount is above Rs. 1 crore.

Distinction in treatment of threshold of Rs 1 crore for financial debt & operational debt

1. There has been clarity in general understanding that a financial debt would include interest. However, various questions have arisen as to whether the claim amount under an operation debt can also include the interest component or it comprises of only the principal amount.
2. This becomes even more important when the principal does not exceed the threshold of Rs. 1 crore while the total claim when calculated along with interest crosses the barrier of the minimum amount.

Judicial Decisions

1. In *Pioneer Urban Land and Infrastructure Ltd. vs. Union of India [(2019) 8 SCC 416]* the Supreme Court clarified that in case of operational debt there is no consideration for time value of money. Thus, this justifies the absence of interest component in the definition of operational debt. However, the judicial position has evolved since then.
2. In a literal interpretation of the statutory provisions, the NCLT in *Vitson Steel Corp (P) Ltd. vs. Capacite Infraprojects Ltd. [C.P. (IB) No. 1579/M-B/C-IV/2019]*, observed that interest cannot be charged in cases where the agreement between the parties does not stipulate the same. Thus, interest cannot be claimed unilaterally as a practise.
3. Further, in *CRBE South Asia Private Limited vs. M/s. United Concepts and Solutions Private Limited [(IB)-797(ND)2021]*, the amount of default shown as operational debt by the applicant was higher than Rs. 1 crore when calculated along with interest. The principal amount in the claim was lesser than Rs. 1 crore. However, *CRBE South Asia*



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challenged the order of NCLT before the National Company Law Appellate Tribunal (“NCLAT”) [Company Appeal (AT) (Insolvency) No. 188 of 2022]. The NCLAT held that excluding interest from the overall claim in cases of operational debt was an erroneous approach and overruled the judgment of NCLT remitting the matter back for fresh consideration.

4. The NCLT observed that a provision for inclusion of interest in the amount of debt was only available in respect of a financial debt and an operational debt could not include the amount of interest.
5. The NCLT held that the amount of interest cannot be added up with the principal amount in calculating the operational debt in compliance of Section 4 of the IBC. This conclusion was based on the definitions of the terms ‘operational debt’ and ‘financial debt’ as defined under the IBC.
6. In *M/s. Wanbury Ltd. vs. M/s. Panacea Biotech Ltd.* (CP No. 8/2016) which marked the difference between an operational debt and a financial debt in terms of the definition provided under the IBC, it was clarified that the former does not include the amount of interest as compared to the later.
7. In *Prashat Agarwal vs. Vikash Parasrampuriah* [Company Appeal (AT) (Ins) No. 690 of 2022], the NCLAT held that since the invoice in this case contained a provision for interest, the claim would include both the principal amount as well interest on delayed payment of the amount which together brought the total operational debt above Rs. 1 crore as per the requirement of Section 4 of IBC.

Whether interest alone can be claimed through IBC proceedings

1. Once it is settled that interest can form part of the claims under applications for insolvency by the operational creditors, a question also arises as to whether interest solely can be claimed by an operational creditor in such proceedings when the principal amount has been repaid.

2. The courts/tribunals have held that interest alone cannot be said to qualify as debt under the IBC and further that filing insolvency proceedings for claiming interest is a gross misuse of the provisions and showcases malicious intent. (Refer: *SS Polymers vs. Kanodia Technoplast Ltd.*)

Conclusion

1. Relying on the two NCLAT rulings (discussed above), the judicial position stands clarified to an extent.
2. Inclusion of interest in the claim amount in cases of operational debts have typically been allowed by courts/tribunals where the invoice clearly stipulates payment of interest on an overdue amount.
3. In *D.F. Deutsche Forfait AG vs. Uttam Galva Steel Ltd.* [C.P. No. 45/I&BP/NCLT/MAH/2017], the NCLT held that it cannot be expected that delay in payments is left uncharged and hence an operational creditor claiming interest is justified.
4. Although the NCLT has been giving differing view on the issue, the settled position as decided by the Appellate Bench (NCLAT) clarifies the statutory position on the subject, i.e., the operational debt for the purposes of Section 9 of the IBC would include the principal as well as the interest component.