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CLAIM TOWARDS LICENSE FEES FOR IMMOVABLE PROPERTY IS AN 'OPERATIONAL DEBT': NCLAT FULL BENCH

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On 05 July 2022, a Full Bench of the National Company Law Appellate Tribunal (**NCLAT**) in *Jaipur Trade Expocentre Private Limited v. M/s Metro Jet Airways Training Private Limited*, Company Appeal (AT) (Insolvency) No. 423 of 2021, held that a claim towards unpaid license fees for an immovable property would constitute an operational debt under the Insolvency and Bankruptcy Code, 2016 (**Code**) and consequently constitute a debt in default for initiating the corporate insolvency resolution process (**CIRP**).

Background

Jaipur Trade Expocentre Private Limited (**Applicant**) entered into a five-year license agreement with Metro Jet Airways Training Private Limited (**Respondent**) in 2017 to take on license a building for the purposes of running an educational establishment.

Upon multiple repeated defaults of the Respondent in paying the monthly license fee, the Applicant-licensor issued a demand notice to the Respondent-licensee under Section 8 of the Code in 2019.

Since there was no response to the demand notice, an application under Section 9 of the Code was filed by the Applicant against the Respondent before the National Company Law Tribunal, Jaipur bench (**NCLT**) for the initiation of CIRP. The NCLT dismissed the application holding that a claim arising out of grant of license to use immovable property would not fall under the category of a claim in respect of providing goods or services as per the definition of "operational debt" under Section 5(21) of the Code, and therefore, a claim for unpaid licence fees was not an 'operational debt' being capable of adjudication under the Code.

The Applicant-licensor preferred an appeal to the NCLAT, wherein a two-member bench referred the following questions of law to a larger three-member bench:

- Whether the three - member bench judgement of the NCLAT in *M. Ravindranath Reddy v. G. Kishan & Ors.*, 2020 SCC OnLine NCLAT 84 ("**M. Ravindranath Reddy**") lays down the correct law?
- Whether claims of the Licensor for payment of License Fee for the use and occupation of immovable premises for commercial purposes is an 'Operational Debt' within the meaning of Section 5(21) of the Code?

Since M. Ravindranath Reddy's case was decided by an three-member bench of the NCLAT, the questions of law were referred to a five-member Bench.

Findings and Observations of the NCLAT Full Bench

The five-member Bench overruled the findings in *M. Ravindranath Reddy* and allowed the appeal and answered the reference as follows:

- *M. Ravindranath Reddy* does not lay down the correct law as Section 14(2) of the Code read with Regulation 32 of the (Insolvency Regulation Process for Corporate Persons) Regulations, 2016 are only for the purpose of deeming essential services after commencement of the CIRP and not to interpret what constitutes an "operational debt" under Section 5(21) of the Code. The NCLAT also overruled its own judgement in *Promila Taneja v. Surendri Designs Pvt. Ltd.*, 2020 SCC OnLine NCLAT 1105, which placed reliance on *M. Ravindranath Reddy*.
- In the facts, the licence agreement required the Applicant-licensor to provide a 'warm shell building with fittings, fixtures, electrical, flooring as per good corporate standards' and the Respondent-licensee was liable for payment of Goods and Services Tax (**GST**), which sufficiently indicated the nature of services provided under the licence agreement. In doing so the NCLAT was cognizant that while Section 3(37) of the Code did not expressly provide for a direct import of definitions from the Central Goods and Service Tax Act, 2017, it was duty bound to expound definitions that find place in legal statutes when they were not provided in the Code.
- The NCLAT placed reliance on the judgement of the Supreme Court in *Keshavlal Khemchand and Sons Private Limited and Ors. v. Union of India and Ors.*, (2015) 4 SCC 770, which observed that when a statute does not contain a definition of a particular expression employed in it, it is the duty of the court to expound the meaning of an undefined expression in accordance with the law of well-established principles of statutory interpretation. In doing so, the NCLAT placed reliance on its judgment of *Anup Sushil Dubey v. National Agriculture Co-operative Marketing Federation of India Ltd. and Anr.*, (2020) SCC OnLine NCLAT 674, wherein the interpretation of the term 'service' as contained in the Consumer Protection Act, 2019 was held to include '*..provision of facilities towards real estate..*'. Expanding the definition of the term 'operation' from Iyer's Law Lexicon, the NCLAT observed that an operational debt is a debt that is incurred in the conduct of principal activities of an enterprise, and hence the Respondent's debt towards license fees for an immovable property to conduct an educational enterprise would be an operational debt under Section 5(21) of the Code.
- NCLAT also referred to the Bankruptcy Law Reforms Committee Report (2015) which observed that a 'lessor who rents out space is an operational creditor' (para 5.2.1.).
- NCLAT distinguished the facts in the present appeal from *M. Ravindranath Reddy* which dealt with a claim for enhancement of lease rent in respect of which legal proceedings had been instituted prior to initiation of proceedings under the Code. .

Comments

This judgement clarifies a category of debts that were sought to be excluded from the Code and in doing so enlarges the interpretation and scope of the Section 5(21) of the

Code, and thus, further enlarges the scope of debts under which the Code can be triggered.

The Respondent is entitled to file a statutory appeal to the Supreme Court of India in terms of the Code against this judgment.

- Thriyambak J. Kannan (Partner) and Oviya Nila Muralidharan (Associate)

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