



## **Lalit Kumar Jain v. Union of India and others AIR 2021: Case Comment**

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### **1. Background**

As India carried out its sturdy legislation on 20th May 2016, to restore and maximize the assets of the company debtor. But as soon as the judgment of Lalit Kumar vs Union of India & Ors came in May 2021, a huge tussle started out, that if the code has grown to be a healing mechanism more than a manner of bringing the corporate debtor back on its feet. With the present judgment, it's clear that the personal guarantor's liability will preserve even after the approval of the resolution plan, or even after the liquidation for a debt-laden agency which was earlier used to get extinguished with the approval or decision. The judgment has also made it hard for Personal Guarantors to say back their cash from the company debtors. This judgment got here a month later the Supreme Court held that all dues payable to Centre, state, or tax authorities will freeze in the event that they had been no longer part of the authorized decision plan, with a purpose to save the personal guarantor fall prey to the sudden claims via other creditor making it greater complicated. The protracted saga of the remedy of personal guarantors under the Insolvency and Bankruptcy Code, 2016 seems to come in the end and put to rest with the help of the Supreme Court by the way of its Latest judgment in Lalit Kumar Jain v. Union of India.

A personal guarantor is a person who's the surety in an agreement of guarantee to a company debtor. Further, "guarantor" means a debtor who's a non-public guarantor to a company debtor and in respect of whom the guarantee has been invoked by way of the creditor and remains unpaid in full or part.

The query of extinguishment of liabilities of the personal guarantor become regarded in the case of *Kundalia Dabriwala v. Haryana Financial Corporation*<sup>1</sup>, in terms of agreement act, held that the legal responsibility of the surety is co-vast with that of the essential debtor, then if the latter's liability is extinguished in complete or in component, then the liability of the surety is also reduced or extinguished. The modern-day judgment has clarified that approval of a resolution plan of a debtor enterprise, does now not have to discharge the liability of a personal guarantor, has now cleared out the way for 75 petitions that have been filed via Corporate guarantors including Anil Ambani, Venugopal Dhoot, Kapil Wadhawan, and so forth.<sup>2</sup>

Further, the present judgment has silently spoke back the concern of the guarantor, with the help of the case of *Vijay Kumar Jain vs. Standard Chartered Bank & Ors*<sup>3</sup> wherein it became held that the board of directors (Personal guarantors) eligible to attend the Committee of Creditors (hereinafter referred to as COC) assembly and also eligible to get a strengthened plan along with observe as such participants of the erstwhile Board of Directors, who are often guarantors, are vitally inquisitive about a resolution plan as such decision plan then binds them. Such a plan may also reduce the debt of the principle debtor, ensuing in cutting down the debt of the guarantor as well, or it may not.

On November 15, 2019, the Union Ministry of Corporate Affairs released a notification introducing provisions of Part III of Insolvency and Bankruptcy Code 2016, which treated the financial debtors and insolvency decision processes regarding public guarantors to corporate debtors. This notification enabled banks to institute insolvency proceedings against the personal guarantor to corporate debtors. The purpose turned into making promoters,

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<sup>1</sup> [2010] 157 COMPCAS 530

<sup>2</sup> Expansion of liabilities of a personal guarantor: a double edge sword - iPleaders

<sup>3</sup> (2019) 20 SCC 455

administrators, or every now and then, the dealing with directors or the chairperson answerable for the loans taken with the help of their firm on their private assure.

The new provisions of the notification were challenged before numerous High Courts. The Supreme Court, whilst exercise its powers under Article 139A to transfer cases and to settle the common questions of law under Article 32 regarding the interpretation and Application of the Code, presided on the matter. This changed into finished to keep away from contradictory rulings via specific High Courts and to authoritatively settle the law.

## **2. Brief Facts**

Lalit Kumar Jain and Others (“Petitioners”) had given personal guarantees to financial institutions and banks in different capacities i.e. as promoters, directors, or chairpersons. After the release of notification, the personal guarantees of the petitioners were invoked in multiple cases. Consequently, the insolvency proceedings of various stakeholders were at different stages; and some at the final stage. Many were issued demand notices and faced insolvency proceedings under the code.

The petitioners had two main contentions; first, that the notification was ultra vires of the powers delegated to the central government, and second, the executive (government) could not apply the provisions of the code selectively to one sub-category of individuals, that is personal guarantors to corporate debtors.

The issue before the Hon’ble Supreme Court in the present case was the validity of the Notification dated 15.11.2019 (“Impugned Notification”) issued with the help of the Central Government. The Central Government issued the Impugned Notification via delegating its powers under Section 1(3) of the Code wherein important provisions of the Code on the subject of personal guarantors to Corporate Debtors were notified. The Impugned Notification was challenged before various High Courts at the ground that the Impugned Notification was ultra vires the Code. All the Writ Petitions filed earlier than numerous High Courts on this regard become transferred to the Hon’ble Supreme Court for final adjudication.

## **3. Issues before the Court -**

1. Whether the Notification Issues on 15<sup>th</sup> November 2019 was valid and intra vires of the powers of the Government and the Authority?
2. Whether sanctioning of a resolution Plan of the Corporate Debtor Discharges the Personal Guarantor to the Corporate Debtor?

#### **4. Judgement**

The idea of step by step implementing the law or legal principles became supported in numerous instances through the apex court which recommended that there's no need or constitutional requirement to put into effect a regulation or policy at once. The discretion is given to extend an enactment by using seeing the area of operation, or to decide when and the way the regulation will be put into impact. The court relied on the report of a Working Group emphasizing the proximity of personal guarantors with corporate Debtors. The notification gave rights to the central government to determine when and how the pending actions in opposition to a personal guarantor to the company debtor may be taken before adjudicating authority.

The court mentioned that the parliamentary intent became to deal with personal guarantors on a special footing from other categories of people. The prospect of impartial processes taking region in different boards will result in uncertain outcomes, though the adjudicating authority changed into the same for the company debtor to whom people stood as personal guarantors. The insolvency method for individuals is in Part III while the process regarding corporate debtors is in Part II. This distinction does not cause incongruity because the discussion board for adjudicating strategies that have been distinct earlier has now grow to be not unusual.

This could in addition help in considering the entire image approximately the asset available and enhance the Committee of Creditors (“CoC”) framing of realistic plan maintaining in mind the lenders’ dues from personal guarantors. Prior to the impugned notification, a notification become issued under Section 1(3) which found out that the code became carried out in degrees, retaining in mind the categories of people to whom its provisions have been to be applied. The notification extends the Code’s application to another class of people which it never meant to. The impugned notification issued under Section 1(3) is, therefore, now not ultra vires of the power; the notification is legitimate. The court sooner or later discovered that the release or discharge of an essential borrower from the debt, through operation of

regulation, or due to liquidation or insolvency proceeding, does no longer ipso facto absolve the surety/guarantor of their liability, which arises out of an unbiased agreement.

And therefore, it was held that the impugned notification is legal and valid.

## 5. Analysis

In our opinion, the judgement didn't maintain the constitutional values of delegated legislation. The stipulation of Section 1(3) of the Code engages the central government to uphold different provisions of the code at various points on schedule, anyway it doesn't allow the public authority to order a piece of the provisions of the code or to apply the provisions on specific classes of people. The "conditional legislation" allows the executive to bring the law into power now and again it might choose. In such legislation, the law has been made in its fulfilment and with extremely restricted extension for additional legislation. The obligation of the central government is to decide the time and way for the law to apply in the country and not to pick the subjects to which the law will apply.

The subsequent issue managed the approval of the resolution plan which brings about the discharge of the principal borrower. The resolution plan, once supported, gets restricting on the corporate debtor, individuals, personal guarantors, and different stakeholders associated with the resolution plan. Passing by the provision of contract law as the "risk of the guarantee is co-extensive with that of the principal person" if the last's obligation is released or extinguished, the responsibility of surety ought to likewise be extinguished as the resolution plan is an agreement. Section 140 of the Indian Contract Act, 1872, accommodates subrogation rights which the personal guarantor can't benefit after the approval of the resolution plan. Nonetheless, the court in the current case relied on the ratio of V. Ramakrishnan<sup>4</sup> where the court saw that the object of the IBC was not to permit personal guarantors to evade their liability once the resolution plan is supported. This, thus, influences the right of a third party to the agreement by not permitting him to petition for subrogation rights and not releasing him of the co-extensive obligation, accordingly contradicting section 30(2)(e) of the Code. An equilibrium must be drawn between the interests of the corporate debtor and the privileges of a personal guarantor. Much of the time the directors are personal

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<sup>4</sup> State Bank of India v. Ramakrishnan, (2018) 17 SCC 394

guarantors and their entitlement to recover from the corporate debtor ought not to be removed detachedly.

Our last dispute against the reasoning of this judgment is that it utilizes the Code with the end resolution of debt recovery, which, as held in different cases, is against the ethos and legislative aim of the code. The proper systems for obligation recuperation are through the SARFAESI, RDDBFI, or cash suits, yet the code ought not to be utilized as an alternative component for debt recovery.

The object of the IBC is for revival of the companies from the debt, after these most recent notification it has been more a recovery forum for the creditors. The overall act will be rebuilt to make the act more suitable as the IBC has an overriding impact it will be made with alert.

## **6. Conclusion**

In the present case, the court needed to choose between two rights – the authoritative right of the personal guarantor and the right of the creditors, which are by and large open public banks. The court picked the latter as a public policy decision. The court in the current case appears to have followed the Benthamite approach of justice. As the debt recovery rates of Indian banks have been horrifying as of in the past few years, the burden at last falls on the taxpayers. This judgment will take a portion of that burden from the shoulders of the taxpayers and will put it on the personal guarantors who are for the most part financially solid and have consented to repay the sum in the event of default.

The repercussions this judgment will have on the fate of personal guarantors can be sweeping. While we may see a dip in the quantity of defaults by personal guarantors, it may get hard to track down a personal guarantor for a business and thusly restricting the chances of finance. It will likewise build the burden on NCLT as more instances of debt recovery will discover their approach to NCLT as opposed to moving toward traditional recovery tribunals and courts.

This instant judgment would carry a murmur of relief to numerous creditors for whom the doorway to the asset pool of the personal guarantors has been opened up under the IBC. The judgment would be a reason for worry for various prominent industrialists who are the promoters of debt loaded companies. As per few reports, personal guarantors adding up to

INR 1.8 lakh crores have been given by promoters of top companies confronting huge debts. Hence, unmistakably the immediate arrangement adds to the bite force of the IBC since the creditors of a corporate debtor will presently have the alternative to continue at the same time against the corporate debtor and its own personal guarantor. The instant judgment is one more choice in advancement of the soul of the IBC is a welcome move.<sup>5</sup>

A quicker compliance method for guarantees is an alluring move on occasion when banks are pushed with bad loans. Thinking about concurrent procedures against both the personal guarantor and the main debt holder, an examination of the insolvency system for personal guarantors suggests more prominent execution of ensures, higher assortments, and, probably, a critical influence to creditors against blundering personal guarantors. Personal guarantors, then again, should practice alert since they have lost their entitlement to recover instalments made under the guarantee contract from the borrower. Different specialized parts of the enforcement method should likewise be reconsidered to keep up with the structure's general efficiency. All things considered, this judgment would make ready for creditors in better recovery of credits as then again would be troublesome for the personal guarantors.

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<sup>5</sup> <https://www.mondaq.com/india/insolvencybankruptcy/1072832/personal-guarantors-to-corporate-debtors-liable-under-the-insolvency-and-bankruptcy-code-2016-supreme-court-of-india>