

National Company Law Tribunal: Will it live up to its promise?

Introduction

In 1999, a committee constituted by the Government of India under Justice V. Balakrishna Eradi (“**Committee**”)¹ examined the existing laws on insolvency of companies and winding-up, with the aim of suggesting reforms to avoid delay involved in such proceedings. Among other issues, the Committee identified the number and duplicity of matters and court proceedings as the most significant reason for the massive delay in dissolution of companies.² Taking reference from the corporate insolvency regime predominant in some countries, the Committee recommended the constitution of a national tribunal which should combine the powers of various forums, such as high courts in restructuring and winding-up, the Company Law Board (“**CLB**”), Board for Industrial & Financial Reconstruction (“**BIFR**”) and Appellate Authority for Industrial & Financial Reconstruction under the Sick Industrial Companies (Special Provisions) Act.

Pursuant to the recommendations of the Committee, the Companies (Second Amendment) Act, 2002 was enacted that provided for an amendment in the then prevailing company law for the composition of a national tribunal. The amendment was met with various judicial challenges which stalled the process. Eventually, Section 408 of the Companies Act, 2013 (“**Act**”) provided for the establishment of National Company Law Tribunal (“**NCLT**”) and the National Company Law Appellate Tribunal (“**NCLAT**”). This section was notified through Ministry of Corporate Affairs (“**MCA**”) notification dated June 1, 2016 wherein NCLT is to start with 11 benches.³ The CLB now stands dissolved.

This newsletter discusses the constitution of NCLT and NCLAT and analyzes the implications of the notification which brings into effect several key sections of the Act.

1. Notification and practical ramifications

After more than a decade of extensive deliberation and delay, MCA issued the notification which has brought into force about 40 sections of the Act, through which NCLT has been granted various adjudicatory and regulatory powers. A brief overview of certain selective provisions is below. As part of its adjudicatory powers, NCLT is empowered to take action in the following:

(a) **Formation:**⁴ In case any false information has been furnished or where there is a material suppression of facts, then, upon an application made to it, the NCLT will give an opportunity

¹ The Eradi committee report on Law Relating To Insolvency And Winding-up Of Companies 2000 available at <http://reports.mca.gov.in/>, last viewed on June 20, 2016

² Clause 3.24 and 3.25 of the Eradi committee report (*supra*)

³ Gazette notifications S.O. 1932 (E), S.O. 1933 (E) and S.O. 1935 (E) dated June 1, 2016 issued by the MCA where it constituted NCLT at 11 benches with two in New Delhi and one each in Mumbai, Ahmedabad, Allahabad, Bengaluru, Chandigarh, Chennai, Guwahati, Hyderabad and Kolkata. There is a need for more benches of NCLT as has been discussed in the conclusion of this newsletter

⁴ These powers are captured in Section 7(5), (6) and (7) of the Act

and hear the company's defense as well consider the liabilities before taking a decision. The outcome of furnishing false information is rather wide and the tribunal is empowered with wide discretionary powers which include liquidation as well as direction to modify the charter documents and removal of the company's name from the register of companies. This is in addition to the personal liability which may be fastened on different people who were involved in the falsification process. Like with many other laws, such persons could be exposed to both monetary and penal consequences. It is unclear how seriously the imprisonment aspect will be enforced but the theoretical risk remains.

(b) *Debentures:* Section 71 of the Act describes the framework for debentures as well as the obligations of the debenture trustees, when appointed. Such trustees are empowered to file applications before the NCLT when they conclude the company's assets are insufficient or are likely to become insufficient to discharge the principal amount. The tribunal will protect the interest of the debenture holders and could, after a proper hearing, pass orders restricting the company from incurring further liabilities. Where such orders are passed and there is non-compliance, then the defaulting officers will be liable for fine and imprisonment which could go up to three years.

(c) *Oppression & Mismanagement:* Section 241 of the Act defines the circumstances where minority shareholders can approach NCLT in certain described situations which tantamount to oppression and mismanagement. It is necessary that such minority should be 100 members or those who hold 1/10th of the capital, whichever is less. Further, such shareholders may also file a complaint before the tribunal if there are material changes in the management or control and which are not in the interest of the creditors, debenture holders or other shareholders. It is critical that the applicant should be able to establish that the change will cause a detrimental effect on the company. If NCLT comes to an affirmative finding then it has wide powers, including liquidation.

Apart from the above, the notification mandates prior approval of the NCLT where civil courts do not have any jurisdiction. These are

- alteration in articles that result in conversion of company from public to private;⁵
- issue fresh redeemable shares;⁶
- consolidate or divide shares that results in a change in voting rights;⁷
- re-opening of accounts and voluntary revision of financial statements;⁸ and
- decision regarding securities during on-going investigation into its affairs.⁹

Moreover, sections with regard to constitution, operation and functioning of NCLT and NCLAT have also been notified.¹⁰

⁵ Section 14(1) of the Act cover the aspects of alteration of articles in public and private companies

⁶ Provision for issue and redemption of preference shares covered under Section 55(3) of the Act

⁷ Power of a limited company to alter its share capital captured under Section 61(b) of the Act

⁸ Tribunals power to order reopening of accounts is provided under Section 130 of the Act

⁹ Powers of the tribunal are captured under Sections 221 and 222 of the Act

¹⁰ Section 407-431 of the Act

2. The Expectations

Given the fact that NCLT combines the powers of different forums the expectations from this regulator, touched below, are rather high.

2.1 Consolidated forum: Before NCLT's constitution, matters involving the same companies or parties were spread across different forums viz., High Courts (*for winding-up and merger/amalgamation schemes*), CLB (*for oppression and mismanagement*) and BIFR (*for being declared sick*). Litigants were forced to move different courts and tribunals for seeking different reliefs causing multiplicity of proceedings and delays due to the dearth of a consolidated redressal tribunal. The NCLT is formed with an aim to merge these various forums and provide a single medium for adjudication of all company matters. Having a consolidated platform will, hopefully, provide a smooth passage for litigants to seek reliefs under one roof. It is further expected to save time and resources and provide more efficiency in corporate dispute resolution.

2.2 Efficiency in redressal of company matters: The NCLT and NCLAT are expected to effectively reduce the pendency of cases, expeditiously dispose-off applications and appeals filed before it. Currently, the High Courts are burdened with company matters including liquidation proceedings. Transfer to NCLT is expected to reduce the burden and help lower the High Court pendency. Additionally, as an appeal from an order of NCLT will lie before the NCLAT, High Courts ought to have a further reduced burden, considering that earlier, appeal from the order of CLB had to be filed before the High Court as well. With the notification of the Insolvency and Bankruptcy Code, 2016¹¹ ("**Code**"), NCLT would offer a completely new and improved process for liquidation of Indian companies. The Code replaces the existing bankruptcy laws and creates a new structure for dealing with insolvency. It provides that NCLT shall be the adjudicating authority having territorial jurisdiction over insolvency proceedings¹² which usually are very protracted. The Code reduces this time span with the help of NCLT.¹³

2.3 Class Action Suits: This concept has finally been introduced under section 245 of the Act. Under these proceedings, a class of investors aggrieved by the same act can jointly file a single suit in one forum, as opposed to individuals filing various suits in different forums which, in turn, prevent litigious duplicity. For example, multiple shareholders can file joint proceedings and seek cumulative relief against oppression by the management.

3. The Shortcomings

Pursuant to the notification, pending CLB cases and certain matters from High Courts and BIFR will be transferred to NCLT. The National Company Law Tribunal Rules, 2016 ("**Rules**") have been notified on July 21, 2016 by the MCA which describe powers of NCLT, its function and operations and procedure of transfer of cases from various forums¹⁴. Rule 73 of

¹¹ <http://www.indiacode.nic.in/acts-in-pdf/2016/201631.pdf> last visited on July 22, 2016

¹² Section 60(1) of the Code

¹³ Section 12 of the Code states that the corporate insolvency resolution process should take place within 180 days from admission of application

¹⁴ The NCLT Rules can be accessed at <http://cdn.caclub.in/wp-content/uploads/mca-notification-dt-21-july-2016-nclt-rules-2016.pdf>, last viewed on July 25, 2016

the Rules make it compulsory for all documents to be electronically filed though it is possible to file manually, with NCLT's prior permission.¹⁵ The Rules further provide that e-filing of documents may not be done directly at the registry but would, instead, be done indirectly by transmitting the documents to "Dedicated Portal Online" which will then electronically transmit the documents to the registry. The Rules are quite detailed and their practical implementation will determine if they will be effective or not. Clearly, for efficient operation the technology and its provider will have to provide seamless services.

Conclusion

Introduction of any new reform comes with its own set of challenges. The effect of notification is that CLB stands immediately dissolved. With only 11 benches currently operative, there will be a huge burden on the tribunal to deal with cases transferred from CLB and other forums. This may serve as an impediment in the transition process. Further, not all provisions with respect to NCLT have been notified, such as provisions related to winding-up, capital reduction, amalgamation and compromises which means that High Court continues to exercise jurisdiction over these matters. Once all the provisions regarding functioning of NCLT are notified, there will be more clarity on the effect this has on dispute resolution.

Overall the constitution of NCLT and NCLAT has paved way for a much needed judicial reform. For now all that can be said is that in the light of increasing globalization and the need to move in-sync with changing times, a landmark step has been taken to promote better corporate dispute redressal mechanism.

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¹⁵ The rules pertaining to e-filing will come into force on the date yet to be notified by the central government in the official gazette