



Arvind Kumar Jain\*

\*Insolvency Professional

[2018] 1 IBJ (Art.) 91

## Real Estate Allottee under the Insolvency and Bankruptcy Code, 2016

Pursuant to the amendment in the Insolvency and Bankruptcy Code, 2016, home buyers have been given certain rights which hitherto were not available to them. The author looks into various issues pertaining to home buyers under the Code vis-a-vis Real Estate (Regulation and Development) Act, 2016.

### Introduction

After the initiation of Corporate Insolvency Proceedings of J P Infratech, there was lot of hue and cry for the rights of home buyers. The home buyers who had applied for allotment for flats to J P Infratech found themselves helpless as they were considered neither the Financial Creditors nor the Operational Creditors in the Corporate Insolvency Resolution Process ('CIRP'). To protect their interest the home buyers made representations to the Government and also approached the Supreme Court. The Supreme Court was also of the opinion that the interest of the home buyers should be protected. Ultimately, On June 6, the Insolvency and Bankruptcy Code, 2016, ('Code') was amended through the Insolvency and Bankruptcy Code (Amendment) Ordinance, 2018. Following the Ordinance, 'allottees', including home buyers under the Real Estate Regulations and Development) Act, 2016 ('RERA'), got the status of Financial Creditors under the Code, with the amendment to the definition of 'financial debt'.

### Allottee under the RERA as Financial Creditor under the Code

As per clause (7) of Section 5 of the Code, 'Financial Creditor' means any person to whom a financial debt is owed and includes a person to whom such debt has been legally assigned or transferred to. As per clause (8) of Section 5 'financial debt' means a debt alongwith interest, if any, which is disbursed against the consideration for the time value of money and includes as per sub-clause (f) of that clause any amount raised under any other transaction, including any forward sale or purchase agreement, having the commercial effect of a borrowing. *Explanation* to this sub-clause further says '(i) any amount raised from an allottee under a real estate project shall be deemed to be an amount having the commercial effect of a borrowing, and (ii) the expressions "allottee" and "real estate project" shall have the meanings respectively assigned to them in clauses (d) and (zn) of Section 2 of the RERA.

As per clauses (d) and (e) of Section 2 of the RERA, 'allottee', in relation to a real estate project, means the person to whom a plot, apartment or building, as the case may be, has been allotted, sold (whether as freehold or

leasehold) or otherwise transferred by the promoter, and includes the person who subsequently acquires the said allotment through sale, transfer or otherwise but does not include a person to whom such plot, apartment or building, as the case may be, is given on rent. 'Apartment', whether called block, chamber, dwelling unit, flat, office, showroom, shop, godown, premises, suit, tenement, unit or by any other name, means a separate and self-contained part of any immovable property, including one or more rooms or enclosed spaces, located on one or more floors or any part thereof, in a building or on a plot of land, used or intended to be used for any residential or commercial use such as residence, office, shop, showroom or godown or for carrying on any business, occupation, profession or trade, or for any other type of use ancillary to the purpose specified. Clause (zn) of Section 2 of the RERA defines 'Real Estate Project' to mean the development of a building or a building consisting of apartments, or converting an existing building or a part thereof into apartments, or the development of land into plots or apartment, as the case may be, for the purpose of selling all or some of the said apartments or plots or building, as the case may be, and includes the common areas, the development works, all improvements and structures thereon, and all easement, rights and appurtenances belonging thereto. The 'Allottee', therefore, under the Code is a Financial Creditor not only for the residential purpose but for the commercial purpose as well.

### **Rights of Home Buyers under the Code and RERA**

An allottee in a real estate project, including a home buyer having attained the status of a Financial Creditor under the Code, has following rights in a CIRP:

- He shall be at par with the banks and the financial institutions as Financial Creditor.
- He shall have a right of representation in the Committee of Creditors (CoC) on its own or through an Authorized Representative in a class of creditors.
- By becoming a Financial Creditor, a home buyer would have priority over Government and Operational Creditors.
- He can also initiate a CIRP proceeding against

defaulting promoters by filing an application with the NCLT under Section 7 of Code on the occurrence of a default, as a Financial Creditor.

'Default' has not been amended in the Code. For initiating insolvency proceedings by a home buyers, default might be either non-delivery of home or not refunding the amount with interest. As per Section 18 of the RERA, if the promoter fails to complete or is unable to give possession of an apartment, plot or building, –

- (a) in accordance with the terms of the agreement for sale or, as the case may be, duly completed by the date specified therein; or
- (b) due to discontinuance of his business as a developer on account of suspension or revocation of the registration under the Act or for any other reason,

he shall be liable on demand to the allottees, in case the allottee wishes to withdraw from the project, without prejudice to any other remedy available, to return the amount received by him in respect of that apartment, plot, building, as the case may be, with interest at such rates as may be prescribed in this behalf including compensation in the manner as provided under the Act. Provided that where an allottee does not intend to withdraw from the project, he shall be paid, by the promoter, interest for every month of delay, till the handing over of the possession, at such rate as may be prescribed. Section 19(4) of the RERA stipulates that the allottee shall be entitled to claim the refund of amount paid along with interest at such rate as may be prescribed and compensation in the manner as provided under the Act, from the promoter, if the promoter fails to comply or is unable to give possession of the apartment, plot or building, as the case may be, in accordance with the terms of agreement for sale or due to discontinuance of his business as a developer on account of suspension or revocation of his registration under the provisions of the Act or the rules or regulations made thereunder.

### **Constraints and Issues pertaining to Home Buyers**

Following are the constraints and hindrances in the ultimate benefits to the home buyers and certain issues which may take shape with the passage of time:

- In the meeting of CoC, the voting powers of home buyers might be very less compared to the voting rights of the banks and financial institutions as Financial Creditors. Hence, they might have little say in the CoC.
- The ultimate aim of the home buyer is get his house for which he has been making payments to the builder for years or to get back his money in case of extreme circumstances. In case of insolvency resolution, the project might be delayed, there might be some haircut in the form of quality or specifications or return of money with some hair cut, etc.
- The home buyers as Financial Creditor shall be represented in the CoC through an Authorised Representative appointed by the Insolvency Resolution Professional ('IRP'). He has to choose one among the three representatives recommended by the IRP. The stand of the homebuyers, therefore might not be represented well as per their requirement. Moreover, the home buyers do not have any power for change of Authorised Representative, if required.
- Whether the home buyer is a secured creditor or an unsecured creditor is a matter of discussion. Clause 30 of Section 3 of the Code defines 'secured creditor' to mean a creditor in favour of whom security interest is created. Clause (31) of that Section defines 'security interest' to mean right, title or interest or a claim to property, created in favour of, or provided for a secured creditor by a transaction which secures payment or performance of an obligation and includes mortgage, charge, hypothecation, assignment and encumbrance or any other agreement or arrangement securing payment or performance of any obligation of any person. Provided that security interest shall not include a performance guarantee. The home buyers' contracts with the builder will ultimately determine whether they are secured or unsecured creditors. As per regulation 21 of the IBBI (Liquidation Process) Regulation, 2016, the existence of a security interest may be proved by a secured creditor on the basis of –
  - (i) the records available in an information utility, if any;
  - (ii) certificate of registration of charge issued by the Registrar of companies; or
  - (iii) proof of registration of charge with the Central Registry of Securitization Asset Reconstruction and Security Interest of India.

It would be difficult for a home buyer to prove its security interest as per regulation 21. In case, the home buyers are treated as unsecured, the order of priority in which proceeds from the sale of liquidation assets are to be distributed, on liquidation, under the Code would be almost at the bottom.

- Most of the home buyers take loans from the banks. While taking loans from the banks, they could have subrogated all their rights to the banks and they would no longer be treated as Financial Creditor. It all would depend upon the tripartite agreement executed by the home buyer with the bank and the builder.

### RERA vis-s vis Code

RERA is a platform where the interest of the home buyer is protected as a consumer but in a Corporate Insolvency Resolution Process (CIRP), the emphasis inter alia, is on maximization of the assets of the Corporate Debtor. In the CIRP, the Code takes care of interests of various stakeholders, creditors including home buyers. Under the Code, the home buyers would have a say in the resolution process as a Financial Creditor by participating in the Committee of Creditors which hitherto they were not having. Though, in the process, he might have to go for some sacrifice. RERA is a platform where the home buyers get relief and is exclusively between the developers and its allottees.

### Conclusion

In the public interest, the government has taken a positive step amending the Code providing big relief to home buyers by treating them as Financial Creditor. There are many issues to be sorted out. How far the interest of the home buyers is protected would depend on the issues taking shape in future.



*Disclaimer : The views and opinions expressed in the article are of the author and it does not reflect the views of ICSI IIP.*



CA Binay Kumar Singhania\*

\*Insolvency Professional

[2018] 1 IBJ (Art.) 94

## Rulings of Attachment on Assets by Different Agencies and its Impact on the Insolvency and Bankruptcy Code Cases

In this article the author reviews rulings of the National Company Law Tribunal/Appellate Tribunal on attachment of assets by different agencies and highlights its impact on the cases decided under the Insolvency and Bankruptcy Code.

### Appellate Tribunal Ruling - Banks to have First Right over Pledged Assets Attached by Enforcement Directorate

In a landmark ruling given by the Appellate Tribunal under the Prevention of Money Laundering Act, 2002 (PMLA) on 2<sup>nd</sup> August, 2018 in the case of *Winsome Diamonds & Jewellery* ('Winsome Diamonds'), where the assets were attached under the PMLA. It was ruled that Enforcement Directorate (ED) cannot claim rights over assets of borrowers suspected of criminal activity, if banks and any other financial institution have created charge over those assets against the financial loans granted to the borrowers.

### Who is Directorate of Enforcement?

Directorate of Enforcement is a specialized financial investigation agency under the Department of Revenue, Ministry of Finance, Government of India, which enforces the following Acts :

*Foreign Exchange Management Act, 1999 (FEMA)* – A civil law where officers are empowered to conduct investigations into suspected contraventions of the Foreign Exchange Laws and Regulations, adjudicate the contraventions and impose penalties on those adjudged to have contravened the law.

*Prevention of Money Laundering Act, 2002 (PMLA)* – A criminal law and ED is empowered to conduct investigations to trace assets derived out of the proceeds of crime, to provisionally attach/ confiscate the same, and to arrest and prosecute the offenders found to be involved in money laundering. There are various crimes which are scheduled under the PMLA and fraud with the banks is one of the scheduled crimes under the PMLA and proceeds of alleged crime will vest with exchequer.

### Facts of Winsome Diamonds Case

Winsome Diamonds is a company where lenders are trying to recover more than Rs 4,600 crore after the company became insolvent because of fraudulent transactions by the promoters, including Jatin Mehta who is under investigation. Winsome Diamonds borrowed Rs 4,617 crore from 14 different banks by 2012 by pledging its properties at many locations. The loans were given to three group companies, Winsome Diamond & Jewellers, Forever Precious Diamond

& Jewellery and Suraj Diamonds. By 2013, these companies started defaulting on loans and were soon declared wilful defaulter and banks initiating recovery process which got stalled by the ED's attachment of assets. "The mortgaged properties are not derived or obtained, directly or indirectly from the criminal activity or the proceeds of crime," the order said.

### Ruling in Winsome Diamonds Case

The Appellate Tribunal ruled in favour of Standard Chartered Bank who was the petitioner in this case. The Appellate Tribunal said that the banks while providing the facilities are bonafide parties and none of the banks have committed any offence. Hence, no PMLA proceedings are pending against the banks. Further, it also stated that the mortgaged properties are security to the loans and cannot be subject matter of attachment particularly when the same were purchased and mortgaged prior to the events of funds diversion and fraud committed by the borrowers. The appellant bank is entitled to recover amounts in the above loan accounts and the appellant bank being the mortgagee/transferee of the interest in the properties is entitled to recover its dues with the sale of the properties. The properties stood transferred by way of mortgage to the appellant bank much before the alleged criminal action," the Tribunal noted in its order. The Appellate Tribunal further said that the banks have priority on assets to recover the loan amount by sale of assets over which their security interest is created, which remains unpaid. In many loan default and fraud cases, the recovery efforts get impeded by similar attachment of properties by enforcement agencies. Bankers said this order speed up resolution of non-performing assets.

### Latest NCLT Order De-attaching Assets from ED in the Case REI Agro Ltd.

On 31<sup>st</sup> August 2018, NCLT, Kolkata Bench passed an order for de-attachment of assets of REI Agro Ltd. Tribunal stated that ED can attach the property acquired through fraudulent means but the distribution of assets can be made through Companies Act which has been superseded by Insolvency and Bankruptcy Code. Liquidator of company, CA. Anil Goel, who is founder of AAA Insolvency professionals LLP, had appealed before Appellate Tribunal for de-attachment of assets. The Appellate Tribunal ordered

de-attachment of assets which were attached on 21<sup>st</sup> February 2018.

### Impact of the Ruling in REI Agro Ltd. Case

The order is expected to provide resolution of cases under the Code where properties and assets mortgaged in favour of banks are stuck in legal battles and multiplicity of proceedings especially in cases of loan frauds. Resolution Applicants either run away from submission of resolution plan or reduce the amount substantially under resolution plan considering the attachment by ED as seen in another city case, *Verrisana Ispat Ltd.* In this case, Insolvency Professional has approached NCLT to exclude the litigation period while calculating Corporate Insolvency Resolution Process ('CIRP') time limit to get best bid for resolution amount in view of hope for de-attachment of assets in view of recent de-attachment orders by Appellate Authority under the PMLA and by the NCLT, Kolkata in other cases. This order shall help clear the confusion and enable banks to recover their funds through sale of mortgages assets. This is useful at a time when banks are pursuing possibilities of NPA resolution at the various Benches of the NCLT. It has been seen that in many cases income-tax department was asked to release the attachment considering moratorium under Section 14 of the Code activated on admission of case with the NCLT. The recent judgement of Supreme Court in the matter of *Monnet Ispat & Energy Ltd.* [SLP (C) No. 6483/2018 dated 10<sup>th</sup> August 2018] has also cleared all apprehensions about the rights of the Income-tax Department under the Code and their priority under the waterfall arrangement under Section 53 of the Code.

### Conclusion

The Code is settling down with most of the apprehensions over the rulings by different courts such as clarity regarding priority of the Income-tax Department (*Monnet Ispat & Energy Ltd.*) ; rights of ED in the cases under IBC (*REI Agro Ltd.*) ; the lien of electricity department on the land against unpaid electricity dues (*Raman Ispat Pvt Ltd.*) ; right to resume the allotted plot or cancel the allotment of industrial plot by state land development agencies (*Vindhya Vasini Pvt Ltd.*)



*Disclaimer : The views and opinions expressed in the article are of the author and it does not reflect the views of ICSI IIP.*