

NON-PAYMENT OF LICENSE FEE IS AN OPERATIONAL DEBT

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NON-PAYMENT OF LICENSE FEE IS AN OPERATIONAL DEBT

In a recent pronouncement in **Jaipur Trade Expocentre Private Limited v. M/s Metro Jet Airways Training Private Limited**[1], (“**Jaipur Trade Case**”), a five-member bench of the Hon’ble National Company Law Appellate Tribunal (“**NCLAT**”) has set aside the decision laid down in *Mr. M. Ravindranath Reddy v. Mr. G. Kishan & Ors.*[2] and held that the claim of a licensor for payment of license fee for use of demised premises for business purposes is an operational debt within the meaning of Section 5(21) of the Insolvency & Bankruptcy Code, 2016 [3] (“**Code**”).

In *M. Ravindranath Reddy* (supra), a three-member Bench of the NCLAT had examined the meaning of ‘essential goods and services’ under Regulation 32 of the Insolvency and Bankruptcy Board of India [4] (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 read with Section 14(2) of the Code [5] and held that lease of immovable property cannot be considered as a supply of goods or rendering of services, and thus, cannot fall within the definition of operational debt.

FACTS

Jaipur Trade Expocentre Private Limited (“**JTE**”) and M/s Metro Jet Airways Training Private Limited (“**MJAT**”) executed a License Agreement dated 15.04.2017 (“**the Agreement**”) for grant of license of a

[1] C.A. (AT) (Ins) No. 423/2021 dated 05.07.2022

[2] C.A. (AT) (Ins) No. 331/2019 dated 17.01.2020

[3] 5. Definitions –

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(21) “operational debt” means a claim in respect of the provision of goods or services including employment or a debt in respect of the 2[payment] of dues arising under any law for the time being in force and payable to the Central Government, any State Government or any local authority;

[4]32. Essential supplies. –

The essential goods and services referred to in section 14(2) shall mean–

(1) electricity;

(2) water;

(3) telecommunication services; and

(4) information technology services,

to the extent these are not a direct input to the output produced or supplied by the corporate debtor

[5]14. Moratorium –

xxx

(2) The supply of essential goods or services to the corporate debtor as may be specified shall not be terminated or suspended or interrupted during moratorium period.

a certain area to be utilised for running an educational establishment for a period of five years. The parties agreed on a license fee of INR 4 Lakhs plus taxes per month. MJAT made a part payment of the license fee through cheques, which were subsequently dishonoured. On account of MJAT's default, JTE moved an insolvency application under Section 9 of the Code against MJAT before the Hon'ble National Company Law Tribunal ("**NCLT**"). The NCLT dismissed the application on the ground that grant of a license for use of immovable property did not fall in the category of providing goods or services. Hence, the amount claimed was not an unpaid operational debt. Aggrieved by this decision, JTE approached the NCLAT.

ISSUES

The issues for examination before the NCLAT were:

- Whether the M. Ravindranath Reddy judgment (supra) lays down the correct law.
- Whether the claim of a licensor for payment of license fee for use and occupation of immovable premises for commercial purposes is a claim of operational debt within the meaning of Section 5(21) of the Code.

JUDGMENTS BY NCLAT

Before analysing the NCLAT order, it is necessary to revisit the precedents relied upon by the parties to buttress their arguments and the NCLAT's view in each of those cases:

- *Mr. M. Ravindranath Reddy v. Mr. G. Kishan & Ors.* ("**Reddy Judgment**")

The matter was considered by a three-member bench of the NCLAT. The question in this case was whether lease of premises by a landlord to the corporate debtor could be treated as providing services to the corporate debtor, and therefore make the landlord, an operational creditor under the Code. While placing reliance on Regulation 32 of the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 read with Section 14(2) of the Code,

the NCLAT held that lease of immovable property could not be considered as supply of goods or rendering of any service. The NCLAT looked into the meaning of essential goods and services under Section 14(2) of the Code, i.e., electricity, water, telecommunication services and information technology services to the extent that these were not a direct input to the output produced or supplied by the corporate debtor. The NCLAT went on to hold that a debt arising without nexus to the direct input to the output produced or supplied by the corporate debtor, could not, in the context of Code, be considered an operational debt, even though it was a claim amounting to debt

- *Anup Sushil Dubey v. National Agriculture Co-Operative Marketing Federation Limited* [6] (“**Anup Dubey Judgment**”)

One of the questions framed in the aforesaid case was whether dues arising from a leave and license agreement were to be construed as an operational debt. Here, the NCLAT was of the opinion that the subject lease rentals arising out of use and occupation of a cold storage unit (being subject matter of the Leave & License Agreement between the parties) were utilised for a commercial purpose, therefore, such claim had to be an operational debt under Section 5(21) of the Code.

- *Promila Taneja v. Surendri Design Private Limited* [7] (“**Taneja Judgment**”)

The question of rent being an operation debt under the Code was again raised and the NCLAT placing reliance on the three-member Bench in the Reddy Judgment, held that dues in the nature of rent of an immovable property would not fall under Section 5(21) of the Code.

The Taneja Judgment is presently under challenge in *Promila Taneja v. Sunderi Design Pvt. Ltd.* [8] before the Supreme Court to settle the controversy raised by the conflicting views taken by the NCLAT as discussed above.

[6] C.A. (AT) (Ins) No. 229/2020 dated 07.10.2020

[7] C.A. (AT) (Ins) No. 459/2020 dated 10.11.2020

[8] C.A. No 4237/2020

NCLAT'S DECISION IN JAIPUR TRADE CASE

The view taken by the five-member NCLAT Bench is briefly summarised below:

- **Agreement was for providing a service under Section 5(21)**

The NCLAT observed that a specific provision for payment of Goods & Services Tax (“GST”) by MJAT was made in the Agreement. This could have only been contemplated qua goods or services that was the subject matter of the Agreement. Had the Agreement not contemplated provision of services to MJAT, there was no occasion for making MJAT liable for GST over and above the license fee. Thus, the Agreement between the parties was regarding services within the meaning of Section 5(21) of the Code.

- **Claims arising out of the Agreement are debt in terms with Section 3(11)**

The Agreement between the parties could squarely be covered in the definition of ‘transaction’ in terms of Section 3(33) of the Code [9] and any claim by JTE for payment of license fee arising from such Agreement would be covered under Section 3(6) of the Code [10]. Hence, any liability or obligation in respect of a claim would become a debt on the part of the Corporate Debtor within the meaning of Section 3(11) of the Code[11]

- **Law laid down in the Ravindranath Reddy Judgment is incorrect**

While considering the Ravindranath Reddy Judgment, the NCLAT opined that reference to Section 14(2) did not cater to the extent and expanse of the meaning of ‘operational debt’. ‘Operational debt’ as defined in Section 5(21) of the Code had a much wider meaning than the meaning of

[9] 3. Definitions –

(33) “transaction” includes an agreement or arrangement in writing for the transfer of assets, or funds, goods or services, from or to the corporate debtor;

[10] 3. Definitions –

(6) “claim” means –

(a) a right to payment, whether or not such right is reduced to judgment, fixed, disputed, undisputed, legal, equitable, secured, or unsecured;

(b) right to remedy for breach of contract under any law for the time being in force, if such breach gives rise to a right to payment, whether or not such right is reduced to judgment, fixed, matured, unmatured, disputed, undisputed, secured or unsecured;

[11] 3. Definitions –

(11) “debt” means a liability or obligation in respect of a claim which is due from any person and includes a financial debt and operational debt;

essential goods and services' specified under Section 14(2). Thus, the observations made by the NCLAT in that case that there had to be a nexus to the direct input or output produced or supplied by the corporate debtor, was a much wider observation not supported by the scheme of the Code.

Discussing **Mobilox Innovations (P) Ltd. v. Kirusa Software (P) Ltd.**[12], the NCLAT placed reliance on Para 5.2.1 of the Bankruptcy Law Reforms Committee Report, 2015 which had recommended that a lessor that the entity rents out space from, is an operational creditor to whom the entity owes monthly rent on a three-year lease. It was the NCLAT's view that the recommendations under the Report were for understanding the nature and context of operational debt, and such illustrations could not be disregarded as irrelevant and meaningless.

Further, the NCLAT observed the dues were on account of license granted for use of premises on warm shell building with fittings and fixtures, electrical, flooring as per good corporate standards. Hence, the licensee was licensed for a particular kind of service for use by the licensee for running a business of educational institution. Thus, debt pertaining to unpaid license fee is fully covered within the meaning of 'operation debt' under Section 5(21).

While the decision of the Supreme Court in *Promila Taneja v. Sunderi Design Pvt. Ltd.* is still awaited, the present decision of the NCLAT is a blessing for entities leasing out commercial spaces on leases providing them with better security and leverage on account of default by their lessees and a footing to have its claims addressed in the resolution process of a lessee corporate debtor.

[12] (2018) 1 SCC 353



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