Between the lines...

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Key Highlights

I. Supreme Court: Related parties cannot be included in the committee of creditors by way of collusive transactions

The Supreme Court (**"SC"**) has in its judgement dated February 1, 2021 in the matter of ***Phoenix Arc Private Limited v. Spade Financial Services Limited and Others [Civil Appeal No. 2842 of 2020]*** (**"Judgement"**) held that those related party financial creditors that cease to be related parties in order to circumvent their exclusion from the committee of creditors, under the first proviso to Section 21(2) of the Insolvency and Bankruptcy Code, 2016 (**"IBC"**), should also be considered as being covered by the exclusion thereunder.

Facts

This Judgement governs two sets of appeals arising from the order of the National Company Law Appellate Tribunal (**"NCLAT"**) dated January 27, 2020. The NCLAT had dismissed the appeal preferred by AAA Landmark Private Limited (**"AAA"**) and Spade Financial Services Private Limited (**"Spade"**) against the National Company Law Tribunal, New Delhi Bench-III (**"NCLT"**) order dated July 19, 2019 (**"NCLT Order"**), which ruled that they needed to be excluded from the committee of creditors (**"CoC"**) formed for the corporate insolvency resolution process (**"CIRP"**) against AKME Projects Limited, the Corporate Debtor (**"Corporate Debtor"**). The first appeal was preferred by Phoenix Arc Private Limited (**"First Applicant/ Appellant"**), which, while agreeing with the NCLAT order of excluding Spade and AAA (collectively referred to as **"Second Applicants/ Respondents"**) from CoC, on account of being related parties of Corporate Debtor, disagreed with their being classified as

financial creditors (**"Financial Creditor"**). Another appeal was independently filed by the Second Applicants to challenge the NCLAT order with regard to their exclusion from the CoC.

Mr. Anil Nanda, is a majority shareholder of Joint Investment Private Limited (**"JIPL"**), which in turn held a stake in Spade and 80% shareholding in the Corporate Debtor. The Corporate Debtor is a part of Anil Nanda Group of Companies (**"Group Companies"**). Mr. Arun Anand was the Group CEO of the Group Companies, which included the Corporate Debtor, from November 26, 2012 to February 14, 2013, and a director of the Second Applicants. Mr. Arun Anand was also a director of the Corporate Debtor up to March 31, 2002. Further, Mr. Arun Anand is the brother-in-law of Mr. Sonal Anand who was a director of the Corporate Debtor from 2007 to 2013, at the time when the relevant transactions between the Second Applicants and the Corporate Debtor took place. After February 2013, Mr. Arun Anand had no relation with the Corporate Debtor.

Spade had filed its claim as a Financial Creditor for a sum of INR 109 crores on May 20, 2018 on the basis of an alleged Memorandum of Understanding dated August 12, 2011 (**"MOU"**) executed with the Corporate Debtor, which stated that Inter Corporate Deposits (**"ICDs"**) were granted to the Corporate Debtor by Spade bearing an interest of 24%, though in actuality only 12% interest was charged. AAA, a wholly owned subsidiary of Spade, had entered into a Development Agreement on March 1, 2012 (**"Development Agreement"**), through which Corporate Debtor sold 38.3% of its development rights in its real estate project, AKME RAAGA, to AAA for INR 32.80 crores. Subsequently, an Agreement to Sell dated October 25, 2012 (**"Agreement to Sell"**), which superseded the Development Agreement was entered into, through which AAA bought a saleable area of 313,928 square feet in AKME RAAGA at a price of INR 43.06 crores. A side letter dated October 25, 2012 (**"Side Letter"**), which was to be read as a part of the Agreement to Sell, noted that the area bought by AAA was 38.3% of AKME RAAGA, and AAA would provide for the cost of its development accordingly.

The CoC was constituted on May 22, 2018. The Interim Resolution Professional (**"IRP"**) rejected the claim of Spade, *inter alia,* on the ground that the claim was not in the nature of a financial debt in terms of Section 5(8) *(Financial debt)* of the IBC, since there was an absence of consideration for the time value of money, that is, the period of repayment of the claimed ICDs was not stipulated. The IRP also rejected the claim of AAA on the ground that its claim as a Financial Creditor was filed after the expiry of the period for filing such a claim.

Aggrieved, the Second Applicants initiated proceedings before the NCLT, which, by its order on May 31, 2018 (**"2018 Order"**) allowed the applications. However, none of the other Financial Creditors, such as the First Applicant, were parties to these proceedings. Subsequently, on an application moved by the First Applicant and Yes Bank, another Financial Creditor of the Corporate Debtor, for the exclusion of Second Applicants from the CoC on the ground that they were related parties to the Corporate Debtor, the NCLT by its order dated July 19, 2019 ruled that Second Applicants were not Financial Creditors to the Corporate Debtor. In an appeal to the NCLAT by the Second Applicants, it was held that the Second Applicants were related parties to the Corporate Debtor, on the ground that, *inter alia,* during the transaction period, Spade led by Mr. Arun Anand was making financial arrangements on the advice of Corporate Debtor led by Mr. Anil Nanda, promoter of Corporate Debtor and Mr. Sonal Anand, brother-in-law of Mr.

Arun Anand. One such arrangement was the MOU. The NCLAT also noted that AAA was a partner of the Corporate Debtor in accordance with Section 5(24)(a) *(Related party)* of the IBC. It further reasoned that Corporate Debtor was acting on the directions of Mr. Arun Anand, who, along with his family, was the majority shareholder in Spade, of which AAA is a wholly-owned subsidiary. Hence, NCLAT came to the conclusion that though the Second Applicants were admittedly Financial Creditors of the Corporate Debtor, the NCLT had rightly excluded the Second Applicants from participation in the CoC, since Mr. Anil Nanda, in concert with Mr. Arun Anand and his family, was trying to gain a backdoor entry into the CoC through the web of companies that were related parties to the Corporate Debtor. Aggrieved with the NCLAT order, both the First and Second Applicants moved the SC.

Issues

1. Whether Second Applicants were Financial Creditors of the Corporate Debtor.
2. Whether Second Applicants were related parties of the Corporate Debtor.
3. Whether Second Applicants should be excluded from the CoC.

Arguments

Contentions raised by the First Applicant:

The issue raised by the First Applicant against the NCLAT order was that while the NCLAT correctly dismissed the appeal file by the Second Applicants, deeming them to be related parties and thereby excluding them from the CoC, the NCLAT wrongly pronounced that the Second Applicants were "admittedly" Financial Creditors. This stance was never taken or admitted by the First Applicant and hence it sought to challenge this part of the NCLAT order. It was argued that the Second Applicants were not creditors, let alone Financial Creditors of the Corporate Debtor, as per Section 5(7) *(Financial creditor)* of the IBC. Further, it was contended that the Development Agreement was collusive in nature. AAA had sought to purchase 38.3% of the development rights in AKME RAAGA as a co-developer or partner. However, the development license granted by the government could not be sub-divided. As a result, the Corporate Debtor and AAA converted the Development Agreement into an unregistered Agreement to Sell. AAA had subsequently executed an unlawful Side Letter with the intention to co-develop the land and sell it in the market. Thus, it was argued that the intent of the parties was to circumvent the laws, government policies and regulations to continue developing the project. It was also argued that the MOU on the basis of which Spade submitted its claim was collusive and unenforceable and such claim was time barred. The IRP rejected the claim of Spade, *inter alia,* on the ground that the claim was not in the nature of a financial debt in terms of Section 5(8) of the IBC since there was an absence of consideration for the time value of money, that is, the period of repayment of the claimed ICDs was not stipulated. The IRP also rejected the claim of AAA on the ground that its claim as a Financial Creditor in Form C was filed after the expiry of the period for filing such a claim.

It was further submitted that Mr. Arun Anand incorporated the Corporate Debtor in 2003, which was subsequently acquired by Mr. Anil Nanda in 2007. During the relevant transactions with the Second Applicants, Mr. Arun Anand

held the position of Consultant or Strategic Advisor to the Corporate Debtor, and later became the Group CEO of the Group Companies of which the Corporate Debtor was also a part. During this period, Mr. Arun Anand's brother in-law, Mr. Sonal Anand, was a director of the Corporate Debtor. Further, he was also the whole-time director of JIPL, a wholly-owned subsidiary of the Corporate Debtor, and held shareholding in Spade, and Mr. Anil Nanda was a promoter/director of the Corporate Debtor. The litigation between Spade and the Corporate Debtor was initiated after the IBC came into force to create a notion of dispute. It was also argued that the provisions of Section 21(2) *(Committee of creditors)* of the IBC must be interpreted in a purposive manner so as to not defeat the fulfilment of the objects of the legislation.

Contentions raised by the Second Applicants:

It was submitted that the issue of whether or not they were Financial Creditors was dealt with by the 2018 Order and this operated as *res judicata.* The question of eligibility of the Second Applicants as Financial Creditors was never raised before the NCLT by First Applicant. The NCLT was strictly meant to deal with whether or not they were related parties of the Corporate Debtor. Subsequently, in the appeal before the NCLAT, the only issue that came into consideration was whether or not they were Financial Creditors. Though the NCLAT adjudged them to be Financial Creditors, it dismissed the appeal on the ground that they were related parties, which according to the Second Applicants, was an error of jurisdiction, since the question of them being related parties was not under consideration.

It was argued that there were no common key managerial personnel or directors between the Corporate Debtor and the Second Applicants during the relevant period of the transactions between 2010 to 2013. The NCLAT had incorrectly held that Mr. Arun Anand was in a position to influence the decision making of the Corporate Debtor, without satisfying the test of "control" established in ***Arcelor Mittal India Private Limited v. Satish Kumar Gupta [(2019) 2 SCC 1].*** Mr. Arun Anand had no decision-making powers, nor could he influence any policy making decision. JIPL and through it, the Corporate Debtor held 1.45% in Spade, below the requisite 2% threshold in Section 5(24)(d) of the IBC. It was also argued that the Corporate Debtor and AAA were not partners according to Section 5(24)(a) of the IBC.

First proviso to Section 21(2) of the IBC denies the right of representation, participation or voting in a meeting of the CoC to a Financial Creditor or an authorized representative of the Financial Creditor, if it is a related party of the corporate debtor. Laying stress on the expression *"'is' a related party of the corporate debtor",* the submission was that the statute applies *in praesenti* on the date of the admission of an application seeking the initiation of the CIRP. It was urged that the existence of a live link of being a related party in the present is a requirement of the statutory provision.

Observations of the Supreme Court

Eligibility as Financial Creditors:

Addressing the question of *res judicata,* the SC did not deem the 2018 Order as *res judicata.* The order was passed without hearing the other Financial Creditors, such as the First Applicant and YES Bank, hence they were well within their rights to seek direction for the exclusion of Second Applicants from the CoC, if they were aggrieved by the terms of the 2018 Order. Considering the question of jurisdiction of the NCLAT, the SC disagreed with the contention that the NCLAT had acted outside of its jurisdiction. On analyzing the NCLT Order, the SC could not accept the submission that the application filed by Second Applicants was rejected only on the basis that they were not Financial Creditors and that there was no determination in regard to their status as related parties, as the NCLT Order had dealt with those issues as well.

The SC observed that under Section 5(7) of the IBC, a person could be categorized as a Financial Creditor if a financial debt is owed to it. Section 5(8) of the IBC stipulates that the essential ingredient of a financial debt is disbursal against consideration for the time value of money. As per the report of the Insolvency Law Committee in 2018, *"The words "time value" have been interpreted to mean compensation or the price paid for the length of time for which the money has been disbursed. This may be in the form of interest paid on the money or factoring of a discount in the payment.".* Money advanced as debt should be in the receipt of the borrower. The borrower is obligated to return the money or its equivalent along with the consideration for a time value of money, which is the compensation or price payable for the period of time for which the money is lent. The SC noted that the IBC recognizes that for the success of an insolvency regime, the real nature of the transactions has to be unearthed to prevent any person from taking undue benefit of its provisions to the detriment of the rights of legitimate creditors. A transaction is collusive when the real agreement between the parties is something other than advancing a financial debt. The SC observed that the MOU on the basis of which Spade staked its claim was unstamped and unregistered and did not stipulate a period of repayment. Hence, the consideration for time value of money was absent, which is an essential ingredient of a financial debt.

Analyzing the observations in the NCLT Order, the SC noted that the Corporate Debtor had entered into multiple agreements with AAA regarding the same property without giving any explanation or rationale regarding variation in the consideration. This showed that the transactions were collusive in nature entered with the purpose of diverting properties of the Corporate Debtor to AAA. The SC opined that the parties converted the Development Agreement into an Agreement to Sell executed along with a Side Letter to circumvent the legal prohibition on splitting a development license in two parts. Thus, the transaction between AAA and the Corporate Debtor was collusive in nature.

Related Parties:

The SC found it extremely crucial to understand the relationship between Mr. Arun Anand and Mr. Anil Nanda. Mr. Arun Anand has held multiple positions in companies which form part of the Group Companies. Further, Mr. Anil

Nanda has himself invested in companies owned by Mr. Arun Anand, and had commercial transactions with them. Through the Second Applicants' own admission, Mr. Arun Anand was appointed as the Group CEO of the Group Companies on approval of Mr. Anil Nanda himself. Mr. Arun Anand's brother in-law, Mr. Sonal Anand, had also been consistently associated with companies in the Group Companies, including the Corporate Debtor and JIPL. Mr. Arun Anand was in control of the Second Applicants during the relevant period. Further, he held positions in the Corporate Debtor or the Group Companies, which included the Corporate Debtor. Mr. Anil Nanda and Mr. Sonal Anand also held positions in the Corporate Debtor and JIPL during this period. Thus, Mr. Arun Anand would be a related party of the Corporate Debtor in accordance with Sections 5(24)(h) and 5(24)(m)(i) of the IBC. While determining whether Mr. Arun Anand participated in the policy-making process of the Corporate Debtor, the SC observed that there was a deep entanglement between the entities of Mr. Arun Anand and Mr. Anil Nanda, and Mr. Arun Anand held such positions at the time of the relevant transactions which could have been used by him to guide the affairs of the Corporate Debtor. The SC thus concluded that Spade undertook the transactions due to the pervasive influence of Mr. Anil Nanda. It was also decided that the transactions between AAA and Corporate Debtor were collusive in nature and thus AAA was a partner of the Corporate Debtor within the meaning of Section 5(24)(a) of the IBC.

Exclusion from the CoC:

The SC observed that the objects and purposes of the IBC are best served when the CIRP is driven by external creditors, so as to ensure that the CoC is not sabotaged by related parties of the corporate debtor. This was the intent behind the first proviso to Section 21(2) of the IBC which disqualifies a Financial Creditor or the authorized representative of the Financial Creditor under Sections 24(5), 24(6) or 24(6A) of the IBC, if it is a related party of the corporate debtor, from having any right of representation, participation or voting in a meeting of the committee of creditors. While considering the issue of interpretation in relation to the first proviso to Section 21(2) of the IBC as to whether the disqualification under the said proviso would attach to a Financial Creditor only *in praesenti,* the SC examined the object and purpose behind the enactment of the said proviso. The SC relied on ***Abhay Singh Chautala v. C.B.I. [(2011) 7 SCC 141],*** where the court did not interpret the word "is" *in praesenti* because that would lead to an absurd result, defeating the purpose of the concerned proviso, that is, Section 19(1) of the Prevention of Corruption Act, 1947. The purpose of excluding a related party of a corporate debtor from the CoC is to obviate conflicts of interest which are likely to arise in the event that a related party is allowed to become a part of the CoC. The SC noted that exclusion under the first proviso to Section 21(2) of the IBC was related not to the debt itself but to the relationship existing between a related party Financial Creditor and the corporate debtor. Therefore, the Financial Creditor who *in praesenti* is not a related party, would not be debarred from being a member of the CoC. However, those related party Financial Creditors that cease to be related parties in order to circumvent the exclusion under the first proviso to Section 21(2) of the IBC, should also be considered as being covered by the exclusion. If this was not done, the related party to the Financial Creditor can devise a mechanism to remove its label of a 'related party' before the corporate debtor undergoes CIRP, so as to be able to enter the CoC and influence its decision making at the cost of other Financial Creditors. The SC observed the presence of a deeply entangled

relationship between Spade, AAA and the Corporate Debtor, when the alleged financial debt arose. It concluded that though their status as related parties no longer existed, it was due to commercial contrivances through which they sought to enter the CoC, that they could not be allowed to be a part of the CoC.

Decision of the Supreme Court

Partially upholding the NCLAT order, the SC held that since the commercial arrangements between Second Applicants and the Corporate Debtor were collusive in nature, they would not constitute a 'financial debt'. Hence, it was held that the Second Applicants were not Financial Creditors of the Corporate Debtor. Mr. Arun Anand and the Second Applicants were related parties of the Corporate Debtor during the relevant period when the transactions on the basis of which the Second Applicants claimed their status as Financial Creditors took place. Thus, it was held that the pervasive influence of Mr. Anil Nanda over these entities was clear, and allowing them in the CoC would definitely affect the other independent Financial Creditors. Contrary to what the NCLAT had observed, the Second Applicants could not be called Financial Creditors.

VA View:

The key takeaway from this Judgement is that the SC has ensured that the sanctity of the CoC is not compromised by the action of a corporate debtor who through its related parties tries to gain backdoor entry into the CoC by way of collusive transactions. Merely because a Financial Creditor conveniently removes the label of related party from itself, just before the corporate debtor enters into CIRP, with the sole intention of participating in the CoC and sabotaging the CIRP, it cannot be granted the advantage of being included in the CoC.

The SC has also recognized that, for the success of the IBC, it is imperative that the true nature of the transactions be unearthed so as to prevent any person from taking undue advantage of its provisions to the detriment of the rights of the rightful creditors and has hence excluded collusive transactions from the ambit of financial debt. Thus, by this path breaking Judgement, the SC has precluded the opportunity for unscrupulous parties from staking a claim in the CoC and exploiting the provisions of the IBC based on collusive transactions to their advantage.

II. Supreme Court: If a corporate debtor has only offered security by pledging shares, without undertaking an obligation to discharge the borrower's liability, then the creditor in such a case will not become 'financial creditor' *vis-à-vis* the corporate debtor as defined under the IBC

The Hon'ble Supreme Court (**"SC"**) has in its judgment dated February 03, 2021 (**"Judgement"**), delivered by a three judge bench, in the matter of ***Phoenix Arc Private Limited v. Ketulbhai Ramubhai Patel [Civil Appeal No.5146 Of 2019],*** held that if a corporate debtor has only offered security by pledging shares, without undertaking an obligation to discharge the borrower's liability, then the creditor in such a case will not become

'financial creditor' *vis-à-vis* the corporate debtor as defined under the Insolvency and Bankruptcy Code, 2016 (**"IBC"**).

Facts

Phoenix ARC Private Limited (**"Appellant"**) filed an appeal under Section 62 of the IBC against the judgment of the National Company Law Appellate Tribunal, New Delhi (**"NCLAT"**) dated April 09, 2019 wherein the NCLAT had dismissed the appeal filed by Appellant and held that pledge of shares in question did not amount to disbursement of any amount against the consideration for the time value of money and that it did not fall within the ambit of Section 5(8)(f) of the IBC. Previously, National Company Law Tribunal, Mumbai (**"NCLT"**) by order dated February 22, 2019 had rejected the miscellaneous application filed by the Appellant under Section 60(5)(c) of the IBC and held that the Appellant is not a financial creditor of Doshion Veolia Water Solutions Private Limited (**"Corporate Debtor"**).

The predecessor of the Appellant, L & T Infrastructure Finance Company Limited (**"Lender"**) advanced a financial facility of INR 40 crores repayable in 72 structured monthly instalments, to Doshion Limited (**"Borrower"**) (the parent company of the Corporate Debtor), by way of a facility agreement dated May 12, 2011 (**"Facility Agreement"**) executed between the Lender and the Borrower. The board of directors of Corporate Debtor passed a resolution on July 26, 2011 to give 'Non-Disposal Undertaking' in favour of the Lender whereby it was authorised to provide an undertaking to the effect that 100% of the Corporate Debtor's shareholding in Gondwana Engineers Limited (**"GEL"**) shall not be disposed of so long as any amounts were due, payable and outstanding under the financial assistance provided by the Lender to the Borrower. The said deed of undertaking was executed by the Corporate Debtor in favour of the Lender (**"Deed of Undertaking"**) on January 10, 2012.

On January 10, 2012, an agreement was also executed between the Corporate Debtor and the Lender by which, 40,160 shares of GEL were pledged as a security (**"Pledge Agreement"**). Subsequently, by agreement dated December 30, 2013 (**"Assignment Deed"**), the Lender assigned all rights, title and interest in the financial facility including any security, interest therein in favour of the Appellant under Section 5 *(Acquisition of rights or interest in financial assets)* of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002.

Subsequently, the Borrower failed to repay the loan as per the terms of the Facility Agreement. Therefore, the Appellant issued a notice dated February 19, 2014 and recalled the financial facility. Further, the Appellant filed an application before the Debts Recovery Tribunal, Ahmedabad.

In the interim, Bank of Baroda (**"Intervenor"**) filed a company petition before the NCLT under Section 7 of the IBC to initiate the corporate insolvency resolution process (**"CIRP"**) in respect of the Corporate Debtor which was admitted by an order dated August 31, 2018.Consequently, the CIRP commenced, thereby the interim resolution professional for the Corporate Debtor was appointed, who was later confirmed as the resolution professional (**"Respondent"**). Subsequently, the Appellant filed a claim for an amount of INR 83,49,85,667/- with the

Respondent. The Appellant stated that pledge of shares by the Corporate Debtor was in essence a guarantee for financial debt and, therefore, Appellant was a financial creditor of the Corporate Debtor. However, the Respondent by e-mails dated September 20, 2018 and November 23, 2018, expressed an opinion that as per the Pledge Agreement, the Corporate Debtor's liability was restricted to pledge of the shares only. The Respondent by e-mail dated December 04, 2018 rejected the claim of the Appellant as financial creditor of the Corporate Debtor on the ground that there was no separate deed of guarantee executed in favour of the Lender by the Corporate Debtor.

Thereafter, the Appellant filed miscellaneous application before the NCLT, seeking a direction to the Respondent to admit the claim of the Appellant as a financial debt with all consequential benefits. However, the NCLT rejected the application. Subsequently, the NCLAT dismissed the appeal filed by the Appellant. Aggrieved by the judgment of the NCLAT, the Appellant filed an appeal before the SC.

The relevant provisions in the instant case include Sections 5(7) *(definition of financial creditor),* 5(8) *(definition of financial debt),* 3(10) *(definition of creditor)* and 3(11) *(definition of debt)* of the IBC.

Issue

Whether the Appellant is a financial creditor *qua* the Corporate Debtor basis the Pledge Agreement and the Deed of Undertaking executed with the Lender.

Arguments

Contentions raised by the Appellant:

There is a debt which is payable by the Corporate Debtor to the Appellant. The Appellant had stepped into the shoes of Lender by virtue of the Assignment Deed. The Appellant is a financial creditor within the meaning of Section 5(8)(b) read with Section 5(8)(i) of the IBC. The Lender (Appellant) had full rights to pursue against the surety even before the Borrower. The Borrower had borrowed a financial facility and therefore, Corporate Debtor undertook a liability, by creating a security interest in the form of pledge of shares of GEL in favour of the Lender.

A concern was raised that if the Appellant was not accepted as financial creditor as per the provisions of the IBC, it consequently would leave the Appellant effectively remediless inasmuch as the Appellant could not enforce the guarantee during the subsistence of moratorium period. Further, if the resolution plan was passed without any redress to the Appellant, the Appellant shall be gravely prejudiced since recovery of the claim amount from the Corporate Debtor will be impossible.

The Corporate Debtor in effect had provided a guarantee to Lender against the debts due from the Borrower, and in case of non-payment, a charge subsisted upon the 100% shareholding of GEL. The liability of the Corporate Debtor, who is the surety, was co-extensive to that of the Borrower under Section 128 of the Indian Contract Act, 1872 (**"1872 Act"**).

Appellant submitted that any security that would permit the right of action against a third party that is not the Borrower, would amount to guarantee. The mere fact that Corporate Debtor has not borrowed money from the Appellant, could not absolve the Corporate Debtor from its liability as guarantor. The term guarantee is not to be understood narrowly but broadly to include any security created by third party to secure repayment of financial debt including a pledge of shares. Therefore, the pledge of shares by Corporate Debtor to secure the loan advanced to the Borrower amounts to a guarantee. The Appellant further submitted that the judgment of the SC in the case of Anuj Jain, Interim Resolution Professional for ***Jaypee Infratech Limited v. Axis Bank Limited and others, [(2020) 8 SCC 401],*** which was also relied upon by the Respondent, had been rendered in a specific facts scenario, which do not apply to the present case.

Contentions raised by the Respondent:

The Appellant is not a creditor of the Corporate Debtor in any nature whatsoever. The Appellant has no right of recovery of any debt from the Corporate Debtor. The Appellant only had a limited right of enforcing and realising the value of the shares held by the Corporate Debtor of GEL which are provided as a security for the financial assistance extended to the Borrower as per the Pledge Agreement.

The Pledge Agreement cannot be equated with guarantee as both are absolutely different in terms of their ramification and implication as per the provisions under the 1872 Act. Section 5(8)(I) of the IBC takes within its ambit any liability arising out of a guarantee for any of the items referred to in sub-clauses (a) to (h) of Section 5(8) of the IBC only, and not any other instrument that is in the nature of a guarantee. The Corporate Debtor has not executed any deed of guarantee with the Appellant to perform the promise, or discharge the liability of a third party in case of his default. In the event of default by the Borrower, the Appellant has the limited right to realise the money by selling the shares pledged. The Corporate Debtor had not promised to repay the debt that was recoverable from the Borrower. The Appellant cannot claim their Pledge Agreement to be a guarantee as there is no deed of guarantee executed.

The Respondent and the Intervenor contended that the object of the IBC is entirely different. IBC is not a mechanism for recovery of any amount. As an admitted fact, the Appellant has already moved the Debt Recovery Tribunal, Ahmedabad, for recovery and realisation of its dues.

Observations of the Supreme Court

Transaction:

The Corporate Debtor was not a party to the Facility Agreement executed between the Borrower and the Lender. It was the Borrower who had promised to repay the loan of INR 40 crores as per the terms of the Facility Agreement. 'Schedule-IV' of the Facility Agreement provided for 'Security Creation' which, *inter alia,* included, a pledge of 100% equity shares together with all accretions thereon of GEL. Subsequently, 40,160 shares of GEL were pledged, by executing the Pledge Agreement and the Deed of Undertaking, between the Lender and the Corporate Debtor. The SC observed that it transpires that since some shares of GEL were also held by the

Corporate Debtor (the subsidiary of the Borrower), the same were also pledged with the Lender as additional security.

Analysing provisions of the IBC and the 1872 Act:

The SC perused the provisions of the IBC and noted that, Section 5(7) of the IBC defines 'financial creditor' as any person to whom a financial debt is owed and includes a person to whom such debt has been legally assigned or transferred to. The word 'guarantee' and 'indemnity' under Section 5(8)(i) of the IBC have not been defined in the IBC. As per Section 3(37) of the IBC, words and expressions used that are not defined in the IBC, but defined in the 1872 Act, shall have the meaning respectively assigned to them.

Therefore, the SC noted that, Section 126 of the 1872 Act defines 'Contract of guarantee' as a contract to perform the promise, or discharge the liability, of a third person in case of his default. The SC observed that, the Corporate Debtor had not entered into a contract to perform the promise, or discharge the liability of Borrower in case of default. The SC noted that the Pledge Agreement was limited to pledge of shares as security. The promise as made by the Borrower in the Facility Agreement to discharge the liability of debt of INR 40 crores was not undertaken by the Corporate Debtor. Therefore, the Pledge Agreement and Deed of Undertaking executed between the Lender and Corporate Debtor could not be termed as contract of guarantee within the meaning of Section 126 of the 1872 Act.

The SC noted that the fundamental requirement for a creditor to be recognized as a financial creditor under Section 5 of the IBC, is that there must be a financial debt which is owed to that person irrespective of him being the principal creditor to whom the financial debt is owed or an assignee in terms of extended meaning. The SC further observed that, the definition, by its very frame, cannot be read so expansive/ infinitely wide, that the essential requirements of disbursement against the consideration for the time value of money could be forsaken in the manner that any transaction could standalone to become a financial debt. Further, the SC noted that Sections 5(7) and 5(8) prescribe the transactions *vis-à-vis* a corporate debtor. Therefore, for the Lender to be designated as a financial creditor of the Corporate Debtor, it had to be proved that the Corporate Debtor owed a financial debt to the Lender.

The SC noted that, the Respondent had relied on two-judge bench judgment of ***Jaypee Infratech Limited v. Axis Bank Limited*** (supra) wherein one of the issues raised was similar to the issue raised in this Judgement, therefore, the paragraphs 46 to 50.2, containing an elaborate analysis on the meaning of 'financial debt', 'financial creditor' under Section 5 of the IBC and 'debt' and 'secured creditor' under Section 3 of the IBC were extensively noted by the SC in this Judgement.

Ambit of a financial creditor and a creditor under the IBC:

The SC noted that the generic term 'creditor' is defined to mean any person to whom the debt is owed. Further, it is clarified that it includes a 'financial creditor', a 'secured creditor', an 'unsecured creditor', an 'operational creditor', and a 'decree-holder'. A "secured creditor" as per Section 3(30) of the IBC means a creditor in whose

favor a security interest is created; and "security interest", as per Section 3(31) of the IBC, means a right, title or interest or claim of property created in favor of or provided for a secured creditor by a transaction which secures payment for the purpose of an obligation.

The SC further noted that, under Section 3(11) of the IBC 'Debt' means a liability or obligation in respect of a claim which is due from any person and that it includes a 'financial debt' and an 'operational debt'.Further, Section 5(8) of the IBC defines 'financial debt' as debt along with interest, if any, which is disbursed against the consideration for the time value of money and the second part of the definition provides instances/ methods to raise financial debt.

The SC observed that the conjoint reading of the statutory provisions with the enunciation of the SC in ***Swiss Ribbons Private Limited and Another. v. Union of India and Others. [(2019) 4 SCC 17],*** clarified the scheme of the IBC, and the intention of the legislature, of the expression 'financial creditor' to mean a person who has direct engagement in the functioning of a corporate debtor; who is involved right from the beginning while assessing the viability of a corporate debtor; engaging in restructuring of the loan as well as in re-organization of a corporate debtor's business.

The SC contrasted the position and role of a financial creditor with that of a person having only security interest over the assets of the corporate debtor. The latter shall have only the interest of realizing the value of its security, there being no other stakes involved and least any stake in the corporate debtor's growth or equitable liquidation, while the former would, not only safeguard its own interests, but would also be interested in rejuvenation, revival and growth of the corporate debtor, thereby safeguarding the interests of other stakeholders. The SC noted, if a person having only security interest over the assets of the corporate debtor is also included as a financial creditor and thereby allowed to have consequential benefits, rights/opinions in the CIRP and/or liquidation process as contemplated under the IBC, the growth and revival of the corporate debtor may be the casualty. Such result would defeat the very objective of the IBC, particularly of the provisions aimed at CIRP.

The SC, therefore, concluded that a person such as the Lender, having only security interest over the assets of the Corporate Debtor, even if falling within the description of 'secured creditor' by virtue of collateral security extended by the Corporate Debtor, would nevertheless stand outside the sect of 'financial creditors' as per the provisions of the IBC. Hence, it would remain a debt alone and cannot partake the character of a 'financial debt' within the meaning of Section 5(8) of the IBC.

Thus, the security interest by way of the Pledge Agreement created in favor of the Lender, made the Lender a secured creditor only. The SC observed that on reading all the defining clauses harmoniously, it is clear that the legislature has maintained a distinction amongst the expressions 'financial creditor' and 'secured creditor'. The SC concluded that every secured creditor and financial creditor would be a creditor; but every secured creditor may not be a financial creditor.

The SC observed that, the analysis as stated above and the consequent ratio of ***Jaypee Infratech Limited v. Axis Bank Limited*** (supra) were completely applicable to the present case, since herein the Corporate Debtor had only extended a security by pledging shares of GEL. The SC observed that therefore, the Pledge Agreement and the Deed of Undertaking, executed subsequent to the Facility Agreement, were security in favour of the Lender, who at best will be secured creditor and not the financial creditor *qua* the Corporate Debtor within the meaning of Sections 5(7) and 5(8) of the IBC.

Decision of the Supreme Court

The SC upheld the decision of the Respondent as approved by the NCLAT that, the Appellant was not a financial creditor of the Corporate Debtor and it also held that the miscellaneous application was rightly rejected by the NCLT.

However, the SC clarified that the observations made in this Judgement were only for deciding the claim of the Appellant as the financial creditor within the meaning of Sections 5(7) and 5(8) of the IBC and, therefore, shall have no bearing on any other proceedings undertaken by the Appellant to establish any of its right(s) in accordance with law. Thereby, the SC dismissed the appeal.

VA View:

The SC distinguished the role of a financial creditor and secured creditor. The SC by this Judgement clarified that if the Corporate Debtor does not owe a financial debt to the Lender, then the Lender cannot be recognized as a financial creditor. The SC observed that, methods for raising debt may include modes prescribed in sub-clauses (a) to (f) of Section 5(8) of the IBC. Further, the judiciary has on multiple occasions clarified without an iota of doubt that for a debt to become 'financial debt', the fundamental principle is that the debt must exist and that it ought to be a disbursal against the consideration for time value of money, even if the mode of raising debt is not necessarily as stated in the section, it must at least have the features which could be traced to such essential elements in the principal clause of Section 5(8) of the IBC.

The SC observed the unique position that the financial creditor holds, due to its own direct involvement in a functional existence of the corporate debtor. The SC observed that the financial creditors are entrusted with the task of ensuring the sustenance and growth of the corporate debtor, akin to that of a guardian. In other words, in the context of CIRP, this class of stakeholder, namely, financial creditor, is entrusted by the legislature with such a role that it would look forward to ensure that the corporate debtor is rejuvenated and gets back on its wheels with reasonable capacity of repaying its debts and to discharge its various obligations. Therefore, the role of financial creditors and the consequential benefits they receive, including the voting rights in the committee of creditors, aim for the resolution of the corporate debtor.

III. Calcutta High Court: If a challenge is regarding lack of jurisdiction of NCLT under the IBC, writ jurisdiction of High Court can be invoked despite availability of alternative remedy under the IBC

In the case of ***Kolkata Municipal Corporation and Another v. Union of India and Others (W.P No. 977 of 2020),*** Calcutta High Court (**"CHC"**) by its judgement dated January 29, 2021, held that if a challenge is made regarding lack of jurisdiction of National Company Law Tribunal (**"NCLT"**) under the Insolvency and Bankruptcy Code, 2016 (**"IBC"**), writ jurisdiction of the High Court could be invoked despite availability of alternative statutory remedy.

Facts

Kolkata Municipal Corporation (**"KMC"**) is a statutory body under the Kolkata Municipal Corporation Act, 1980 (**"1980 Act"**). Pursuant to exercise of its statutory powers under the 1980 Act, KMC seized certain office premises of the assessee-corporate debtor (**"Assessee"**) for non-payment of tax dues. When the debt of the Assessee came within the purview of corporate insolvency resolution process (**"CIRP"**), the resolution professional in question approached the NCLT for handover of the Assessee's premises. The NCLT passed an order on January 17, 2019 lifting the attachment on the premises and directed KMC to hand over the premises to liquidation by an order dated January 31, 2020. KMC then had filed the writ petition with the CHC challenging handover of physical possession of the office premises.

Issues

1. Whether writ jurisdiction of the High Court under Article 226 *(power of high courts to issue certain writs)* of the Constitution of India, 1949 (**"Article 226"**) could be invoked despite availability of alternative remedy under the IBC.

2. Whether the property having been seized by KMC for non-payment of statutory dues by the Assessee could be subject matter of CIRP.

Contentions of KMC

KMC being a statutory body, had taken possession of the Assessee's premises in exercise of its statutory powers. This was an independent statutory exercise and could not be interdicted by the NCLT as per the IBC. As per ***Embassy Property Developments Private Limited v. State of Karnataka and Others [2019 SCC OnLine SC 1542]*** (**"Embassy"**), the powers of NCLT under Section 60 *(adjudicating authority for corporate persons)* of the IBC were circumscribed by the authority of the interim resolution professional, as provided under Section 18 *(duties of interim resolution professional)* of the IBC. As per Section 18(1)(f)(vi) of the IBC, control and custody of any asset to be taken by an interim resolution professional has to be subject to the determination of ownership by a court or authority. Since KMC is a statutory body, determination of ownership by taking possession and subsequent attachment and sale falls within its domain. Exercise of power, therefore, by the interim resolution professional, would be subject to KMC's authority. Further, as per Embassy, writ jurisdiction of CHC could be invoked despite

availability of an alternative remedy. This is because the challenge herein pertains to the nature of jurisdiction of the NCLT, and not wrongful exercise of available jurisdiction.

Contentions of respondent no. 3

As such, all issues pertaining to properties of a corporate debtor and rights or obligations could be decided by the NCLT. Reference was made to the definition of "property" under Section 3(27) of the IBC, and it was contended that Section 18(1)(f) of the IBC provided that an interim resolution professional could take control and custody of assets subject to determination of ownership by a court or authority. Basis Embassy, if NCLT had been conferred the jurisdiction to decide all types of claims with the property of a corporate debtor, Section 18(1)(f)(vi) of the IBC would not make the task of the interim resolution professional, in taking control and custody of an asset on which the corporate debtor has ownership right, subject tothe determination of ownership of a court or other authority. The right of the interim resolution professional to take control and custody, as such, is not completely subject to determination of ownership by courts or authorities. Moreover, it could not be said that the NCLT must yield to the determination by courts or other authorities in all cases, in so far as the right to determination of ownership of properties of a corporate debtor was concerned. As per Embassy, a decision taken by a statutory/government body in relation to a matter within the realm of public law, could not be brought within the fold of expression "arising out of or in relation to the insolvency resolution" as provided in Section 60(5) of the IBC. The legal position with respect to the aforesaid is clear as the Supreme Court (**"SC"**) had created a distinction between proceedings which had attained finality, fastening liability upon the corporate debtor, and all other matters. Therefore, a distinction must be drawn in respect of matters which are relevant for CIRP on the issue of debt or property of the company; and other matters. All such other issues would be beyond NCLT's jurisdiction. Even if a matter is within the jurisdiction of the NCLT, a distinction must be drawn between matters which have a direct bearing on CIRP, that is, directly pertaining to a debt or property of the corporate debtor and other matters. The jurisdiction of other courts or other tribunals could not be transgressed upon. In the present case, the question involved directly related to the property of the corporate debtor and, therefore, was within the purview of the NCLT. KMC herein, was also merely an operational creditor and it did not matter under the IBC if a creditor was a statutory creditor or not. KMC had also submitted itself to the jurisdiction of the NCLT by lodging its claim. It could not contend now that its attachment for recovery of claim was outside the NCLT's jurisdiction. Moreover, there was a remedy of appeal available under Section 61 (Appeals and Appellate Authority) of the IBC and, therefore, the writ petition should not be entertained. It had been previously held by the SC in ***Whirlpool Corporation v. Registrar of Trade Marks, Mumbai and others [(1998) 8 SCC 1]*** (**"Whirlpool Corporation"**) that where there was an appellate remedy, the court does not entertain writ petitions unless the order was either passed without jurisdiction or in violation of natural justice. In ***Commissioner of Income Tax and others v. Chhabil Dass Agarwal [(2014) 1 SCC 603]*** (**"Chhabil Dass"**), the SC held that interference is not warranted under Article 226 unless extraordinary circumstances were made out. The SC had previously followed the principal of entertaining writ petitions only under strict exceptions.

Contentions of the resolution professional (respondent no. 4)

There is no distinction between statutory and operational debts. As such, even statutory dues or crown debts are considered as operational debt as under Section 18(1)(f) of the IBC. The provisions of the IBC indicate that the interim resolution professional has to take control and custody of assets over which the corporate debtor has ownership rights, which may or may not be in possession of the corporate debtor, or any asset subject to determination of ownership by a court or authority. In the instant case, KMC has only attached the asset of the corporate debtor and is in possession of it. The asset has not been sold and, therefore, the ownership is still with the corporate debtor. As per Section 36(3)(a) and (b) *(provisions relating to liquidation estate)* of the IBC, it was argued that asset attached by KMC would become part of the liquidation estate. Herein, KMC had filed a claim during CIRP and it would have to await the outcome of the process and distribution of assets as per Section 53 *(Distribution of assets)* of the IBC in the liquidation proceeding. It was contended that as per ***Commissioner of Income Tax v. Monnet Ispat and Energy Limited [Special Leave to Appeal (C) No. (S) 6483 of 2018]*** even crown debts do not take precedence over secured creditors. Moreover, basis a reading of the provisions of the IBC, the NCLT had jurisdiction to pass such orders. As per Section 238 *(Provisions of this code to override other laws)* of the IBC, the IBC also has an overriding effect over other laws. It was contended that as per ***Sulochna Gupta and Another v. RBG Enterprises Private Limited [2020 SCC OnLine Ker 4153],*** a writ petition is not maintainable against an NCLT order.

Observations of the Calcutta High Court

With regard to exercise of power conferred upon High Courts under Article 226, the CHC referred to the judgement in Embassy. The CHC noted SC's view that despite availability of a statutory remedy under a special statute, distinction between lack of jurisdiction and wrongful exercise of jurisdiction must be factored and taken into account if Article 226 is sought to be invoked. In this instance, KMC had invoked Sections 217 to 220 *(Chapter XVI – payment and recovery of taxes)* of the 1980 Act to attach the Assessee's office premises, so that it could be potentially sold. KMC had argued that exercise of such powers is beyond the IBC's purview and could not fall within the ambit of powers conferred upon either the resolution professional or the NCLT under the IBC. It was also noted by the CHC that the issue under consideration herein was regarding absence of jurisdiction, and not wrongful exercise of available jurisdiction. Therefore, this clearly fell within the contours of Article 226. As per Whirlpool Corporation, alternative remedy would not be a bar where order or proceedings are without jurisdiction. This in line with the judgement in Chhabil Dass, would allow court's interference under Article 226. The powers of the High Court under Article 226 are wide and there is no such express limitation on the same. While the rules of self-imposed restraint could not be ignored, this was a rule of discretion and not of compulsion. A coherent reading of the decisions of the SC would make it clear that while a wrongful exercise of available jurisdiction would not be sufficient to invoke Article 226, absence of the same could allow such invocation. Therefore, in this instance the writ petition is maintainable. For addressing the second issue, the decision in Embassy was once again referred to. As per Embassy a decision taken by a government or statutory authority in relation to a matter which was in the realm of public law, could not, by any stretch of imagination, be brought

within the fold of the phrase "arising out of or in relation to the insolvency resolution". It was noted in Embassy that if the NCLT had jurisdiction to decide all types of claims to the property of a corporate debtor, the provisions of the IBC would not have tasked the interim resolution professional to take control and custody of assets subject to the determination of ownership by a court or other authority. The next aspect to be considered was whether an asset for which control and custody is sought to be taken by the interim resolution professional, is sub-judice before a court or authority for the purpose of "determination of ownership". In the instant case, KMC followed procedure as laid down under the 1980 Act and took possession of the office property upon non-payment of taxes. There was no scope for any further determination of ownership of the property. In the absence of any successful challenge, KMC's claims also attained finality and fastened a liability on the corporate debtor. KMC's claim would therefore become an operational debt under the IBC. The powers conferred upon the NCLT under Section 60 of the IBC are circumscribed by Section 18(f)(vi) of the IBC. Under Section 60(5) of the IBC, this exercise of power would fall within the ambit of "arising out of or in relation to the insolvency resolution". Therefore, the finalized claim of KMC would become the subject matter of CIRP under the IBC. The concerned resolution professional had jurisdiction to take control and custody of the Asseessee's property. It is also notable that even though KMC is a statutory body, per the provisions of the IBC, its claims could not gain precedence over other secured creditors.

Decision of CHC

KMC's writ petition under Article 226 against the order passed by the NCLT was maintainable. However, its claims would still be the subject matter of CIRP.

VA View:

KMC's primary intention to prove that Assessee's premises would fall outside the purview of the NCLT did not attain fruition, however, its petition was ruled to be maintainable by the court, whilst elaborating on the ambit of Article 226.

Powers of the court under Article 226 are expansive. Nevertheless, these powers must be exercised with caution and restraint. The factor of restraint becomes relevant when there is already an alternative statutory remedy available. In this case, the CHC extensively dwelt upon the 'self-imposed restriction' principle. It affirmed that availability of statutory remedy did not act as a bar towards invocation of Article 226. In essence, if the primary challenge rooted from either a lack of jurisdiction or violation of natural justice, court's powers under Article 226 could be exercised. This strengthens the point that the principle of self-imposed restriction is not a fixed and definitive rule. Its application would ultimately depend upon the context, as evidenced by the facts of this case.

IV. Delhi High Court: Order terminating arbitration proceedings under Section 32(2)(c) of Arbitration and Conciliation Act, 1996 is not an award

The Delhi High Court (**"DHC"**) has in its judgment dated January 12, 2021 in the matter of ***M/s PCL Sunconv. M/s National Highway Authority of India [O.M.P. (T) (COMM.) 80/2020],*** held that an order terminating arbitration proceedings under Section 32(2)(c) of the Arbitration and Conciliation Act, 1996 (**"ACA"**) is not an award, and can be disputed under Section 14(2) of the ACA.

Facts

The National Highway Authority of India (**"Respondent"**) had invited bids for *"Four laning and strengthening of the existing two lanes between Km. 317 and Km. 65 on NH-2, in the State of U.P. and Bihar for construction package IV-A: Contract Agreement No. GTRIP/5.".* Pursuant to the same, M/s.PCL Suncon (**"Petitioner"**), a joint venture constituted by Progressive Construction Limited and SUNCON Construction Berhard, Malaysia, submitted its bid on December 15, 2001. The Petitioner's bid was accepted and by a letter dated February 23, 2002, the Petitioner was awarded the contract for an amount of INR 3,96,47,78,901/-. Pursuant thereto, a formal agreement between the parties was executed on March 28, 2002 (**"Contract"**). Due to a dispute arising between the parties, the Petitioner invoked the arbitration clause under the Contract, *inter alia,* claiming INR 57,84,00,000/- towards overstay/ overhead charges; INR 2,50,00,000/- as refund of the liquidated damages deducted by the Respondent; and INR 40,04,000/- for rehabilitation of Bridge 58/1. For the purpose of constituting the arbitral tribunal, the Petitioner nominated Justice E. Padmanabhan as its nominee and the Respondent appointed Mr. S. R. Pandey as its nominee, and both the nominated arbitrators nominated Mr. B. Majumdar as the presiding arbitrator (**"Presiding Arbitrator"**). With the appointment of the Presiding Arbitrator on August 3, 2015, the arbitral tribunal was constituted ("**Arbitral Tribunal"**) where upon the Petitioner filed its statement of claims to which the Respondent filed its counter claims before the said Arbitral Tribunal. The Arbitral Tribunal last sat on October 11, 2017, when the arguments on behalf of the Petitioner were heard and dates for further hearings were allotted on January 16, 2018, January 17, 2018 and January 18, 2018. However, the said hearings were cancelled due to non-availability of Justice E. Padmanabhan who subsequently resigned as an arbitrator and requested the Petitioner to nominate another arbitrator in his place. Copies of Justice E. Padmanabhan's resignation letter were forwarded to the other co-arbitrators as well.

The Petitioner attempted to appoint a substitute arbitrator but the process was delayed as the persons who were approached by the Petitioner, did not consent to be appointed as an arbitrator, and in addition, the authorized officer of the Petitioner, who was pursuing the matter on its behalf, abandoned his assignment due to personal reasons. Consequently, on April 20, 2020, the Arbitral Tribunal passed the impugned order terminating the arbitral proceedings under Section 32(2)(c) of the ACA (**"Order"**). The Petitioner, however, did not receive any communication from the remaining two arbitrators informing it of their intention to terminate the arbitral proceedings nor was the said Order communicated to the Petitioner. On May 22, 2020, the Petitioner sent a letter to the Respondent and the arbitrators, nominating Mr. Subhash I. Patel as its nominee arbitrator and requested

the Presiding Arbitrator to schedule a hearing. In response to the same, the Petitioner was informed about the Order by a letter dated May 27, 2020.

In the Order, the arbitrators had noted that hearings could not be fixed as no response had been received from Justice E. Padmanabhan to the communication letters sent by the Presiding Arbitrator. It was further noted that there was also lack of initiative on the part of the Petitioner as no proposal had been made for fixing any new dates to proceed with the adjudication process. The Petitioner was accordingly advised to check the convenience of Justice E. Padmanabhan for further hearings, but while the Arbitral Tribunal was awaiting the Petitioner's response, Justice E. Padmanabhan had by a letter dated February 19, 2019, resigned as an arbitrator and requested the Petitioner to nominate another arbitrator. The arbitrators noted that more than a year had elapsed and the Petitioner had not appointed an arbitrator in his place. The arbitrators noted that because of the deadlock, the continuation of proceedings had become impossible and accordingly, terminated the arbitral proceedings under Section 32(2)(c) of the ACA. The Petitioner, thereafter, filed the present petition under Section 14(1)(a) read with Section 15 of the ACA before the DHC, against the said impugned Order.

Issue

Whether the Order terminating arbitration proceedings under Section 32(2)(c) of ACA is an award.

Arguments

Contentions raised by the Respondent:

The Respondent, *inter alia,* contended that the present petition was not maintainable as the entire arbitral proceedings had been terminated in terms of Section 32(2)(c) of the ACA and this was not a case where arbitrators had withdrawn from the proceedings or the mandate of any arbitrator had been terminated as contemplated under Section 14(1)(a) of the ACA. It was further argued that the Petitioner could approach the court under Section 15 of the ACA only in a case where the arbitrator had withdrawn from the arbitral proceedings or had become *de jure* or *de facto* unable to perform its functions. In such circumstances, a substitute arbitrator could be appointed. However, in a case where the entire arbitral proceedings had been terminated, there was no case for appointing any arbitrator under Section 15(2) of the ACA. The Respondent referred to the decision of the Division Bench of the Calcutta High Court in ***The India Trading Company v. Hindustan Petroleum Corporation Limited [2016 SCC OnLine Cal 479]*** and basis the same, contended that the decision of the Arbitral Tribunal to put an end to the proceedings was a final award, which could be challenged only by way of an application for setting aside the same under Section 34(2) of the ACA. The Respondent contended that in view of the said decision, the recourse to an application under Section 14 of the ACA was not available to the Petitioner. In addition, reference was also made by the Respondent to the decision of a ***Coordinate Bench of DHC in Angelique International Limited v. SSJV Projects Private Limited and Another [2018 SCC OnLine Del 8287],*** wherein the court had accepted the contention that the termination of proceedings in respect of the claim filed by the petitioner would amount to an arbitral award, which could be challenged only by a petition under Section 34 of the ACA. It was also contended

that the Petitioner was responsible for the delay in appointment of an arbitrator in place of Justice E. Padmanabhan and therefore, the decision of the Arbitral Tribunal to terminate the arbitral proceedings could not be faulted.

Contentions raised by the Petitioner:

The Petitioner on the other hand contended that it was well settled that an order terminating the proceedings under Section 32(2) of the ACA could not be considered as an award. The Petitioner submitted that termination of the arbitral proceedings on account of non-prosecution of claims also could not be construed as an award and which could be challenged under Section 34 of the ACA. It was further argued that the abovementioned decision in ***Angelique International Limited v. SSJV Projects Private Limited and Another [2018 SCC OnLine Del 8287]*** (supra) struck a discordant note inasmuch as it held that only a petition under Section 34 of the ACA would be maintainable against an order terminating the arbitral proceedings under Section 32(2)(c) of the ACA. It was argued that the said decision was per *in curiam* as it ignored the binding decisions of the DHC in ***Bridge and Roof Co. (India) Limited v. Guru Gobind Singh Indraprastha University and Another [2017 SCC OnLine Del 10412], Puneet Kumar Jain v. MSTC Limited and Others [MANU/DE/7910/2017], Shushila Kumari and Another v. Bhayana Builders Private Limited [2019 SCC OnLine Del 7243], Gangotri Enterprises Limited v. NTPC Tamil Nadu Energy Company Limited [(2017) 237 DLT 690]*** and ***Pandit Munshi and Associates Limited v. Union of India and Others [2015 (2) ARB LR 40 (Delhi)].*** Lastly, the Petitioner argued that the Order was liable to be set aside as no pre-emptory notice was issued by the arbitrators before proceeding to terminate the arbitral proceedings.

Observations of the Delhi High Court

The DHC observed that, as per Section 34 of the ACA, *"(1) Recourse to a Court against an arbitral award may be made only by an application for setting aside such award in accordance with sub-section (2) and sub-section (3)."* The use of the word 'only'in Section 34(1) of the ACA was significant and it clearly implied that except under Section 34 of the ACA, no other recourse was available against an arbitral award, to which Part-I of the ACA applied. The contention that the present petition was not maintainable and the only recourse available to the Petitioner was to file an application under Section 34 of the ACA was founded on the assumption that the impugned Order was an award. Clause (c) of Sub-section (1) of Section 2 of the ACA, defines an 'arbitral award' to include an interim award. Section 31 of the ACA provides for the form and the content of an arbitral award. The question as to the distinction between an award and an order of an arbitral tribunal had been a subject matter of a number of rulings. It was now well settled that an award constituted a final determination of a particular issue or a claim in arbitration.

It was also observed that Section 32 of the ACA drew a clear distinction between a final arbitral award and interim orders passed by an arbitral tribunal. In terms of Section 32(1) of the ACA, arbitral proceedings stood terminated by a final award or by such orders as were specified under Section 32(2) of the ACA. In ***Rhiti Sports Management Private Limited v. Power Play Sports and Events Limited [2018 SCC OnLine Del 8678],*** the DHC had noted that *"A*

plain reading of Section 32 of the Act indicates the fact that the final award would embody the terms of the final settlement of disputes (either by adjudication process or otherwise) and would be a final culmination of the disputes referred to arbitration.....To put it in the negative, any procedural order or an order that does not finally settle a matter at which the parties are at issue, would not qualify to be termed as 'arbitral award'."

As opposed to the reasoning held in ***Angelique International Limited v. SSJV Projects Private Limited and Another [2018 SCC OnLine Del 8287]*** by the DHC, the Supreme Court (**"SC"**) had, in the case of ***Indian Farmers Fertilizer Cooperative Limited v. Bhadra Products [(2018) 2 SCC 534]*** considered the question of whether an award on the issue of limitation could be considered to be an interim award and whether the decision on the point of limitation was a matter of jurisdiction and therefore, be covered under Section 16 of the ACA and held that since the award had finally determined one of the issues between the parties, the same could be considered as an interim award inasmuch as it finally determined a claim that could not be re-adjudicated all over again. Thus, in order for a decision of the arbitral tribunal to qualify as an award, the same must finally decide a point at which the parties are at issue. In cases where the same is dispositive of the entire dispute referred to the arbitral tribunal, the said award would be a final award, which would result in termination of the arbitral proceedings. In light of the above, the DHC observed that, it was clear that an order which terminated the arbitral proceedings as the arbitral tribunal found it impossible or unnecessary to continue the arbitral proceedings, would not be an award. This was because it did not answer any issue in dispute in arbitration between the parties but was an expression of the decision of the arbitral tribunal not to proceed with the proceedings. Section 32 of the ACA made a clear distinction between an award and an order under Sub-section (2) of Section 32 of the ACA. Indisputably, an order under Sub-Section (2) of Section 32 of the ACA was not an award.

Further, the DHC observed that the Order passed by the arbitrators expressly stated that the arbitral proceedings were terminated under Section 32(2)(c) of the ACA as in their view, it had become impossible to continue with the said proceedings. Indisputably, an order terminating the proceedings under Section 32(2)(c) of the ACA could be impugned under Section 14(2) of the ACA. The Respondent's contention that even though an application under Section 14(2) of the ACA may be filed, the present application which is under Section 14(1)(a) and Section 15 of the ACA is not maintainable, appeared to be unpersuasive. A plain reading of Sub-section (2) of Section 14 of the ACA indicated that unless otherwise agreed by parties, a party could apply to a court to decide on the question of termination of the mandate, if a controversy remained concerning any of the grounds referred to in Sub-section 14(1)(a) of the ACA.

Decision of the Delhi High Court

Allowing the petition, the DHC noted that, although the arbitrators had passed the Order, it was not disputed that a notice intimating that they were contemplating terminating the proceedings was not issued to the Petitioner, prior to passing of the Order. However, it could not be denied that the Petitioner was responsible for the stalling of the proceedings as it had inordinately delayed the appointment of an arbitrator. Whilst the DHC was of the view that the Petitioner ought not be rendered remediless to urge its claims, the Respondent's contention that the

Petitioner must be visited with costs was merited. Hence, the DHC set aside the impugned Order, albeit, subject to payment of costs of INR 25,000/- by the Petitioner.

Since the Petitioner had already nominated an arbitrator, Mr. Subhash I. Patel, the Arbitral Tribunal was directed to resume the arbitration proceedings. The Arbitral Tribunal was further directed to conclude the arbitral proceedings as expeditiously as possible and preferably within one year from date of the DHC's judgement.

VA View:

In light of the previous judgments on same question of law and interpretation, dealt with and decided by the SC, the DHC has fittingly interpreted Section 32 and Section 34 of the ACA, to distinguish between an 'award' and an 'order'.

Aside from the clear intent of the legislation, which is evident in the text of Section 32, it would appear logically inconsistent to treat a procedural order as an award, while provision has been given for both in the law and in the way they are to be dealt with in case parties to a contract want to challenge the same before a court of law. Also, considering that the impugned Order itself stated that the same was passed under Section 32 (2)(c) of the ACA, to treat it as an award under Section 32 (1) would have been inappropriate.

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