Insolvency and Bankruptcy Code, 2016

PENDENCY OF A CHALLENGE TO AN ARBITRAL AWARD BARS INITIATION OF CORPORATE INSOLVENCY RESOLUTION PROCESS

The Supreme Court of India in K. Kishan v. M/S Vijay Nirman Company Pvt. Ltd. recently held that the pendency of an application under Section 34 of the Arbitration and Conciliation Act, 1996 bars the initiation of the corporate insolvency resolution process

Brief Facts & Issues

In the instant case[1], a sub-Contract Agreement was signed between the respondent and the M/s Ksheerabad Constructions Pvt. Ltd. (for short 'KCPL') for works related to construction and widening of the existing highway. Additionally, a separate agreement was signed between KPCL and M/s SDM Projects Private Limited, Bangalore, leading to a tripartite Memorandum of Understanding between KCPL, M/s SDM Projects Pvt. Ltd. and the respondent.

Thereafter, disputes arose between the parties which were referred to an arbitral tribunal that delivered its award on 21 January 2017 (hereinafter referred to as "**Award**"). In this regard, certain claims in favour of the respondent were allowed.

Subsequently, the respondent issued a notice to KCPL under Section 8 of the Insolvency and Bankruptcy Code, 2016 (hereinafter referred to as "**Code**") to pay the claims. KCPL, within 10 days of receipt of the aforementioned notice, disputed the notice, stating that the claims are the subject-matter of an arbitration proceeding and that the respondent owes larger amounts to KCPL.

Thereafter, KCPL filed a petition under Section 34 of the Arbitration and Conciliation Act, 1996 (hereinafter referred to as "**Act**") to challenge the Award.

Consequently, the respondent filed a petition under section 9 of the Code to initiate corporate insolvency resolution process against KCPL. The National Company Law Tribunal (hereinafter referred to as "**NCLT**") admitted the petition for the reason that it was irrelevant that a Section 34 petition was pending and because there was no stay of the Award by the court.

An appeal was filed by KCPL before the National Company Law Appellate Tribunal (hereinafter referred to as "**NCLAT**"), however the appeal was dismissed on the grounds that the non-obstante clause contained in Section 238 of the Code would override the Act and that since Form V of Part 5 of the Insolvency & Bankruptcy (Application to Adjudicating Authority) Rules, 2016 requires particulars of an order of an arbitral panel adjudicating on the default, this would have to be treated as "a record of an operational debt", as a result of which the petition would have to be admitted.

KCPL thereafter preferred an appeal before the Supreme Court. The issue before the Supreme Court was whether the IBC can be invoked in

[1] Civil Appeal No 21825 of 2017

respect of an operational debt where an Arbitral Award has been passed against the operational debtor, which has not yet been finally adjudicated upon.

The appellant contested against the admission of the section 9 petition contending that the object of the Code is not to replace the debt adjudication and enforcement under the Act or any other statutes and that the pendency of a Section 34 petition under the Act is reflective of a real dispute between the parties. Moreover, the appellant reasoned that if the cross-claims of the appellant, which were earlier rejected by the arbitral tribunal, are subsequently held to be wrongly dismissed, then the appellant would not then owe any money to the respondent.

The respondent submitted that insolvency proceedings do not get delayed because of a pending application to set aside the judgment, by relying on insolvency laws in foreign jurisdictions such as Singapore, United Kingdom, and Australia. Furthermore, the respondent argued that Section 238 of the Code is a non-obstante clause which will override provisions of the Act.

Judgement

The Supreme Court heavily relied on its landmark judgment in Mobilox Innovations Private Limited v. Kirusa Software Private Limited[2], and stressed that with respect to operational creditors, the Code cannot be used to bypass the adjudicatory and enforcement process of a debt contained in other statutes. Moreover, the object of the Code is to initiate the insolvency process against a corporate debtor only in cases where a real dispute between the parties as to the debt owed clearly does not exist.

Furthermore, the Court held that in respect of an operational debt, the only thing needed to be determined is whether the said debt can be said to be disputed. In this regard, the Court held that the filing of a Section 34 petition against the Arbitral Award indicated that there was a pre-existing dispute which developed in the first stage of the arbitral proceedings and would continue even after the Award, till the conclusion of the final adjudicatory process under Sections 34 & 37 of the Act. Additionally, the possibility of the appellant to succeed on its cross-claims is sufficient to state that the operational debt cannot be said to be an undisputed debt.

The Court also upheld the case of the appellant that Section 238 of the Code does not apply to the present case because there were no inconsistencies between the provisions of the Code and the Act. Thus, the Supreme Court reversed the NCLAT judgment with regard to this aspect.

[2] (2018) 1 SCC 353