

Between the lines...

June, 2018

Key Highlights

- I. **Delhi High Court: Sale of pledged shares as per Depositories Regulations valid even without prior notice to the pledgor**
- II. **Supreme Court: There is no bar to plea of jurisdiction under Section 34 of Arbitration Act even if no objection was raised under Section 16 before the arbitral tribunal**
- III. **Supreme Court holds that non-signatories to arbitration agreements can be made parties to domestic arbitrations**
- IV. **NCLAT excludes time from CIRP period during which CoC could not function**

I. **Delhi High Court: Sale of pledged shares as per Depositories Regulations valid even without prior notice to the pledgor**

The Delhi High Court in the case of ***Tendril Financial Services Private Limited and Others v. Namedi Leasing and Finance Limited and Others*** (decided on April 3, 2018) held that sale of pledged shares in dematerialized form in accordance with the provisions of the Depositories Act, 1996 and regulations made thereunder is valid even if no prior notice is served to the pledgor under Section 176 of the Indian Contract Act, 1872.

Facts

Morepen Laboratories Limited ("**Morepen**") had availed a financial facility from Morgan Securities and Credits Private Limited ("**Morgan**"). In order to secure the aforesaid facility, Tendril Financial Services Private Limited and others ("**Plaintiffs**") had pledged 15,00,000 equity shares of Blue Coast Hotels and Resorts Limited ("**Blue Coast**") owned by them to Morgan. Pursuant to the amount remaining unpaid by Morepen to Morgan, a dispute arose

between the parties, which was referred to the sole arbitrator. Eventually, parties settled and entered into a settlement agreement setting out the mode and manner of repayment of the amount due to Morgan which was published by the arbitrator in its award.

Morepen defaulted in discharging its liability within the stipulated time as mentioned in the award. As a result, Morgan filed an execution petition for execution of the arbitral award to invoke the pledged shares. Simultaneously, Morgan sold the pledged shares, without taking prior permission from the executing court and without the Plaintiffs being put to a prior notice of such sale. Plaintiffs filed suit before the Delhi High Court for the reliefs of declaration that the sale/transfer of the pledged shares is illegal, void and of no effect and a permanent injunction to re-transfer the said shares. The following issue came up for determination:

Issue

Whether sale of shares of Plaintiffs in Blue Coast by Morgan without serving a legal notice to Plaintiffs in terms of Section 176 of the Indian Contract Act, 1872 ("**Contract Act**") is valid?

Relevant Provisions

Section 176 of the Contract Act:

176. Pawnee's right where pawnor makes default.—*If the pawnor makes default in payment of the debt, or performance; at the stipulated time of the promise, in respect of which the goods were pledged, the pawnee may bring a suit against the pawnor upon the debt or promise, and retain the goods pledge as a collateral security; or he may sell the thing pledged, on giving the pawnor reasonable notice of the sale.*

Regulation 58(8) of the Securities and Exchange Board of India (Depositories and Participants) Regulations, 1996 ("**Depositories Regulations**"):

58. Manner of creating pledge or hypothecation.—*(8) Subject to the provisions of the pledge document, the pledgee may invoke the pledge and on such invocation, the depository shall register the pledgee as beneficial owner of such securities and amend its records accordingly.*

Arguments

Plaintiffs contended that the pledge agreement contemplated two stages: First, invocation of pledge which did not divest the Plaintiffs of title in the shares; and second, actual sale of shares, whereof the Plaintiffs were to stand divested of the title to shares. Plaintiffs submitted that as per the Letters of Pledge, simple invocation of pledge by Morgan would not amount to sale of shares to Morgan. Thus, invocation could not extinguish the property rights of the Plaintiffs in those shares which, if necessary, had to be sold in open market, after giving notice of such sale, for realization of dues if any of Morgan from Morepen. Hence, no sale of pledged shares could take place without the Plaintiffs being put to a prior notice of such sale in accordance with Section 176 of the Contract Act.

Morgan argued that since the shares were not in physical form, but in fungible form, the provisions of the Contract Act relating to pledge are not relevant and the provisions of the Depositories Act, 1996 ("**Depositories Act**") will apply. Under Regulation 58 of the Depositories Regulations, the beneficial ownership in the shares changes on invocation and it is only the adjustment which takes place on sale. After invocation of the pledge, Blue Coast had made a public announcement that Morgan has become the beneficial owner of the shares. The said sale was effected after obtaining permission of Securities & Exchange Board of India because the said shares were under the 5% circuit breaker limit. Further, sale and purchase of shares were effectuated through market mechanism and in such case the trading system of Stock Exchange is anonymous and does not permit the buyer to know who the seller is and vice-versa.

Observations of the Delhi High Court

The Delhi High Court observed that a notice under Section 176 of Contract Act is in derogation of Regulation 58 of the Depositories Regulations. There is no place for a prior notice under Section 176 of Contract Act, in the scheme of Regulation 58(8) of the Depositories Regulations. On the contrary, Regulation 58(9) of the Depositories Regulations requires the depository to, after amending its records under Regulation 58(8), inform the respective depository participants of the pledgor and the pledgee in respect of amendment of records and mandate the said participants to inform the pledgor and the pledgee.

While Section 176 of the Contract Act provides for a notice to pledgor prior to effecting sale, Regulation 58 of the Depositories Regulations provides for notice post invocation of pledge. On such invocation, beneficial ownership of pledged shares changes from that of the pledgor to that of the pledgee, which is equivalent to sale under Section 176 of Contract Act. Thus, to hold that a prior notice under Section 176 of Contract Act is also required in the case of pledge of dematerialised shares would interfere with transparency and certainty in the securities market, rendering fatal blow to the Depositories Act and Depositories Regulations and the object of enactment thereof. The Delhi High Court further added that though the selling of pledged shares without issuing a notice under Section 176 of the Contract Act is bad in law, but still it cannot be held void, as the new buyer will continue to be a pledgee. Also, it would have been unfair to the pledgee if the pledgor was allowed to restrain dealing of pledged shares and at the same time, neither redeem nor offer to redeem the pledged shares, thereby defeating the pledge. Since the suit was pending before the court for 12 years, the Delhi High Court held that even if reasonable notice under Section 176 was not given, the Plaintiffs during pendency of suit have had sufficient notice and therefore the balance of convenience, in such circumstances, will lie in favour of the defendants.

Decision of the Delhi High Court

The Delhi High Court held that the sale of pledged shares without notice is valid.

VA View

The aforesaid judgment is a welcome addition to the series of judgments based on the principle that special law prevails over the general law. Relying on the earlier judgments of the Bombay High Court, the Delhi High Court has held that pledge of dematerialized shares is governed solely by the Depositories Act and the Depositories Regulations. Taking the said view into account, the Delhi High Court further held that “*Section 176 of the Contract Act is derogatory to Regulation 58 of the Depositories Regulations*”. It was observed that on invocation of pledged shares under Regulation 58 of the Depositories Regulations, beneficial ownership of pledged shares changes from that of the pledgor to the pledgee, which is equivalent to sale under Section 176 of Contract Act.

The reasoning given for the aforesaid ratio is that provision of notice under Section 176 of the Contract Act is for the benefit of the pledgor and has no element of public law or public interest. If a provision is given in law for personal benefit and is not provided in public interest, it can always be waived by that person. Since, in the instant case, the

Plaintiffs in the Letters of Pledge and under arbitral award, have waived such requirement of prior notice before effecting the sale, no prior notice was required to be given as per Section 176 of the Contract Act. Therefore, it is advisable that pledgees of dematerialized shares ensure that the primary pledge agreement as well as any subsequent settlement agreements provide for provision of waiver of prior notice before invocation of pledge and transfer of shares. This case will also serve as a precedent in laying down the principle that if a suit is pending for sufficiently long period of time, then the plaintiff will be deemed to have sufficient notice and therefore the balance of convenience in such circumstance will lie in favour of the defendants.

II. Supreme Court: There is no bar to plea of jurisdiction under Section 34 of Arbitration Act even if no objection was raised under Section 16 before the arbitral tribunal

In the case of *M/s Lion Engineering Consultants v. State of M.P. and Others* (decided on March 22, 2018), Hon'ble Supreme Court held that there is no bar to raise the plea of jurisdiction by way of an objection under Section 34 of the Arbitration and Conciliation Act, 1996, even if no such objection has been previously raised under Section 16 in front of the arbitral tribunal.

Facts

M/s Lion Engineering Consultants ("**Appellant**") and the Government of Madhya Pradesh ("**Respondent**") entered into a works contract for consultancy and implementation services for construction of a building. Dispute arose between the parties for non-payment of bills by the Respondent and the associated claims. An arbitrator was appointed as per the provisions of Arbitration and Conciliation Act, 1996 ("**Arbitration Act**") who gave the award in favor of the Appellant, which was challenged by the Respondent under Section 34 of the Arbitration Act.

The Respondent sought to amend its objections as regards the jurisdiction of the arbitrator to entertain the dispute under the Arbitration Act. Respondent pleaded that contract being a 'works contract' and the Respondent being one of the parties to the contract, the jurisdiction lies with the arbitration tribunal constituted under the Madhya Pradesh Madhyastham Adhikaran Adhiniyam, 1983, which is a state legislation governing arbitration in respect of disputes arising out of execution of works contract. However, the court rejected the amendment to objection raised by the Respondent on the ground that the amendment was sought beyond the period of limitation. The Respondent filed a writ petition under Article 227 of the Constitution of India in the Madhya Pradesh High Court, which allowed the said amendment to be carried out in the Respondent's objections and held that "*when the objection is in respect of jurisdiction over subject matter it is immaterial at what stage it is taken*". Aggrieved by the said decision of the Madhya Pradesh High Court, the Appellant filed a civil appeal before the Hon'ble Supreme Court under which the following question came up for determination:

Issue

Whether is there any bar to plea of jurisdiction being raised by way of an objection under Section 34 of the Arbitration Act, even if no such objection was raised under Section 16 before the arbitral tribunal?

Relevant Provisions

Sections 16 of the Arbitration Act:

16. Competence of arbitral tribunal to rule on its jurisdiction.—(2) A plea that the arbitral tribunal does not have jurisdiction shall be raised not later than the submission of the statement of defence; however, a party shall not be precluded from raising such a plea merely because that he has appointed, or participated in the appointment of, an arbitrator.

(3) A plea that the arbitral tribunal is exceeding the scope of its authority shall be raised as soon as the matter alleged to be beyond the scope of its authority is raised during the arbitral proceedings.

(5) The arbitral tribunal shall decide on a plea referred to in sub-section (2) or sub-section (3) and, where the arbitral tribunal takes a decision rejecting the plea, continue with the arbitral proceedings and make an arbitral award.

(6) A party aggrieved by such an arbitral award may make an application for setting aside such an arbitral award in accordance with section 34.

Section 34(2) of the Arbitration Act:

Section 34 - Application for setting aside arbitral award.—(2) An arbitral award may be set aside by the Court only if—

(b) the Court finds that—

(i) the subject-matter of the dispute is not capable of settlement by arbitration under the law for the time being in force, or

(ii) the arbitral award is in conflict with the public policy of India.

Arguments

Appellant in the given case submitted that the amendment to the objections could not be allowed beyond the period of limitation as the same will be affecting the vested rights of a party. Further, Appellant argued that the objection having not been raised under Section 16(2) of the Arbitration Act before the arbitrator, could not be raised under Section 34 of the Arbitration Act before the court. Reliance was placed on the judgement of Supreme Court in case of **MSP Infrastructure Limited v. Madhya Pradesh Road Development Corporation Limited** (decided on December 5, 2014) (“**MSP Infrastructure Limited**”) to contend that as per scheme of the Arbitration Act, all objections to jurisdiction of whatsoever nature must be taken at the stage of submission of statement of defense and must be

dealt with under Section 16 of the Arbitration Act. Further, with regard to applicability of Madhya Pradesh Madhyastham Adhikaran Adhiniyam, 1983, Appellant submitted that while interpreting the term “public policy of India” under Section 34(2)(b) of the Arbitration Act, where the question arises out of a conflict between an action under a State law and an action under the Union law, the term public policy of India must necessarily be understood as being referable to the policy of the Union.

The Respondent argued that legal plea arising on undisputed facts is not precluded by Section 34(2)(b) of the Arbitration Act. Even if an objection to jurisdiction is not raised under Section 16 of the Arbitration Act, the same can be raised under Section 34 of the Arbitration Act. It is not even necessary to consider the application for amendment as it is a legal plea, on admitted facts, which can be raised in any case. The Respondent further went on to submit that the observations in *MSP Infrastructure Limited* as referred by the Appellant, do not lay down the correct law.

Observations of the Supreme Court

Supreme Court examined and observed that there is no bar to plea of jurisdiction being raised by way of an objection under Section 34 of the Arbitration Act even if no such objection was raised under Section 16, as both stages are independent to each other. Supreme Court further observed that observations in (paragraphs 16 and 17 of) *MSP Infrastructure Limited* do not lay down the correct law. Supreme Court also observed that it does not agree with the observation in the said case of *MSP Infrastructure Limited*, which held that the public policy of India does not refer to a state law and refers only to an all India law.

Decision of the Supreme Court

The Hon’ble Apex Court held that the public policy of India refers to law in force in India whether state law or central law and thereby overruled the observations to the contrary in paragraphs 16 and 17 of the judgment in *MSP Infrastructure Limited*. Supreme Court ordered that since amendment application is not pressed by the Respondent, the appeal is rendered infructuous. Further, the Supreme Court directed that the matter be taken up by the trial court for consideration of objections regarding jurisdiction of arbitrator under Section 34 of the Arbitration Act.

VA View

This judgement of the Hon’ble Supreme Court has widened the scope of Section 34(2)(b) of the Arbitration Act. Earlier, in accordance with the observation of Supreme Court in case of *MSP Infrastructure Limited*, it was mandatory for parties to arbitration, to raise the plea of jurisdiction under Section 16 of the Arbitration Act before the arbitral tribunal first and then only the same was allowed to be raised while challenging the arbitral award under Section 34. Overruling the aforesaid observation in case of *MSP Infrastructure Limited*, the Supreme Court held that plea of lack of jurisdiction of arbitral tribunal can be raised under Section 34 of the Arbitration Act for the first time even if the same has not been raised earlier under Section 16 in the statement of defense.

The Supreme Court has also widened the scope of the term “public policy of India” under Section 34 of the Arbitration Act and held that public policy of India refers to any law which is in force in India, whether it is state law or central law. Though this order is founded on the basic principle that the objection with respect to jurisdiction can be raised at any stage, however, its impact would ultimately delay the procedure, which will in turn contradict the object of the Arbitration Act, that is to resolve the dispute without unnecessary delay. Further, the question that if the Arbitration Act being a central law can be excluded by the Madhya Pradesh Madhyastham Adhikaran Adhiniyam, 1983, which is a state law, is left unanswered considering it to be purely a legal plea to be dealt by the concerned court.

III. Supreme Court holds that non-signatories to arbitration agreements can be made parties to domestic arbitrations

Supreme Court in case of ***Ameet Lalchand Shah and Others v. Rishabh Enterprises and Another*** (decided on May 3, 2018) held that in case of domestic arbitrations, parties to ancillary agreements without an arbitration clause can also be impleaded to arbitration if the main/principal agreement envisages arbitration. Supreme Court further held that mere allegations of fraud by a party cannot be sufficient to evade arbitration and the courts can refuse a reference to arbitration only if they find that there are serious allegations of fraud which make a virtual case of criminal offence.

Facts

Rishabh Enterprises (“**Respondent**”) executed four separate agreements with three different parties, namely, (a) Equipment and Material Supply Contract and Engineering, Installation and Commissioning Contract with M/s Juwi India Renewable Energies Private Limited (“**Juwi India**”) in relation to a Solar Plant; (b) Sale and Purchase Agreement with Astonfield Renewables Private Limited (“**Second Appellant**”); and (c) Equipment Lease Agreement with Dante Energy Private Limited (“**Third Appellant**”). The Second Appellant and Third Appellant are promoted by Ameet Lalchand Shah (“**First Appellant**”) (Juwi India, First Appellant, Second Appellant and Third Appellant are collectively referred as “**Appellants**”). Of all the agreements executed by Respondent with the abovementioned parties, the agreement with Second Appellant did not contain an arbitration clause.

Under Sale and Purchase Agreement with the Second Appellant, Respondent purchased certain products to be leased to Third Appellant under the Equipment Lease Agreement. A dispute arose between Second Appellant and Respondent under Sale and Purchase Agreement where Respondent alleged that Second Appellant committed misrepresentation and criminal breach of trust for the equipment procured. Another dispute arose between Third Appellant and Respondent under Equipment Lease Agreement where Respondent alleged that Third Appellant defaulted on the payment of rent.

Owing to the disputes between the parties, Third Appellant issued a notice invoking arbitration clause. However, Respondent preferred a civil suit before Delhi High Court against Appellants levelling various allegations including fraud and misrepresentation. On receipt of notice and summons in the suit, Appellants preferred an application under Section 8 of the Arbitration and Conciliation Act, 1996 ("**Arbitration Act**") seeking reference of the dispute between the parties to arbitration pertaining to all the four agreements. Single judge of the Delhi High Court dismissed the application of Appellant holding that the agreement between Respondent and Third Appellant cannot be treated as the principal agreement and the agreements between Respondent and Second Appellant and Respondent & Juwi India cannot be said to be ancillary agreements to the same. It also held that since Respondent has made serious allegations of fraud and filed a criminal complaint, the dispute cannot be referred to arbitration. The Division Bench of the Delhi High Court concurred with the pronouncement of Single judge. Aggrieved by the decision of Division Bench of Delhi High Court, Appellants filed civil appeal before the Supreme Court, where following questions came up for determination:

Issues

Issue 1: Whether all the four agreements are inter-connected to refer the parties to arbitration despite there being no arbitration clause in the Sale and Purchase Agreement between Respondent and Second Appellant?

Issue 2: Whether reference of the dispute between the parties to arbitration can be refused by the court on the ground of allegations of fraud levelled against Appellants?

Arguments

Issue 1: Respondents argued that the Delhi High Court rightly relied upon the case of ***Sukanya Holdings (P) Limited v. Jayesh H. Pandya and Another*** (decided on April 14, 2003) ("***Sukanya Holdings***") in rejecting the arguments of Appellant and held that as per Part-I of the Arbitration Act, parties who are not signatories to the arbitration agreement (in this case, Second Appellant under Sale and Purchase Agreement) cannot be referred to arbitration. While distinguishing the facts of the present matter with ***Chloro Controls India Private Limited v. Severn Trent Water Purification Inc. and Others*** (decided on September 28, 2012) ("***Chloro Controls***"), which held that non-signatories can be parties to an arbitration agreement for cases arising under Part-II of the Arbitration Act, the Respondents submitted that Appellants cannot rely upon the case of *Chloro Controls* as the case of *Sukanya Holdings* was not overruled by the case of *Chloro Controls*. It was contended by Respondent that Sale and Purchase Agreement with Second Appellant under which huge money was parted with, is the main agreement having no arbitration clause and hence cannot be referred to arbitration.

The arguments of Appellants on this issue were not summarized in the judgement.

Issue 2: Appellants placed reliance on ***A. Ayyasamy v. A. Paramasivam and Others*** (decided on October 4, 2016) ("***Ayyasamy***"), to contend that there were no serious allegations in the plaint to decline reference of the matter to arbitration. It was submitted that mere allegations of fraud were not sufficient to detract from the performance of

the obligation of the parties in terms of the agreement and to dismiss the application to refer the matter to arbitration.

Respondent contended that since the allegations of fraud were levelled against the Appellants, the dispute could not be referred to arbitration. It was further contended that fraud had not been alleged merely to circumvent arbitration. It was averred in the plaint that from inception, the intention of Appellants was to cheat Respondent and Respondent were made to part with large sums of money on the basis of the misrepresentation made by Appellants.

Observations of Supreme Court

Issue 1: Supreme Court held that a careful perusal of all the 4 agreements indicates that all the agreements were for the single purpose which was to commission solar plant at Uttar Pradesh. Commissioning of the solar plant was a commercial understanding between the parties and it was effected through several agreements. The Equipment Lease Agreement (with the arbitration clause) with the Third Appellant for commissioning of the solar plant was the principal agreement and the Sale and Purchase Agreement (without the arbitration clause) with the Second Appellant was its ancillary agreement.

Further it was held that the averments in the plaint also prima facie indicate that all the four agreements were inter-connected and that First Appellant is the promoter and controlling man of both Second Appellant as well as the Third Appellant. Even though the Sale and Purchase Agreement did not have any arbitration clause, it was clearly linked with the main Equipment Lease Agreement. Therefore, the dispute between the parties to various agreements could be resolved only by referring all the four agreements and the parties thereon to arbitration.

Supreme Court also referred to the Arbitration and Conciliation (Amendment) Act, 2015 which brought an amendment to Section 8 of the Arbitration Act to bring it in line with Section 45 of the Arbitration Act. The language of amendment to Section 8 of the Arbitration Act is clear that judicial authority before which an action is brought in a matter which is the subject of an arbitration agreement shall refer the parties to arbitration notwithstanding any prayer, judgment, decree or order of the Supreme Court or any other court. Therefore, judgement in case of *Sukanya Holdings* would not apply in light of the amendment to Section 8 of the Arbitration Act.

Issue 2: Examining the second issue, the Supreme Court held that in case of *Ayyasamy*, it was held that to impart a “sense of business efficacy” to the commercial transactions, mere allegation of fraud is not a ground to nullify the effect of arbitration agreement between the parties. Arbitration clause need not be avoided and parties can be relegated to arbitration where merely simple allegations of fraud touched upon internal affairs of parties is levelled. In the case at hand, the allegations were not serious enough to warrant a refusal to refer the parties to arbitration.

Decision of Supreme Court

Supreme Court set aside the decision of Division Bench of Delhi High Court and held that despite no arbitration agreement between the parties, the dispute arising from the Sale and Purchase Agreement between Respondent and the Second Appellant could be referred to arbitration as it was ancillary to and interconnected with the main Equipment Lease Agreement with an arbitration clause. It also held that the allegations of fraud against the Appellants were not serious enough to refuse a reference to arbitration.

VA View

Soon after the decision of the Supreme Court in case of ***Cheran Properties Limited v. Kasturi and Sons Limited*** (decided on April 24, 2018), which held that arbitral award would be binding on a third party who is not a signatory to the arbitration agreement, this judgement comes in a streak of judgements that have decided issues on the contentious subject of non-signatories being a party to arbitration. The Indian jurisprudence on this subject had a breakthrough with the *Chloro Controls* case which interpreted Section 45 (Power of judicial authority to refer parties to arbitration) of the Arbitration Act to hold that in certain instances non-signatories could also be made parties to arbitrations. However, judgment in case of *Chloro Controls* was only limited to international commercial arbitrations. The present judgement extends the *Chloro Controls* ratio to domestic arbitration taking the aid of the amended Section 8 of the Arbitration Act which is pari-materia to Section 45 of the Arbitration Act. The argument used is that ancillary or supplementary agreements would be bound by the arbitration clause of the main agreement. In light of this decision it would be prudent for parties to ensure that all the agreements related to the same transaction have similar dispute resolution clauses to avoid confusion and if arbitration is not preferred for any part of the transaction, then to exclude it from the main agreement altogether.

IV. NCLAT excludes time from CIRP period during which CoC could not function

The National Company Law Appellate Tribunal (“NCLAT”) in the matter of ***Quinn Logistics India Private Limited v. Mack Soft Tech Private Limited and Others*** (decided on May 8, 2018) allowed extension of corporate insolvency resolution process (“CIRP”) even when 270 days’ time period had expired as for more than half of such period, Committee of Creditors (“CoC”) could not function due to stay on CIRP by interim order of the National Company Law Tribunal (“NCLT”), Hyderabad.

Legal framework

Under Section 12 of the Insolvency and Bankruptcy Code, 2016 (“Code”), CIRP is required to be completed within a period of 180 days from the date of admission of the application to initiate CIRP. However, CoC can pass a resolution at its meeting, by a vote of 75% of the voting shares, to enable the resolution professional to move to NCLT for extension of CIRP period beyond such period. After the enactment of the Insolvency and Bankruptcy Code

(Amendment) Ordinance, 2018, the said voting share of 75% by CoC has been reduced to 66%. NCLT can grant extension in such cases for a period not exceeding 90 days and such extension cannot be granted more than once.

Facts

The application for initiation of CIRP of Mach Soft Tech Private Limited was admitted by NCLT, Hyderabad on August 11, 2017. On January 16, 2018, the period of CIRP was extended by NCLT, Hyderabad for a further period of 90 days.

There were several applications pending before NCLT, Hyderabad in this matter. On various occasions during CIRP, the proceedings before CoC were stayed by NCLT, Hyderabad. Counsels for the financial creditor, resolution applicant and resolution professional, had argued before NCLT that for about 160 days, the proceedings before CoC could not continue in view of NCLT, Hyderabad orders keeping proceedings before CoC in abeyance. It was contended that the interim orders of NCLT, Hyderabad virtually resulted in stay of CIRP and CoC meetings were stalled. Since CIRP period was to expire in May, 2018, the parties submitted that CIRP period to be extended for the period covered by interim orders.

NCLT, Hyderabad had granted extension till the next date of hearing (May 15, 2018) after taking into account the pending applications in the matter. Quinn Logistics India Private Limited ("**Financial Creditor**") preferred an appeal for modification of the aforesaid order of NCLT, Hyderabad, where the following question came up for determination:

Issue

Whether CIRP can be extended notwithstanding the maximum period allowed for CIRP under the Code had expired and whether the period of 166 days for the purpose of counting the total period of CIRP can be excluded as CIRP could not proceed for business during the aforesaid period on account of interim directions passed by the NCLT, Hyderabad?

Arguments

Learned counsel for Financial Creditor cited several cases before NCLT, Hyderabad in support of the extension of CIRP period. One such case was of **Quantum Limited v. Indus Finance Corporation Limited** (decided by NCLAT on February 20, 2018). In this case, NCLT, Mumbai had rejected the application for extension of time as the application was filed after expiry of the original period of 180 days of CIRP. NCLT, Mumbai had noted that there was no provision for revival of CIRP period to provide another 90 days' extension as mentioned under Section 12(2) of the Code especially when earlier 180 days period is complete, by the time application has been filed before NCLT. On an appeal, NCLAT granted extension, noting that, there was no provision mandating that the application was to be filed within 180 days. NCLAT also observed that it was duty on the part of NCLT to extend the period to find out whether a suitable resolution plan is to be approved instead of going for liquidation, which is the last recourse on failure of CIRP.

A time chart was also submitted by Financial Creditor before NCLAT to show that there was delay in CIRP due to proceedings pending before NCLT, Hyderabad.

Observations of NCLAT

NCLAT discussed its previous decisions in which extension of CIRP period was granted. One important case discussed was NCLAT Order in the matter of ***M/s. Shilpi Cable Technologies Limited v. Macquarie Bank Limited*** (decided on January 22, 2018) in which NCLAT had excluded the time period during which resolution professional could not function pursuant to its orders from CIRP period of 180 days. NCLAT also took note that several other benches of NCLT had also excluded period during which the process was stalled from CIRP period, on the facts and circumstances in each case.

NCLAT observed that if justified reasons exist, CIRP period can be extended beyond 270 days. NCLAT proceeded to give certain examples of grounds or circumstances, for which the intervening period can be excluded from the total period of 270 days, such as:

- (a) If CIRP is stayed by court, NCLT or NCLAT;
- (b) If resolution professional is unable to function for any reason during CIRP;
- (c) If there is an intervening period between the order of admission and the date on which the resolution professional takes charge;
- (d) If order is reversed by NCLT, NCLAT or Supreme Court and final orders are passed to enable the resolution professional to complete CIRP;
- (e) If CIRP is set aside by NCLAT or order of NCLAT is reversed by Supreme Court;
- (f) Any other circumstances justifying exclusion of certain period from CIRP.

However, NCLAT made it clear that, “.... after exclusion of the period, if further period is allowed the total number of days cannot exceed 270 days which is the maximum time limit prescribed under the Code.”

NCLAT took note of the fact that CIRP was stalled for 166 days due to interim order passed by NCLT, Hyderabad and therefore directed that such period be excluded for the purpose of counting CIRP period in the matter.

Decision of NCLAT

The order passed by NCLT, Hyderabad was modified to the extent that CIRP period was extended for 166 days. The resolution professional and CoC were allowed further period of 166 days to complete CIRP.

VA View

Several nuances of law under the Code are still evolving. Usually during CIRP period, there are several litigations, for example, there can be applications challenging the appointment of resolution professional, challenging the proceedings of CoC, etc. If in such matters, CoC proceedings are stayed for considerable time, CIRP is virtually stalled. The Code provides a very strict timeframe within which CIRP is to be completed. If CIRP is not completed within the statutory timeframe, the consequence is liquidation of the corporate debtor. Thus, if considerable time is lost and no work could be undertaken due to pending proceedings, it is unjust to count such time lost in the already limited time allowed to finish CIRP under the Code. NCLAT order rightly pointed out several instances as grounds due to which such intervening period should not be counted towards CIRP period. The judgment bodes well with the underlying objective of the Code and iterates that CIRP period is the period during which CoC and resolution professional are able to function and CIRP can be carried on without any hindrance, either by way of stay of CIRP or otherwise.



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