

# Between the lines...

May, 2018

## Key Highlights

- I. NCLT allows consideration of revised offer by UltraTech Cement Limited upholding the objective of IBC in the insolvency resolution of Binani Cement Limited
- II. Resolution Plan cannot be rejected on the ground of delay emanating from document internally circulated by the Resolution Professional or the Committee of Creditors
- III. Entity in liquidation can now be sold as a going concern
- IV. Supreme Court on denial of insurance claim and arbitrability of dispute

### I. NCLT allows consideration of revised offer by UltraTech Cement Limited upholding the objective of the IBC in the insolvency resolution of Binani Cement Limited

The Kolkata Bench of the National Company Law Tribunal (“NCLT”) in the case of *Bank of Baroda v. Binani Cement Limited* (decided on May 2, 2018) directed the Resolution Professional (“RP”) and the Committee of Creditors (“CoC”) to consider the revised offer made by UltraTech Cement Limited (“UTCL”). Further, the NCLT directed the RP to allow the suspended board of directors and the operational creditors to attend the meeting of the CoC in compliance with Section 24(3) of the Insolvency and Bankruptcy Code, 2016 (“IBC”).

#### Facts

In the matter of corporate insolvency resolution process (“CIRP”) of Binani Cement Limited (“Corporate Debtor”), various applications were filed by the promoter director, the unsecured financial creditors and the operational creditors of the Corporate

Debtor and UTCL. The brief facts leading to various applications by the aforesaid persons and entities are as follows: The RP appointed various advisors and outsourced most of work thereby incurring exemplary costs. Rajputana Properties Private Limited (“RPPL”) was declared as the H1 bidder by the CoC. However, the RP had not completed the process of verification of claims of the operational creditors. The resolution plan of RPPL provided for discriminatory treatment *inter se* the creditors of the Corporate Debtor. UTCL, one of the resolution applicants, submitted a revised offer, higher than that offered by RPPL, in consonance with the object of maximisation of value of assets. However, the same was not considered by the RP and the CoC as it was submitted after the last date for submission of the bid.

## Issues

**Issue 1-** Whether the RP exceeded his power in appointing professionals, outsourcing the work in violation of Circular No. IP/003/2018 issued by the Insolvency and Bankruptcy Board of India (“IBBI”) and incurring exemplary cost in violation of any of the provisions of IBC?

**Issue 2-** Whether non-consideration of revised offer of UTCL amounts to violation of any provisions of IBC and is against the objects of IBC?

**Issue 3-** Whether there is a discrimination against the unsecured financial creditors who should be at par with other financial creditors and the resolution plan submitted for the approval is contrary to the scheme of IBC?

**Issue 4-** Whether the RP has ignored any of the operational creditors’ claims and not honoured their claims as alleged by the operational creditors?

## Relevant Provisions

For a better understanding of the issues it is pertinent to reproduce the relevant provisions of IBC, Regulations and circular hereunder:

Section 21(3): *“Where the corporate debtor owes financial debts to two or more financial creditors as part of a consortium or agreement, each such financial creditor shall be part of the committee of creditors and their voting share shall be determined on the basis of the financial debts owed to them.”*

Section 24(3): *“The resolution professional shall give notice of each meeting of the committee of creditors to: (a) members of Committee of creditors (b) members of the suspended Board of Directors or the partners of the corporate persons, as the case may be; and (c) operational creditors or their representatives if the amount of their aggregate dues is not less than ten per cent. of the debt.”*

Schedule I of IBBI (Insolvency Professionals) Regulations, 2016 (“**Insolvency Professionals Regulations**”)

Regulation 25: *“An insolvency professional must provide services for remuneration which is charged in a transparent manner, is a reasonable reflection of the work necessarily and properly undertaken, and is not inconsistent with the applicable regulations.”*

Regulation 27: *“An insolvency professional shall disclose all costs towards the insolvency resolution process costs, liquidation costs, or costs of the bankruptcy process, as applicable, to all relevant stakeholders, and must endeavour to ensure that such costs are not unreasonable.”*

Circular No. IP/003/2018: *“An insolvency resolution professional shall not outsource any of his duties and responsibilities under the Code.”*

## **Arguments**

**Issue 1** - The promoter director alleged that the RP failed to comply with National Company Law Appellate Tribunal's order by not permitting the director to attend the entire meeting of the CoC and in violation of Section 24 of IBC. He challenged the conduct of RP as malafide to cause wrongful loss to the Corporate Debtor by making unnecessary delegations to the firm in which he is a partner at unreasonable costs and outsourcing majority work in violation of Circular No. IP/003/2018. The RP argued that the directors did not appear in person and hence, their representatives were asked to wait outside during crucial discussions because the discussion was regarding sensitive issues concerning diversion of funds and fraudulent transfers. He added that there was no provision prohibiting him from appointing persons from a firm in which he is partner.

**Issue 2** - UTCL made the following three allegations: (i) the resolution plan of UTCL was not considered or given an opportunity of being heard by the RP even though the evaluation criteria as applied resulted in UTCL coming close in scoring; (ii) the revised offer was made 43 (forty-three) days before the expiry of the CIRP as per Section 12 of IBC. However, it was not considered and no opportunity of being heard was given, thereby preventing UTCL from competing with other resolution applicants; and (iii) the decision taken by the CoC approving the resolution plan of RPPL, in its meeting held on March 14, 2018, was completely illegal and arbitrary since certain applications filed in this matter were pending before the NCLT. The RP, RPPL and the CoC unanimously contended that UTCL intends to obstruct the smooth operation of CIRP and aims to put the Corporate Debtor into liquidation. Further, it was contended by the RP that (i) the revised offer was sent by e-mail; (ii) it was not in accordance with the process document laid down by the CoC; and (iii) the offer was beyond the time stipulated under the process document as formulated by the CoC.

**Issue 3** - Arbitrary haircuts were given to the claims of SBI Hong Kong and Export Import Bank of India ("**EXIM**") as against their counterparts. Both these applicants also challenged verification of 100% of IDBI Bank ("**IDBI**") and Edelweiss Asset Reconstruction Company Limited's claim in spite of non-invocation of guarantee by the Corporate Debtor. The reasoning was based on the ruling of NCLT, Principal Bench, New Delhi in another matter, that the corporate debtor must invoke guarantee before CIRP failing which, the claim does not qualify a debt. The RP stated that the enhancement of the claim amount of IDBI was allowed based on negotiations of RPPL with lenders in the lenders forum meeting and the RP had no role in the offer made in the resolution plan of RPPL. No other arguments were raised by the RP.

**Issue 4** - Operational creditors alleged that their claims had been ignored by the RP and that he did not attempt to provide proportionate benefit. They were not permitted to attend any of the meetings of the CoC so as to have an effective representation in violation of Section 24(3)(c) of IBC. The RP contended that verification of claims was an ongoing process and he will consider the claims as and when information is received.

## **Observations of the NCLT**

**Issue 1** - The NCLT did not find any relevance in the argument of the RP not permitting the representatives of the directors to attend the entire meeting since IBC permits any eligible person to send his representative. Dealing with the allegations of making unnecessary delegations, the NCLT referred Regulations 25 and 27 of the Schedule I of Insolvency Professionals Regulations which mentions that the insolvency process costs should not be unreasonable. Taking a look at the expenses, it was found that the volume of work was not proportionate to the amount of expense incurred. The appointments were therefore held to be at unreasonable costs thereby causing a financial burden to the Corporate Debtor.

**Issue 2** - The NCLT observed the following: (i) neither IBC, nor the rules and regulations framed thereunder prohibit submission of revised offer by way of e-mail. Therefore, non-acceptance of the revised offer on this ground violates the objective of IBC since it prevents the maximization of the value of assets of the Corporate Debtor; (ii) the Insolvency Professionals Regulation directs that the insolvency professional must maintain his independence from external forces in professional relationships and not rely solely on the process document. The RP is duty bound to accept the offer and convene a meeting of the CoC; and (iii) when the revised offer was made, the CIRP period under IBC had not expired. IBC does not restrict the RP or the CoC from accepting revised offers in addition to the offer already made by a resolution applicant.

**Issue 3** -The NCLT found that the entire claim of IDBI was verified and admitted by the RP despite un-invoked guarantee issued by the Corporate Debtor in favour of IDBI and RPPL allowed the entire claim on a condition that IDBI consents to its resolution plan. This influence of majority lenders to get their claims satisfied by RPPL amounts to discrimination against the two banks, SBI Hong Kong and EXIM.

**Issue 4** -The NCLT held that a duty is cast upon the RP to verify all the claims of the operational creditors before a resolution plan is placed before the CoC. Further, haircut in varying proportion was offered to operational creditors and not uniformly to all the creditors which is not contemplated under IBC. The same factors adds strength to the contention of operational creditors that their claims were not considered strictly by the RP in accordance with IBC.

## **Decision of the NCLT**

The NCLT ruled that:

1. The period of litigation stands excluded from the CIRP period;
2. The revised offer and resolution plan submitted by UTCL is to be considered by the RP and placed before the CoC;
3. The CoC is also to reconsider the resolution plan of RPPL, if RPPL raises the offer above that of UTCL; and
4. The RP is directed to comply with the provisions of IBC in submitting the revised offer before the CoC and in issuing notice to the director of the suspended board of the Corporate Debtor. Notice is also to be issued one among the operational creditor who filed the application in this matter as a representative if the requirement of Section 24(3) of IBC is satisfied.

## VA View

The CIRP of Binani Cement Limited is one of the few resolutions wherein the creditors are being repaid in full without any haircuts. By directing the RP and CoC to consider the revised bid of UTCL, NCLT has ensured the maximization of value of assets of the Corporate Debtor in furtherance of the objective of IBC. The most benefited parties in the entire process are the stakeholders of the Corporate Debtor.

While the law around CIRP is still evolving, the NCLT has taken the RP to task for not being transparent in its dealings with the Corporate Debtor and for not performing its duties under IBC by himself and delegating most of the work to an affiliate firm in which he is interested, at the cost of resolution applicant. This order ensures that the RP henceforth, will avoid unnecessary appointments of third parties and that he is independent of the committee of creditors in his decision-making. Further, reports suggest that “hybrid model” is being proposed, where the top three contenders based on technical parameters will bid through an online system with the avowed objective to help maximise value of the asset for lenders and to enhance the transparency in the resolution process.

## II. Resolution Plan cannot be rejected on the ground of delay emanating from document internally circulated by the Resolution Professional or the Committee of Creditors

In case of *Punjab National Bank v. Bhushan Power & Steel Limited* (decided on April 23, 2018), National Company Law Tribunal, Principal Bench, New Delhi (“NCLT”) held that the resolution plan of an applicant shall not be rejected on the ground of delay emanating from document internally circulated by the resolution professional or the committee of creditors specifying the last date of submission of resolution plan to a selected group of persons in terms of unamended provisions of Insolvency and Bankruptcy Code, 2016 (“IBC”).

### Facts

In a Corporate Insolvency Resolution Process (“CIRP”) initiated by Punjab National Bank under Section 7 of IBC against Bhushan Power and Steel Limited, Committee of Creditors (“CoC”) was constituted and Resolution Professional (“RP”) was appointed. Pursuant to public notice issued inviting Expression of Interest (“EOI”), applications were invited to participate in the resolution process within the timelines prescribed under Regulation 39(1) of unamended Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 (“Regulations”) read with Section 25(2)(h) of IBC. Meanwhile, IBC and Regulations were amended, which provided that resolution plan is required to be submitted within the timeline prescribed by RP.

Liberty House Group Pte Limited (“Liberty House”) submitted its EOI after passing of deadline with a request to CoC to allow participation in the resolution process of BPSL. The last date for submission of resolution plan was fixed by CoC as January 1, 2018, which was repetitively revised and extended to February 8, 2018. Liberty House submitted its resolution plan on February 20, 2018 to be considered in the meeting of CoC scheduled on February 22, 2018, which

was rejected by CoC for late submission. Aggrieved by the decision of CoC, Liberty House filed an application before NCLT and the following question came up for determination:

### Issue

Whether delay in filing of resolution plan on account of document internally circulated by RP or CoC can be considered as a ground for rejecting the resolution plan placed by any person with regard to CIRP commenced under unamended IBC and Regulations?

### Arguments

Liberty House argued that the resolution plan submitted by it cannot be rejected as the public notice inviting EOI was issued with reference to Regulation 39(1) of the unamended Regulations, which provided that an *endeavour* was to be made for submitting a resolution plan 30 days before expiry of the maximum period permitted under Section 12 of IBC that is 180 days or 270 days, as the case may be. The public notice further provided that the detailed process and deadline for submission of resolution plan were to be separately communicated to the potential resolution applicant. However, no other public notice has ever been issued by RP fixing to any timeline for submission of plan nor any such information was ever communicated to Liberty House or publicly announced. Liberty House contended that if the amended Regulation 39 of the Regulations were to be applied, then a fresh public notice was required to be issued post amendment of the Regulations and IBC.

On the other hand, RP argued that Liberty House submitted the EOI and resolution plan much beyond the due date and it also failed to furnish qualification documents which were *sine qua non* for consideration of resolution application. Those who fulfilled the qualification criteria were provided the 'process document' and the date of submission of resolution plan was clearly mentioned in the 'process document'.

Supporting the arguments of RP, CoC relied on the judgement of Supreme Court in case of **Sorath Builders v. Shreejkrupa Buildcon Ltd. & Anr.** (decided on February 20, 2009), and contended that the terms of tender have to be strictly construed and submission of bids beyond deadline would not only derail the entire process but would result into injustice to other bidders. Speed is essence of IBC and allowing the present application would open floodgates for other resolution applicants.

Relying on the judgment of Supreme Court in case of **M/s Synergy Steels Limited v. Petroleum and Natural Gas Regulatory Board** (decided on October 9, 2015), Tata Steel Limited, an applicant, who submitted the resolution plan within prescribed time, argued that a person who comes after the deadline has no *locus standi* to challenge the tender conditions. Further, once it is found that a level playing field has been created according to the norms laid down in Article 14 of the Constitution, any party requesting to create a non-level playing field must not be heard.

### Observations of the NCLT

NCLT examined the provisions of IBC and Regulations and observed that under unamended Regulation 39 of Regulations, a resolution applicant shall *endeavour* to submit a resolution plan 30 days before the expiry of the

maximum period permitted under Section 12 of IBC for completion of CIRP. Regulation 39 of the Regulations uses the word 'endeavour' which according to the dictionary meaning implies that sincere and earnest efforts are required to be made which leaves a room for further concession. After issuance of public notice, RP has not issued any other public notice notifying the criteria which might have been laid down by CoC. Hence, in the absence of issue of new public notice in terms of amendment, the original public notice would prevail with regard to the period for receipt of resolution plan application. Since the period of 180 days for completion of CIRP was extended to 270 days, the resolution plan submitted by Liberty House was well within the expiry of 240 days that is 30 days prior to expiry of the maximum period permitted under Section 12 of IBC for completion of CIRP. NCLT further observed that in the new regime, consideration of a resolution plan of another competitor would advance the object of IBC in maximisation of the assets of the corporate debtor and may provide better solution in restructuring the stressed assets.

### Order of the NCLT

NCLT held that the resolution plan of the Liberty House shall not be rejected on the ground of delay emanating from process document or any other document internally circulated by the RP or the CoC and therefore directed the RP and CoC to consider the resolution plan submitted by Liberty House. NCLT further held that the time period spent on litigation will be excluded from the maximum period prescribed for completion of CIRP.

### VA View

The NCLT Order is first of its kind where NCLT directed the RP and CoC to consider the resolution plan submitted by an applicant even after missing two deadlines, one for submission of EOI and other for submission of the resolution plan. NCLT also observed that IBC does not permit the division of the process firstly by inviting EOI and then by asking to file the resolution plans. In furtherance to support the object of IBC, NCLT in instant case ruled that if speed is of the essence of the whole process, then it must be remembered that one consolidated process is better suited to CIRP than splitting the process in various parts.

This NCLT Order will serve as a precedent in laying down the principle that amended provisions of IBC and Regulations would not apply to cases where the public notice inviting EOI was made prior to the amendments. Further, this NCLT Order suggests that issuance of fresh public notices post amendment will allow application of the amended Regulations and IBC to CIRPs commenced prior to the amendments.

### III. Entity in liquidation can now be sold as a going concern

The Insolvency Bankruptcy Board of India, by Notification dated March 27, 2018 (*effective from April 1, 2018*), amended the Insolvency and Bankruptcy Board of India (Liquidation Process) Regulations, 2016 ("**Liquidation Regulations**"). The Insolvency and Bankruptcy Board of India (Liquidation Process) (Amendment) Regulations, 2018 ("**Amendment Regulations**"), inter alia, amended Regulation 32 of the Liquidation Regulations which relates to the manner in which assets of the corporate debtor are to be realised.

### **Liquidation under the insolvency regime**

Under the Insolvency and Bankruptcy Code, 2016 (“**IBC**”), Section 33 provides for the initiation of liquidation of the corporate debtor in case of the following:

- If the adjudicating authority (“**Authority**”) does not receive a resolution plan before the maximum period permitted for completion of the corporate insolvency resolution process (“**CIRP**”);
- If the Authority rejects the resolution plan;
- If the committee of creditors (“**CoC**”) decides to liquidate the corporate debtor during CIRP; and
- If the Authority determines that the corporate debtor has contravened the provisions of the resolution plan, on an application made by any person other than the corporate debtor, whose interests are prejudicially affected by such contravention.

IBC further provides for appointment of liquidator, his powers and duties, the order in which the proceeds from the sale of the liquidation assets are to be distributed, etc.

The Liquidation Regulations prescribe the eligibility criteria for appointment as liquidator, procedure of claims and realization of assets, etc. Chapter VI of the Liquidation Regulations provides for realization of assets of the corporate debtor such as matters relating to the manner and mode by which the assets are to be realized, valuation of assets, etc. IBC and relevant regulations thereunder also provide for voluntary liquidation.

### **Position before and after the amendment**

Before the amendment, Regulation 32 of the Liquidation Regulations provided for selling of liquidation assets on a standalone basis or either by selling the assets in a slump sale or selling set of assets collectively. The Amendment Regulations inserted two new provisions in Regulation 32:

- The Liquidator can now sell the liquidation assets in parcels; and
- The Liquidator is empowered to sell the corporate debtor as a going concern.

The latter provision can be construed as a provision which attempts to allow the liquidator to save the legal existence of the corporate debtor in deserving cases and thereby serve the interest of various stakeholders, especially employees of the corporate debtor. Prior to amendment, the employees, in liquidation, were to lose their jobs and various stakeholders were left with little or no value after the liquidation. The amendment gives another chance of saving the existence of the corporate debtor if the CIRP fails.

### **Decision of the National Company Law Tribunal, Kolkata Bench (“NCLT Kolkata”) in the case of Gujarat NRE Coke Limited, corporate debtor (“Gujarat NRE Case”)- Precursor to the amendment**

Under the insolvency regime introduced by IBC, the decision of the NCLT Kolkata in Gujarat NRE Case is relevant in



the context of sale of an entity under liquidation as a going concern. NCLT Kolkata delivered an order on January 11, 2018, allowing sale of corporate debtor as going concern.

### **Facts**

In Gujarat NRE Case, the corporate debtor had filed application for initiation of CIRP which was admitted by NCLT Kolkata on April 7, 2017. The resolution plan submitted by one resolution applicant, RARE Asset Reconstruction Company, was not approved by CoC as CoC members having a total voting share of 84.03% voted against the resolution plan. Interestingly, the Chief Commercial Officer of the corporate debtor, purported to be representing all the employees, came forward to submit a resolution plan on their behalf. It was conveyed to the resolution professional that the employees were concerned about their livelihood as the corporate debtor was set to face liquidation and that the resolution plan of employees should be taken into consideration. However, it was informed that given the strict timelines under IBC, their resolution plan was unlikely to be taken up for consideration.

### **Arguments on behalf of employees before NCLT Kolkata**

It was submitted that the corporate debtor had about 1,178 employees including workers and had overcome its period of crisis by making operational profits in recent months. It was further submitted that the corporate debtor was in a position to make payments to all employees, contractual employees and workers engaged at its plant. The argument on behalf of the workforce of the corporate debtor was that by closing the company and by discharging 1,178 employees, their families, numerous small vendors, suppliers, contractors, job workers and transporters of the company totalling about 10,000 people will be affected. It was stressed upon before NCLT Kolkata that sale of assets of the corporate debtor as a going concern was necessary to save the livelihood of several workers. It was stated that, *“Hon'ble Supreme Court and High Court has often directed the sale of assets of the company as a going concern with the object of preserving the employment and protecting the livelihood of its employees and workmen, and has done so even in case when the company has been lying closed for a number of years”*.

### **Order of NCLT Kolkata**

By order dated January 11, 2018, the corporate debtor went into liquidation and necessary directions were issued. However, NCLT Kolkata took note of the fact that the corporate debtor had made operational profit and also of the fact that a large number of employees and workers of the corporate debtor were to lose their livelihood. NCLT Kolkata, after discussing a Supreme Court decision, issued direction to the liquidator to make an attempt to dispose of the corporate debtor as a going concern and allowed a maximum period of 3 months from the date of the order for selling the corporate debtor as a going concern.

### VA View

This is indeed a welcome amendment. Earlier, the courts used to take a call as to whether it should allow the sale of the entity in liquidation as a going concern based on the facts and circumstances of each case. However, the amendment has incorporated the provision for sale of corporate debtor as a going concern in the statutory framework itself. Now the liquidator has an option to sell the entity as a going concern and thereby protect the livelihood of workers and the interest of various stakeholders. However, the amendment gives only an option to the liquidator and therefore the liquidator and the adjudicating authority will have to exercise their judgment in the interest of all stakeholders.

### IV. Supreme Court on denial of insurance claim and arbitrability of dispute

Supreme Court in the case of ***Oriental Insurance Company Limited v. Narbheram Power and Steel Private Limited*** (decided on May 2, 2018) held that the arbitration clause in an agreement entered between two parties is required to be strictly construed.

#### Facts

Narbheram Power and Steel Private Limited (“**Respondent**”) had a factory in Odisha for which they had taken fire industrial all risk policy for insurance from the Oriental Insurance Company Limited (“**Appellant**”). Due to cyclone in 2013, the Respondent suffered loss for which it had claimed insurance from the Appellant. The claim was not settled by the Appellant and consequently by communication dated January 21, 2017, Respondent invoked the arbitration agreement and nominated an arbitrator to adjudicate over the disputes. Appellant denied to refer the dispute to arbitration, and therefore Respondent filed an application in the High Court under Section 11 of the Arbitration and Conciliation Act, 1996 (“**Act**”) for appointment of arbitrator by the court. High Court appointed one of its retired judges as arbitrator which was challenged by the Appellant in the Supreme Court and the following question came up for determination:

#### Issue

Whether the dispute is arbitrable as per the arbitration clause in the insurance policy obtained by the Respondent from the Appellant?

#### Arguments

It was submitted on behalf of the Appellant that the dispute could not be referred to arbitration as it had not accepted the claim of the Respondent. The Appellant also argued that the High Court was not right in concluding that the arbitration clause suffered from ambiguity and was to be purposively read failing which the arbitration clause was to become meaningless. On the other hand, the Respondent argued that denial of the claim was on

quantum of liability only and there was no non-acceptance of the liability altogether by the Appellant, and therefore, the dispute is arbitrable.

### **Precedents discussed by the Supreme Court**

Out of the several cases discussed by the Supreme Court in this judgment, two cases which will help understand the issue under consideration better are discussed below. The facts of these case are identical to the facts in the matter discussed herein.

- Decision of the Supreme Court of India in the case of ***The Vulcan Insurance Company Limited v. Maharaj Singh and Another*** (decided on October 3, 1975):

The facts of this case were such that the respondent had taken advance of money on the security of the factory premises and for that purpose, a mortgage deed came to be executed in favour of the bank. The bank took several insurance policies to insure the mortgage properties. A fire broke at the factory premises and the insurance company was informed of the same. However, the insurance company repudiated the claim under the policy. On initiation of arbitration by the insured, the insurer claimed that it had repudiated the insurance claim and hence the arbitration clause in the policies was rendered inoperative. One of the questions before the court was whether in view of the repudiation of liability by the insurance company under clause 13 of the insurance policy, dispute raised could be referred to arbitration.

Clause 13 of the insurance policy provided that the action or suit had to be commenced within 3 months of the claim being rejected by the insurance company. Clause 18 provided that difference arising as to the amount of any loss or damage were to be referred to arbitration. The Court observed that repudiation of the claim could not amount to the raising of a dispute as to the amount of any loss or damage alleged to have been suffered and therefore the dispute raised was not covered by the arbitration clause. The court was of the view that as soon as the claim was rejected, which was not related to the amount of any loss or damage, the only remedy open to the claimant was to commence a legal proceeding, namely, a suit, for establishment of the liability of the insurer.

With respect to the clause which made the award of an arbitration a condition precedent to any right of action or suit, the court held that when an arbitration clause was not operative on the dispute raised then it was wholly unreasonable, almost impossible, to hold that still the parties have to obtain an award before starting any legal proceeding.

- Decision of the Madras High Court in the case of ***Jumbo Bags Limited v. The New India Assurance Company Limited*** (decided on March 10, 2016):

Petitioner had taken standard fire and special perils insurance cover for manufactured goods from the respondent insurance company. Due to a fire accident, the petitioner suffered huge loss and lodged claim with the insurance company. However, the respondent insurance company repudiated the petitioner's claim on the

ground that it was not a reasonable, fair and bona fide estimation of loss and alleged that the quantum of loss was exaggerated and supported by manipulated documents. The petitioner submitted the dispute of this nature was to be adjudicated by an independent arbitrator while the insurance company contended that the dispute was not in relation to the quantum of the claim, but one of total repudiation, which was not within the ambit of arbitration clause. Arbitration clause provided that dispute or difference arising as to the quantum to be paid under the policy was to be referred for arbitration. However, under the clause, no difference or dispute was to be referred to arbitration if the insurance company had disputed or had not accepted liability under the insurance policy.

The question before the court was whether in view of the total repudiation of the insurance claim, the petitioner could still seek the remedy of arbitration for adjudication of the disputes or whether arbitration as a remedy stood excluded. The court referred to several precedents, including the case of ***The Vulcan Insurance Company Limited*** (discussed above).

The Court held that the remedy of arbitration was not available to the petitioner in view of the arbitration clause specifically excluding the mode of adjudication of disputes by arbitration, where a claim was repudiated in toto by the insurance company and the only remedy available was of a civil suit. The Court observed, “*If a contra view is to be taken, it would amount to creation of an arbitration clause over a subject matter where there is no such clause*”.

### Observations of the Supreme Court

The Supreme Court noted the arbitration clause in the insurance policy, which stated, inter alia, “*It is clearly agreed and understood that no difference or dispute shall be referable to arbitration as hereinbefore provided, if the Company has disputed or not accepted liability under or in respect of this policy.*” As per the clause, only the dispute on quantum to be paid under the insurance policy was to be referred to arbitration. The Supreme Court discussed certain precedents including the cases discussed above and noted that the parties were bound by the clauses enumerated in the policy and the court cannot, in such cases, transplant any equity to the same by rewriting a clause. Relying on the Supreme Court decision in the case of ***The Vulcan Insurance Company Limited*** (discussed above), the Supreme Court was of the view that if a clause stipulates that under certain circumstances there can be no arbitration, and they are demonstrably clear, then the controversy pertaining to the appointment of arbitrator has to be put to rest.

The Supreme Court held that in the present case, the communication of the insurance company was nothing else but denial of liability by the insurer in toto which was not a dispute pertaining to quantum. According to the Supreme Court, the parties were bound by the terms and conditions agreed under the policy including the arbitration clause in it and the only remedy available to the Respondent was to institute a civil suit.

## Decision of the Supreme Court

The appeal was allowed and the order passed by the High Court was set aside.

### VA View

This judgment reiterates the position that the arbitration clause has to be construed strictly to give full effect to the intention of the parties. A court cannot sit in judgment and rework the clause originally agreed between the parties. In this case, as the dispute was specifically excluded from arbitration as per the arbitration clause agreed between the parties, the court gave full effect to the understanding between the parties by not referring the matter for arbitration.



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