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I. NCLT: Dismisses appeal against refusal to register share transfer in a public company; upholds JVA and AoA clauses

The National Company Law Tribunal (**"NCLT"**), Mumbai in the matter of ***Riverdale Infrastructures Private Limited v. Kirloskar Ebara Pumps Limited, Ebara Corporation and Kirloskar Brothers Limited*** *(decided on May 26, 2020),* dismissed the appeal against refusal to register share transfer in a public company, thereby upholding the validity of clauses of joint venture agreement and articles of association.

Facts

Kirloskar Ebara Pumps Limited (**"KEPL"**) was incorporated pursuant to a joint venture agreement dated January 27, 1988 (**"JVA"**) between Ebara Corporation (**"Ebara"**) and Kirloskar Brothers Limited (**"KBL"**). KEPL had a total of 68 shareholders with Ebara holding 2,25,000 shares of KEPL. KEPL, Ebara and KBL are hereinafter collectively referred to as **"Respondents"**.

In terms of Clause 6.01 of JVA and Article 51(b) of Articles of Association of KEPL (**"AoA"**), a party was barred from transferring its shares unless prior written consent was obtained from the other party; and, in case either party offers to transfer any such shares with the consent of other party, such other party shall have the Right of First Refusal (**"RoFR"**) of such offer. Under Clause 11.02 of JVA, in the event of refusal, if no reply is communicated within 3 months to offering party, it may sell the shares so offered to any third party within 3 months thereafter.

In December 2016, Ebara had offered to sell its shares to KBL. Even after several rounds of discussion, the parties could not arrive at an amicable resolution regarding the terms of sale. Thereafter, in March 2017, Ebara sold its shares to

Riverdale Infrastructures Private Limited (**"Appellant"**) under a Share Sale and Purchase Agreement (**"SSPA"**). KEPL refused to register the transfer as Ebara had failed to obtain prior written consent of KBL as required under the JVA and AoA. Aggrieved by this, the Appellant filed an appeal with NCLT, Mumbai to strike down Clause 6.01 of JVA and Article 51(b) of AoA to the extent that they were ultra vires Section 58 of the Companies Act, 2013 (**"Companies Act"**) and to direct KEPL to register the transfer of shares.

Issue

Whether the refusal by KEPL to give effect to the registration of shares acquired by the Appellant from Ebara is permissible within the framework of law, given that KEPL is a public company, and public companies, by definition, cannot restrict transfer of shares as is permissible in a private company.

Arguments

Contentions raised by the Appellant:

The counsel for Appellant contended that the two requirements under the JVA and AoA, namely, prior consent of non-exiting party, and, pre-emptive right to acquire the shares of exiting party, are inter-linked. The right to consent (or to reject consent, as the case may be) is a right in aid of first refusal, intrinsically embedded in the very same provisions. If they were not inter-linked; it would amount to an unconditional restriction on transfer of shares without consent of other party, which would have the effect of converting KEPL into a private limited company. Such an agreement would also not be valid under proviso to Section 58(2)of the Companies Act *(recognizes enforceability of a contract or arrangement between two or more persons in respect of transfer of securities even in a public company where shares are freely transferable)* because the said proviso is not a proviso to Section 2(68) and Section 2(71) of the Companies Act defining a private company and public company respectively. If a public company could put a blanket restriction on transferability of shares by virtue of said proviso, it would in effect render nugatory the basic difference between a private and public company.

It was further contended that KBL had consistently evaded responding to the offer made by Ebara. Therefore, the non-reply constitutes deemed refusal after completion of 3 months period. The consent to proceed with transfer to third party in line with Clause 11 of JVA and Article 51(b) of AoA was implicit in such rejection.

Contention raised by the Respondents:

The primary contentions of Ebara:

The provision of prior written consent cannot be an absolute embargo at the instance of one party, which would permit such party to impose harsh conditions whereby other party would not be able to exit. The parties only intended to incorporate a RoFR and not anything more. If prior written consent is considered as a condition precedent in addition to RoFR, it would amount to an absolute prohibition, which is impermissible in law and unenforceable even under proviso to Section 58(2) of the Companies Act. Upon rejection of Ebara's offer by KBL, no additional consent from KBL would be required.

The primary contentions of KEPL and KBL:

In rejecting the transfer, KEPL was bound by the terms of JVA and AoA. A mere restriction in a contract as between two or more shareholders in respect of transfer of shares, in terms of proviso to Section 58(2) of the Companies Act cannot be held to be contrary to the definition of a public company. The JVA does not violate Section 58(2) of the Companies Act as it binds only 2 out of the 68 shareholders.

A proviso operates as an exception and not the general rule laid down. (Relying on ***S. Sundaram Pillai and Others v. R. Pattabiraman and Others [(1985) 1 SCC 591]*** and ***Ali M.K. v. State of Kerala [(2003) 11 SCC 632]***. Thus, by the proviso to Section 58(2)of the Companies Act, a contract or arrangement between two or more persons in respect of transfer of securities was enforceable, as an exception to the general rule.

In the judgment of Honourable Bombay High Court in ***Bajaj Auto Limited v. Western Maharashtra Development Corporation Limited [(2015) (4) Bom CR 299],*** which was also affirmed by Honourable Supreme Court on January 9, 2019,the pre-emption agreements relating to transferability of shares of a public company entered into by two or more shareholders under proviso to Section 58(2) were held to be valid and enforceable.

Observations of the NCLT

The observations of NCLT, Mumbai were as follows:

(i) The principle of law embodied in the proviso to Section 58(2) of the Companies Act is not in conflict with the definition of a public company under Section 2(71)of the Companies Act. There is nothing in law that stops two or more shareholders from entering into a covenant containing clauses for pre-emption. This was recognized through judicial pronouncements under earlier Companies Act, 1956, and was then embodied in proviso to Section 58(2) of the Companies Act, 2013.

(ii) Both parties knew fully well the consequences of their contract.

(iii) KEPL cannot be expected to be run in violation of the AoA without inviting trouble for itself. It had no option but to refuse the transfer.

(iv) Only a civil court can decide whether the contract itself contains clauses that are too onerous or incapable of performance. The fact that Ebara did not opt for novation, rescission or alteration of the contract, shows that it did not think that the contract was unfair.

(v) Under Clause 7.6 of the SSPA *(requiring the Appellant to sign and deliver to KBL a letter agreeing to comply with and be bound by the terms of the JVA),* Ebara effectively accepted its responsibility under the JVA and shifted it to the Appellant. This shows that neither Ebara nor Appellant found the terms of JVA to be onerous or contrary to the law. In case the Appellant found the terms of JVA to be unfair, the choice was always open to it to approach a civil court for alteration of the contract.

Order of the NCLT

The appeal against refusal to register the transfer of shares was dismissed by NCLT.

VA View :

The primary object of allowing free transferability of shares in a public company is to ensure that the interest of investors is not hampered by refusal on part of the company to register the transfer without assigning any sufficient reason and to ensure that the shareholders are able to monetize their shares freely. However, a consensual arrangement between two or more shareholders to incorporate a pre-emption clause in respect of transfer of shares does not impede the legal mandate of free transferability of shares. Such an agreement, by its very terms, binds only the contracting parties and does not in any way impose the restriction on all the shareholders of the company to sell its shares only to other existing members.

The proviso to Section 58(2) of the Companies Act expressly recognizes the validity of such private arrangements between two or more shareholders of a public company. By this order, NCLT, Mumbai re-affirms the same and clarifies that requirement of prior consent of the non-exiting party for transfer of shares by exiting party does not infract the proviso to Section 58(2) of the Companies Act and is not in conflict with the definition of a public company. It cannot amount to changing the character of a public company to a private company. If the case be so, it would render the said proviso a nullity.

II. NCLAT: To prevent detriment to the liquidation process and other secured creditors, company not having a minimum of 60% value in the security interest could not be allowed to realize security interest under the provisions of SARFAESI Act, 2002

The present appeal arose from order dated November 20, 2019 (**"Impugned Order"**) passed by the National Company Law Tribunal, Chennai (**"NCLT"**). By way of the Impugned Order, the NCLT had dismissed the liquidator's application seeking permission to enable the sale of assets of 'Surana Power Limited' (**"SPL"**) on the basis of consent given by majority of the secured creditors. The National Company Law Appellate Tribunal (**"NCLAT"**) by its judgment *(decided on June 18, 2020)* set aside the Impugned Order passed by the NCLT.

Facts

The NCLT had passed an order on January 20, 2019 initiating Corporate Insolvency Resolution Process (**"CIRP"**) against SPL under Section 9 *(application for initiation of corporate insolvency resolution process by operational creditor)* of the Insolvency and Bankruptcy Code, 2016 (**"IBC"**). However, when no resolution came to be approved, SPL was ordered to be liquidated and Mr. Srikanth Dwarakanath (**"Appellant Liquidator"**) was appointed as the liquidator.

Before the CIRP had been initiated, Bharat Heavy Electricals Limited (**"Respondent Company"**) had secured an ex-parte award on January 24, 2018 (**"Arbitral Award"**) against SPL in an arbitration proceeding. Basis the Arbitral Award: (i) lien was created on the equipment and goods lying at the site of SPL (**"Secured Assets"**); (ii) a charge was created over entirely or partially erected facilities at SPL's site; (iii) the Secured Assets on which a lien had now been created in favour of the Respondent Company owing to the Arbitral Award, had already been hypothecated to all other secured creditors by a deed of hypothecation dated September 24, 2010 (**"Hypothecation Deed"**).

The Appellant Liquidator had not been able to commence liquidation process earlier as some of the secured creditors had not intimated their decision concerning relinquishment of securities, well in time. The Respondent Company was one of the last remaining secured creditors required to intimate its decision on relinquishment. However, by letter dated August 23, 2019, the Respondent Company expressed unwillingness to relinquish its security interest. In fact, all other secured creditors had relinquished their security interest into the liquidation estate of SPL.

The Appellant Liquidator, however, was not able to proceed with any sale of asset without the receipt of relinquishment of security interest from all the secured creditors. Therefore, the Appellant Liquidator approached the NCLT seeking permission to sell all assets of SPL. The Appellant Liquidator's application came to be rejected by way of the Impugned Order. Thereafter, this appeal was filed before NCLAT to challenge the Impugned Order.

Issue

Whether all the assets of SPL could be sold owing to non-relinquishment of security interest by the Respondent Company, when other secured creditors having value of 73.76% had already relinquished their security interest.

Arguments

Contentions of the Appellant Liquidator:

The NCLT had not appreciated that ten out of eleven secured creditors, representing 73.76% (in value of the admitted claims) of the total secured assets had already relinquished their security interest into the liquidation estate of SPL. It was only because of the Respondent Company's unwillingness to relinquish its security interest that the Appellant Liquidator had been unable to proceed with the sale of assets.

Further, the secured creditors other than the Respondent Company had a prior charge over the Secured Assets by way of the Hypothecation Deed. Notably, the Hypothecation Deed was executed in the year 2010, much before the Arbitral Award which was passed in the year 2018.

The NCLT had also failed to consider that IBC did not provide for different categories of secured creditors either based on the nature of charge/ security interest or on the basis of the rankings of the respective charge. The Appellant Liquidator was to attempt the sale of SPL assets on a slump sale basis, however owing to the Respondent Company's unwillingness to relinquish its security interest, the Appellant Liquidator was unable to conduct the sale as aforesaid. The Respondent Company's refusal, had created a 'deadlock situation' wherein SPL assets could not be sold due to the proviso to Regulation 32 *(sale of assets, etc.)* of the Insolvency and Bankruptcy Board of India (Liquidation Process), Regulations, 2016 (**"Liquidation Process Regulations"**). As per the proviso, an asset which is subject to security interest is not to be sold unless the security interest therein has been relinquished to the liquidation estate. The view taken by the NCLT violated the 'waterfall mechanism' provided under Section 53 *(distribution of assets)* of IBC.

Furthermore, during the pendency of this present appeal, the Respondent Company had written a letter dated January 27, 2020 to the Appellant Liquidator, inter alia, notifying its intention to realize security interest in respect of the Secured Assets.

Contentions of the Respondent Company:

It was contended that the Respondent Company had exercised its rights as per Section 52 *(secured creditor in liquidation proceedings)* of IBC. The exercise of the Respondent Company's rights under Section 52 of IBC could not be subjected to the majority of the security creditors who had relinquished their security interest. As under Section 52(1)(b) of IBC, the Respondent Company had chosen to realize its security interest as per section 52(iv) of IBC.

As per section 52(iv) of IBC, a secured creditor may enforce, realise, settle, compromise or deal with the secured assets in accordance with such law as applicable to the security interest being realised and to the secured creditor and apply the proceeds to recover the debts due to it. The right of the Respondent Company under Section 52 of IBC is unqualified and unbridled. Such right could not be subjected to the majority of other secured creditors having relinquished their security interests.

Further, SPL had never acquired unencumbered right, title or interest in the Secured Assets. Therefore, hypothecation of the Secured Assets would always be subject to the Respondent Company's lien. The Respondent Company also cited the decision of the NCLAT in ***JM Financial Asset Reconstruction Company Limited v. Finquest Financial Solutions Private Limited and Others [2019 SCC OnLine NCLAT 918].***

Observations of the NCLAT

The NCLT had rejected the application filed by the Appellant Liquidator primarily because the Respondent Company was a secured creditor, and could proceed under Section 52 of IBC to realize its security interest. The Appellant Liquidator could not cause the sale of asset filed under Section 52 of IBC in the manner specified under Section 53 (distribution of assets) of IBC unless the security interest was relinquished by the Respondent Company. All secured creditors representing value of 73.76% in the secured assets had relinquished their security interest in the liquidation estate of SPL. This would have enabled the Appellant Liquidator to proceed under Regulation 32 of the Liquidation Process Regulations and dispose all SPL assets.

However, in light of the proviso to Regulation 32 of the Liquidation Process Regulations and on account of the Respondent Company's unwillingness to relinquish its security interest, the Appellant Liquidator could not sell SPL assets.

The NCLT had held that the Respondent Company's lien had a preference over the hypothecation created in favour of other secured creditors. The NCLAT noted that the NCLT had failed to appreciate that all secured creditors were on the same footing, irrespective of the mode of creation of charge. The Respondent Company, was a secured operational creditor by the Arbitral Award, by way of which, the Respondent Company was claiming lien over the Secured Assets. While, all other secured creditors, that is, (financial creditors) had relinquished their security interest, the Respondent Company's refusal had created a deadlock situation.

Clearly, as per the proviso to Regulation 32 of the Liquidation Process Regulations, the Appellant Liquidator could not proceed to sell all SPL assets. This was despite the fact that more than 73% of the secured creditors had already relinquished their security interests.

Decision of the NCLAT

The Respondent Company is a secured creditor at par with ten other remaining secured creditors. The enforcement of security interest is governed under Section 13 *(enforcement of security interest)* of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (**"SARFAESI Act"**). Further, as per Section 13(9) of the SARFAESI Act, any steps about the realization of assets by the secured creditors required confirmation from creditors having at least 60% of the value of total debt.

It would be prejudicial to stall the liquidation process because of a single creditor having value of only 26.24% in the secured assets when other secured creditors having value of 73.76% had already relinquished their security interest into the liquidation estate of SPL. The Respondent Company did not hold a superior charge from the rest of the secured creditors.

Further, Section 13 of the SARFAESI Act would be applicable in this case, in order to end the deadlock, and the decision of majority secured creditors would be made binding on the dissenting Respondent Company. Moreover, the facts of the case in ***JM Financial Asset Reconstruction Company Limited v. Finquest Financial Solutions Private Limited and Others [2019 SCC OnLine NCLAT 918]*** were different from the instant case. This is because in the aforesaid case, NCLAT was dealing with the issue whether more than one secured creditor could enforce security interest simultaneously under Section 52 of IBC. In the instant case, the question was if the Respondent Company had a right to realize its security interest as per section 52 of IBC.

In the instant case, the Appellant Liquidator had already concluded that the Respondent Company's lien on the Secured Assets was not exclusive. Further, since the Respondent Company did not have at least 60% value in the total security interest, the Respondent Company could not exercise right to realize its security interest. If the Respondent Company was to be allowed to do so, it would be detrimental to the process of liquidation and interest of ten other remaining secured creditors. The Impugned Order was set aside and the Appellant Liquidator was directed to complete the process of liquidation.

VA View:

This is a progressive view taken by the NCLAT in protecting the interests of the majority of the secured creditors. The liquidation process should not have been affected given the facts and circumstances of this case.

In the instant case, ten out of eleven creditors holding more than 73% of the total debt had already consented to relinquishing their security interests. As far as the Respondent Company was concerned, there were two main reasons that were working in opposition to its submissions. First and foremost, it did not have 60% of the value in the secured interest and secondly, as far as the Secured Assets were concerned, it neither had an exclusive charge, nor a superior charge from the rest of the secured creditors.

If the sale of SPL assets would have been stalled merely because the Respondent Company without having the requisite value of at least 60% debt was unwilling to relinquish its interest, it would have been very detrimental to the liquidation process and would have affected the remaining ten other creditors.

In view of the provisions of IBC, a secured creditor's claim could be allowed only if they had met the minimum threshold of 60% of the debt. Accepting the Respondent Company's claim, therefore, would have affected the entire liquidation process and set a bad judicial precedent.

III. NCLT, Mumbai: Reference to arbitration in an insolvency petition under Insolvency and Bankruptcy Code, 2016

The National Company Law Tribunal, Mumbai (**"MNCLT"**) has, by an Order dated June 9, 2020 (**"Order"**), allowed an application under Section 8 *(power to refer parties to arbitration where there is an arbitration agreement)* of the Arbitration and Conciliation Act, 1996 (**"ACA"**) thereby referring a matter pending before it to arbitration. The said Section 8 application was filed by Indus Biotech Private Limited (**"Corporate Debtor"**) for settlement of a dispute between the Corporate Debtor and Kotak India Venture Fund-I (**"Financial Creditor"**). Upon allowing the Section 8 application, the MNCLT dismissed the company petition that had been filed before it by the Financial Creditor, under Section 7 of the Insolvency and Bankruptcy Code, 2016 (**"IBC"**) towards seeking the initiation of Corporate Insolvency Resolution Process (**"CIRP"**) against the Corporate Debtor.

Facts

Brief facts of the case are that in the years 2007-2008, four entities of the Kotak Private Equity Group namely, (i) Kotak India Venture Fund-I (Financial Creditor), (ii) Kotak India Venture (Offshore) Fund, (iii) Kotak Mahindra Investments Limited and, (iv) Kotak Employees Investment Trust - (collectively referred to as the **"Kotak Group"**), subscribed to the share capital of the Corporate Debtor under four separate share subscription and shareholders agreements. In all, the Kotak Group invested INR 27,00,00,000 towards subscribing to equity shares and Optionally Convertible Redeemable Preference Shares (**"OCRPS"**) of the Corporate Debtor.

Thereafter, the Financial Creditor sought to have the Corporate Debtor make a Qualified Initial Public Offering (**"QIPO"**) of its securities and opted to convert the OCRPS held by it into equity shares, in view of Regulation 5(2) of the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2018, which mandates that any company which has any outstanding convertible securities or any other right which would entitle any person with any option to receive equity shares of the issuer, is not entitled to make a QIPO.

During the QIPO process, a dispute arose between the Corporate Debtor and the Financial Creditor and the other entities of the Kotak Group with regard to the conversion formula to be applied while converting the OCRPS held by them into equity shares of the Corporate Debtor. While the Kotak Group sought to apply a calculation formula upon application of which they would collectively hold approximately 30% of the total paid-up share capital of the Corporate Debtor, the Corporate Debtor wanted to apply a formula under which the Kotak Group would hold about 10% of the total paid-up share capital of the Corporate Debtor.

In terms of the 2007 Share Subscription and Shareholders Agreement (**"SSSA"**), the OCRPS issued thereunder were to be redeemed by the Corporate Debtor on or before April 15, 2019. Upon conversion of the OCRPS and the consequent QIPO being stalled due to the dispute between the parties and failure of the Corporate Debtor to redeem the said OCRPS within the aforementioned date, the Financial Creditor filed a company petition under Section 7 of the IBC on August 16, 2019, seeking the initiation of CIRP against the Corporate Debtor. Thereafter, by a letter dated September 20, 2019, the Corporate Debtor sought to refer the dispute between the parties to arbitration under the provisions of the arbitration clause of the 2007 SSSA. Consequently, the Corporate Debtor filed an Interlocutory Application (**"IA"**) before the MNCLT under Section 8 of the ACA.

Issue

Whether the provisions of the ACA would prevail over the provisions of the IBC? If so, under what circumstances?

Arguments

Contentions raised by the Corporate Debtor:

The Corporate Debtor, *inter alia,* contended that a reading of the arbitration clause of the 2007 SSSA showed that the parties had bound themselves to settle any dispute, controversy or claim arising out of, relating to or in connection with the 2007 SSSA, to be finally settled by arbitration.

It was further contended that in essence, the dispute between the parties are in relation to: (i) valuation of the Financial Creditor's OCRPS; (ii) right of the Financial Creditor to redeem such OCRPS when it had participated in the process to convert its OCRPS into equity shares of the Corporate Debtor; and (iii) fixing of the QIPO date, all of which together constitute more than one *bona fide* and substantial dispute between the parties under the 2007 SSSA since August 2018.

It was further submitted that the Corporate Debtor was a highly profitable and debt-free company. It was contended that the Financial Creditor had itself benefitted by receiving dividends from the Corporate Debtor in excess of INR 13 crores on an investment of approximately INR 19 crores. Hence, the Corporate Debtor was clearly not in need of resolution.

The Corporate Debtor also submitted that the underlying company petition is in the nature of a 'dressed-up' petition, inasmuch as the real dispute between the parties is with regard to matters pertaining to the agreement reached between the parties and interpretation of its various clauses and therefore, the provisions of the IBC ought not to be used as a pressure tactic to extort money from profitable companies.

The Corporate Debtor also highlighted that Section 8 of the ACA, which provides power to a judicial authority before which an action is brought to refer parties to arbitration, is mandatory in nature.

Contentions raised by the Financial Creditor:

The Financial Creditor, on the other hand, submitted that the only issue to be decided in the present matter is whether the reliefs claimed are capable of being referred to arbitration or being granted by an arbitral tribunal. If the answer is no, then the present IA should be dismissed, and the underlying company petition should be heard on merits.

The Financial Creditor further contended that a Section 7 petition under the IBC (being an insolvency petition) belongs to that class of litigation which is incapable of being referred to arbitration on account of being a cause/ dispute *in rem*. The Financial Creditor submitted that initiation of CIRP cannot be granted by an arbitrator. The Financial Creditor also submitted that a Section 7 petition under the IBC is not for recovery of debts and that the IBC is a code for dealing with insolvency, either for revival or for liquidation. Only upon there being a debt and default based on a claim, should the NCLT decide to admit the petition.

It was contended that the existence of an arbitration clause can never affect a Section 7 petition under the IBC. The Financial Creditor referred to certain judgments in which the *ratio decidendi* was that while deciding the scope of a Section 8 petition under the ACA, only such disputes or matters which an arbitrator is competent or empowered to decide, can be referred to arbitration.

It was further argued that, in a Section 7 petition under the IBC, the claim itself may be disputed. It was also contended that the notice for redemption was given on March 31, 2019, at which point of time, there was no reference to arbitration. The Financial Creditor submitted that the first reference to arbitration was made only on September 20, 2019, which was after the filing of the petition under Section 7 of IBC on August 16, 2019. Therefore, the present IA was only an attempt by the Corporate Debtor to wriggle out of the CIRP. It was contended that this was a diversionary tactic to prevent the main company petition from being argued. The Financial Creditor also submitted that as per the 2007 SSSA if the QIPO did not take place by the assigned date, the investment would be redeemable. If unredeemed, it was to be treated as a 'debt'.

Observations of the National Company Law Tribunal, Mumbai

The MNCLT observed that seeking a reference to arbitration in a petition filed under Section 7 of the IBC was something that was *res integra.* The MNCLT relied on the judgment of ***Booz Allen and Hamilton v. SBI Home Finance Limited [(2011) 5 SCC 532]*** where it was held by the Supreme Court that "*generally and traditionally, all disputes relating to rights in personam are considered to be amenable to arbitration; and all disputes relating to rights in rem are required to be adjudicated by courts and public tribunals, being unsuited for private arbitration. This is not however a rigid or inflexible rule. Disputes relating to subordinate rights in personam arising from rights in rem have always been considered to be arbitrable.*"

The MNCLT further noted that it was a settled law that *generalia specialibus non derogant* – special law prevails over general law - and the Supreme Court in the case of ***Consolidated Engineering Enterprises v. Principal Secretary, Irrigation Department and Others [(2008) 7 SCC 169]*** had held that the ACA is a special law, consolidating and amending the law relating to arbitration and matters connected therewith or incidental thereto. Reiterating the Supreme Court's view in the judgement of ***Hindustan Petroleum Corporation Limited v. Pinkcity Midway Petroleums [(2003) 6 SCC 503],*** the MNCLT was of the view that where an arbitration clause exists, the court has a mandatory duty to refer any dispute arising between the contracting parties to arbitration.

With respect to Section 7 of the IBC, the MNCLT referred to ***Innoventive Industries Limited v. ICICI Bank, [(2017) SCC OnLine NCLAT 70]*** where the National Company Law Appellate Tribunal held that sub-section (5) of Section 7 of the IBC provides for admission or rejection of application of a financial creditor where the adjudicating authority is satisfied that the documents are complete or incomplete. In other words, the statute mandates the adjudicating authority to ascertain and record satisfaction as to the occurrence of default before admitting the petition. Mere claim by the financial creditor that the default has occurred is not sufficient. Therefore, in a Section 7 petition under the IBC, there has to be a judicial determination by the adjudicating authority as to whether there has been a 'default' within the meaning of Section 3(12) of the IBC.

Decision of the National Company Law Tribunal, Mumbai

In allowing the application, the MNCLT held that the facts of the case did not seem to convey satisfactorily that a default had occurred. Unnecessarily pushing an otherwise solvent, debt-free company into insolvency, was not a very desirable result at that stage. The disputes that formed the subject matter of the underlying company petition were all arbitrable since they involved valuation of the shares and fixing of the QIPO date. Therefore, an attempt should be made to reconcile the differences between the parties and their respective perceptions.

Accordingly, the application under Section 8 of the ACA filed by Corporate Debtor was allowed and the company petition under Section 7 of the IBC filed by the Financial Creditor was dismissed.

VA View:

While the MNCLT has in the present case allowed the application for arbitration under Section 8 of the ACA, the judgment clearly demonstrates that the decision was made purely on the basis of the facts and circumstances peculiar to the present case. In passing the said Order, the MNCLT has not gone by the general principle laid down by the Supreme Court in its decision in the case of ***Booz Allen and Hamilton v. SBI Home Finance Limited, [(2011) 5 SCC 532]*** wherein it was held that matters concerning insolvency are non-arbitrable and beyond the jurisdiction of an arbitrator.

In this context, it would be pertinent to note that in the case of ***Shalby v. Dr. Pranav Shah [2018 SCC OnLine NCLT 137],*** the National Company Law Tribunal, Ahmedabad (**"NCLT Ahmedabad"**) was faced with a similar application for reference to arbitration in an insolvency petition pending before it wherein, the tribunal proceeded to dismiss the said application and also imposed costs upon the applicant. While dismissing the said application, the NCLT Ahmedabad held that irrespective of an arbitration clause in the agreement between the parties, the arbitrator does not have jurisdiction over the subject matter of an insolvency petition.

The orders passed by the MNCLT, Supreme Court and the NCLT Ahmedabad in the abovementioned matters is based on the facts applicable to each case. However, the MNCLT's decision in the present matter should, to a certain extent, deter the initiation of CIRP against healthy, debt-free companies purely as a pressure tactic before an already burdened judiciary.

IV. NCLAT: Contract termination notice issued to the Corporate Debtor post initiation of CIRP stayed

The National Company Law Appellate Tribunal (**"NCLAT"**), in the case of ***Tata Consultancy Services Limited v. Vishal Ghisulal Jain*** *(decided on June 24, 2020)* has decided that a contract termination notice issued by Tata Consultancy Services Limited (**"Appellant"**) to S.K Wheels Private Limited (**"Corporate Debtor"**), a company undergoing Corporate Insolvency Resolution Process (**"CIRP"**) under the Insolvency and Bankruptcy Code, 2016 (**"IBC"**) should be stayed.

Facts

The Appellant and the Corporate Debtor entered into an agreement on December 01, 2016 (**"Facilities Agreement"**) to avail services from the Corporate Debtor to enable conduct of examinations deploying National Technology Infrastructure for the Appellant's clients. By order dated March 29, 2019, the National Company Law Tribunal, Mumbai (**"NCLT"**) initiated CIRP proceedings against the Corporate Debtor.

Subsequently, since the Corporate Debtor failed to remedy alleged breaches to the Facilities Agreement, the Appellant terminated the same by termination notice dated June 10, 2019. Pursuant to the same, the Corporate Debtor filed proceedings before the NCLT seeking, *inter alia,* stay of the termination notice issued by the Appellant.

The NCLT by an order dated December 18, 2019 granted an interim stay of the termination notice issued by the Appellant, in order to enable the Corporate Debtor to remain a going concern.

The Appellant was aggrieved by the same on the grounds that the NCLT failed to appreciate the arbitration agreement contained in Clause 12(d) of the Facilities Agreement, and failed to appreciate that a valid notice of termination was issued by the Appellant, which were, in the Appellant's view not in contravention to Section 14 of the IBC.

Issue

Whether the termination of the Facilities Agreement is valid pursuant to Section 14 of the IBC.

Arguments

The Appellant stated that the NCLT had failed to appreciate that a valid notice of termination was issued by the Appellant and that the notice of termination was not in contravention of Section 14 of the IBC.

The Corporate Debtor stated that as per the Facilities Agreement, the Corporate Debtor was under the obligation to, *inter alia,* fit the premises with the materials as per specification mentioned in the agreement and provide certain facilities. Previously, when there was a situation pertaining to non-compliance with the terms of the Facilities Agreement, the parties had discussed the same and mutually resolved the same.

Further, it was stated that all the deficiencies were cured at the cost of the Corporate Debtor. Furthermore, meetings were held in April and May, 2019, whereby, the Interim Resolution Professional intimated the Appellant that no prejudice would be caused to the Appellant and all the services and facilities would be provided as contained in the Facilities Agreement. The learned counsel for the Corporate Debtor further submitted that the Appellant issued termination notice as per the Clause 11(b) of the Facilities Agreement, however, the same was not in accordance with the said clause. As per the abovementioned Clause 11(b), a 30 days' notice needs to be given in the event of any material breach by either party. However, no notice was received in this case by the Corporate Debtor.

The Appellant stated that the Appellant noticed the material breaches of obligations by the Corporate Debtor including deployment of personal lacking requisite level of scale, non-adherence of design guidelines, non-replacement of furniture and air conditioners, etc., pursuant to which multiple notices were issued, however, the Corporate Debtor failed to remedy the contractual breaches which led to the serving of a termination notice. To this, it was stated by the Corporate Debtor they have cured all the deficiencies and the termination notice after the initiation of CIRP is against the main object of the IBC.

Observations of the NCLAT

The NCLAT observed that per the termination clause, it is mandatory to issue notice to the party in the event of a material breach and if the same is not cured, the aggrieved party was liable to terminate the agreement. It was observed that in view of Section 14 of the IBC, once a moratorium was imposed by the adjudicating authority and on appointment of Interim Resolution Professional, the Interim Resolution Professional will be at the helm of affairs of the company in view of the suspension of the board of directors of the Corporate Debtor.

Further, the IBC sets out the duty of Resolution Professional to preserve and protect the assets of the Corporate Debtor and lays down the functions he may perform in order to ensure the same.

It was observed that as per the IBC, post the initiation of the CIRP, the Corporate Debtor shall function and continue its business activities. It is the duty of the Interim Resolution Professional/ Resolution Professional, as the case may be, to keep the Corporate Debtor as a going concern.

Decision of the NCLAT

The appeal was disposed, and it was held that the NCLT rightly stayed the termination of notice and there is no illegality in the order passed by the NCLT.

VA View:

This judgement can have interesting and wide ramifications. Curiously, the NCLAT has not expanded or provided any reasoning for why and how the provisions of Section 14 are applicable in such cases. A purposive approach has been taken by the NCLAT by stating that the main aim of the IBC is to encourage sale of a corporate debtor on a going concern basis and not liquidation.

The NCLAT reasoned that in order to keep the corporate debtor viable, the termination of the contract should be stayed for the time being. The absence of any specific reasoning as to how the IBC empowers the NCLT/ NCLAT, as the case may be, to interfere in commercial agreements may result in the order being challenged on substantive grounds.

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