

October, 2022

NEW DELHI | MUMBAI | BENGALURU

## Key Highlights

- I. Supreme Court: The actual gain or loss is immaterial, but the motive for making a gain is essential.**
- II. Supreme Court: CIRP can be initiated against Corporate Debtor without proceeding against Principal Borrower.**
- III. Supreme Court: Discretion of the Arbitral Tribunal to grant post-award interest on part of the aggregate sum due.**
- IV. NCLAT: Erstwhile resolution professional has no right to be heard before being replaced under Section 27 of the Insolvency and Bankruptcy Code.**

### **I. Supreme Court: The actual gain or loss is immaterial, but the motive for making a gain is essential.**

The Supreme Court ("SC") has, in its judgment dated September 19, 2022, in the case of **Securities and Exchange Board of India v. Abhijit Rajan [Civil Appeal No. 563 of 2020]**, held that in deciding cases pertaining to insider trading, the actual gain or loss is immaterial, but the motive for making a gain is essential.

#### **Facts**

Abhijit Rajan ("**Respondent**") was the chairman and managing director of Gammon Infrastructure Projects Limited ("**GIPL**") till September 20, 2013. Thereafter, he ceased to be the chairman and managing director, but continued to be a director of GIPL.

In the year 2012, GIPL was awarded a contract by National Highways Authority of India ("**NHAI**"). For the execution of the project, GIPL set up a special purpose vehicle called Vijayawada Gundugolanu Road Project Private Limited ("**VGRPPL**").

Similarly, Simplex Infrastructure Limited ("**SIL**") was awarded a contract by NHAI in Jharkhand and West Bengal. For the execution of the project, SIL set up a special purpose vehicle called Maa Durga Expressways Private Limited ("**MDEPL**").

GIPL entered into two shareholders agreements with SIL. Under these agreements, GIPL was to invest in MDEPL and SIL was to invest in VGRPPL for their respective projects. The mutual investments were to be tuned in such a manner that GIPL and SIL would hold 49% equity interest in each other's projects.

However, on August 9, 2013 the board of directors of GIPL passed a resolution authorizing the termination of both shareholders agreements. On August 22, 2013, the Respondent sold about 144 lakhs shares (approx.) held by him in GIPL. On August 30, 2013, GIPL made a disclosure to the National Stock Exchange of India ("**NSE**") and Bombay Stock Exchange ("**BSE**") regarding the termination of two shareholders agreements.

Pursuant to an input received from NSE, about the aforesaid transaction and the possibility of the trading having taken place on the basis of unpublished price sensitive information ("**UPSI**"), Securities and Exchange Board of India ("**SEBI**") conducted a preliminary enquiry. After completion of the preliminary enquiry, SEBI passed an *ex parte* interim order holding prima facie that the Respondent violated the provisions of The Securities and Exchange Board of India Act, 1992 ("**SEBI Act**") and consequently restraining the Respondent from buying, selling or dealing in securities and accessing the security markets directly or indirectly. This *ex parte* interim order was also confirmed by a confirmatory order, passed after providing an opportunity of hearing to the Respondent.

In the interregnum, SEBI completed the investigation and issued certain directions on March 21, 2016, followed by a show cause notice dated March 29, 2016. The show cause notice was addressed not only to the Respondent, but also to another company 'Consolidated Infrastructure Company Private Limited' ("**CICPL**") and two of its directors. The noticees filed their replies and after giving an opportunity of hearing to the noticees, the Whole-Time Member ("**WTM**") passed an order, by which the WTM held the Respondent guilty of insider trading and hence liable to disgorge the amount of unlawful gains made by him. The show cause notices issued to the others, namely, CICPL and its directors were closed without any directions, on the ground that no case was made out against them.

Challenging the said order of the WTM, the Respondent filed a statutory appeal before the Securities Appellate Tribunal ("**Tribunal**"). The appeal was allowed by the Tribunal by an order and it is against the said order that SEBI has come up with the above appeal in the SC.

## Issues

- i. Whether the information regarding the decision of the board of directors of GIPL to terminate the two shareholders' agreements can be characterized as 'price sensitive information' within the meaning of Section 2(ha) of the Securities and Exchange Board of India (Prohibition of Insider Trading) Regulations, 1992 ("**PIT Regulations**").
- ii. Whether the sale by the Respondent of the equity shares held by him in GIPL, under peculiar and compelling circumstances in which he was placed, would fall within the mischief of 'insider trading' in terms of Regulation 3(i) read with Regulation 4 of the PIT Regulations.
- iii. Whether SEBI should have taken into account the last trade price of the day on which information was disclosed instead of the trade price of the next day.

## Arguments

### Contentions by SEBI:

SEBI contended that proportionality is a dangerous and subjective ground in matters involving insider trading, especially since one-third of the total number of directors of a listed company are independent directors and even transactions involving thousands of crores might be a minor proportion to the turnover, if the company is very large in size. SEBI also contended that Regulations 3 and 4 of the PIT Regulations contain an absolute prohibition against insider trading and such a statutory prohibition cannot be diluted by arguing that the total value of the contracts terminated by the company was just a minor percentage of the order book value and the total turnover of the company. The *de minimis* syndicate has no application to insider trading, as it introduces an element of subjectivity.

Further, in any case the total value of the contracts terminated on both sides was nearly INR 2,600 crores and hence the information relating to the termination of the contracts was definitely likely to materially affect the price of the securities of the company under Regulation 2(ha).

It was also stated by SEBI that explanation (vi) under Section 2(ha) which speaks about "significant changes in policies, plans or operations of the company" cannot limit the scope of the main part of the definition and in this case as a matter of fact the price of the share dropped in just one day and the Respondent avoided a loss of INR 85 lakhs. SEBI argued that bona fide intentions or grounds of necessity, such as those pleaded in this case, cannot frustrate the object of strict ban on insider trading, especially when the expression "lawful excuse" as used in about 88 central statutes to justify non-compliance, is conspicuously absent in the PIT Regulations. Also, that in any case, SEBI took note of the situation in which the Respondent was placed, warranting the necessity to sell the shares and hence confined the final order only to disgorgement, which is merely in the nature of restitutionary relief.

Further, the intimation regarding the termination of the contracts was given to the BSE at 1.05 p.m. and to NSE at 2.40 p.m. on September 3, 2013 and the trading concluded at 3:30 p.m. and hence the adoption of the closing price on September 3, 2013 would not correctly determine either the gains made or the losses averted. Therefore, the question of SEBI taking the closing price as on September 3, 2013 did not arise.

### Contentions by the Respondent:

The Respondent contended that the primary object of insider trading regulations anywhere in the world is to prohibit an insider from taking advantage of asymmetrical access to UPSI over others who do not have such access and that the question whether an information is price sensitive or not, would depend upon its potency to materially impact, upon publication, the price of the securities.

The Respondent also contended that by its very nature, the issue is barely a question of fact or at the most, a mixed question of fact and law which will not fall within the scope of Section 15Z (*Appeal to Supreme Court*) of SEBI Act warranting interference by this Court.

Further, one of the key factors which the courts take into account while interpreting the circumstances revolving around transactions such as the one in question, is the purpose for which the transaction was effected. Apart from looking into the purpose of the transaction, courts have also taken into account other circumstances such as the scale of the transaction, pattern of trading and honesty in responses during the proceedings.

In the case on hand, the information in question, namely, the termination of the shareholders' agreements actually resulted in GIPL gaining total control of a larger project and that in other words what was lost by the termination was far lesser

than what was gained and hence the information relating to the termination of the agreements was actually a favourable and not adverse information.

The Respondent noted that GIPL's investments in the project of SIL represented 0.05% of GIPL's order book and 0.7% of its turnover and that a project with a small percentage of the order book and a miniscule percentage of the turnover cannot ipso facto become material for information about it to become UPSI.

The Respondent contended that the failure of the Respondent to meet the obligation towards Corporate Debt Restructuring ("CDR") package would have led to GIL filing for bankruptcy. Further, every penny of the sale proceeds of the shares, was transferred by the Respondent towards the implementation of CDR package, a fact that SEBI itself has accepted. Hence, it is a misconception to think that he made unlawful gains that ought to be disgorged.

Furthermore, SEBI itself exonerated the co-noticee, namely, CICPL, on the ground that its sale of shares was on account of a pressing need to meet a margin shortfall to its stock broker. Thus, SEBI applied two different yardsticks, one in respect of the Respondent and another in respect of the co-noticee in the very same proceeding, which necessitated interference by the Tribunal.

### **Observations of the Supreme Court**

The SC noted that an appeal under Section 15Z (*Appeal to Supreme Court*) of SEBI Act concerns appeals with 'any question of law arising out of the order of the Tribunal'. The focus of Section 15Z is on 'any question of law' and not 'any substantial question of law'.

The SC observed that in order to find out if a person is guilty of violation of Regulation 3 of the PIT Regulations, the courts should address the following questions namely: (i) is he an insider?; (ii) did he possess or have access to any information relating to the company?; (iii) whether such information was price sensitive?; (iv) whether the information was unpublished?; and (v) whether he dealt in securities by subscribing, buying, selling or agreeing to do any of these things in any securities.

The SC noted that one important fact namely, that the price sensitivity of an information has a correlation directly to the materiality of the impact that it can have on the price of the securities of the company. An information may materially affect the price of the security of a company either positively or negatively. The effect should be material and not completely insignificant.

Keeping the above parameters in mind and coming to the facts of the case on hand, it was clear, (i) that the Respondent was certainly an insider, as he was a chairman and managing director of GIPL till September 20, 2013 and was a party to the resolution of the board of directors authorising the termination of the shareholders' agreements; (ii) that the information relating to the termination of both the shareholders' agreements that the Respondent had, would certainly fall under the category of "significant changes in policies, plans or operations of the Company" under Regulation 2(ha)(vii) of the PIT Regulations; (iii) that the Respondent dealt in securities by selling 144 lakhs shares, a month before his resignation as chairman and managing director; and (iv) that the termination of the shareholders' agreements was disclosed to the NSE and BSE after the sale of the shares, which made the information relating to the termination of the agreements unpublished as on the date of the sale.

Therefore, it may appear at first blush, that the Respondent, who was an insider and who possessed information which was both unpublished and price sensitive, was guilty of the charge of insider trading as he undoubtedly dealt in securities.

While it is true that the actual gaining of profit or sufferance of loss in the transaction, may not provide an escape route for an insider against the charge of violation of Regulation 3 of the PIT Regulations, one cannot ignore normal human conduct. If a person enters into a transaction which is surely likely to result in loss, he cannot be accused of insider trading. In other words, the actual gain or loss is immaterial, but the motive for making a gain is essential.

The cancellation of the shareholders' agreements resulted in GIPL gaining very hugely in terms of order book value. In such circumstances an ordinary man of prudence would expect an increase in the value of the shares of GIPL and would wait for the market trend to show itself up, if he actually desired to indulge in insider trading. However, the Respondent did not wait for the information about the market trend, after the information became public because he had to dispose of his shares as well as certain other properties for the purpose of honouring a CDR package.

Therefore, the Tribunal was right in thinking that the Respondent had no motive or intention to make undeserved gains by encashing on the UPSI that he possessed. As a matter of fact, the Tribunal found that the closing price of shares rose, after the disclosure of the information. This shows that the UPSI was such that it was likely to be more beneficial to the

shareholders, after the disclosure was made. Any person desirous of indulging in insider trading, would have waited till the information went public, to sell his holdings. The Respondent did not do this, obviously on account of a pressing necessity.

The SC observed that the allegation of insider trading cannot be measured in terms of the value of the contracts terminated and the percentage of shares sold and that the theory of proportionality cannot be applied in such cases. The magnitude of what an insider did, in relation to the size of the company, may not have a bearing upon the question whether someone indulged in insider trading or not, but what is sought to be encashed by the insider should be an information which if published is likely to materially affect the price of the securities of the company. It is true that the *de minimis* rule has no application to insider trading, as it introduces an element of subjectivity. Hence, the SC did not go on the basis that GIPL's investments in the project of SIL represented 0.05% of GIPL's order book value and 0.7% of its turnover.

The SC had gone on the basis that the termination of both the agreements put GIPL in a more advantageous position, in which one would have expected the price of the securities to rise. The normal human conduct would be to wait for this event to happen. This event could have happened only after the publication of the information in question. The fact that the Respondent did not wait to take advantage of the situation, convinced the SC that the Respondent's intention was not to indulge in insider trading.

The contention that SEBI took note of the situation in which the Respondent was placed, and the dire need that he had to sell the shares, and that therefore SEBI confined the final order only to disgorgement, is neither here nor there. The argument is actually an argument of convenience. It so happened that according to SEBI the closing price of the stock on September 3, 2013 showed favourable position for the Respondent and SEBI was able to calculate as though the Respondent made a profit.

### Decision of the Supreme Court

The SC, on issue no. 1, held that the information regarding the termination of the two shareholders' agreements can be characterized as price sensitive information, in that it was likely to place the existing shareholders in an advantageous position, once the information came into the public domain. In such circumstances, on issue no. 2, the SC held that the sale by the Respondent would not fall within the mischief of insider trading, as it was somewhat similar to a distress sale, made before the information could have a positive impact on the price of the shares.

Accordingly, there was no necessity to go into issue no. 3 and that the impugned order of the Tribunal did not call for any interference. Hence, the appeal was dismissed.

#### VA View:

The present appeal clearly demonstrates the complexity in adjudicating insider trading cases. Distinguishing between mens rea and profit motive, the SC held that, in respect of matters under the PIT Regulations, the test that is to be applied is of profit motive, that is, whether the insider's actions were an attempt to gain from the UPSI in his possession. In other words, mere possession of UPSI and acting on it are not sufficient to prove insider trading.

While the actual profit or loss incurred is immaterial, the SC has clearly identified the intent behind penalizing insider trading, that is to prevent insiders from making illicit gains. However, the requirement of profit motive may involve a great deal of subjectivity. The decision in the present matter may have far-reaching effects in the manner in which insider trading cases are decided by regulators.

## II. Supreme Court: CIRP can be initiated against Corporate Debtor without proceeding against Principal Borrower.

The Supreme Court ("SC") has in its judgment dated September 6, 2022 in the matter of ***K. Paramasivam v. The Karur Vysya Bank Limited and Others [Civil Appeal No. 9286 of 2019]*** held that the Corporate Insolvency Resolution Process ("CIRP") can be initiated against the corporate debtor without proceeding against the principal borrower.

### Facts

Mr. K. Paramasivam ("**Appellant**") is the promoter, shareholder and suspended director of Maharaja Theme Parks and Resorts Private Limited ("**Corporate Debtor**"), which had stood as guarantor for the credit facilities granted by Karur Vysya Bank ("**Financial Creditor/ Respondent**") to three entities, namely, (i) Sri Maharaja Refineries, a Partnership Firm;

(ii) Sri Maharaja Industries, a proprietary concern of K. Paramasivam; and (iii) Sri Maharaja Enterprises, a proprietary concern of P. Sathiyamoorthy.

Upon failure on part of the principal borrowers to repay the loan, the Financial Creditor filed an application under Section 7 (*Initiation of corporate insolvency resolution process by financial creditor*) of the Insolvency and Bankruptcy Code, 2016 ("IBC") for initiation of the CIRP of the Corporate Debtor, on account of the corporate guarantee(s) extended by the Corporate Debtor to secure the loans availed by each of the above-named borrowers. In view thereof, the National Company Law Tribunal, Chennai ("**NCLT/ Adjudicating Authority**") admitted the Corporate Debtor under CIRP, by order dated April 8, 2019.

Thereafter, the NCLT order dated April 8, 2019 was challenged before the National Company Law Appellate Tribunal, New Delhi ("**NCLAT**"), which came to be dismissed, by order dated November 18, 2019. Aggrieved by the impugned order dated November 18, 2019 passed by the NCLAT, the Appellant preferred an appeal before the SC.

## Issue

Whether an action under Section 7 (*Initiation of corporate insolvency resolution process by financial creditor*) of the IBC can be initiated by a financial creditor, against a corporate person, in relation to a corporate guarantee, given in respect of a loan advanced to the principal borrower, who is not a corporate person?.

## Arguments

### Contentions raised by the Appellant:

The Appellant submitted that the Corporate Debtor does not fall within the definition of '*corporate guarantor*' in terms of Section 5(5A) of the IBC, wherein '*corporate guarantor*' is defined as a corporate person who is the surety in a contract of guarantee to a corporate debtor. As such, the Appellant contended that it has not stood as guarantor in respect of a loan, which was granted to a corporate person. In order to substantiate the aforesaid contention, the Appellant referred to the definition of '*corporate person*' provided under Section 3(7) of the IBC:

*"(7) "corporate person" means a company as defined in Clause (20) of Section 2 of the Companies Act, 2013 (18 of 2013), a limited liability partnership, as defined in Clause (n) of Sub-section (1) of Section 2 of the Limited Liability Partnership Act, 2008 (6 of 2009), or any other person incorporated with limited liability under any law for the time being in force but shall not include any financial service provider;"*

The Appellant submitted that on a conjoint reading of Section 5(5A), Section 3(7) and Section 3(8) of the IBC, it is clear that a corporate guarantor is the surety in a contract of guarantee to a corporate debtor. However, the principal borrowers herein, not being corporate debtor; as such, the Corporate Debtor is not a corporate guarantor as defined under Section 5(5A) of the IBC.

### Contentions raised by the Respondent:

The Respondent submitted that the question of law as to whether an action under Section 7 of the IBC can be initiated by a financial creditor, against a corporate person, in relation to a corporate guarantee, given by that corporate person, in respect of a loan advanced to the principal borrower, who is not a corporate person; has already been settled by the Supreme Court in the recent judgment of **Laxmi Pat Surana v. Union Bank of India and Another [Civil Appeal No. 2734 of 2020]** ("**Laxmi Pat Surana**"). Hence, the position of law is clear that CIRP can be initiated against a corporate entity who has stood as guarantor to secure the dues of a non-corporate entity as a financial debt, which accrues to the corporate person, in respect of guarantee given by it, once the borrower commits default.

## Observations of the Supreme Court

The SC examined the terms "financial creditor" as defined under Section 5(7) of the IBC, "creditor" as defined under Section 3(10) of the IBC, "financial debt" as defined under Section 5(8) of the IBC, "debt" as defined under Section 3(11) of the IBC and "claim" as defined under Section 3(6) of the IBC.

Upon examination of the above-mentioned terms, the SC observed that undoubtedly, a right or cause of action arises on part of the lender (financial creditor) to proceed against the principal borrower, as well as the guarantor in equal measure, in case of any default in repayment of debt. Further, even if the principal borrower fails to discharge its obligation in respect of the debt, it would still be deemed as if the default was committed by the guarantor itself. In this regard, SC referred to Section 128 of the Indian Contract Act, 1872 which clearly provides that the obligation of the guarantor is

coextensive and coterminous with that of the principal borrower. The SC further observed that as a consequence of such default, the status of the guarantor metamorphoses into a debtor or a corporate debtor if it happens to be a corporate person, within the meaning of Section 3(8) of IBC. Further, the term “default” as defined under Section 3(12) of the IBC would mean non-payment of debt when whole or any part or instalment of the amount of debt has become due or payable and is not paid by the debtor or the corporate debtor, as the case may be.

Hence, SC observed that this argument on part of the Appellant could not be accepted that since the principal borrower is not a corporate person, the financial creditor could not have invoked remedy under Section 7 of the IBC against the corporate person who had merely stood as a guarantor to secure such loan account. The financial creditor can still proceed against the guarantor being a corporate debtor, consequent to the default committed by the principal borrower.

SC further observed that if the contentions raised by the Appellant were to be accepted, it would lead to diluting or narrowing the purview of the term “corporate debtor” occurring in Section 7 of IBC, which means a corporate person, who owes a debt to any person. It was further observed that the term “debt” as defined under Section 3(11) of the IBC is broad enough to include liability of a corporate person on account of guarantee extended by it to secure a loan by any person including not being a corporate person in the event of default committed by the latter. It would still be a “financial debt” of the corporate person, arising from the guarantee extended by it, within the meaning of Section 5(8) of the IBC.

SC arrived at the conclusion that upon harmonious and purposive construction of the relevant definitions and provisions of the IBC, it is not possible to extricate the corporate person from the liability (of being a corporate debtor) arising on account of the guarantee extended by it in respect of loan given to a person other than corporate person. Hence, the liability of the guarantor is coextensive with that of the principal borrower.

Further, in the Laxmi Pat Surana judgment, SC had made it clear that CIRP can be initiated against the corporate guarantor without proceeding against the principal borrower.

### Decision of the Supreme Court

The SC held that in view of the issues raised in the present appeal having been already settled in the Laxmi Pat Surana judgment, it is clear that liability of the guarantor is co-extensive with that of the principal borrower. Hence, Financial Creditor can proceed against the guarantor without first suing the principal borrower.

The SC held that there is no reason to interfere with the concurrent findings of the NCLT and NCLAT, and therefore dismissed the appeal.

#### VA View:

The SC has put this question to rest that under Section 7 of the IBC, CIRP can be initiated against a corporate entity who has given a guarantee to secure the dues of a non-corporate entity as a financial debt accrues to the corporate person in respect of the guarantee given by it once the borrower commits default. In such a scenario, the guarantor would be the corporate debtor.

Further, the SC has reiterated its recent decision in Laxmi Pat Surana, whereby it was held by a three-judge bench that the liability of the guarantor is co-extensive with that of the principal borrower and that the financial creditor can very well proceed against the guarantor without first proceeding against the principal borrower.

### III. Supreme Court: Discretion of the Arbitral Tribunal to grant post-award interest on part of the aggregate sum due.

The Division Bench of Supreme Court (“SC”), vide its judgment dated September 1, 2022 in the matter of **Morgan Securities and Credits Private Limited v. Videocon Industries Limited [Civil Appeal No. 5437 of 2022]** held that the arbitral tribunal has discretion under Section 31(7)(b) of the Arbitration and Conciliation Act, 1996 (“Act”) to grant post-award interest only on a part of the aggregate sum due.

#### Facts

Morgan Securities and Credits Private Limited (“Appellant”) had entered into an agreement, under which Videocon Industries Limited (“Respondent”) availed of certain bill discounting facilities from the Appellant. The Appellant had

disbursed INR 5,00,32,656/- under the agreement.

The Respondent defaulted in repayment of the dues as a consequence of which, the Appellant issued demand notice for repayment of the dues along with overdue interest. However, when the Respondent failed to repay the sums, the Appellant issued a notice invoking arbitration clause provided under the agreement.

The sole arbitrator rendered the award in favour of the Appellant and decreed the claim of the Appellant for the amount of INR 5,00,32,656/-. Following was the interest granted in respect of the principal claimed:

- Interest at the rate of 21 % per annum from the date of default to the date of the demand notice;
- 36% per annum with monthly rests from the date of the demand notice to the date of award ("**Pre-award Interest**"); and
- 18% per annum on the principal amount, that is, INR 5,00,32,656/- from the date of award to the date of payment ("**Post-award Interest**").

The Post-award Interest was granted at the rate of 18% per annum only on the principal amount, by following the judgment of the Hon'ble SC in the matter of *State of Haryana and Others v. S.L. Arora and Company., [(2010) 3 SCC 690]* ("**S.L. Arora**").

The Appellant challenged the arbitral award under Section 34 (*Application for setting aside arbitral awards*) of the Act before the Delhi High Court ("**DHC**"), on the ground that the Post -award Interest of 18% per annum should be granted on the total sum awarded, inclusive of both principal and Pre-award Interest. By a judgment dated February 7, 2019, the single Judge dismissed the petition holding that the arbitrator had in his discretion restricted the Post-award Interest to the principal amount and that the Court would not interfere with the exercise of discretion by the arbitrator.

The appeal against the judgment of the single Judge was carried before the division bench of the DHC, which was dismissed by a judgment dated February 26, 2020 ("**Impugned Judgment**"), on the ground that since the arbitral tribunal in its discretion, had granted Post-award interest @18% per annum on the principal amount, the provisions of Section 31(7)(b) of the Act would not be applicable, as the statutory rate of interest as provided in the Section 31(7)(b) applies to those cases only, where the arbitral award is silent on post-award interest. The Appellant then preferred a Special Leave Petition ("**SLP**") before the SC challenging the Impugned Judgment.

## Issues

- i. Whether the phrase '*unless otherwise directs*' in Section 31(7)(b) of the Act only provides the arbitrator the discretion to determine the rate of interest or both the rate of interest and the 'sum' it must be paid against.
- ii. Whether the arbitrator has the discretion to grant Post-award Interest on a part of the aggregate sum.

## Arguments

### Contentions raised by the Appellant:

The Appellant relied on the judgment dated November 25, 2014 in the matter of *Hyder Consulting (U.K.) Limited v. Governor, State of Orissa [(2015) 2 SCC 189]* ("**Hyder Consulting**"), which overruled the judgment in *S.L. Arora* wherein, it was held that the arbitral tribunal had the authority to grant interest on interest under Section 31(7) of the Act. The Appellant contended that if pre-award interest is awarded on the principal sum, then the aggregate of the principal and the pre-award interest is the 'sum' on which post-award interest *must be* granted. On the basis of the said judgment, the Appellant tried to buttress the argument that, once pre-award interest is granted on the principal sum under Section 31(7)(a) of the Act, the interest award loses its character as interest and takes the colour of the awarded 'sum' for the purposes of post-award interest under Section 31(7)(b) of the Act.

Further, Appellant argued that since the arbitral award was silent on post-award interest on the component of interest, the Appellant was entitled to the statutory rate of interest on the aggregate of the principal and pre-award interest, as provided under Section 31(7)(b) of the Act. The Appellant contended that even if the judgment of *S.L. Arora* was to be taken into consideration, the learned Judges in that matter as well held that the only discretion that the arbitral tribunal had under Section 31(7)(b) of the Act was to decide the 'rate' of post-award interest. Thus, the Arbitrator does not have the discretion to determine the 'sum' on which the post-award interest is to be granted.

### Contentions raised by the Respondent:

The Respondent argued that Section 31(7)(b) is qualified by the phrase “*unless the award otherwise directs*”. Therefore, Section 31(7)(b) would only be applicable only when an arbitral award is silent on the component of post-award interest. Under Section 31(7)(b) of the Act, the arbitrator has the discretion to (a) grant post-award interest; (b) determine the quantum over which the post-award interest should be granted; and (c) determine the rate at which the interest should be calculated.

The Respondent pointed out that in Hyder Consulting, the larger bench of the Court overruled the judgment dated January 29, 2010 of S.L. Arora, to the extent that the latter decision held that the arbitral tribunal does not have the power to award interest over interest. However, in Hyder Consulting, it was not held that it is mandatory that the post-award interest ought to only be granted on the aggregate of the principal and the pre-award interest.

### Observations of the Supreme Court

SC analysed Section 31(1) of the Act, the judgment in S.L. Arora and Hyder Consulting to make the following observations:

- i. Section 31 provides for the “*form of content of arbitral award*”. Section 31(7)(a) provides for pre-award interest, that is for the period between the date on which the cause of action arose and the date on which the award is made. Section 31(7)(b) provides for post-award interest, between the date of award to the date of payment.
- ii. In S.L. Arora, SC interpreted the expression ‘sum’ in Section 31(7) and held that Section 31(7) does not make any reference to the payment of interest or interest on interest. The “sum directed to be paid by the award” refers to the award of “sums on substantive claims”, that is, the principal amount. In the absence of a provision enabling the grant of compound interest, such a power cannot be read into the provisions either for the pre-award period or for the post-award period. The discretion under Section 31(7)(b) to award interest for the post-award period is not subject to any contract and if the arbitrator does not exercise the discretion by awarding post-award interest, then the mandated interest of 18 % shall be awarded. If the award provides interest at a specified rate till the date of payment, then Section 31(7)(b) is silent on the post-award interest.
- iii. In Hyder Consulting, the learned Judges overruled the decision in S.L. Arora. SC held that it is apparent that vide Section 31(7)(a) of the Act, the Parliament intended that an award for payment of money may be inclusive of interest and the ‘sum’ of the principal amount plus interest may be directed to be paid by the arbitral tribunal.
- iv. The SC observed that Justice Bobde only made a passing reference to the phrase ‘*unless the award otherwise directs*’ in Section 31(7)(b), in paragraph 13 of Hyder Consulting to hold that post-award interest is a statutory mandate and that the arbitrator only has the discretion to determine the rate of interest to be awarded on such ‘sum’ arrived at after merging of interest with the principal; the two components having lost their separate identities. While, Justice Sapre held that ‘*unless the award otherwise directs*’ meant that the post-award interest is a statutory mandate and the arbitrator only has the discretion to decide the rate of such post-award interest, Justice Bobde on the other hand, did not specifically interpret the phrase. Thus, SC only dealt with a limited issue- *whether post-award interest could be granted on the aggregate of the principal and the pre-award interest*. The said judgment does not deal with the aspect of the discretion of the arbitrator to determine the post-award interest on a part of the aggregate sum.

### Decision of the Supreme Court

The relevant extract of Section 31(7) of the Act is reproduced hereinbelow, which provision has been dealt with and interpreted by the SC in the present judgment:

#### “31. Form and contents of arbitral award-

.....  
 (7) (a) Unless otherwise agreed by the parties, where and in so far as an arbitral award is for the payment of money, the arbitral tribunal may include in the sum for which the award is made interest, at such rate as it deems reasonable, on the whole or any part of the money, for the whole or any part of the period between the date on which the cause of action arose and the date on which the award is made.

(b) A sum directed to be paid by an arbitral award shall, unless the award otherwise directs, carry interest at the rate of eighteen per centum per annum from the date of the award to the date of payment.”  
 (emphasis supplied)

Firstly, the SC clarified that Section 31(7)(a) and (b) of the Act are qualified. The placement of the phrase of the ‘unless otherwise agreed by the parties’ at the beginning of clause (a) of Section 31(7) of the Act, qualifies the entire provision, meaning thereby, that the discretion of the arbitral tribunal to determine pre-award interest, would come into picture,

only if the parties have not agreed anything to the contrary in respect of applicability of interest. In case, the parties have an arrangement in respect of applicability interest on the payment of money, the arbitral tribunal would be bound to determine the interest on the basis of such agreement between the parties. On the contrary, the placement of the phrase 'unless the award otherwise directs' before 'carry interest at the rate of eighteen percent' in Section 31(7)(b) only qualifies the rate of interest and not the 'sum' directed to be paid by an arbitral award. This implies that Section 31(7)(b) of the Act only provides for statutory rate of 18% p.a. on the 'sum', which statutory rate would be triggered only when the arbitral tribunal has not determined the quantum/rate of post-award interest.

Thus, SC held that Section 31(7)(a) confers wide discretion upon the arbitrator to grant pre-award interest. The discretion is wide enough for the arbitrator to determine:

- (a) the rate of reasonable interest,
- (b) the sum on which interest is to be paid, that is, whether on the whole or any part of the principal amount and
- (c) the period for which payment of interest is to be made- whether it should be for the whole or any part of the period between the date on which the cause of action arose and the date of the award.

SC held that the statutory rate of interest at the rate of 18% per annum in Section 31(7)(b) of the Act is only contemplated in a situation where the arbitration award is silent on post-award interest and cannot mean to take away the discretion of the arbitrator to decide the quantum of post-award interest. The discretion of the arbitrator can only be restricted by an express provision to that effect. Finally, the SC held that the arbitrator must exercise the discretionary power to grant post-award interest reasonably and in good faith, taking into account all relevant circumstances.

Therefore, SC held that the arbitrator has the discretion to award post-award interest on a part of the 'sum' and thus, in the instant case, the grant of post-award Interest only on the principal claim was held to be well within the discretion of the arbitral tribunal.

#### VA View:

The SC in Hyder Consulting settled the law in respect of authority of the arbitral tribunal to grant interest on interest from the date of award, thereby, overruling the decision in S.L. Arora. The present judgment does not delve into the aspect of 'interest on interest', however, the judgment rightly points out that the judgment of Hyder Consulting did not effectively interpret the qualifying phrases contained in Clauses (a) and (b) of Section 31(7) of the Act, thereby, not dealing with the aspect of "discretion of the arbitral tribunal" while granting pre-award and post-award interest.

The present judgment adds clarity to the ruling in Hyder Consulting and goes on to explain the nature and scope of discretion which was intended to be embedded in the provision by the legislators, thereby, leaving no room in the Act for curtailing or restricting it. Thus, the key takeaways from the judgment are as follows:

- i. The arbitral tribunal cannot grant interest on the 'sum' under Section 31(7)(a) of the Act contrary to the arbitration agreement between the parties on account of the qualifying phrase "unless otherwise agreed by the parties";
- ii. In the absence of any such agreement in respect of grant of interest on the 'sum' claimed, the arbitral tribunal has the discretion under Section 31(7)(a) of the Act to: (a) grant or refuse interest, (b) determine the rate of interest, (c) determine the 'sum' on which interest is to be granted, which may be on the whole or part of the money claimed and (d) determine the period for which pre-award interest is to be granted;
- iii. The arbitral tribunal has the discretion to determine (i) whether further rate of interest can be granted under Clause (b) of Section 31(7) of the Act, (ii) determine the 'sum' on which the further interest (which can either be the aggregate of the principal amount and the pre-award granted under Clause (a) of Section 31(7) of the Act, or part of the aggregate claim and (iii) the rate of interest to be granted;
- iv. Only in the event where no post-award interest is specified by the arbitral tribunal under Clause (b), the statutory rate of interest would be applicable to the award, that is, eighteen percent per annum, by virtue of the qualifying phrase "unless the award otherwise directs" in Clause (b);
- v. The interest so imposed under Section 31(7) of the Act is to be at such rate as the arbitral tribunal deems reasonable.

#### IV. NCLAT: Erstwhile resolution professional has no right to be heard before being replaced under Section 27 of the Insolvency and Bankruptcy Code.

The National Company Law Appellant Tribunal, Principal Bench, New Delhi ("NCLAT") has in its judgement dated

September 2, 2022 ("**Judgement**"), in the matter ***Sumat Kumar Gupta v. Committee of Creditors of M/s. Vallabh Textiles Company Limited [Company Appeal (AT) (Insolvency) No. 1037 of 2022]*** held that when the Committee of Creditors ("**CoC**") decides to replace the resolution professional under Section 27 (*Replacement of resolution professional by CoC*) of the Insolvency and Bankruptcy Code, 2016 ("**IBC**") and an application is filed before the National Company Law Tribunal ("**Adjudicating Authority/ NCLT**") for approval, the erstwhile resolution professional would have no right to be heard before the Adjudicating Authority, before being replaced.

## Facts

In the instant case, M/s. Vallabh Textiles Company Limited ("**Corporate Debtor**") was admitted into Corporate Insolvency Resolution Process ("**CIRP**") pursuant to which Mr. Sumat Kumar Gupta ("**Appellant**") was appointed as the resolution professional of the Corporate Debtor.

However, the CoC in its meeting dated June 4, 2022, decided with 100% vote, to replace the Appellant with another resolution professional namely Mr. Rajiv Khurana.

Consequently, an application was filed before the Adjudicating Authority by Punjab National Bank ("**Financial Creditor**"), for replacement of the Appellant and the NCLT vide its order dated July 7, 2022 ("**Impugned Order**"), allowed the application and Mr. Rajiv Khurana was appointed as the resolution professional of the Corporate Debtor in place of the Appellant.

Aggrieved by the Impugned Order passed by the NCLT, the Appellant preferred an appeal before the NCLAT.

## Issue

Whether an erstwhile resolution professional has the right to be heard before being replaced under Section 27 (*Replacement of resolution professional by CoC*) of the IBC in consonance with the principles of natural justice.

## Arguments

### Contentions raised by the Appellant:

The Appellant submitted that the NCLT passed the Impugned Order for replacement of the resolution professional of the Corporate Debtor, without giving him an opportunity of being heard and without issuing any notice to him. The Appellant further contended that when the Impugned Order was being passed by the Adjudicating Authority, he was entitled for an opportunity of being heard in consonance with the principles of natural justice.

Moreover, Section 27 of the IBC that provides for replacement of the resolution professional by the CoC does not exclude applicability of natural justice. Therefore, he was entitled for the opportunity of being heard before being replaced.

The Appellant cited the observations of the judgment in ***MCL Global Steel Private Limited and Another v. Essar Projects India Limited and Another [Company Appeal (AT) (Ins.) No. 29 of 2017]*** ("**Essar Projects Case**"), wherein paragraph 50 of the judgment of the Hon'ble Calcutta High Court in ***Sree Metaliks Limited and Another v. Union of India and Another [Writ Petition 7144(W) of 2017]*** was relied upon. In the said case, the Hon'ble Calcutta High Court held that a person cannot be condemned unheard and that where a statute is silent on the right of hearing and it does not in express terms oust the principles of natural justice, the same can and should be read into. When the Adjudicating Authority receives an application under Section 7 (*Initiation of corporate insolvency resolution process by financial creditor*) of the IBC, it must afford a reasonable opportunity of hearing to the corporate debtor as Section 424 (*Procedure before Tribunal and Appellate Tribunal*) of the Companies Act, 2013, mandates it to ascertain the existence of default as claimed by the financial creditor in the application.

### Contentions raised by the CoC:

The CoC refuted the submissions of the Appellant and contended that Section 27 of the IBC does not contemplate any opportunity to be given to the resolution professional by the Adjudicating Authority, before passing an order approving the resolution of the CoC for replacement of such resolution professional.

The CoC further submitted that as per the scheme delineated by Section 27 of the IBC, replacement of a resolution professional is complete when a resolution is passed for replacement with 66% votes of the CoC and the Adjudicating Authority is communicated the name of the new resolution professional, for approval.

In order to support its submissions, the CoC relied on the following judgements passed by the NCLAT:

1. ***Punjab National Bank v. Kiran Shah, Insolvency Resolution Professional of ORG Informatics Limited [Company Appeal (AT) (Ins) No. 749 of 2019]*** (“PNB Case”), wherein it was held that the CoC is not required to record any reason or ground for replacing the resolution professional, which may otherwise call for proceedings against such resolution professional. The CoC having decided to remove the resolution professional, does not entitle the Adjudicating Authority to interfere with such decision, till it is shown that the decision of the CoC is perverse or without jurisdiction.
2. ***Bank of India v. Nithin Nutritions Private Limited [Company Appeal (AT) (Ins.) No. 497 of 2020]***, (“Nithin Nutritions Case”) wherein it was held that the law nowhere provides for the CoC to give reasons for replacing the resolution professional.
3. ***Committee of Creditors of LEEL Electricals Limited through State Bank of India v. Leel Electricals Limited through its Interim Resolution Professional, Arvind Mittal [Company Appeal (AT) (Insolvency) No. 1100 of 2020]*** (“Leel Electricals Case”), wherein it was held that in the face of CoC resolution being passed with more than the requisite majority, it cannot lie in the mouth of the resolution professional that any of his legal rights have been infringed.

### Observations of the NCLAT

The NCLAT observed that a reading of Section 27 of the IBC clearly provides that when the CoC is of the opinion that a resolution professional appointed under Section 22 (*Appointment of resolution professional*) of the IBC, is required to be replaced, it may replace him with another resolution professional in the manner prescribed under Section 27 of the IBC. The manner provided under Section 27(2) of the IBC, is that a resolution be passed at the meeting of the CoC by 66% voting share to replace the resolution professional and to appoint another resolution professional, subject to a written consent from the proposed resolution professional.

The NCLAT further observed that Section 27 of the IBC does not contemplate any opportunity of hearing to the resolution professionals by the Adjudicating Authority before approving the proposal of a new resolution professional. The CoC is required to merely forward the name of the proposed resolution professional to the Adjudicating Authority, which in turn forwards the name of the proposed resolution professional to the Insolvency and Bankruptcy Board of India for its confirmation. Section 27 in no way indicates that a resolution professional is to be made a party and is to be issued a notice before taking a decision to appoint another resolution professional.

Besides, looking to the purpose and object of the IBC, where timeline is an essential factor to be taken into consideration at all stages, there is no warrant to permit a Lis (suit) to be raised by the resolution professional, challenging his replacement by the CoC. When the decision is by votes of a collective body, that is the CoC, such decision is not easily assailable and replacement of a resolution professional is complete as per the scheme of Section 27 when the resolution is passed by the CoC with requisite 66% voting share.

With regard to the contention of the Applicant that Section 27 does not exclude applicability of the principles of natural justice, the NCLAT observed that the said Section of the IBC excludes the principles of natural justice, by implication, and it is clear that the scheme nowhere provides for any opportunity to the Appellant for hearing.

The NCLAT further observed that the Essar Steel Case, relied upon by the Appellant, provides for hearing under Section 7 (*Initiation of corporate insolvency resolution process by financial creditor*) and Section 9 (*Application for initiation of corporate insolvency resolution process by operational creditor*) of the IBC, which is for an entirely different purpose and that the principle laid down in the Essar Steel Case cannot be imported to the instant case.

### Decision of the NCLAT

The NCLAT asserted the view laid down in the judgements relied upon by the CoC, namely the PNB Case, the Nithin Nutritions Case and the Leel Electricals Case. Undisputedly, the replacement of resolution professional is complete when the required decision is taken by the CoC in its meeting with requisite majority.

Therefore, there being no grounds to interfere with the Impugned Order of the NCLT approving the replacement of the resolution professional, the NCLAT dismissed the appeal filed by the Appellant.

**VA View:**

The NCLAT through this Judgement threw light on the legislative intent of Section 27 (*Replacement of resolution professional by CoC*) of the IBC. It has rightly held that when a resolution professional has been replaced by the CoC in the manner prescribed under Section 27(2) of the IBC, which is by 66 % voting share, such decisions are not amenable to challenges easily. The scheme delineated by Section 27 of the IBC, in no way indicates that a resolution professional is to be made a party and is to be issued a notice before taking a decision to appoint another resolution professional. The provisions of Section 27 of the IBC are self-explanatory in nature, and therefore, do not entitle the resolution professional of the right to be heard before the Adjudicating Authority, before being replaced.

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