



K. Kishan v. M/s Vijay Nirman Company Pvt. Ltd. (Supreme Court, 14 August 2018)

BRIEF BACKGROUND

The Respondent entered into a Contract with one M/s Ksheerabad Constructions Pvt. Ltd. (“**KCPL**”, a company associated with the Appellant). When disputes arose under the Contract, they were referred to an Arbitral Tribunal, which delivered an arbitral award dated 21 January 2017 (“**Award**”) against the Appellant / KCPL. Under the Award, sums of Rs. 1,71,98,302/- and Rs. 13,56,98,624/- were granted in favour of the Respondent, under different heads of claims, and the counter claims made by the Appellant / KCPL were rejected. Notably, during the arbitral proceedings, KCPL had admitted liability against the sum of Rs. 1,71,98,302/-.

After the receipt of the Award, the Respondent sent a notice under section 8 (“**Section 8 Notice**”) of the Insolvency and Bankruptcy Code, 2016 (“**IBC**”) to KCPL, demanding payment of an amount of Rs. 1,79,00,166/-. KCPL disputed the invoice referred to in the Section 8 Notice, on the basis that the Respondent allegedly owed KCPL greater amounts (which KCPL had sought under the counter claims and which had been rejected by the Arbitral Tribunal).

KCPL then filed a petition under Section 34 (“**Section 34 Petition**”) of the Arbitration and Conciliation Act, 1996 (“**the Arbitration Act**”) challenging the Award.

Subsequently, the Respondent filed a petition under Section 9 (“**Section 9 IBC Petition**”) before the National Company Law Tribunal (“**NCLT**”), on the basis that the amount sought under the Section 8 Notice was an ‘operational debt’ to be paid by KCPL. Although KCPL had admitted before the Arbitral Tribunal that the Respondent was entitled to the amount of Rs. 1,71,98,302/- as granted under the Award, it argued that since it had filed a Section 34 Petition challenging the Award, the Section 9 IBC Petition would not be maintainable on account of a pre-existing dispute¹.

The NCLT, and thereafter the National Company Law Appellate Tribunal (“**NCLAT**”), did not agree with KCPL’s contention², and admitted the Section 9 IBC Petition. Thus, the Appellant / KCPL filed the present appeal before the Supreme Court (“**SC**”).

ISSUE & FINDINGS

The issue which arose before the SC was whether the provisions of the IBC can be invoked by parties to recover amounts under an arbitral award passed against the operational debtor, although the award has not attained finality.³

The Appellant firstly brought to the SC’s notice, the decision in *Mobilox Innovations Private Limited v. Kirusa Software Private Limited*⁴, wherein the SC had observed that the object of the IBC was not to replace the adjudication and enforcement of debts under other statutes, including the Arbitration Act. It had further been noted in the said judgment that once a real dispute – and not necessarily a *bona fide* one – existed between the parties regarding the ‘operational debt’, the IBC could not be resorted to. The Appellant thus argued that the pending Section 34 Petition clearly demonstrated a real dispute existing between the parties.

The Respondent argued that the Appellant had admitted before the Arbitral Tribunal that the amount of Rs. 1.71 crore was a debt due to the Respondent, and therefore no dispute existed regarding the same.

Based on the principles laid down in *Mobilox Innovations*, the SC, in the present case, observed that the mere factum of a challenge against an arbitral award would be sufficient to demonstrate that a dispute existed regarding the amount under such award. The SC reiterated that the object of the IBC was to bring insolvency proceedings against a debtor only in cases where a real dispute as to the debt owed does not exist.

Based on its above reasoning, the SC held that the Section 9 IBC Petition was not maintainable as IBC proceedings cannot be instituted in respect of a debt under an arbitral award which is undergoing a challenge under section 34 or 37 of the Arbitration Act.

¹ Sub-section 9(5) of the IBC provides that:

“The Adjudicating Authority shall, within fourteen days of the receipt of the application under sub-section (2), by an order—

(i)...

(ii) reject the application and communicate such decision to the operational creditor and the corporate debtor, if—

...

(d) notice of dispute has been received by the operational creditor or there is a record of dispute in the information utility; or

..”

² While the NCLT based its order on the fact that the claim stood admitted and there was no stay on the Award, the NCLAT observed that Section 238 of the IBC would override the provisions of the Arbitration Act.

³ S. 35 of the Arbitration Act

⁴ (2018) 1 SCC 353, [*“Mobilox Innovations”*].

The SC noted the Respondent's argument that the Appellant had admitted its liability vis a vis the claimed amount. However, since the rejection of the Appellant's counter claims by the Arbitral Tribunal was also being challenged by the Section 34 Petition, and since these counter claims far exceeded the amount of Rs. 1.71 crores admitted by the Appellant, there was, by implication, a dispute as to whether the Appellant was required to pay the Respondent the said sum.

Further, regarding the NCLAT's observation that section 238 of the IBC would override the Arbitration Act, the SC elucidated that this was only applicable in case of an inconsistency, which was not the scenario in the present case. It was clear to the SC that, given the facts, the operational debt was a disputed one, and insolvency proceedings could therefore not be instituted.

CONCLUSION

Nearly a year on from the *Mobilox Innovations* judgment, this present judgment should bring further relief to operational debtors against whom arbitral awards are issued. It has been a widely recognised principle (even prior to the enactment of the IBC) that insolvency proceedings should not be used as a tool for debt recovery. This judgment brings much welcome clarity that valid petitions under sections 34 and 37 of the Arbitration Act against an arbitral award will constitute a real dispute as to the operational debt owed. This is supported by the understanding that such award is not final and binding on the parties as it is being challenged. Such a position of law should prevent operational creditors from prematurely resorting to the IBC instead of seeking enforcement of the award⁵ as a strategy to pressurize the operational debtor.

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⁵ Even an enforcement proceeding itself, may be subject to a stay under section 36 of the Arbitration Act in light of a challenge to an award under S. 34 of the Arbitration Act.