Does The Restoration Of An Appeal Filed Under Section 37 Of The Arbitration and Conciliation Act (1996) Constitute A Pre-Existing Dispute Under The IBC?
written by Juhi Chandel | December 3, 2021

In M/S Jai Balaji Industries Vs. D. K. Mohanty & Anr., 2021, the Operational Creditor (OC) filed an appeal before the Supreme Court under Section 62 of Insolvency and Bankruptcy Code, 2016, (Code) against the order passed by National Company Law Appellate Tribunal, (NCLAT). NCLAT held that the Operational Debt claimed by the OC was not free from pre-existing dispute and subsequently set aside the admission order passed by the National Company Law Tribunal (NCLT).

Facts - Section 37 Of The Arbitration and Conciliation Act

The OC and Corporate Debtor (CD) entered into two Memorandums of Understanding (MoU) on August 13th 2003 and March 11th 2004, whereby CD agreed to supply, respectively, 1 lakh and 7 lakh metric tons of iron ore per month to the OC. A dispute ensued between the parties regarding supply and payment, which lead the OC to invoke the arbitration clause and the matter was taken up in arbitration proceedings. Two separate arbitral awards were passed in relation to the respective MOUs in favour of the OC where under the CD was held liable to make payment of INR 4.44 crores and INR 2.79 crores respectively.

Soon after the awards were passed, the CD – by way of petitions under Section 34 of the Arbitration and Conciliation Act, 1996 (Act) – challenged the validity and legality of the awards. However, the appeal was dismissed by the District Court, Barasat by its orders dated February 27th 2012 and February 29th 2012 respectively. The orders of the District Court were challenged once again by the CD by filing appeals under Section 37 Of The Arbitration and Conciliation Act before the High Court of Calcutta and the same was dismissed due to the non-appearance of the CD.

On December 17th 2019, the CD moved respective applications for the restoration of appeals and the same was allowed by the High Court after finding sufficient cause for non-appearance on the date of hearing. Consequently, both the appeals under Section 37 Of The Arbitration and Conciliation Act of 1996 were revived for fresh adjudication. In the meantime, before the restoration of the appeals, the appellant sent two separate demand notices under Section 8 of the Code to CD, claiming Operational Debts of INR 7,75,13,684 and INR 5,62,01,258 respectively.

The CD replied to the demand notices asserting, that there existed a dispute and the arbitration proceedings is still pending which pre-dated the receipt of the demand notice. Further, the CD also stated that the applications for restoration of appeals were pending in the High Court, which was filed much before the receipt of demand notices and with advance notice to the OC. Thus, the CD asserted, that the matter of debt owed was sub-judice and no operational debt is payable to OC.

NCLT Order

Notwithstanding the replies sent by the CD, the OC filed a Petition under Section 9 of the Code before NCLT seeking initiation of CIRP against CD. NCLT admitted the Petition on the basis that the OC served demand notices to the respondent company under Section 8 of the Code and on the date of filing of applications under Section 9 of the Code, no proceedings were pending in challenge to the arbitral awards and hence, no dispute as to the debt owed to the appellant was existing on the relevant dates.

NCLAT Order

The CD, aggrieved by the order passed by the NCLT, preferred an appeal before the Appellate Tribunal (NCLAT) under Section 61 of the Code. The NCLAT held that it can be seen from the record that the entire basis for the Section 8 Notice is that the Appeals preferred by the 'Corporate Debtor' under Section 37 of the A&C Act, 1996 were dismissed for default on 22.11.2019.

The issue that was determined in the aforenoted Judgement 'K. Kishan' (Supra) is that the Code cannot be invoked in respect of an 'Operational Debt' where an Arbitral Award has been passed against the 'Corporate Debtor' but which has not yet been finally adjudicated upon. Further, the filing of the Sections 34 & 37 of A&C Act, 1996 against an Arbitral Award implies that a pre-existing dispute which culminates at the first stage of proceedings in an Award, continues even after the Award, at least till the final adjudicatory process under Sections 34 & 37 is completed.

In the instant case, the 'Corporate Debtor' filed an Application for restoration on 17.12.2019, the Demand Notice was issued on 14.02.2020 and the Section 37 Of The Arbitration and Conciliation Act Appeal has been restored to its original number on 02.03.2020. We observe that the Arbitration Proceedings are still pending before the Hon'ble High Court of Kolkata and therefore we have no doubt in holding that there is a Pre-Existing Dispute between the parties, prior to the issuance of the Section 8 Demand Notice.

Supreme Court

The Supreme Court dismissed the appeal stating:

1. That the OC asserts itself to be an Operational Creditor, for the reason of having a claim against the CD, which was the subject matter of arbitration proceedings and led to the arbitral awards in its favour. According, to the OC, the challenge to arbitral awards came to an end with the dismissal of appeals filed under Section 37 Of The Arbitration and Conciliation Act of 1996. Hence, the notices were sent demanding payment of the amount due, for which the CD was in default.
2. The entire approach of the OC seems to be founded on a basic misconception that the Code has provided another avenue for enforcing money recovery by the Creditor against the Corporate Debtor. The submissions made by the OC seeking to maintain its Petition under Section 9 of the Code proceed squarely contrary to the elementary principles concerning the object and purpose of the Code.

3. The NCLAT took note of the fact that the applications, though sworn on 29th February 2020, were filed only on March 2nd 2020. Thus, a wishful attempt of the OC to use the default dismissal of appeals for initiation of CIRP had also lost its ground on the date of filing of the applications under Section 9 of the Code.
4. There could be a case where restoration is not applied for and there could also be a case where restoration is declined, which might put an effective end to the dispute but, when restoration of the appeal is granted, it definitely re-activates the dispute. In fact, for the purpose and in the scheme of the Code, even pendency of an application for restoration is sufficient to bring the matter within the four corners of "pre-existing dispute".
5. The NCLT had proceeded from an altogether wrong angle and even while passing the order on 30th September 2020, did not pause to consider that the appeals stood restored on the date of filing of the applications under Section 9 and therefore, the hyper-technical stance of the OC was also knocked out. The NCLT had, in fact, totally misconstrued the clear and emphatic expositions in K. Kishan (supra).
6. Further, it was held that the Appellate Tribunal (NCLAT) has set aside the orders passed by the Adjudicating Authority (NCLT) and has rightly closed the proceedings against the CD. There is absolutely no reason to consider any interference at the instance of the OC. Accordingly, the appeal was dismissed.

   To conclude, the issue with respect to "pre-existing dispute" was determined in 'K. Kishan' (Supra) wherein it
   was stated that the OC cannot initiate CIRP proceedings against the CD until the arbitral award passed against the CD is
   pending for final adjudication. Accordingly, in M/S Jai Balaji Industries Vs. D. K. Mohanty & Anr, though at the time of filling the application
   under Section 9 of the Code, the appeal under Sections 34 & 37
   of the Act was dismissed due to the non-appearance of the CD and later restored, the Supreme Court dismissed the appeal with the stance: when restoration of the appeal is granted, it definitely re-activates the dispute.

   https://ibbi.gov.in/uploads/order/842f71422879645e611b2affc8f480d9.pdf

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