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COURT UPHOLDS CONSTITUTIONAL VALIDITY OF INSOLVENCY AND BANKRUPTCY CODE, 2016 [*SWISS RIBBONS PRIVATE LIMITED & ANR. VERSUS UNION OF INDIA & ORS.*]: AN OVERVIEW

INTRODUCTION AND BACKGROUND

Issues relating to insolvency of corporate companies were governed by the Companies Act, 2013 and disputes were heard by the respective High Courts of India, however the provisions of the Companies Act, 2013 were found inadequate in addressing these problems. As a result, a new insolvency regime with an aim for resolution of insolvency was proposed based on the Report of Bankruptcy Law Reforms Committee dated 4th November 2015. Pursuant to this, the Insolvency and Bankruptcy Code, 2016 **("IBC")** was finally given presidential assent on 28th May, 2016, to consolidate the laws relating to insolvency problems faced by the partnership firms, individuals and corporate entities.

In the year 2018, various petitions were filed before the Hon'ble Supreme Court of India **("SC")** challenging the constitutional validity of various provisions pertaining to IBC. The SC bench consisting of Justice R.F. Nariman and Justice Naveen Sinha upheld the constitutional validity of IBC on 25th January 2019 in the landmark case of *Swiss Ribbons Private Limited & Anr. Versus Union of India & Ors.*[1] This present judgment has considered all contentions leading to the unconstitutionality of IBC and has established the foundation for its implementation.

SC relied upon the arguments of the Respondent i.e. Union of India, represented by Attorney General of India, Mr. K. K. Venugopal and Solicitor General of India, Mr. Tushar Mehta while upholding the effectiveness of IBC. Another compelling factor for sustaining IBC was Government's initiative to tackle the crisis of non-performing assets **("NPA")** through the enactment of IBC by bringing new amendments from time to time.

KEY OBSERVATIONS OF SC

The key observations of this present judgment have been detailed herein below:

1. Section 29A of IBC is not 'retrospective' in nature

Section 29A lists the persons who are not eligible to submit a resolution plan. It was contended by Petitioner i.e. Swiss Ribbons Private Limited represented by Senior Advocate, Mr. Mukul Rohtagi that Section 29A retrospectively violates the rights of erstwhile promoters to participate in the Corporate Insolvency Resolution Process **("CIRP")** for the Corporate Debtor. While deciding the issue, SC relied on *Arcelor Mittal India Private Limited* v. *Satish Kumar Gupta and Ors.*[2] along with various other judgments and held that Section 29A does not disturb any vested rights, as a resolution applicant does not have any vested right that can be disturbed. It was further observed that a person or any other person acting jointly or in concert with such person falling under Section 29A has no vested right to apply for a resolution applicant by submitting a resolution plan, if he is an undischarged insolvent, a willful defaulter etc., as mentioned under Section 29A of the IBC. Thus, concluding that Section 29A is not *retrospective* in nature.

2. Upheld Section 29A of IBC in its "entirety"

The Petitioners challenged the validity of Section 29A (j) read with Section 5 (24) of IBC. It was contended that merely a relative of an ineligible person cannot be a sufficient reason to deprive such person from being a resolution applicant.

SC relied upon *Attorney General for India and Ors. vs. Amratlal Prajivandas and Ors.*[3] and observed that all the persons listed in Section 5 (24) shows that such persons or category of persons must be related/ connected with business activity of resolution applicant within the meaning and scope of Section 24A (j) and in the absence of showing that such person is *"connected"* with the business activity of the resolution applicant, such person cannot possibly be disqualified under Section 29A (j).

3. Resolution professional has no adjudicatory powers

[1] MANU/SC/0079/2019

[2] MANU/SC/1123/2018; Civil Appeal Nos. 9402-9405/2018 [decided on 04.10.2018]

[3] (1994) 5 SCC 54

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While observing the said issue, SC relied upon Section 18 of IBC i.e., duties of interim resolution professional along with Sections 38 to 42 of IBC with regard to "claims" for stating the duties of interim resolution professional and certain CIRP Regulations. In furtherance to the aforesaid, SC observed that: *"resolution professional is given the administrative powers as opposed to quasi-judicial powers".*

SC also highlighted the difference between the liquidator and resolution professional and observed that Sections 41 and 42 shows that liquidator "determines" the value of claims admitted under Section 40 of IBC and such determination is a "decision", which is quasi- judicial in nature and which can be appealed against the adjudicating authority. Whereas, the resolution professional cannot act in a number of matters without approval of Committee of Creditors ("**CoC**") under Section 28 of IBC which can replace one resolution professional with another in case of non satisfactory performance by a two-thirds (2/3rd) majority; thereby making resolution professional a facilitator of CIRP. Thus, it was concluded that the resolution professional has only administrative powers and no adjudicatory powers.

4. Clarity in interpretation of Section 29A (c) of IBC

It was submitted by Petitioners that this provision treats unequals as equals and thus violates Article 14 of Indian Constitution. The SC held that there is no vested right in an erstwhile promoter of a corporate debtor to bid for the immovable/movable property of the corporate debtor in liquidation.

Further, SC upheld the validity of period of one (1) year from the date of classification as NPA till the date of commencement of CIRP for excluding a person from being disqualified under Section 29A. It observed in Para 71 of judgment that: "…*a person is a defaulter when an installment and/or interest on the principal remains overdue for more than three months, after which, its account is declared NPA. During the period of one year thereafter, since it is now classified as a substandard asset, this grace period is given to such person to pay off the debt. During this grace period, it is clear that such person can bid along with other resolution applicants to manage the corporate debtor. This policy cannot be found fault with. Neither can the period of one year be found fault with, as this is a policy matter decided by the RBI and which emerges from its Master Circular, as during this period, an NPA is classified as a substandard asset."*

5. Establishment of circuit benches

The Petitioners argued that establishment of the Appellate Court, i.e., NCLAT only in New Delhi and not in any other states of India is creating a problem as people from various states have to travel to New Delhi as against when earlier they could have sought their respective High Courts. They argued that it is contrary to SC's judgment on *Madras Bar Association vs. Union of India*[4] wherein Apex Court directed for establishment of permanent benches at the seat of every High Court. The SC has directed the Government to set up circuit benches within a period of 6 months from the date of the order.

6. Intelligible differentia between financial and operational creditors

The Petitioners argued that there is no real difference between financial creditors and operational creditors. In this regard, SC in Para 27 of judgment took the view that most of financial creditors particularly banks and financial institutions are secured creditors whereas most operational creditors are unsecured. The nature of the loan agreements with financial creditors is different from contracts with operational creditors for supplying goods and services.

SC further stated that financial creditors since beginning were involved in assessing the viability of corporate debtor and can therefore engage in restructuring of the loan as well as reorganization of corporate debtor's business when there is financial stress, which the operational creditors cannot perform. Thus, preserving the corporate debtor as a going concern, while ensuring maximum recovery for all creditors being the objective of the Code, SC held that there is clear intelligible differentia between financial creditors and

[4] (2014) 10 SCC 1

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operational creditors which has a direct relation to the objects sought to be achieved by IBC.

7. Constitutionality of Section 12A of IBC

It was contended that Section 12A of IBC allowing a limit of ninety percent (90%) of CoC to withdraw the insolvency application was arbitrary and violates Article 14 of the Indian Constitution. SC while observing the issue relied upon Insolvency Law Committee Report 2018 and Regulation 30A of CIRP Regulations. SC observed and stated that: *"…This high threshold has been explained in the ILC report as all financial creditors have to put their heads together to allow such withdrawal as, ordinarily, an omnibus settlement involving all creditors ought, ideally, to be entered into. This explains why ninety percent, which is substantially all the financial creditors, have to grant their approval to an individual withdrawal or settlement. For all these reasons, we are of the view that Section 12A also passes constitutional muster."*

Thus, SC upheld the constitutional validity of Section 12A and held that CoC does not make the last decision on the subject and if the CoC arbitrarily rejects the withdrawal claim then under Section 60 of IBC, the NCLT/ NCLAT can always set aside such an arbitrary decision.

8. Exclusion of MSME from the ambit of Section 29A

SC upheld the exclusion of micro, small and medium enterprises from eligibility criteria under Section 29A on the rationale that other resolution applicants may not be forthcoming for filing resolution plan for MSMEs, which will then lead to liquidation of MSMEs and not resolution.

9. Section 53 does not violate Article 14 of the Indian Constitution

The Petitioners contended that in the event of liquidation, operational creditors will never get anything, as they are below the rank of other creditors including financial creditors and thus Section 53 (1) (f) is discriminatory.

Dealing with this contention, SC relied upon various reports of Bankruptcy Law Reform Committee, Notes on Insolvency and Bankruptcy Bill and Insolvency Law Committee Report 2018 and concluded that unsecured debts are of various kinds and as long as there is legitimate interest sought to be protected which are related to the objects of IBC, Article 14 of Constitution does not get infracted by Section 53 of IBC.

The provision creates an intelligible differentiation between financial debts and operational debts, which are unsecured and this is directly related to purpose of IBC.

CONCLUSION

This judgment of the SC of India shall certainly impact a wide range of stakeholders in corporate insolvency. The SC has also provided much needed clarity on the roles and responsibilities of the resolution professionals and in the light of this judgment, the resolution professionals are only permitted to discharge certain administrative functions.

The SC, in addition to the strongly endorsing the IBC, has upheld the constitutional validity of the same and has paved way for its effective implementation by the Government. The idea of the SC behind this judgment was to highlight and reiterate the original intention of the IBC, which is to effectively revive and resolve any insolvency being faced by any corporate debtor.

However, the true impact of this judgment and its implementation shall rest on the quantum of speedy resolutions.

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SEAT OF ARBITRATION CAN BE THE PLACE OF ARBITRATION: AN ANALYSIS

INTRODUCTION

With the increasing commercialization and global transactions, the way businesses work today has changed tremendously, especially when it comes to transactions involving multinational companies from various jurisdictions. Consequentially, due to issues in conflict of laws between two or more jurisdictions, transactions involving entities from different jurisdictions invite the supervisory jurisdictions of their respective nation's legal system thus giving rise to substantial delays in international commercial arbitrations. In such a conflicting situation it becomes essential to understand the concept of seat and venue under the Arbitration and Conciliation Act, 1996.

CONCEPT OF SEAT AND VENUE

Seat of Arbitration:

The "seat" of arbitration refers to the applicable law administering the arbitration procedures. When laws of a particular jurisdiction are determined by the parties to govern the arbitral proceedings, then that law administers the said arbitral proceedings. However, in case the parties have not determined the law for governing the conduct and procedure of arbitration, expressly or by implication, then such arbitration shall be determined by the law of the place of the "seat" of arbitration.

Place of Arbitration:

Section 20 of the Arbitration and Conciliation Act, 1996 defines 'Place of Arbitration' as:

> *"(1) The parties are free to agree on the place of arbitration.*
>
> *(2) Failing any agreement referred to in sub-section (1), the place of arbitration shall be determined by the arbitral tribunal having regard to the circumstances of the case, including the convenience of the parties.*
>
> *(3) Notwithstanding sub-section (1) or sub-section (2), the arbitral tribunal may, unless otherwise agreed by the parties, meet at any place it considers appropriate for consultation among its members, for hearing witnesses, experts or the parties, or for inspection of documents, goods or other property"*[5].

It is understood that this section not only enables the parties to choose the "place" of arbitration thereby completely permitting the parties to choose the favorable legal systems and the procedure in which the arbitration can be governed. In short, the place of hearing is the physical location where the hearing is held.

If the "seat" or "place" of the arbitration is not determined in the arbitration agreement executed between the parties, then the said arbitration agreements shall be read and interpreted in a comprehensive way to settle the "seat" along with the jurisdiction of the adjudicating court. However, in the event the parties have mutually agreed on and have determined a "venue" but not a "seat" in their arbitration agreement, then the adjudicating court shall consider the connected factors to determine the "seat" of arbitration.

SEAT OF ARBITRATION CAN BE PLACE OF ARBITRATION: AN INSIGHT

The Hon'ble Supreme Court of India **("SC")** on 25th September 2018 in Union of India vs. Hardy Exploration and Production (India) Inc. [6], decided on the applicability of laws in a post-award arbitration proceedings in a case where the parties have agreed upon only the "venue" of arbitration and not the "seat" of arbitration. In the present case, Hardy

[5] Section 20 of the Arbitration and Conciliation Act, 1996.
[6] (2018) 7 SCC374; https://www.sci.gov.in/supremecourt/2016/34525/34525_2016_Judgement_25-Sep-2018.pdf.

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Exploration and Production (India) Inc. **("Hardy Exploration")** entered into a production-sharing contract with the Indian Government for the extraction, development and production of hydrocarbons in a geographic block in South-East India. Disputes arose between the parties with regard to appraisal period and relinquishment of rights of Hardy Exploration and thus it was referred to arbitration by Hardy Exploration. The arbitration clause in the agreement specified Kuala Lumpur, Malaysia as the "venue" of the arbitration. Arbitration was conducted in Kuala Lumpur. In 2013, a final award was rendered in favor of Hardy Exploration allowing Hardy Exploration back into the block for another three (3) years and also awarded an interest on its original investment in the said block until it was reinstalled. The legal propriety of said award was challenged by the Indian Government under *Section 34*[7] before the Hon'ble High Court of Delhi. Hardy Exploration resisted the Section 34 challenge on the basis that Indian Courts could not have jurisdiction to entertain the challenge under Section 34 because the seat of the arbitration was Kuala Lumpur and Part I of the Arbitration Act would not be applicable. The Hon'ble High Court of Delhi ruled in favour of Hardy Exploration. The Indian Government appealed the decision of Hon'ble High Court of Delhi before the Hon'ble SC.

The Hon'ble SC interpreted the arbitration agreement between the parties and the reference to the UNCITRAL Model Law on International Commercial Arbitration 1985 ("Model Law") to determine the seat of arbitration. The question that arose before the SC in this case was:

> *"17. When the arbitration agreement specifies the "venue" for holding the arbitration sittings by the arbitrators but does not specify the "seat", then on what basis and by which principle, the parties have to decide the place of "seat"…"*

Depending upon the facts, the SC ruled that since the arbitration agreement did not provide for a seat, the determination of the juridical seat would have to be made by the arbitral tribunal. The SC held that merely because the arbitrator had held the meeting at Kuala Lumpur and signed the award does not amount to determination of seat. The sittings at various places are relatable to venue. It cannot be equated with the seat of arbitration or place of arbitration. On this basis, the SC set aside the decision of the Hon'ble High Court of Delhi and found that Indian courts would have jurisdiction to entertain the Section 34 challenge. The SC held that, when a "place" is agreed upon; it gets the status of seat which means the juridical seat. The terms "place" and "seat" are used interchangeably. When only the term "place" is stated or mentioned and no other condition is postulated, it is equivalent to "seat" and that finalises the facet of jurisdiction. But, if a condition precedent is attached to the term "place", the said condition has to be satisfied so that the place can become equivalent to seat.

In another case of *Enercon (India) Ltd and Others vs. Enercon GmbH and Another*[8], the SC faced similar questions with regards to the "seat" and "venue" of arbitration.

The juridical seat of arbitration comprises of the choice of that country's compelling law. In this case, a distinct situation arose wherein the "venue" of arbitration was specified in the arbitration agreement and "seat" of arbitration was not determined by the parties. As the "venue" of arbitration was specified to be London but there were no specifications of the "seat", the courts of UK were supposed to have original jurisdiction since it would be most closely connected, but Indian courts passed contra orders assuming its jurisdiction due to the purview for interpretation in the recitals of the arbitration agreement. At last Hon'ble SC resolved the issues of the parties relying on judgments of numerous foreign and Indian courts and also determined the law for international arbitration for disputes in India, i.e.:

> "*Where the parties have failed to choose the law governing the arbitration proceedings, those proceedings must be considered, at any rate prima facie, as being governed by the law of the country in which the arbitration is held, on the ground that it is the country most closely connected with the proceedings."*

[7] Section 34 of The Arbitration and Conciliation Act, 1996 states Application for setting aside of an arbitral award.

[8] (2014) 5 SCC 1

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Similarly, in the case of ***Shashoua vs. Sharma***[9]**,** the arbitration agreement provided for London as the "venue" of the arbitration but was silent as to the "seat". The English High Court concluded that London would be the seat of the arbitration because it was designated as the arbitral "venue" and because the arbitration clause provided for arbitration to be conducted in accordance with the ICC Rules. The SC held that if the parties had intended to name a "venue" that was distinct from the "seat" they would have specifically named both.

Taking into considerations the above landmark judgments, it can be determined that the place of arbitration can be understood to be the seat of arbitration if the juridical seat of arbitration is not mentioned in the agreement, depending upon the facts and circumstances of each case.

CONCLUSION

Thus, the Hon'ble SC in its recent ruling in the case of *Union of India vs. Hardy Exploration and Production (India) Inc.* clarified the long standing conflict between "seat" and "venue" in the arbitration agreement.

The SC ruled that the "venue" of an arbitration could not, *ipso facto*, be considered to be its "seat" and that the "place" could be equated with "seat" only if it had no conditions precedent attached to it. The term "place" does not ipso facto become equivalent to "seat", and only when the conditions precedents are satisfied can the "place" take the position of "seat". On the other hand, however, the term "venue" can become "seat", if something else is added to it as a concomitant.

Though the SC determined this ruling, the reality that whether a "place" or "venue" is the seat depends on a contextual analysis of the facts of the case. It thus becomes pertinent to be aware that the arbitration clauses be drafted in a manner which is not ambiguous and is capable of reflecting the true intentions of the parties. In case of conflict between "seat" and "venue", the arbitration agreement should be capable to impart a fair and reasonable understanding of the parties to avoid any future jurisdictional disputes.

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[9] [2009] EWHC 957

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LEX REVISORS

1. **MCA introduces E- Form AGILE (INC-35)**

The Ministry of Corporate Affairs *vide* its notification dated 29th March, 2019 by insertion of Rule 38A, has notified the Central Government that, the application for incorporation of a company under Rule 38 of Companies (Incorporation) Third Amendment Rules, shall be accompanied by an e-form AGILE (INC-35) containing an application for registration of (a) GSTIN (Goods and Services Tax Identification Number) with effect from 31st March, 2019; (b) EPFO (Employees Provident Fund Organization) with effect from 8th April, 2019; and (c) ESIC (Employee State Insurance Corporation) with effect from 15th April, 2019.

The objective behind filing an e-form AGILE along with SPICe *(Simplified Proforma for Incorporating Company electronically)* e-form (INC-32), at the time of registration of the company is that the company would automatically be enrolled for GST, ESIC and EPFO. It would enable a single window clearance, where along with the registration of a new company taking registrations under the mentioned authorities would be simplified and hassle-free.

[For details refer to *http://www.mca.gov.in/Ministry/pdf/companiesINC3rdAmendmentRules_30032019.pdf*]

2. **Cabinet approves National Policy on Software Products, 2019**

The National Policy on Software Products 2019 received approval from Union Cabinet, chaired by the Prime Minister Shri Narendra Modi on 28th February 2019 to develop India as a Software Product Nation. The policy aims to formulate several schemes, initiatives, projects and measures for the development of software products sector in the country. The policy has a robust outlay with five main objectives to establish the country as a global software product nation. The policy also aims a ten-fold increase in Indian software industry's share in the global markets.

[For details refer to *www.pib.nic.in/Pressreleaseshare.aspx?PRID=1566747*]

3. **Cabinet approves the National Mineral Policy, 2019**

The National Mineral Policy, 2019 received approval from Union Cabinet, chaired by the Prime Minister Shri Narendra Modi on 28th February 2019 to ensure transparency, better regulation and enforcement, balanced social and economic growth as well as sustainable mining practices. It replaces the National Mineral Policy, 2008 and the foundation of its review was established in *Common Cause versus Union of India & others*. This 2019 Policy aims for a sustainable mining sector development while catering to the issues of affected persons especially in the tribal areas. It also envisages focusing on 'Make in India' initiative and Gender sensitivity issues. The Policy proposes to grant the status of industry to "mining activity" to boost financing of mining for private sector and for acquisitions of mineral assets in other countries by private sector. It further aims to propose a long term export import policy for the mineral sector to provide stability and as an incentive for investing in large scale commercial mining activity.

[For details refer to, www.pib.nic.in/*Pressreleaseshare.aspx?PRID=1566734*]

4. **SEBI's Circular on Physical Settlement of Stock Derivatives dated 8th February 2019**

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The Securities and Exchange Board of India *vide* its circular dated 8th February, 2019 has stated that in addition to the existing schedule of stock derivatives moving to physical settlement, the derivatives on stock meeting the eligibility criteria specified by the regulator herein will also be physically settled. The circular aims to curb excessive speculation, which creates excessive volatility in the market by restraining daily volatility of stock to 10%. Under physical settlement, traders will have to compulsorily take delivery of shares on the expiry day against their derivative positions. The proposed circular aims to bring in a balance between equity cash and derivative segments.

[For details refer to, *https://www.sebi.gov.in/legal/circulars/feb-2019/physical-settlement-of-stock-derivatives_42021.html*]

5. **SEBI's Circular Format for annual secretarial audit report and annual secretarial compliance report for listed entities and their material subsidiaries**

The Securities and Exchange Board of India *vide* its circular dated 8th February, 2019 has introduced a new Regulation 24A to SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 which states that, *"Every listed entity and its material unlisted subsidiaries incorporated in India shall undertake secretarial audit and shall annex with its annual report, a secretarial audit report, given by a company secretary in practice, in such form as may be prescribed with effect from the year ended March 31, 2019."* This was earlier recommended in a report by the Kotak Committee and thus later this circular was issued. The annual secretarial compliance report is an additional requirement and SEBI has also prescribed the format, as Annexure A to their original circular, in which the report must be produced by practicing company secretaries. The purpose of inserting this regulation is to keep a check on the compliance of listed entity and its material unlisted subsidiaries to applicable SEBI Regulations and circulars and/or guidelines issued there under.

[For details refer to, *https://www.sebi.gov.in/legal/circulars/feb-2019/format-for-annual-secretarial-audit-report-and-annual-secretarial-compliance-report-for-listed-entities-and-their-material-subsidiaries_42015.html*]

6. **Empanelment of insolvency professionals to be appointed as administrators**

The Securities and Exchange Board of India has issued a circular dated 2nd April 2019 pertaining to empanelment of insolvency professionals to be appointed as administrators and other incidental matters under the regulator's framework. An administrator has to be a person registered as an insolvency professional with the Insolvency and Bankruptcy Board of India (IBBI) and empanelled with the board from time to time. According to the circular, during the pendency of the insolvency assignment, the appointed administrator shall neither withdraw consent nor surrender registration to the IBBI or membership to the Insolvency Professional Agency (IPA). The main objective behind this is to enable independent and autonomous insolvency proceedings and ensure the investor's money has been refunded.

[For details refer to, *https://www.sebi.gov.in/legal/circulars/apr-2019/empanelment-of-insolvency-professionals-ips-to-be-appointed-as-administrator-remuneration-and-other-incidental-and-connected-matters-under-the-securities-and-exchange-board-of-india-appointment-of-_42592.html*]

7. **Court cannot appoint arbitrator when the contract containing arbitration clause is insufficiently stamped**

The Hon'ble Supreme Court of India on 10th April 2019, in the case of *Garware Ropes Limited vs. Coastal Marine Constructions & Engineering Limited, Civil Appeal No. 3631 of 2019* examined the effect of an arbitration clause

contained in an insufficiently stamped contract and held that such arbitration clause has no existence until the contract is duly stamped. The Court was of the opinion that, "*When an arbitration clause is contained "in a contract", it is significant that the agreement only becomes a contract if it is enforceable by law. Under the Indian Stamp Act, an agreement does not become a contract, i.e., not enforceable by law, unless it is duly stamped.*" Hence, the Stamp Act applies to the agreement or transaction as a whole. *Therefore, even a plain reading of Section 11(6A), when read with Section 7(2) of the Arbitration and Conciliation Act 1996 and Section 2(h) of the Indian Contract Act 1872, would make it clear that an arbitration clause in an agreement would not exist when it is not enforceable by law.*" Hence, the Court cannot appoint any arbitrator if the agreement itself is not enforceable.

[For details refer to, *https://www.sci.gov.in/supremecourt/2018/12561/12561_2018_Judgement_10-Apr-2019.pdf*]

8. Amendment under Section 7 (1) of IBC, 2016

The Ministry of Corporate Affairs *vide* its notification dated 1st March, 2019 states that the following persons may file an application for initiating corporate insolvency resolution process against a corporate debtor before the Adjudicating Authority, on behalf of the financial creditor: (a) a guardian; (b) an executor or administrator of an estate of a financial creditor; (c) a trustee (including a debenture trustee); *and* (d) a person duly authorised by the Board of Directors of a Company.

[For details refer to, *https://www.ibbi.gov.in/legal-framework/notifications*]