

# Effect of Pending Arbitration Proceedings and Initiation of CIRP by Operational Creditor

## Abstract

Under the scheme of Insolvency and Bankruptcy Code, 2016, a pending arbitration proceeding act as a pre existing dispute and hence bars initiation of insolvency proceeding by an Operational Creditor. However this rule of general application is subject to certain exceptions as held in various judgements of NCLT and NCLAT. The author seeks to examine and clearly bring out a picture of those exceptions where a proceeding under the Arbitration and Conciliation Act, 1996 does not act as a bar to insolvency resolution process.

**Keywords:** Arbitration and Insolvency; Arbitration as A Bar to Insolvency; Pre Existing Dispute.

## Introduction

Under the Insolvency & Bankruptcy Code, 2016, an Operational Creditor can initiate insolvency resolution against any defaulting Corporate Debtor, only if there is no pre existing dispute regarding the transaction.<sup>1</sup> An ongoing arbitration proceeding is indeed a dispute which would prevent the Operational Creditor from initiating the Insolvency Resolution Process. However, through various judgements, the NCLAT has clarified the extent to which a proceeding under Arbitration and Conciliation Act, 1996 bars the Operational Creditor from initiating the Insolvency Resolution against any defaulting Company<sup>2</sup>. In this article, various important rulings of NCLAT are being analysed to determine the scope of impact of arbitration proceedings on Insolvency Initiation by the Operational Creditor.

## Aim of the Study

The author aims to analyse the judgements of NCLT and NCLAT regarding pending arbitration proceedings and their impact on initiation of insolvency resolution process by an Operational Creditor.

## Whether Arbitration Proceeding is a Dispute

Section 5(6) of the I&B Code, 2016 defines dispute as:

“dispute” includes a suit or arbitration proceedings relating to—

(a) the existence of the amount of debt;

(b) the quality of goods or service; or

(c) the breach of a representation or warranty;”

This definition includes arbitration proceedings in the ambit and meaning of the term dispute for the purposes of CIRP in Part II of the Code. The definition of dispute becomes relevant in case an Operational Creditor chooses to initiate CIRP against a defaulting Corporate Debtor under Section 8 of the Code. As per Section 8 of the Code, the Operational Creditor is required to serve, upon the occurrence of a default, a notice to the corporate debtor wherein a period of ten days is to be provided for the debtor to respond to the notice proving the existence of a ‘dispute’. In case, the Corporate Debtor is able to prove a pre-existing dispute, then the Operational Creditor is barred for initiating CIRP against the Corporate Debtor.

In such a situation, it becomes imperative to determine the scope of dispute for the purposes of the I&B Code, 2016. As per the definition of the term “Dispute” given in Section 5 (6) of the Code, it includes any arbitration proceedings. It implies that an Operational Creditor cannot initiate Insolvency Proceedings against a Corporate Debtor in cases where an arbitral proceeding is ongoing. Any pending arbitral proceeding shall act as a bar to initiation of insolvency proceedings in case of Operational Creditors. Now, it is important to understand the meaning of “Arbitration Proceeding”.



**Ganesh Prasad Pandey**

Assistant Professor,  
Deptt. of Law,  
Chanakya National Law  
University,  
Patna

**Meaning of “Arbitration Proceedings”**

Under Arbitration, if there is prior agreement between the parties to refer any dispute to the arbitration before referring to any court or tribunal. Such an arbitration clause is binding on the parties and the arbitration proceedings can be invoked only by the parties to the arbitration agreement. An arbitration proceeding can be invoked by sending a notice for initiating the arbitration as per the terms of the arbitration clause in the agreement. Section 21 of Arbitration Act, 1996 provides that the arbitral proceedings commence on the date on which a request for that dispute to be referred to arbitration is received by the respondent. Further, section 3(2) of the Arbitration Act, 1996 provides that the communication is deemed to have been received on the day it is so delivered. Reading sections 21 and 3(2) in conjunction, an arbitral proceeding is commenced the moment the debtor sends a written communication requesting the reference to arbitration, which is received by the creditor.

So, once the notice for arbitration has been sent by either party to the other for initiating the arbitration proceedings and the same has been delivered, an arbitration proceeding for the purposes of the I&B Code, 2016 is said to have become pending and thereby evidencing a “pre-existing” dispute.

**Can Arbitration proceedings be started during moratorium**

In the case of *Alchemist Asset Reconstruction Company Limited Vs. M/s Hotel Gaudavan Private Limited & Ors*<sup>3</sup>, passed on October 23, 2017, the Hon’ble apex court has held that the effect of the Moratorium that comes into effect vide Section 14 (1) (a) of the Insolvency and Bankruptcy Code, 2016 (“I&B Code”) is that the arbitration that may be instituted after the aforesaid Moratorium is *non est* in law.

**Whether an Arbitration Agreement is itself a bar to CIRP U/s 8**

Can an Operational Creditor be barred from initiating the CIRP U/s 8 of I&B Code, if it has entered into an arbitration agreement with the Corporate Debtor. In the case of *Achenbach Buschhütten CmbH & Co vs. Arcotech Ltd*<sup>4</sup>, it was argued that an arbitration agreement would bar the Operational Creditor from approaching the Adjudicating Authority for initiating the CIRP. The Hon’ble NCLAT while rejecting this argument held that an Arbitration agreement won’t come under the scope and meaning of dispute until it has commenced.

**Whether Challenge to Arbitral Award comes under Dispute**

The Hon’ble NCLAT in the case of *Annapurna Infrastructure Pvt Ltd & Anor v Soril Infra Resources Ltd*<sup>5</sup>, has held that an arbitral award concludes the disputes between parties and is a valid record of default under the Indian Insolvency and Bankruptcy Code, 2016 (the IBC or Code) and that the pendency of proceedings for execution of an arbitral award or a judgment and decree does not bar an operational creditor from preferring any petition under the Code.

**Arbitral Award is an Evidence of Default**

In the case of *Ksheeraabd Constructions Pvt. Ltd. Vs. Vijay Nirman Company Pvt. Ltd*<sup>6</sup>, Hon’ble NCLAT has held that for the purpose of Section 9 of the ‘I&B Code’, the application to be preferred under Form-5 of the Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016 (hereinafter referred to as “Rules, 2016”) as per which, the order passed by Arbitral panel/Arbitral Tribunal has been treated to be one of the documents/records and evidence of default, as apparent from Part V of Form 5.

As an order of arbitral tribunal decides the dispute, the same can undoubtedly be considered as a binding document/evidence of default. As held by the NCLAT in *Soni Infra* case, the arbitral award shall act as an evidence of default and any proceeding for the execution of the same does not create any bar on initiation of insolvency against the defaulting Corporate Debtor.

**Conclusion**

It is interesting to see that NCLAT has gone on to strike a balance between the I&B Code, 2016 and Arbitration Act, 1996 through its judicial pronouncements. As the NCLAT has held in the case of *Arcotech Ltd (Supra)* that an arbitration agreement shall not be a bar to initiation of insolvency proceedings by an operational creditor and that a dispute within the meaning of Section 5(6) is to be construed only after the arbitration proceedings are to be commenced. So, it can be safely concluded that though “Arbitration Agreement” in itself is not a bar to the Operation Creditor for initiating the CIRP against the defaulting Corporate debtor, once the arbitration proceedings have been commenced as per Section 21 of the Arbitration Act, 1996, the Operational Creditor is precluded from initiating CIRP against the Corporate Debtor during the pendency of the arbitration proceedings. However, as per the judgement of Hon’ble NCLAT in case of *Soril Infra (Supra)* the pendency of proceedings for execution of an arbitral award or a judgment and decree does not bar an operational creditor from preferring any petition under the Code.

**References**

1. See Section 8 of Insolvency and Bankruptcy Code, 2016
2. See Section 5(6) of the I&B Code, 2016.
3. *Alchemist Asset Reconstruction Company Limited Vs. M/s Hotel Gaudavan Private Limited & Ors, Civil Appeal number 16929 of 2017 SC*
4. *Achenbach Buschhütten CmbH & Co vs. Arcotech Ltd, CA (AT) (Insolvency) No. 97 of 2017*
5. *Annapurna Infrastructure Pvt Ltd & Anor v Soril Infra Resources Ltd, Company Appeal (AT) (Insolvency) No. 32 of 2017*
6. *Ksheeraabd Constructions Pvt. Ltd. Vs. Vijay Nirman Company Pvt. Ltd., Company Appeal (AT) (Insolvency) No. 167 of 2017, Date of Order: 20.11.2017.*