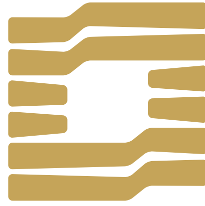

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DISPUTE RESOLUTION NEWSLETTER

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It gives us immense pleasure to circulate the April 2024 edition of the Luthra and Luthra Law Offices India's Dispute Resolution Newsletter. In this edition, we have primarily focused on the recent legal developments in the field of Arbitration, Insolvency, Civil, Commercial and Taxation Laws. Accordingly, we have covered key judgments passed by the Hon'ble Supreme Court, High Court(s) and other tribunals for the period of February - March 2024. We hope you enjoy reading our newsletter.

SUPREME COURT

Claims submitted with proof by a Creditor cannot be overlooked even if filed under a wrong Form[1]

The Hon'ble Supreme Court through the bench comprising of the Chief Justice DY Chandrachud, Justices JB Pardiwala and Manoj Mishra have laid down the law that Form(s) prescribed, under Insolvency and Bankruptcy Code, 2016 ("**IBC**") and Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 ("**CIRP Regulations**"), for submitting claims with the Resolution Professional ("**RP**") during the CIRP are directory in nature. It has also been held that a claim cannot be rejected merely because it was submitted in a different Form.

In the facts of the case, the Appellant, a statutory body, had allotted a plot to the Corporate Debtor by way of lease for a residential project, against payment of premium. The Corporate Debtor defaulted in payments of instalments towards premium. Consequently, CIRP proceedings were initiated against the Corporate Debtor. The Appellant submitted its Claim as a Financial Creditor. However, the RP treated the Appellant as an Operational Creditor, and accordingly, called the Appellant to submit another form, which the Appellant did not comply with. In the meantime, the Committee of Creditors ('**CoC**') approved a resolution plan and presented it to Adjudicating Authority NCLT, which was also approved. Thereafter, the Appellant filed application(s) before NCLT challenging the resolution plan, the RP's decision to treat the Appellant as an Operational Creditor, all further actions, and recalling of NCLT's plan approval order. These challenges were rejected by NCLT, and the Appeal was also dismissed by National Company Law Appellate Tribunal ("**NCLAT**"). Consequently, the Appellant preferred an Appeal before the Hon'ble Supreme Court.

The Hon'ble Supreme Court extensively analysed the provisions of IBC as well as the CIRP Regulations. The Apex Court specifically referred to Regulation 7 (Claims by Operational Creditors), Regulation 8 (Claims by Financial Creditors), Regulation 12 (Submission of Proof of Claims) and Regulation 13 (Verification of Claims) of the CIRP Regulations and observed that language of Regulation(s) 7 and 8 is rooted in claimants own understanding if they are a Financial Creditor or Operational Creditor. Further, the claims must be accompanied by the proof in terms of Regulation 12 which are to be verified by the RP in terms of Regulation 13.

[1] *Greater Noida Industrial Development Authority v. Prabhjit Singh Soni and Another*, 2024 SCC OnLine SC 122.

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Upon verification, the RP must maintain a list of creditors, which is to be updated in terms of Regulation 12A (Updation of claim). Thus, the Court concluded the essence of the procedure that the requirement of Form to be submitted was directory and not mandatory, but the proof of claim was important. Further, the Court observed that the NCLT has the inherent power to recall its own Order.

The Supreme Court, in the case at hand, held that the grounds taken by the Appellant in the application(s) were valid for seeking recall of the order approving the resolution plan. Further, the Court also observed that the Resolution Plan did not meet the requirements of Section 30(2) of the IBC and held that without the approval of the Appellant, a Statutory Authority, the Resolution Plan cannot be implemented. The Supreme Court while allowing the Appeal set aside the order approving the resolution plan and remanded the resolution plan back to the CoC for being reconsidered as per parameters set out under IBC.

The judgment is a substantial addition to the insolvency jurisprudence in India as it holds that the RP cannot reject a claim merely on the ground that it has not been submitted by the Creditor in the prescribed Form, provided that the Creditor has submitted supporting proof for its claim. Further, the judgment reaffirms that the NCLT has the inherent power to recall its own order.

Goods kept outside notified bonded warehouse with proper officer's permission not liable for confiscation under Customs Act[2]

In a significant ruling, the Supreme Court, through a bench comprising Justice Ujjal Bhuyan and Justice B.V. Nagarathna, have held that goods kept outside a notified bonded warehouse but within the importer's premises with the explicit permission of the proper officer cannot be treated as improperly removed from the warehouse, thus, cannot be made liable for confiscation under Section 71 of the Customs Act, 1962 ("**CA Act**").

The Appellant had imported second-hand steel mill machinery and parts. These parts were stored in a public bonded warehouse notified within the Appellant's factory premises, without payment of customs duty. Owing to heavy rains and a paucity of space, appellant sought and was granted permission by the Superintendent of Customs to keep a portion of the goods outside the bonded warehouse while still within the confines of the factory premises.

The Custom officials while conducting search confiscated the cases which were placed outside the bonded warehouse and imposed duty and penalties on the Appellant for the confiscated and lost cases. The duty and penalties were confirmed by the Commissioner of Customs and Central Excise as well as Customs, Excise and Service Tax Appellate Tribunal ("**CESTAT**").

[2] *Bisco v Commissioner of Customs and Central Excise,* 2024 INSC 231.

The Appellant preferred an Appeal to Hon'ble Supreme Court, which was partially allowed. The Court held that the demands related to the cases placed outside bonded warehouse was unjustified as they were kept outside with the permission in terms of Section 64(d) of the CA Act. However, demands for duty and penalty for missing cases was upheld for their being unauthorized removal.

This judgment holds immense significance as it clarifies the applicability of Section 71 of the CA Act in cases where goods are kept outside the bonded warehouse with appropriate permission. The ruling emphasizes that such goods should not be treated as improperly removed from the warehouse, and consequently, they are not liable for confiscation or penalties. This judgment provides much-needed relief to importers who may face similar situations due to unforeseen circumstances such as adverse weather conditions or lack of storage space within the designated bonded warehouse. The apex court's decision also highlights the importance of obtaining proper permission from the appropriate authorities and maintaining clear communication and documentation in such cases to avoid potential legal complications.

HIGH COURT

Arbitrator's appointment hit by Section 12(5) read with Seventh Schedule of Arbitration Act cannot be upheld despite finality of Arbitral Institution's decision[3]

The Bombay High Court, through Justice Bharati Dangre, has held that an arbitrator's appointment, which is hit by Section 12(5) read with the Seventh Schedule of the Arbitration and Conciliation Act, 1996 ["**Arbitration Act**"], cannot be upheld despite the finality accorded to the decision of an arbitral institution under its rules.

The case involved a dispute arising out of three sale contracts for the supply of US Coal. The parties had agreed to refer their disputes to the Mumbai Centre for International Arbitration (MCIA) under the MCIA Rules, 2017.

Upon a dispute arising, MCIA appointed a Partner at a law firm as the Sole Arbitrator. Petitioners objected to the appointment on the ground that arbitrator's law firm had previously represented Respondent's group companies, rendering the arbitrator ineligible under Section 12(5) r/w the Seventh Schedule of the Arbitration Act. Despite the petitioner's objections, the MCIA Council rejected the challenge to the arbitrator's appointment.

Aggrieved, the petitioner filed petitions under Section 14 r/w Section 11 of the Arbitration Act before the Bombay High Court, seeking termination of the arbitrator's mandate. The

[3] *Era International v. Aditya Birla Global Trading India Private Limited & Ors.*, 2024 SCC OnLine Bom 835.

respondents contended that the petition was not maintainable, as the decision of the MCIA Council was final and binding under the MCIA Rules.

The High Court, however, held that the remedy under Section 14(2) of the Arbitration Act, which allows a party to apply to the Court to decide on the termination of an arbitrator's mandate, cannot be excluded merely because the parties have agreed to institutional arbitration. The Court emphasized that the Arbitration Act does not distinguish between *ad hoc* and institutional arbitration, and the stages of judicial intervention permitted by the Act remain available to parties in both facets.

The Court further held that an arbitrator who falls within the ambit of Section 12(5) read with the Seventh Schedule becomes *de jure* ineligible to act as an arbitrator, and this ineligibility goes to the root of the appointment. The only way to waive this ineligibility is through an express agreement in writing between the parties, as per the proviso to Section 12(5) of Arbitration Act. Applying these principles to the case at hand, the Court found that the arbitrator's appointment was indeed hit by the Seventh Schedule, as her law firm had a significant commercial relationship with the Respondents. The Court directed the MCIA to substitute the arbitrator and appoint an independent arbitrator within four weeks.

This judgment is significant as it clarifies that the provisions of the Arbitration Act, particularly those related to the independence and impartiality of arbitrators, will prevail over institutional rules in cases of conflict. The ruling emphasizes the importance of ensuring the integrity of the arbitral process and the need for strict adherence to the statutory requirements for arbitrator appointments.

Commercial Courts Act, 2015 takes away right of appeal even in suits instituted prior to its enactment and subsequently transferred to Commercial Division[4]

In a significant ruling, a Division Bench of the Calcutta High Court, comprising Justice I.P. Mukerji and Justice Biswaroop Chowdhury, has held that the Commercial Courts Act, 2015 ("CC Act") takes away the right of appeal, whether substantive or procedural, even in suits instituted prior to its enactment and subsequently transferred to the Commercial Division.

The case involved appeals filed by the Appellants against an order passed by a single judge of the High Court dismissing their applications for amendment of the written statement and for leave to adduce further evidence by recalling witness in a commercial suit. The Respondent objected to the maintainability of the appeals on the ground that under Section 13 of the CC Act, only specified appeals can be entertained by the court, and the impugned order was not appealable.

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[4] *Sabri Properties Pvt. Ltd. & Ors. v. Frostees Exports (India) Pvt. Ltd.*, 2024 SCC OnLine Cal 2530.

The Appellants contended that since the suit was instituted as an ordinary suit in 2015 and subsequently transferred to the Commercial Division after the coming into force of the CC Act, the right of appeal against the impugned order available under Clause 15 of the Letters Patent was preserved and not taken away by the transfer of the suit.

The High Court held that Section 13 of the CC Act relates to the appealability of orders passed by a court exercising commercial jurisdiction, and it clearly stated that irrespective of anything laid down in any other law, including the Letters Patent of a High Court, an appeal would lie only from those judgments, decrees, and orders provided therein and from no other.

The Court held that Section 15(3) of the CC Act makes it clear that even in suits where the procedure for getting the suit ready for hearing was not complete, the provisions of the CC Act would apply to complete those procedures. Moreover, Section 21 of the CC Act provided that it shall have an overriding effect over any inconsistent provisions in any other law. Accordingly, the High Court held that the CC Act expressly takes away any right of appeal, whether substantive or procedural, that a litigant had before the transfer of a suit to the Commercial Division, and that after such transfer, the provisions of the Act would apply to the suit. Consequently, the Appellants had no right of appeal against the impugned order, and the appeals were dismissed on the ground of maintainability.

This judgment is significant as it clarifies the applicability of the CC Act to suits instituted prior to its enactment and subsequently transferred to the Commercial Division. It emphasizes that the CC Act has an overriding effect and takes away the right of appeal, even if such right existed under any other law prior to the transfer of the suit. The ruling emphasizes on the need for litigants to be mindful of the provisions of the CC Act while pursuing remedies in commercial disputes.

NCLAT

Secured Creditors have the right to choose the method of debt realization in liquidation proceedings[5]

The NCLAT has upheld the right of a secured creditor to choose the method of realizing their debt in liquidation proceedings under the IBC. The judgment, delivered by a three-member bench comprising Justice M. Venugopal, Justice Sharad Kumar Sharma, and Mr. Jatindranath Swain, emphasizes the primacy of a secured creditor's rights and the overriding effect of the IBC over the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 ("**SARFAESI Act**").

The Appellant, a financial creditor, challenged the decision of the liquidator classifying the Appellant as an unsecured financial creditor, despite having a significant collateral security

[5] *Canara Bank Asset Recovery Management Branch v. S. Rajendran*, 2024 SCC OnLine NCLAT 390.

provided by the Corporate Guarantor. The Appellant sought to enforce its rights as a secured creditor under the Transfer of Property Act, 1882, ("**TPA**") while the Respondent contended that the Appellant failed to provide necessary documents to establish its security interest, as required by the IBBI (Liquidation Process) Regulations, 2016 ("**Liquidation Regulations**"). The Adjudicating Authority observed that non-registration of a security interest would not vitiate debt recovery, however, in view of provisions contained in Companies Act, 2013, IBC and Liquidation Regulations, the security interest created becomes void against the Liquidator. The Appellant approached NCLAT impugning the order passed by the Adjudicating Authority.

The NCLAT allowed the appeal and directed that the Appellant Bank be treated as a secured creditor in the liquidation proceedings. The NCLAT noted that a secured creditor has the right to prefer a winding-up petition after obtaining a decree from the Debt Recovery Tribunal and is not obligated to resort to its security. The Bench emphasized that it is the duty of the Adjudicating Authority to consider the rights of a secured creditor to realize its security interest before the assets of the corporate debtor are handed over to the liquidator. The NCLAT also highlighted the legislative intent behind Sections 52 and 53 of the IBC, which provide options for secured creditors to either enforce their security interest or relinquish it and participate in the distribution of assets.

Crucially, NCLAT held that since IBC overrides the SARFAESI Act, the liquidator ought not prefer a petition praying for directions to the Secured Creditor, to respond to his request for relinquishment of Security Interest over the Assets of the Corporate Debtor. The bench held, in the facts of the case, that the liquidator's decision to classify the appellant as an unsecured financial creditor was illegal and invalid, as it contravened the Appellant's statutory rights.

This ruling is significant as it clarifies the interplay between the IBC and the SARFAESI Act, affirming the primacy of the IBC in liquidation proceedings. The judgment also serves as a reminder to liquidators to respect the rights of secured creditors and not compel them to relinquish their security interest. The NCLAT's decision is expected to provide greater certainty and protection to secured creditors in insolvency proceedings, reinforcing the objectives of the IBC in facilitating a fair and efficient resolution process.

CESTAT

CESTAT distinguishes between 'Commission' and 'Incentive' received by air freight agents; holds 'Incentive' not liable to service tax under Business Auxiliary Services category[6]

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[6] *Wig Air Freight Pvt. Ltd. v. The Commissioner of Central Goods and Service Tax, New Delhi*, Service Tax Appeal No. 50177 of 2019 with Service Tax Appeal No. 50345 of 2019 (CESTAT, New Delhi).

CESTAT has held that incentives received by an air freight agent from airlines are not liable to service tax under the category of Business Auxiliary Services ("**BAS**"). The judgment was delivered by a bench comprising Ms. Binu Tamta, Member (Judicial) and Mr. P.V. Subba Rao, Member (Technical).

The Appellant had received amounts termed as 'incentives', 'discounts', and 'market price adjustments' from airlines. The Revenue Authorities levied service tax on these amounts under the BAS category, contending that they were in nature of consideration for services provided by the Appellant to the airlines in promoting their business.

The CESTAT, relying on the Larger Bench decision in *Kafila Hospitality & Travels Pvt. Ltd.*[7] held that for an activity to be considered as promotional under the BAS category, the service provider must actively promote or endorse the client's service. In the present case, the Appellant was merely negotiating with airlines for booking space or slots on behalf of their clients/exporters for shipment of their consignments and was not promoting the airlines' business.

The Tribunal distinguished between 'commission' and 'incentive', noting that 'commission' had a direct nexus to the booking service provided by the Appellant, whereas 'incentive' was the profit earned by the Appellant from the difference between the price charged to their clients and the price negotiated with the airlines. The CESTAT held that the incentive was not received on account of rendering any service but was a result of a trading activity, which is not taxable under the Finance Act, 1994.

Guided by the Larger Bench's observation that incentives are not to be construed as 'consideration' for the purpose of levying service tax, the CESTAT concluded that no service tax could be levied on the incentives received by the Appellant. The Tribunal also held that the terms 'incentive', 'discount', and 'market price adjustment' used in the Cargo Sales Report were all part of the same category of income and should be treated alike. Thus, the CESTAT allowed the appeal filed by the Appellant, setting aside the service tax demand on 'incentives' as well as the consequent interest and penalty.

This judgment is significant as it clarifies the tax treatment of incentives received by air freight agents from airlines and reaffirms the principle that service tax can only be levied on consideration received for rendering a taxable service. The ruling is expected to provide relief to air freight agents and bring clarity to the taxation of incentives in the service tax regime.

[7] *Kafila Hospitality & Travels Pvt. Ltd*. 2021 (47) GSTL 140 (Tri.-LB)

This newsletter is only for general informational purposes, and nothing in this newsletter could possibly constitute legal advice (which can only be given after being formally engaged and familiarizing ourselves with all the relevant facts). However, should you have any queries, require any assistance, or clarifications with regard to anything contained in this newsletter (or Dispute Resolution in general), please feel free to contact the Dispute Resolution team at any of the contacts listed below. © Luthra & Luthra Law Offices India 2024. All rights reserved.

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