A COMPARISON OF ARBITRATION OF INSOLVENCY DISPUTES IN INDIA AND IN THE INTERNATIONAL SPHERE

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Introduction

The concept of Arbitration provides for a form of dispute resolution where parties could discuss and settle their issue without reliance on any tradition dispute resolution system. This comes especially handy when it comes to international disputes, as disputes can be resolved without the need of any issues regarding the determination of jurisdiction.

Arbitration can also be made applicable for a multitude of issues, and hence is a versatile form of dispute resolution. The concept of Insolvency is one of the many areas which Arbitration seems to provide a solution over, but unlike other subjects of law, the issue of arbitrating insolvency disputes comes off as a double edged sword, as on one hand, convenience and issue of jurisdiction are removed, while on the other hand lies issue regarding enforcement, and how certain legislations partly or do not allow for Arbitration for the resolution of international insolvency disputes.

Hence, the main aim of this project is to firstly look into the interconnection between Arbitration and Insolvency, and on what manner is Arbitration used to resolve disputes of insolvency across the international spectrum. Lastly, an analysis will be made into the manner in which Arbitration and Insolvency are interlinked in India, and the changes which are to be brought to the present system.

Interlink between Arbitration and Insolvency

Arbitration and Insolvency are 2 topics, aiming to consolidating similar interests for parties, but at the same time, the manner in which the interests of the parties are protected are different in both cases.

Insolvency in simple terms aims at providing solutions to the creditors of a person who is unable to pay back its dues. It aims at maximizing the value of the debtor and its assets, and ensuring that all shareholders against whom a default is made have their defaults settled to such maximum extent as possible, if not fully[1].

Arbitration on the other hand is a form of alternate private dispute resolution system, in contrast to a case of insolvency involving multiple shareholders and interested parties. It is also a system in which parties have a say in the manner in which a resolution is to be approached, and provided that the jurisdiction of law allows for it, it is a means of settling any dispute between parties. The first main difference is regarding how Arbitration is a more personal and interest driven form of dispute resolution[2].

Insolvency is constantly driven by the various legal systems which are applicable on the party which is defaulting, creating a chance of having territorial disputes in international disputes. Unlike arbitration, it can be seen on how the procedure to be followed for Insolvency is fixed and strict, there lies specialized processes determined by law, with separate law and legal tribunals for enforcement being present[3]. This is mainly to ensure consolidation and resolution of all disputes associated with a default, and to ensure a streamlined process protecting the interests of those against whom a party has defaulted.

In the case of arbitration, it can be seen on how the element of confidentiality and processes being decided by the parties ensures that there lies an easier process in adjudicating disputes, ensuring that there lies an easy solution which is also cost effective in nature, and this is the reason why various economic powers encourage the adjudication of disputes through such means[4].

In the case of an insolvency dispute, the aggrieved parties have 2 means of ensuring that disputes are being adjudicated, through the insolvency process which has been set or through arbitration. This leads to a dispute, with regard to what is termed as "Choice of Forum"[5], where it can be seen on how parties to the dispute have to choose between the option of settling their

[1] CROSSROADS OF INSOLVENCY AND ARBITRATION, (Ishaan Madaan & Christian T. Campbell eds., 2022).
[2] *Id.*
[3] Shaun Matos, *ARBITRATION AGREEMENTS AND THE WINDING-UP PROCESS: RECONCILING COMPETING VALUES*, 72 INT. COMP. LAW Q. 309 (2023).
[4] Reza Shahrokhi & Akshay Gandotra, *Arbitration and Insolvency - Streamlining Scope of Arbitrability*, KLUWER ARBITR. BLOG 5 (2023).
[5] CROSSROADS OF INSOLVENCY AND ARBITRATION, *supra* note 1.

disputes via arbitration or through the means of insolvency process. Depending on the interests of the parties, they can evaluate and choose the method which is most favorable to them[6].

But often, we can see the role of countries deciding on insolvency laws to be binding on insolvency disputes, either partly or fully, as insolvency procedure is a consolidated set of procedures aimed at ensuring swift recovery of the default satisfying the interests of all the effected parties. Hence in such a situation, it can be seen on how there lies no choice for parties except for submitting themselves to the insolvency process.

Arbitration and Insolvency in the International Sphere

Various legislations interlink Arbitration and Insolvency in various manners, and this differentiation varies based on jurisdiction. The first major country which is evaluated would be the United States of America. In the USA, it could be seen on how the policy of distinguishing between core and non – core issues is important for determining of certain issues can be arbitrable, and the same can also be applied in the case of the topic of Insolvency also.

This distinguishment between various statutory law and Arbitration can be seen in all elements of US Law. This can be seen through the analysis of the case of *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth Inc*[7] in which it was held on how there lies a need to respect the capacity of foreign tribunals, and on how foreign tribunals are allowed to arbitrate on disputes. Further support is given for arbitration, as Justice Blackman states on how there lies no need to assume that arbitration cannot provide an adequate mechanism, that arbitration cannot resolve any dispute[8].

But, while reaffirming the benefits and imposing trust on arbitration, the element of clash of arbitration and domestic legislation (in this particular case regarding antitrust law) has been resolved through means of what is stated as "Second Look" Doctrine[9]. As per this doctrine, an arbitration can be undertaken on any matter, but for the enforcement of any arbitration award, there lies a need for courts to have a second look comparing the award with American Law and

[6] *Id.*
[7] Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth Inc, 473 U.S. 614 (1985)
[8] Robert B Kovacs, *A Transnational Approach to the Arbitrability of Insolvency Proceedings in International Arbitration*, 1 INT. INSOLV. INST. 118 (2012).
[9] *Id.*

to ensure that such award is not in conflict with such award[10].

The Second Look doctrine is only taking into consider Domestic Law, and law of the foreign country would not be taken into consideration to evaluate an arbitral award. This can be seen from the case of *Northrop Corporation. v Triad International Marketing S.A*[11] where the court held that an arbitral award is enforceable as it is not in contrary to the law of the USA, while for such international dispute which is between USA and Saudi Arabia, the particular award is unenforceable in Saudi Arabia.

It is not just law, but also public policy which checks if Arbitration is possible, and if any award is enforceable for such arbitration. It can be seen from the case of *Parsons & Whittemore Overseas Inc. v. Societe Generale De L'Industrie Du Papier*[12] where even when an award was enforceable by law, it was held to unenforceable as it would contravene US's public policy against Egypt due to the Arab – Israeli War[13].

Furthermore, it can also be seen through the case of *Shearson/American Express, Inc. v. McMahon*[14] on how with regard to any such issue, when there lies a competing interest between arbitration and any statute, exception to arbitration can be made when there lies an "contrary congressional command or intent".

Hence, from all of these cases, we can see on how Arbitration as a subject can be integrated with any and all domestic law provided that such arbitration or its award is not in contrast with domestic law for international awards, or is not contrary to public policy.

Now particularly for Bankruptcy related disputes, along with consonance with domestic laws and public policy, it becomes important to determine what core and non-core issues is. The Bankruptcy Code does not define what are core and non – core issues, these terms are expanded through means of various case laws. In the case of *In Re Wood*,[15] it was held on how core proceedings are those proceedings which involve a right created by federal bankruptcy law and such matters which arise in Bankruptcy, and on how it includes proceedings which are integral

[10] Neil Hannan, *INTERNATIONAL COMMERCIAL ARBITRATION AND CROSS BORDER INSOLVENCY*, 17 INT. TRADE BUS. LAW REV. 31 (2014).
[11] Northrop Corporation. v Triad International Marketing S.A, 593 F. Supp. 928 (1984)
[12] Parsons & Whittemore Overseas Inc. v. Societe Generale De L'Industrie Du Papier, 508 F.2d 969
[13] Kovacs, *supra* note 8.
[14] Shearson/American Express, Inc. v. McMahon, 482 U.S. 220 (1987)
[15] In Re Wood, 825 F.d 90, 97(t Cir. 1987)

to the Bankruptcy Process. As per the case of *Sanders Confectionary Prods. Inc. v. Heller Fin. Inc*[16], it was held on how core issues include all those issues which cannot exist outside the scope of Bankruptcy. In *N. Am. v. NGC Settlement Tr. & Asbestos Claims Mgmt. Corp*[17]., it was held on how core matters include those issues involving substantive rights arising out of a bankruptcy code[18]. In the case of *In re Lehman Bros. Holdings Inc*[19], it was further expanded on how any matter central to a collective bankruptcy process also can be a core issue[20].

In the case of In Re Electric Machine Enterprises, it was held on how any proceedings can be said to be non – core provided that the proceedings do not have any substantive rights which are being invoked on the basis of federal bankruptcy law, and such a dispute, thought interlinked with bankruptcy can also exist outside of bankruptcy.

Hence, it can clearly be seen on how Bankruptcy Courts have jurisdiction over any such issues which are core in nature, with what is seen as a core and non – core issue being determined on a case to case basis. Further citing the case of *In Re Electric Machinery case*[21], it was held on how arbitration can be availed for non – core issues on insolvency and bankruptcy, and it is upto the consent of the parties to refer to the court.

In the case of *Hays & Co v. Merrill Lynch*[22], it was held on how for any non – core issue, the Bankruptcy Courts cannot interfere in the enforcement any arbitration award, unless and until it could prove that the arbitral award is in violation of either of the text, the history or purpose of the Bankruptcy Code[23]. This was further emphasised in the case of *MBNA America Bank v. Hill*[24], where it was held on how generally, the courts do not have the discretion to deny arbitration for matters non – core in nature, or for those matters related merely to arbitration[25]. This is subject to the conditions that the arbitration is not in conflict with the code and jeopardizes its objectives. Such issue of conflict is to be analysed on a case to case basis.

[16] Sanders Confectionary Prods. Inc. v. Heller Fin. Inc, 973 F.2d 474 (6th Cir. 1992)
[17] N. Am. v. NGC Settlement Tr. & Asbestos Claims Mgmt. Corp, 118 F.3d 1056, 1064 (5th Cir. 1997)
[18] CROSSROADS OF INSOLVENCY AND ARBITRATION, *supra* note 1.
[19] In re Lehman Bros. Holdings Inc, 415 B.R. 77
[20] Kovacs, *supra* note 8.
[21] In Re Electric Machinery, 479 F.3d 791 2007
[22] Hays & Co v. Merrill Lynch, 885 F.2d 1149
[23] Kovacs, *supra* note 8.
[24] MBNA America Bank v. Hill, 436 F.3d 104 (2006)
[25] CROSSROADS OF INSOLVENCY AND ARBITRATION, *supra* note 1.

In Australia, it could be seen on how the issue of Arbitration and Insolvency, both these spheres of law are able to coexist and collaborate with each other due to a series of multiple judicial decisions. This can be seen from the case of *Incitec Ltd v Alkimos Shipping Corporation*[26] where it was held by Justice Alsop on how there lies a need to give "width, flexibility and amplitude" with regard to enforcement of arbitration clauses. But, this it is just encouraging arbitration, but does not explicitly suggests arbitration as a solution. This can be seen from the case of *ACD Tridon Inc v. Tridon Australia*[27], where it was held by the Federal Court on how there is no presumption of favourability of arbitration[28].

In the case of *Comandate Marine Corp v Pan Australia Shipping Pty Ltd*[29], the clash between that of arbitration and national laws was discussed. While not emphasising in detail, the Federal Court in this case clearly stated on how with evolution of international law, it could be seen on how disputes of intellectual property, competition, and among many subjects also includes insolvency. Hence, in such a case, it can be seen on when there lies a legitimate public interest in any such subject matter, any form of private dispute resolution such as that of an arbitration are not possible and hence while arbitration is allowed, the only element determining if an issue is arbitrable or not is public policy[30].

Hence, it could be seen on how insolvency matters have not been specifically dealt through the judiciary. But the judiciary in itself is allowing any matter governed by a public law to be subject to arbitration, provided that it does not go against public interest. There does not lie any judicial decisions involving determination of insolvency of arbitrability, but the legal framework of the country clearly allows for arbitration of insolvency disputes, with the scope of arbitration being much wider than that of the USA.

In England, it could be seen on how the Legal System is similar to Australia but providing a much simpler link between subjects such as arbitration and insolvency. This is because in England, there is explicit recognition by law on the topics which cannot be arbitrated, with it being implied that a party can arbitrate a dispute, as seen from a reading of the judgment in the case of *Fiona Trust & Holding Corporation v Privalov*[31]. Furthermore, in the case of *Soleimany*

[26] Incitec Ltd v Alkimos Shipping Corporation, [2004] FCA 698
[27] ACD Tridon Inc v. Tridon Australia, [2002] NSWSC 896
[28] Kovacs, *supra* note 8.
[29] Comandate Marine Corp v Pan Australia Shipping Pty Ltd, [2008] 1 Lloyd's Rep. 119
[30] Hannan, *supra* note 10.
[31] Fiona Trust & Holding Corporation v Privalov, [2007] UKHL 40

v. Soleimany[32] on how other than that of the law explicitly stating that a matter cannot be arbitrated, a dispute cannot be arbitrated only when the dispute is such that it cannot be arbitrable, or is such that an arbitrator would not be able to lawfully enforce the contract.[33] In this particular case, it was also held on how any award made on a basis of a contract which is illegal cannot have its award enforced. This is one of the cases where an illegal activity, such as bribing in this particular case goes against public interest and hence can be interpreted as such[34].

In England, just like Australia, there lies the situation where there have been very less decisions which involves insolvency and arbitration, and usage of arbitration as a form of dispute resolution for insolvency. This has been done in light with the Insolvency Act of 1996, which allows for a trustee of any entity which is undergoing bankruptcy to be bound to any arbitration clause which it has agreed with any other party. This, along with the liberal judicial interpretation in UK allowing for arbitration of most legal disputes also allows for arbitration to be a form of insolvency disputes[35].

A case which expands on this principle will be the case of *Fulham Football Club (1987) Ltd v Richards*[36]. In this particular case, the judges cited the legal jurists Mustill and Boyd for determining if an insolvency is arbitrable or not.

In this particular case, it was held on there must be a hard core, specific set of situations which determine the situations in which a dispute cannot be arbitrated. This is based on Section 103 of the Arbitration Act which allows for the government to decide by law on what disputes are arbitrable and what are not.

Secondly, as per this decision, it was held on how arbitration can be used to handle disputes of insolvency, but at the same time is not able to wind up company, or take any order which effects the interests of third parties. But other than that, all other disputes arising from such insolvency can be referred to arbitration.

[32] Soleimany v. Soleimany, [1999] QB 785
[33] Kovacs, *supra* note 8.
[34] CROSSROADS OF INSOLVENCY AND ARBITRATION, *supra* note 1.
[35] Kovacs, *supra* note 8.
[36] Fulham Football Club (1987) Ltd v Richards, [2011] EWCA Civ 855

Arbitration of Insolvency Proceedings in India

In India, it could be seen on how there lies a stark difference from the general trend followed in the International Community over the issue of arbitrability of insolvency proceedings. This is because of the Insolvency and Bankruptcy Code (hereby referred as IBC for short) thoroughly regulating insolvency proceedings, and judicial decisions subsequently expanding on the scope of this particular issue.

When we look into the IBC, it can be seen on how it was mainly created as a consolidated law governing all aspects of Insolvency in India. This Act, under Section 14(a) clearly mentions on how when there lies any moratorium which is declared by NCLT, there cannot be the continuation of any proceedings in any arbitration panel. It is a singular legislation mainly ensuring that the scope of insolvency is governed by law alone[37].

In the case of *Alchemist Asset Reconstruction Company v. Hotel Gaudayan*[38], it was held on how once a Corporate Insolvency Resolution Plan (CIRP) has been enacted, there cannot lie any other arbitration proceedings. But this is subject to the restrictions where arbitration is allowed for matters which increase the value of the assets of the corporate debtor, and if such arbitration does not adversely affect the CIRP proceedings.

So here, we can see on how based on the statute, there is an explicit bar on arbitration proceedings with regard to any insolvency when there also lies insolvency proceedings initiated against a party.

The court has clearly laid down the conditions under which a dispute can be non – arbitrable. The first and landmark case is that of *Vidya Drolla v. Durga Trade Corporation*[39]. In this particular case, a test was held to determine what all elements are not arbitrable in nature. Among many elements, it also includes that any award which is related to an action in rem, and is such that it is stated to be explicitly non - arbitrable, or effects the public at large, all such issues are non – arbitrable in nature.

But this still leaves the avenue of arbitration being allowed without CIRP proceedings, over

[37] Alipak Bannerjee & Payel Chatterjee, *Arbitration and Insolvency Collission - An Indian Perspective*, 1 INT. BAR ASSOC. 4 (3 June 20211).
[38] Alchemist Asset Reconstruction Company v. Hotel Gaudayan, AIR 2017 SC 5124
[39] Vidya Drolla v. Durga Trade Corporation, (2021) 2 SCC 1

which there lie multiple judicial decisions which clarify the scope of this issue. One of the first and most important cases in this matter is that of *Swiss Ribbons Private Ltd. v. Union of India*[40]. In this particular case, it was held on how for any insolvency proceedings which are entered into under Section 7 of the IBC are proceedings in rem, as the insolvency of a company impacts multiple third parties, including the public at large. This is a stance often contrary to that of arbitration, where proceedings are in personam, the interested parties in the dispute are the parties involved in the arbitration and no other[41].

In the case of *Booz Allen and Hamilton v. SBI Home Finance*[42], it was held on for any subject matter which is not arbitrable, the court cannot refer parties to the arbitration despite the existence of an arbitration clause[43].

Another important case law is that of M/S Emaar Mgf v. Aftab Singh. In this particular case, the scope of the Arbitration Act being applicable on to various types of disputes was looked into. In this particular case, the Supreme Court held on how when there lies a special legislation, the provisions of such legislation are given priority. Hence, there cannot be any proceedings made under the Arbitration Act.

The case of Swiss Ribbons and Booze Allen were cited by the court in the landmark judgment of Indus Biotech v. Kotak India Venture Fund. In this particular case, insolvency proceedings are filed against an entity by a party, while there already exists an arbitration clause between the parties. In this particular case, citing Swiss Ribbons, it was held on how insolvency is a proceeding in rem and hence cannot be arbitrated. Citing Vidya Drolia v. Durga Trading Corporation, it was held on how since there lies an issue in rem pending, it cannot be arbitrated.

Furthermore, in the case of KK Ropeways ltd. v. Billion Smiles Hospitality, it can be seen on how arbitration and IBC proceedings cannot run simultaneously.

Possible Changes to be integrated for the Present Indian Laws on Arbitration and Insolvency

Unlike most legislations, it can clearly be observed here India is one of the very few legal

[40] Swiss Ribbons Private Ltd. v. Union of India, (2019) 4 SCC 17
[41] Alipak Bannerjee and Payel Chatterjee, *supra* note 37.
[42] Booz Allen and Hamilton v. SBI Home Finance, (2011) 5 SCC 532
[43] Hannan, *supra* note 10.

systems that explicitly bans insolvency matters from being arbitrated. This is in contrary to the US where subject to restrictions set by the legislature, there lie minimal bars. In Australia, USA and UK, the element of any arbitration against public policy being restricted can also be observed.

This causes a major issue as most international jurisdictions are open to allow arbitration in specialized legislations, while India refuses to do the same. This ensures that for an insolvency proceedings, parties have no other choice, except to follow the process of insolvency as set in the IBC. It is also to be noted on how the IBC clearly prohibits Arbitration Proceedings post the beginning of the CIRP Process.

It was seen in the USA on how when a statute specifically prevents its subject matters to be arbitrated, then such issues cannot be arbitrated. This is done as the legislation for which it is created has been explicitly designed to function in a certain manner, and this will ensure that procedures as set in specialized legislations are followed properly. Hence, despite the need for change with regard to arbitration of insolvency proceedings, the element under Section 8 preventing arbitration proceedings to be initiated post CIRP proceedings is to be retained.

But in India, there is a bar on arbitrations on insolvency as a whole, even if a CIRP proceeding has not been entered into. This however is often disadvantageous as parties would be able to reach a favourable settlement, and the element of considering insolvency proceedings in rem severely disadvantages the possibility of swift resolution of insolvency disputes. For this, the best method would be to amend Section 8 allowing for arbitration issues before CIRP proceedings to be allowed for. If not, the judicial decisions as held in Vidya Drolia and Indus Biotech are to be repealed with newer judicial decisions expanding the scope of arbitration.

Conclusion

In conclusion, it can be observed on how India has a very rigid system which imposes insolvency proceedings strictly onto the parties involved in such an issue, and does not provide a scope for alternate dispute resolution, by means of Arbitration of issues. Through means of judicial decisions, insolvency as a subject in itself has been forbidden from insolvency, while the IBC states on how any and all legal proceedings cannot continue further once CIRP proceedings are undertaken. Hence in contrary to the international system which wants to further the scope of arbitration in insolvency, the same push cannot be seen in India. It is for

this reason that a major amendment of the IBC is required to allow for such arbitration to be integrated as a part of insolvency in India.

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