

## Termination of related party agreements during a CIRP

In a recent case of *Hemalata Hospitals Limited vs. Sh. Siba Kumar Mohapatra RP of Medirad Tech India Limited* (“**Hemalata Case**”),<sup>1</sup> the National Company Law Tribunal New Delhi Bench (Court-II) (“**NCLT Delhi**”) adjudicated on the continuation of related party agreements during the corporate insolvency resolution process (“**CIRP**”) and upheld the termination of related party agreements by the resolution professional (“**RP**”) during the CIRP. NCLT Delhi approved the same as (a) it was done after obtaining the approval of the committee of creditors (“**CoC**”) with at least 66% vote and (b) it was required by the successful resolution applicant under its resolution plan.

### Brief Facts

1. Medirad Tech India Limited (“**Corporate Debtor**”) was the owner of Hemalata Hospital & Research Centre, a specialty hospital based on Bhubaneswar (“**Hospital**”). The Corporate Debtor had entered into a service agreement dated September 1, 2006, with its related party i.e., Hemalata Hospitals Limited (“**Related Party**”) to manage and run the medical services in the Hospital (“**Service Agreement**”).
2. Subsequently, the Corporate Debtor and the Related Party had executed (a) a lease agreement dated December 13, 2013, to lease the Hospital including equipment, furniture and fixtures to the Related Party (“**Lease Agreement**”); and (b) a supplementary agreement dated January 1, 2014, to amend the Lease Agreement (“**Supplementary Agreement**”). The Service Agreement, Lease Agreement and Supplementary Agreement are collectively referred to as “**Related Party Agreements**”.
3. On December 8, 2021, NCLT Delhi had admitted the application filed by India SME Reconstruction Company Limited under Section 7 of the Insolvency and Bankruptcy Code, 2016 (“**IBC**”) and initiated the CIRP of the Corporate Debtor. NCLT Delhi had appointed Mr. Siba Kumar Mohapatra as an interim resolution professional, who was subsequently confirmed as the RP.
4. During the CIRP, the RP received resolution plans from various bidders. All the prospective resolution applicants had a concern with the Related Party Agreements and implementation of the resolution plans was conditional upon the termination of the Related Party Agreements.
5. By an email dated May 23, 2022, the RP sought the approval of the CoC for termination of the Related Party Agreements (which was also a condition under the various resolution plans received).
6. After both the COC members (comprising 100% of the COC) conveyed their no-objection for termination of the Related Party Agreements, the RP had sent a termination notice to the Related Party and terminated the Related Party Agreements.

<sup>1</sup> IA. NO. 2750/ND/2022 in CP (IB) No. 1243(ND)/2018.

7. The resolution plan that was received from successful resolution applicant i.e., Asian Institute of Oncology Private Limited (“SRA”) (which included a condition that the Related Party Agreements had to be terminated) was ultimately approved by CoC with a 100% vote.
8. Consequently, the Related Party filed an application before NCLT Delhi under section 60(5) of IBC, *inter alia*, to set aside the act of termination of the Related Party Agreements.

## Issues before NCLT Delhi

NCLT Delhi had to primarily decide two issues:

1. Issue 1: Whether the RP can terminate the Related Party Agreements during the CIRP.
2. Issue 2: Whether on approval of the resolution plan, the SRA is empowered to terminate the Related Party Agreements via the relevant clauses in the resolution plan.

## Analysis and Findings of NCLT Delhi

After considering the submissions of the parties, NCLT Delhi ruled as follows:

1. Issue 1:
  - a) As per section 25 of the IBC, RP is not under any obligation to deal with related party transactions. As per section 28(1)(f) of the IBC read with section 28(3) of the IBC, a resolution professional requires prior approval of the CoC (with a 66% vote) to undertake or carry out related party transactions.
  - b) In the present matter, all the prospective resolution applicants had a concern with the Related Party Agreements and implementation of the resolution plans was conditional upon the termination of the Related Party Agreements. Instead of giving approval for continuation of the related party transactions in terms of the Related Party Agreements, the CoC in its wisdom approved the termination of the Related Party Agreements. Therefore, there was no illegality by the RP in termination of the Related Party Agreements.
2. Issue 2:
  - a) NCLT Delhi observed that as per Regulation 39(6) of the Insolvency Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016, the resolution plan must take effect notwithstanding the requirement of the consent of the members or partners of the Corporate Debtor.
  - b) NCLT Delhi relying on the judgements in the case of *IDBI Bank vs. Jaypee Infratech Limited*<sup>2</sup> and *State Bank of India vs. Bhushan Steel Limited*<sup>3</sup>, held that related party agreements can be sought to be terminated in the resolution plan. Accordingly, it rejected the application of the Related Party, being devoid of merits.

## Conclusion

NCLT Delhi has interpreted section 28(1)(f) of IBC to include a right of the RP to terminate related party transactions as long as the approval of the committee of creditors with a minimum 66% vote is obtained. This may prove to be useful in situations where a corporate debtor’s operations are dependent on contracts with related parties and such operations are suffering due to non-cooperation from such related party during the CIRP. It would provide the RP and the CoC with the ability to terminate such contracts and enter into new contracts with non-related parties to revive and continue operations of a corporate debtor during the CIRP period.

This decision of NCLT Delhi is a welcome move for a successful resolution applicant who wishes to take over the management of the corporate debtor pursuant to the approved resolution plan. NCLT Delhi has followed the view of

<sup>2</sup> IA. NO. 2836/PB/2021, IA. NO. 3457/PB/2021 IA. NO. 3306/PB/2021, and IA. NO. 2521/PB/2022 in CP (IB) No.-77(ALD)/2017.

<sup>3</sup> CA No. 244(PB)/2018, CA No. 186(PB)/2018, CA No. 217(PB)/2018 & CA No. 176(PB)/2018 in CP (IB)-201(PB)/2017.

the Supreme Court in the matter of *IDBI Bank vs. Jaypee Infratech Limited*<sup>4</sup> that a successful resolution applicant has the right to include relevant clauses in its resolution plan to seek termination of the related party transactions. This would avoid any dependence on the erstwhile promoters or management of the corporate debtor and enable a resolution applicant to successfully turn around the affairs of the corporate debtor.

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**This Prism has been prepared by:**



**Aashit Shah**  
Partner



**Siddharth Mataliya**  
Senior Associate



**Bhoomika Kumar**  
Associate

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<sup>4</sup> *Supra* note 4.



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