BEFORE THE HON'BLE SUPREME COURT OF INDIA

CIVIL APPEAL NO. DIARY NO. 22417 OF 2019

COMMITTEE OF CREDITORS OF ESSAR STEEL INDIA LIMITED

...APPELLANTS

VERSUS

SATISH KUMAR GUPTA AND ORS. **...RESPONDENTS**

WRITTEN SUBMISSIONS ON BEHALF OF THE COMMITTEE OF CREDITORS

I. BACKGROUND

1. The present submissions are being filed on behalf of the committee of creditors of Essar Steel India Limited ("**Corporate Debtor**") (hereinafter referred to as the "**Committee of Creditors**").

2. The National Company Law Appellate Tribunal, New Delhi ("**Appellate Authority**") vide its judgement dated 4 July 2019 (the "**Impugned Judgement**") with respect to the corporate insolvency resolution process ("**CIR process**") of the Corporate Debtor while disposing off various appeals filed against the common order dated 8 March 2019 passed by the National Company Law Tribunal, Ahmedabad ("**Adjudicating Authority**") with respect to the approval of the resolution plan of ArcelorMittal India Private Limited ("**Arcelor**") ("**Approved Resolution Plan**") in relation to the corporate insolvency resolution process of the Corporate Debtor ("**CIR Process**"), has effectively re-written the entire statute and has impinged upon the exclusive legislative domain by re-writing the provisions of the Insolvency and Bankruptcy Code, 2016 (the "**Code**") by:

   (a) curtailing the role and authority of the committee of creditors constituted under the provisions of the Code to an extent that effectively

the committee of creditors is bereft of any role and authority inter alia in respect to approval of a resolution plan;

(b) expanding the jurisdiction of the Adjudicating Authority as well as the Appellate Authority beyond the legislative prescriptions including *inter alia* to alter, amend and literally substitute the entire commercial terms of a consented / approved resolution plan; and

(c) transgress upon the basic tenet of a resolution plan under the Code i.e. the consent between the committee of creditors on account of approval of voting majority in excess of 66% and the resolution applicant, by completely modifying and substituting the Approved Resolution Plan.

3. Proceeding upon the aforestated misconceived conclusions about the power and authority of the adjudicating authority and appellate authority *vis-à-vis* the role and authority of the committee of creditors, the Appellate Authority has proceeded to return the following findings:

(i) Financial creditors and operational creditors deserve equal treatment under a resolution plan and accordingly, re-distributed the proceeds payable under the Approved Resolution Plan so that all financial creditors and operational creditors be paid 60.7% of their admitted claims;

(ii) Financial creditors cannot be classified basis their security interest for the purpose of distribution and thereby directing that each financial creditor (whether secured or unsecured) with a claim more than Rs. 1 crore be paid 60.7% of its admitted claim;

Therefore, effectively, the Appellate Authority has entirely altered the terms of the resolution plan without the consent of the Committee of Creditors and the resolution applicant, Arcelor, and has effectively taken away the authority

and power vested with the Committee of Creditors under the Code to approve or reject a resolution plan.

4. The Impugned Judgement has jeopardized the CIR Process of one of the largest non-performing assets of the country and has shockingly un-settled otherwise settled principles of law recognising and protecting the rights of the secured creditors on account of a complete mis-reading of the Code, thereby endangering the national economic interest of the country. The appeal has been filed *inter alia* on the following grounds, each of which are being raised without prejudice to one another.

5. Before adverting to each of the grounds of challenge in the captioned appeal, the Petitioners seek to establish its foremost contention that unlike what has been sought to be done by the Apppellate Authority in the Impugned Judgement (i.e. treat all creditors equally so that all receive equal pro rated recovery under a resolution plan), the Code treats all creditors differently in reference and respect to their respective differential bargains. Therefore, it is the stand of the Petitioners that it is just, proper and equitable for each of the creditors to be treated differently in terms of their respective legal rights and commercial bargains under a resolution plan and accordingly, classification and sub-classification of creditors is permissible while proposing, approving and implementing a resolution plan.

II. CLASSIFICATION OF CREDITORS INTO DIFFERENT CLASSES AND SUB-CLASSES: LEGAL RATIONALE

6. The provisions of the Code provide for broad classification of creditors as financial and operational creditors on the basis of nature of transaction between the creditor and the corporate debtor. The said classification is a broad classification on the basis of nature of trasanction between the creditors

and the corporate debtor. Merely because there is a broad categorization of creditors under the Code, the Code does not mandate identical treatment of differently situated creditors (either *inter se* between the financial and operational creditors or *intra* each class of creditors). Rather, the foundation of the Code is based on equitable treatment of different classes of creditors recognizing that different class of creditors deserve different treatment and not all creditors can be treated equally.

7. The resolution applicant is expected to take into account differential bargains of creditors with the corporate debtor while proposing payment terms under a resolution plan. Equally, the committee of creditors while approving a resolution plan is entitled and fully justified in reckoning the differential bargains and ensuing differential rights and status of different creditors while accepting a resolution plan and even negotiate and seek modification of the resolution plan in reference to the same.

8. Admittedly, under the scheme of the Code, financial creditors as a class have been given superior status and rights as againsts the operational creditors. The said scheme of the Code has also been upheld in this Hon'ble Court's judgment in ***Swiss Ribbons Private Limited vs. Union of India, 2019 SCC Online SC 73.*** Furthermore, even within the financial creditors there is further differentiation and differential rights *inter alia* on the basis of availability and value of security interest. Equally, amongst the operational creditors there is further sub-classification and division amongst the operational creditors on the very basis of definition which includes workmen and employees, trade creditors as well as the government. Further, there may be operational creditors who are a separate class in themselves on account of availability of security.

9. The provisions of the Code clearly recognize and respect security interests and rights attached thereto during insolvency resolution as evident from the following:

(i) Definition of term "creditor" under Section 3(10) specifically includes and recognizes secured and unsecured creditors in addition to the financial and operational creditors;

(ii) Section 3(30) and 3(31) of the Code in turn defines the terms "secured creditor" and "secured debt". Notably, the definition of secured creditors is not limited to only financial creditors. The very availability of security interest in favour of a creditor distinguishes it from other creditors irrespective of nature of underlying transaction – i.e. financial lending or operational.

(iii) Section 20(2)(c) **prohibits the interim resolution professional from creating security interest on encumbered property to raise interim finance, without the prior consent of the secured creditors** having security interest over such encumbered property;

(iv) In fact, **no security interest can be created on the assets of the corporate debtor, even by the resolution professional, without the approval of the committee of creditors under Section 28(1)(b) of the Code**, requiring 66% of voting share to permit the same;

(v) **At the time of filing of the claims** to the interim resolution professional / resolution professional, as the case maybe, the prescribed formats under the Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 ("**CIR Regulations**") formulated under the mandate of Section 240 of the Code **require**

creditors to disclose and describe the security interest (if any) and valuation thereof;

(vi) **The status and details of security interest in favour of secured creditors is required to be included as part of the information memorandum** prepared under Section 29 of the Code read with Regulation 36 of the CIR Regulations, listing out the relevant information as regards the financial position of the corporate debtor including details of security interest and details of litigations. Notably, in terms of **Section 30(1) of the Code, a resolution plan is to be prepared on the basis of information memorandum**, which as stated above would include *inter alia* details of security interest.

10. Therefore, entire scheme of Code is designed to respect and give due weightage to one of the most fundamental differentiation amongst creditors i.e. the availability and value of security interest created in favour of different creditors.

11. Creation of security interest in favour of a creditor makes it a secured creditor and by virtue of such security interest, a prior property interest is created in favour of a creditor. This right to property has been protected under common law; Section 48 and 58 of the Transfer of Property Act, 1882 as well as recognized under Article 300A of the Constitution of India. Equally, Section 77 of the Companies Act 2013 also recognizes the rights of a secured creditor upon due registration of the charge in accordance with the provisions of the said Act. In fact, even under the erstwhile regime, while the waterfall under Section 529 of the Companies Act, 1956 gave preferential treatment to crown debts, such preferential treatment was only vis-à-vis unsecured debts and the crown was not accorded a preferential right for recovery of its debts over a

mortgagee or pledgee of goods or a secured creditor.[1] Therefore, recognition of security interests and the precedence of the claim of a secured creditor vis-à-vis other creditors is inherent in the legal principles governing the insolvency and pre-insolvency regimes of our country.

12. It is in deference to the said well protected legal rights of a secured creditor that the entire scheme of the Code recognizes and re-inforces the special rights and status of the secured creditor.

13. The Hon'ble Appellate Authority in a brazen manner has abrogated the entire concept of security interest and legal rights attached thereto during insolvency resolution by assuming that the only classification permissible under the Code is that of financial and operational creditors. There is no provision under the Code which contradicts Section 48 of the Transfer of Property Act, 1882 or Section 77 of the Companies Act, 2013 and hence, the vital constitutional right to property of the secured creditors during the insolvency resolution process cannot be presumed to have been taken away *sub-silenco*. The legal rights attached to the security interst cannot be presumed to have taken away by the Code without an express provision to this effect.

14. Attention in this regard is drawn to the judgement of this Hon'ble Court in ***ICICI Bank Limited v. SIDCO leathers Limited & Ors.*, (2006) 10 SCC 452** wherein this Hon'ble Court while holding that deprivation of a legal right (*for instance a security interest on the assets of the corporate debtor)* existing in favour of person cannot be presumed in construing a statute and unless the statute provides to the contrary, has observed:

> *"**While enacting a statute, the Parliament cannot be presumed to have taken away a right in property**. Right to property is a*

[1] See ***Dena Bank v. Bhikhabhai Prabhudas Parekh and Co. and Ors.***, (2000) 5 SCC 694; ***Bombay Stock Exchange v. V.S. Kandalgaonkar***, (2015) 2 SCC 1

constitutional right. Right to recover the money lent by enforcing a mortgage would also be a right to enforce an interest in the property. The provisions of the Transfer of Property Act provide for different types of charges. ***In terms of Section 48 of the Transfer of Property Act claim of the first charge holder shall prevail over the claim of the second charge holder and in a given case where the debts due to both, the first charge holder and the second charge holder, are to be realized from the property belonging to the mortgagor, the first charge holder will have to be repaid first. There is no dispute as regards the said legal position.***

...

Such a valuable right, having regard to the legal position as obtaining in common law as also under the provisions of the Transfer of Property Act, must be deemed to have been known to the Parliament. Thus, while enacting the Companies Act, the Parliament cannot be held to have intended to deprive the first charge holder of the said right. Such a valuable right, therefore, must be held to have been kept preserved...

...

If the Parliament while amending the provisions of the Companies Act intended to take away such a valuable right of the first charge holder, we see no reason why it could not have stated so explicitly. Deprivation of a legal right existing in favour of a person cannot be presumed in construing the statute. *It is in fact the other way round and thus, a contrary presumption shall have to be raised."*

[Emphasis Supplied]

15. Therefore, security interest created in favour of secured creditors is a constitutionally protected legal right of the secured creditors and the same cannot be altered by a resolution plan except by a collective vote of the committee of creditors under Section 30(4) of the Code with requisite majority of vote resulting in a resolution plan binding on all stakeholders upon approval by the Adjudicating Authority under Section 31 of the Code.

16. It is relevant to note under a resolution plan when proceeds are allocated to the secured creditors then the security interest ordinarily stands released and such release of a secured creditor's right to the property is based on consent of requisite majority of committee of creditors after negotiations between resolution applicant and the committee of creditors while keeping in mind the differential bargains amongst different creditors and the corporate debtor.

17. Respectfully, the aforesaid is in recognition of the principles of equitable treatment enshrined under the Code (*and adopted globally in various insolvency regimes*) which recognise that different creditors have struck fundamentally different commercial bargains with the debtor (e.*g., through the grant of security, higher interest rate for the unsecured, shorter repayment terms for the operational creditors, etc*.) and therefore, differential treatment of creditors that are not similarly situated may be necessary as a matter of equity and fairness rather than being opposed to it.[2]

18. This principle of equitable treatment which recognises that different classes of creditors deserve different treatment and not all creditors can be treated equally is one of the foundational principles of the Code (as recognized by this Hon'ble Court in *Swiss Ribbons*). This principles is also expounded under the United Nations Commission on International Trade Law Legislative Guide ("**UNCITRAL Legislative Guide**")[3] (*referred to by the Hon'ble Supreme Court in Swiss Ribbons as quoted above*) which records that:

"Ensuring equitable treatment of similarly situated creditors

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[2] **American Jurisprudence, Vol. 9, 2d**, (2006) Pg. 45-55

[3] Refer UNCITRAL Legislative Guide, Vol. 12 of the Convenience Compilation @ Pg. 25 & 26

7. The objective of equitable treatment is based on the notion that, in collective proceedings, creditors with similar legal rights should be treated fairly, receiving a distribution on their claim in accordance with their relative ranking and interests. This key objective recognizes that all creditors do not need to be treated identically, but in a manner that reflects the different bargains they have struck with the debtor. *This is less relevant as a defining factor where there is no specific debt contract with the debtor, such as in the case of damage claimants (e.g. for environmental damage) and tax authorities. Even though the principle of equitable treatment may be modified by social policy on priorities and give way to the prerogatives pertaining to holders of claims or interests that arise, for example, by operation of law, it retains its significance by UNCITRAL Legislative Guide on Insolvency Law ensuring that the priority accorded to the claims of a similar class affects all members of the class in the same manner****. The policy of equitable treatment permeates many aspects of an insolvency law, including the application of the stay or suspension, provisions to set aside acts and transactions and recapture value for the insolvency estate, classification of claims, voting procedures in reorganization and distribution mechanisms.*** *An insolvency law should address problems of fraud and favouritism that may arise in cases of financial distress by providing, for example, that acts and transactions detrimental to equitable treatment of creditors can be avoided."*

[***Emphasis Supplied***]

19. Similarly, a report by **International Monetary Fund titled Orderly & Effective Insolvency Procedures – Key Issues**, provides that all insolvency procedures must aim for equitable treatment. The report notes as follows[4]:

> "*Equitable Treatment. A common feature of all insolvency proceedings is their collective nature. Unlike other laws (e.g., foreclosure laws), an insolvency law is designed to address a situation in which a debtor is no longer able to pay its debts to its creditors generally (rather than individually) and, in that context, provides a mechanism that will provide for the equitable treatment of all creditors…* ***equitable treatment does not require equal treatment. On the contrary, to the extent that different creditors have struck fundamentally different commercial bargains with the debtor*** *(e.g., through the granting of security),* ***differential treatment of creditors that are not similarly situated may be necessary as a matter of equity***."
>
> [***Emphasis Supplied***]

20. Even under the framework of Article 14 enshrined in our Constitution protecting equality, the Constitution envisages classification as long as the same is made on sound rationale, based on an intelligible differentia and is being carried out in order to obtain the object of the Code. The following observations of this Hon'ble Court in ***T.M.A. Pai Foundation and Ors.* v. *State of Karnataka and Ors.*, (2002) 8 SCC 481** would be of relevance:

> *"346. 'Equality' which has been referred to in the Preamble is provided for in a group of Articles led by Article 14 of the Constitution which says that the State shall not deny to any person equality before the law*

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[4] See report by **International Monetary Fund titled Orderly & Effective Insolvency Procedures – Key Issues, Vol. 13 @ Pg. 157**

or the equal protection of the laws within the territory of India. ***Although stated in absolute terms Article 14 proceeds on the premise that such equality of treatment is required to be given to persons who are equally circumstanced. Implicit in the concept of equality is the concept that persons who are in fact unequally circumstanced cannot be treated on par.***

...

348. The equality, therefore, under Article 14 is not indiscriminate. ***Paradoxical as it may seem, the concept of equality permits rational or discriminating discrimination. Conferment of special benefits or protection or rights to a particular group of citizens for rational reasons is envisaged under Article 14 and is implicit in the concept of equality. There is no abridgment of the content of Article 14 thereby--but an exposition and practical application of such content.****"*

[Emphasis Supplied]

21. Classification however cannot be based on micro distinctions and irrelevant considerations. In this regard, attention of this Hon'ble Court is also drawn towards the following observations of this Hon'ble Court in ***State of Jammu & Kashmir* v. *Triloki Nath Khosa & Ors.*, 1974 (1) SCC 19**:

"31. …*Classification, however, is fraught with the danger that it may produce artificial inequalities and therefore, the right to classify is hedged in with salient restraints, or else, the guarantee of equality will be submerged in class legislation in as quadrating as laws meant to govern well marked classes characterized by different and distinct attainments.* ***Classification, therefore, must be truly founded on substantial differences which distinguish persons grouped together from those left out of the group and such differential attributes must***

bear a just and rational relation to the object sought to be achieved.

32. Judicial scrutiny can therefore extend only to the consideration whether the classification rests on a reasonable basis whether it bears nexus with the object in view…"

[*Emphasis Supplied*]

22. Therefore, in conclusion it may be stated that inherent in the concept of equality under Article 14 of the Constitution, is the requirement of treating equally those who are equally situated and classification in itself is inherent in the concept of equality as long as the same is made on sound rationale based on an intelligible differentia and has nexus with the object thereof. Further, such classification ought to be substantial and straightforward and not based on micro distinctions.

23. As demonstrated above, classification between different creditors basis their differential bargains including security interest is based on substantial differentiation between the creditors and hence, is constitutionally permitted. Clearly, the Appellate Authority has erred in not appreciating the same and completely wiping out the inter-se distinction between the financial and operational crediors.

III. CLASSIFICATION OF CREDITORS BASIS THE NATURE OF DEBT AND / OR SECURITY INTEREST IS A SINE QUA NON FOR ANY INSOLVENCY LAW

24. Secured credit and creation of security interest is integral to any financial sector of any economy and serves categorical economic goals. While on one hand, security interests created help mitigate risks of the creditors by increasing the likelihood of repayment (*especially in events of default*), it also allows better availability of credit by increasing the appetite of financial institutions to give credit in recognition of the predictability of repayment and

thereby resulting in better availability of capital in the economy to fuel economic growth.

25. The presence of a sound secured credit market with defined priorities and treatment of the respective security interests incentivizes banks and financial institutions to assess the likelihood of recovery of their dues and mitigation of the deterioration of their claims. At the same time, existence of secured credit with well-defined priorities also enables the debtors to assess the availability of affordable credit (*secured credit being available at lower margins as compared to unsecured debt*) while keeping in view their own asset base.[5]

26. It is an established principle that the rights of creditors and the priorities of claims established prior to insolvency proceedings under commercial or other applicable laws should be upheld in an insolvency proceeding to preserve the legitimate expectations of creditors and encourage greater predictability in commercial relationships. While certain priority or privileged claims (*such claims of workmen*) may be attributed priority to the general priority of secured credit based on social considerations. However, the recognition of security interests while determining the priorities in an insolvency law is a *sine qua non* and non-recognition of the pre-insolvency rights and security interests would lead to the loss in significance of security interest in the credit markets and such unpredictability would lead to increase in cost of debt.[6]

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[5] *Refer to the* ***IMF Paper on Development of Standards for Security Interest****, Pascale De Boeck & Thomas Laryea, Counsel, IMF Legal Department*

[6] *See* **(a)** ***Report of the Company Law Committee 1952*** headed by Shri C. H. Bhabha; **(b)** ***Report on Company Law by Expert Committee on Company Law*** headed by Dr. Jamshed J. Irani dated 31 May 2005; **(c)** ***Report of the Bankruptcy Law Reform Committee Report*** of November 2015; **(d)** the ***Legislative Guide on Insolvency Law issued by the United Nations Commission on International Trade Law***; and **(e)** the ***World Bank Report*** of 2015 titled ***Principles for Effective Insolvency and Creditor / Debtor Regimes***.

27. Keeping in view the aforesaid principle, differently placed classes of creditors based on substantial distinctions (*such as nature of the debt, status of the claim (i.e. disputed, contigent), the security interests and the value and nature of security*) are to be given differential treatment for it to be equitable and fair amongst all the classes of creditors and mere initiation of a resolution process under the provisions of the Code does not override the differential bargains made by the creditors with the corporate debtor prior to the commencement of an insolvency. It is keeping the above in mind that in fact the Code itself seeks to classify different claims differently and it is with this intent that a creditor is required to furnish details of its security interest and valuation at the time of submission of its claim to the resolution professional in accordance with the provisions of the Code and its related regulations. Similarly, even the information memorandum (prepared by the resolution professional) is required to contain information and details of security interest as well as details of any pending litigation etc. For instance the information regarding workmen and employees is separately provided for in the information memorandum from the information regarding the government dues or other operational creditors, so that the different bargains even within a class are to be segregated to ensure equitable treatment based on the individual nature of such claim.

28. It is pertinent to state that the differential bargains amongst the creditors' class are negotiated to provide for clear mutual rights and status in a situation of insolvency/financial distress and it would defeat the very purpose of creation of security, if such differential bargains are ignored during insolvency/insolvency resolution. Rather, one of the primary purpose of a creditor negotiating a security or superior priority rights from the debtor for disbursement of a loan is to mitigate risks, and while the said risk may be low

at the time of disbursement, the true usage and purpose of a security/priority payment arrangements would arise at the time of a corporate debtor defaulting or undergoing a financially stressful period (*such as insolvency resolution*). Thus, ignoring differential rights of different classes of creditors, apart from being contrary to law, would have seriously adverse consequences on the debt market, lead to increased risk and cost lending (*a consequence apposite to the object and purpose of the Code to promote lending and entrepreneurship*) and run contrary to the legitimate expectation of the secured creditor regarding availability of security interest during financial distress of the corporate entity.

29. The following extract from **Wood, Philip R, "*Principles of International Insolvency*", Sweet Maxwell (1995)**, would be of relevance in understanding the principles of security recognition during insolvency followed across the globe,

> "***Secured Creditors are super-priority credtiors on insolvency. Security must stand up on insolvency which is when it is needed most.*** *Security which is valid between the parties but not as against the creditors of the debtor is futile.* ***Bankruptcy laws which freeze or delay or weaken or de-prioritise security on insolvency destroy what the law created. Hence, the end is more important than the beginning.***"
>
> [***Emphasis Supplied***]

30. Recognition of security in any bankruptcy / reorganization plan is a principle globally accepted and followed as evident from the following extract from **Wood, Philip R, "*Principles of International Insolvency*", Sweet Maxwell (1995)** demonstrating recognition of security during Chapter 11 proceedings:

> "*By contrast, the US Chapter 11 plan is the subject of very detailed legislation. The bare bones of the matter are that the debtor in possession has an exclusive right during the first 120 days to formulate and file a plan. This right of the debtor to propose his own version does not apply in England and Japan and has caused much creditor*

resentment in the US. There must be a disclosure statement followed by creditor voting (for which purpose creditors are divided in to priority classes) and confirmation by the court. ***Broadly the plan has to meet certain basic requirements which broadly reflect the "absolute priority rule" (super- priority creditors, secured creditors, administrative expenses, priority creditors- employees, taxes and the like- ordinary unsecured creditors, junior creditors and finally equity) with no class being impaired unless all creditors of a lower class receive nothing.*** *The court can bind dissentient creditors (the "cram-down") if certain tests are met, based on observance of the absolute priority rule and non- discrimination between creditors of the same class.*

Once the plan has been confirmed, the debtor is discharged from all debts which arose prior to confirmation except as provided in the plan so that the confirmed plan governs the obligations of all parties."

[***Emphasis Supplied***]

31. Respectfully, if an equitable approach recognizing the respective bargains and rights of different classes of creditors as a part of a resolution process are not adopted and the principles of the purported "equality" under the Impugned Judgement are upheld, the secured financial creditors with good security interest will always be incentivised to vote for liquidation rather than resolution, as they would have better rights and status if the corporate debtor was to be liquidated rather than a resolution plan being approved, which defeats the entire objective of the Code i.e. resolution of the distressed asset.

32. The absurdity of the Impugned Judgment further comes to fore from the fact that the scheme of the Code allows for the sale of a corporate debtor as a going concern during liquidation and similarly under insolvency resolution an attempt is being made for resolving the financial affairs of a corporate debtor as a going concern. While as per the Impugned Judgement security interests would be recognised during the sale of the corporate debtor as a going concern

during liquidation, the same security interests would stand abrogated for resolving the financial affairs of a corporate debtor as a going concern during insolvency resolution.

33. It is thus, more than evident that differently placed classes of creditors are bound to be given differential treatment under a resolution plan for it to be equitable and fair amongst all the classes of creditors and mere initiation of a resolution process cannot completely override the differential bargains made by the creditors with the corporate debtor prior to the commencement of an insolvency. The concept of differential treatment to different classes of creditors is ingrained in any principle of fairness and equitable and rather equal treatment of different classes of creditors as has been done by the Appellate Authority in the facts of the present case, is unfair and in-equitable.

IV. HEALTH OF FINANCIAL SECTOR IS CRITICAL FOR OVERALL HEALTH AND GROWTH OF ECONOMY

34. Health of the financial sector of an economy has a rippling effect on the overall health and growth of an economy as a whole. There is convincing economic analysis which proves that financial sector development plays a vital role in facilitating economic growth and poverty reduction and these argument are supported by overwhelming empirical evidence from both cross-country and country specific studies. Therefore, economically, it is an accepted position that health of financial sector of any economy is perhaps the single most important economic factor contributing to growth and positive stimulus in an economy. Further, there is also general consensus that growth requires a stable macro-economic environment. Financial sector's greater ability to reduce risks through risk sharing and diversification enables an economy to better absorb economic shocks, leading to a more stable macro-

economic environment which supports growth. Stability and growth in macro-economic level thus, not only benefits financial creditors but equally the operational creditors.[7]

35. Secured credit operates on the basis of intermediation deposits made on the basis of savings and carries a liability to pay interest to depositors. Failures to do so can create panic and run on the banks. It can result in a generic economic crisis if a claim is set in. Further, recovery of banks' credit enhances credit circulation or availability of credit to the society. The mounting NPAs restrict credit availability and increases provisioning. Banks become averse to taking risks. The economic growth suffers. Therefore, recovery of secured credit has to be given great priority.

36. The Impugned Judgement decision of the Hon'ble Appellate Authority in the present CIR process has however, completely wiped off the certainty and predictability of the insolvency regime in so far as risk sharing amongst financial and operational creditors is concerned and it was in this context that the legislature had to step in by way of latest amendments to clarify that the risk allocation towards financial creditors (*mainly consisting of secured creditors and having superior rights under law)* is different than the operational creditors and thus, cannot be treated at parity during insolvency resolution.

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[7] Refer to Article by **Asian Development Bank** titled "***Financial Sector Development, Economic Growth, and Poverty Reduction: A Literature Review***" of October 2009, **ADB Economics** – Working Paper Series No. 173. Also refer to article titled "***Benchmarking Financial Systems around the World***" of August 2012, Policy Research Working Paper 6175 by **World Bank**

V. ECONOMIC RATIONALE FOR DIFFERENTIAL RIGHTS, STATUS AND TREATMENT OF OPERATIONAL AND FINANCIAL CREDITORS

37. This Hon'ble Court in ***Swiss Ribbons*** has already recognised the economic rationale for differential rights and status and treatment of operational and financial creditors under the Code, and has already upheld the scheme and provisions of the Code treating operational and financial creditors differently while holding:

> "*27. According to us, it is clear that most financial creditors, particularly banks and financial institutions, are secured creditors whereas most operational creditors are unsecured, payments for goods and services as well as payments to workers not being secured by mortgaged documents and the like. The distinction between secured and unsecured creditors is a distinction which has obtained since the earliest of the Companies Acts both in the United Kingdom and in this country.* ***Apart from the above, the nature of loan agreements with financial creditors is different from contracts with operational creditors for supplying goods and services. Financial creditors generally lend finance on a term loan or for working capital that enables the corporate debtor to either set up and/or operate its business. On the other hand, contracts with operational creditors are relatable to supply of goods and services in the operation of business. Financial contracts generally involve large sums of money. By way of contrast, operational contracts have dues whose quantum is generally less.*** *In the running of a business, operational creditors can be many as opposed to financial creditors, who lend finance for the set up or working of business.* ***Also, financial creditors have specified repayment schedules, and defaults entitle financial creditors to recall***

a loan in totality. Contracts with operational creditors do not have any such stipulations. *Also, the forum in which dispute resolution takes place is completely different. Contracts with operational creditors can and do have arbitration clauses where dispute resolution is done privately.* ***Operational debts also tend to be recurring in nature and the possibility of genuine disputes in case of operational debts is much higher when compared to financial debts.*** *A simple example will suffice. Goods that are supplied may be substandard. Services that are provided may be substandard. Goods may not have been supplied at all. All these qua operational debts are matters to be proved in arbitration or in the courts of law. On the other hand, financial debts made to banks and financial institutions are well-documented and defaults made are easily verifiable.*

28. ***Most importantly, financial creditors are, from the very beginning, involved with assessing the viability of the corporate debtor. They can, and therefore do, engage in restructuring of the loan as well as reorganization of the corporate debtor's business when there is financial stress, which are things operational creditors do not and cannot do.*** *Thus, preserving the corporate debtor as a going concern, while ensuring maximum recovery for all creditors being the objective of the Code,* ***financial creditors are clearly different from operational creditors and therefore, there is obviously an intelligible differentia between the two which has a direct relation to the objects sought to be achieved by the Code.***"

[***Emphasis Supplied***]

38. In this context, it is necessary to reiterate that economically, financial creditors (*usually secured*) and operational creditors (*which are often unsecured*

creditors) are incomparable and have significantly different business models and hence, deserve un-equal treatment:

(i) Financial creditors are in the **business of lending money** with only way to earn profit by earning interest on money lent with **very low margin, i.e. generally such margin being hardly about 1-4%** after deducting the cost of capital (*interest to be paid to its public depositors and other costs*) from the interest chargeable on money lent. In this regard, reference may be made to the data made available by the Reserve Bank of India in its report on Trend and Progress of Banking in India, 2017-18 which reflects that the net interest margin[8] of Indian Banks for FY 2017-18 is averaged at 2.5%. Similarly, the global trend for net interest margin was at 3.3% for banks in United States of America and 1.6% in United Kingdom in the year 2016, as per the data published on the website of World Bank;

(ii) The finance provided by the financial creditors (along with a mix of equity) is typically either for capital expenditure by the corporate debtor which results in creation of assets or for working capital purposes which results in liquidity for the corporate debtor to enable it to make payment towards operational expenses. Thus, financial creditors are either the capital providers for a company who enable to create assets or provide working capital or to enable the company to run its business operations whereas the operational creditors are beneficiaries of the working capital and in fact get paid for the goods and services provided by them to the corporate debtor, out of the working capital available with the

[8] Net Interest Margin means the net interest income (*i.e. difference between the interest income and the interest expenses*) divided by average interest earning assets.

corporate primarily consisting of the finance provided by the banks. Accordingly, the working capital injected by the financial creditors, results in a trickle-down effect in the economic and operational cycle of the corporate debtor benefitting all stakeholders, including operational creditors. In fact many of the operational creditors themselves function on the strength of the finance from these various financial creditors and the health / recovery by banks has a direct co-relation with the capital available with them for granting loans including the operational creditors.

(iii) Inherent in **operational creditors' business is higher risk with higher profit margin and shorter cyclical repayments** (*ranging anywhere between 10-50% margin depending on nature of goods or services provided by it*).[9] In fact operational creditors enter into their contracts with a corporate debtor with full awareness that assets of the corporate debtor are encumbered and secured in favor of the secured creditors and it is because of the subservient value of their contractual credit provision that operational creditors function on high profit margins. This is an economic reality as well as statutory reality.

(iv) **Operational creditors have shorter credit cycle and therefore have a more accessible exit option on default by stopping supply to the corporate debtor, once they realize that corporate debtor's business is in difficulty. Financial creditors can exit** on their long term loans either upon re-payment of the full amount which is spread over several years or upon default by re-calling the entire facility and/or

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[9] *Reference may be has to the market research carried out by* ***India Brand Equity Foundation, a trust established by the Ministry of Commerce and Industry in the year 2013*** *as regards the oil and gas sector.*

enforcing the security (*which may also include protracted litigation*) which is a time consuming and lengthy process. Apart from this, an operational creditor at the time of entering into a contract with the corporate debtor is aware of the risk of termination of the contract by the corporate debtor on account of various factors involved in trading like the corporate debtor finding alternative suppliers or change in production methodology or technological advancements etc. Whereas there is relatively low termination risk for a financial creditor as once the loan is disbursed the contract terminates upon repayment of all outstanding debt or enforcement of security as set out above.

(v) **Operational creditors have better and more easily exercisable exit option** as they have an ability to exit and stop doing business with a defaulting debtor at the earliest signs of distress seek other customers so as to mitigate their losses or insist on clearance of pending amounts and/or seek adequate safeguards for payment such as letters of credit or advance bank guarantees etc to mitigate further risk. Whereas the financial creditors' only exit is by repayment and in fact, for ensuring improved prospects of repayments, the financial creditors often are required to grant bridge funding to ensure that the projects are completed and the debtor turns profitable to repay back the monies advanced.

(vi) **Financial creditors are a part of a heavily regulated banking system** and are bound by the policy framework of the banking regulator on account of the involvement of public money. Therefore, if the loan account of an entity reflects signs of / is in distress / is non-performing, the financial creditors are required to provide for adequate provisions (*which restricts its ability to lend further to the said entity and*

sometimes even to that sector and reduces its ability to earn profits on such further lending at reduced rates) as well as restructure such loans (*which typically results in foregoing the unpaid interest*).

39. Therefore, there is a legally and economically valid basis and rationale for separate classification and prioritization of creditors as financial and operational creditors and the same is not violative of any constitutional mandates including right to equality and fair treatment, as already held by this Hon'ble Court in *Swiss Ribbons* judgement.

VI. DISASTROUS IMPACT ON PENDING INSOLVENCY PROCESSES AS WELL AS BANKING INDUSTRY AND THE NATIONAL ECONOMY

40. Respectfully, the interpretation adopted in the Impugned Judgement will have a disastrous impact on the banking industry and national economy in every possible manner. Equating financial creditors with operational creditors, and disregard of security interests of financial creditors and rights attached thereto, would lead to severe plunge in recovery rate to the banks and financial institutions during insolvency resolution process and thus, expose the banks and financial institutions to grave financial distress. It is ironical that the Code which was admittedly enacted to reduce the burden of non-performing assets ailing the Indian banking system and provide an efficient statutory platform for insolvency resolution and debt restructuring is being interpreted in a manner so as to take away the established rights of the secured financial creditors and force them to share resolution proceeds with all other unsecured and operational creditors with entirely different risk-reward profile, at a pari passu basis. This would only cause further distress in the banking industry and force the government to contribute towards banks' equity to continue to be in compliance with Basel II norms of capital adequacy. This will result in serious

damage to the Indian economy as a whole and dilapidate the entire banking system.

41. The view taken by the Appellate Authority under the Impugned Judgement by proposing "equal treatment" is grossly myopic and completely overlooks the impact of the same on pending insolvency resolution processes by creating uncertainty and unpredictability with respect to otherwise commercially acceptable norms of lending restructuring and priority in distribution in context of a distressed asset as well banking industry as a whole.

42. Furthermore, if the security interests during insolvency resolution are to be abrogated, the entire banking and lending landscape in India (*based on centuries old principles*) would undergo a change as the above abrogation would lead to increase in the risk of capital, lending at higher interest rates, nullifying of the basis and rationale of Reserve Bank of India's provisioning norms. Hence, the above would result in unavailability and/or inaccessibility of credit and thus, achieve an economic result exactly opposite to the object of the Code to promote entrepreneurship and give impetus to the availability of credit.

VII. THE IMPUGNED JUDGEMENT IS WITHOUT JURISDICTION AND IN COMPLETE CONTRAVENTION OF THE LAW LAID DOWN BY THIS HON'BLE COURT IN K. SASHIDHAR V. UNION BANK OF INDIA

43. The Appellate Authority is a creature of the Code and therefore, its power and scope of jurisdiction is bound within the four corners of the Code. Therefore, the Impugned Judgement modifying the Approved Resolution Plan and nullyfying the commercial decision of the Committee of Creditors is beyond the jurisdiction prescribed under Section 61 of the Code.

44. It is submitted that a "Resolution plan" is a commercial proposal with negotiated terms of restructuring of financial affairs of a corporate debtor and is within the commercial domain of the committee of creditors. The Code does not confer any jurisdiction on the Appellate Authority and / or the Adjudicating Authority to examine the commercial and technical aspects/ decisions of the Committee of Creditors such as the viability and feasibility of a resolution plan and the commercials therein (*including but not limited to the distribution of proceeds under a resolution plan*).

45. Respectfully, the provisions of the Code only prescribe limited jurisdiction of the Appellate Authority under Section 61(3) of the Code with respect to an appeal filed against an order approving a resolution plan i.e. such jurisdiction being restricted to (a) the approved resolution plan being in contravention of the provisions of any law for the time being in force; (b) there being a material irregularity in the exercise of powers by the resolution professional during the corporate insolvency resolution period; (c) the operational creditors not having been paid a minimum of the liquidation value due to them (*as prescribed under Section 30(2)(b) of the Code*); (d) the insolvency resolution process costs having not been provided for repayment in priority to all other debts; and (e) non-compliance of the criteria prescribed by the Insolvency and Bankruptcy Board of India ("**IBBI**").

46. Therefore, so long as a resolution plan provides / ensures that **(a)** the operational creditors are being paid a minimum of their liquidation value i.e. an amount which shall not be less than the amount to be paid to the operational creditors in the event of liquidation of the corporate debtor under section 53 or their share in resolution proceeds in reference to Section 53 waterfall (whichever is higher) ("**Minimum Resolution Proceeds**"); and **(b)** the

insolvency resolution process costs having been provided for repayment in priority to all other debts, all the other commercial and technical aspects are in the exclusive the domain of the committee of creditors in terms of the provisions of the Code[10] and the Code does not confer any jurisdiction on the Adjudicating Authority to examine the commercial aspects of a plan including the amounts being given to one stakeholder or the other. Therefore, once a resolution plan passes the muster of the minimum prescriptions (*inter alia in the nature of safeguards for operational creditors*) within the parameters of the Code and the relevant related regulations issued thereunder, the same is binding on all stakeholders and cannot be judicially reviewed.[11]

47. It is respectfully submitted that it is a settled position of law that a tribunal being a creature of a statute (*such as the Adjudicating Authority and the Appellate Authority under the Code*) is bound within the four corners of the said statute and cannot exercise its jurisdiction beyond / outside the scope prescribed under the statute.[12]

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[10] Reference may be had to the entire scheme of the Code as contained *inter alia* in Sections 7, 9 and 10 of the Code where the Adjudicating Authority has limited jurisdiction to determine default for admission of process; Sections 15 to 29 regarding division of role and authority between resolution professional and committee of creditors, particularly S 25(2)(h); and Sections 30 and 31 of the Code regarding approval of resolution plans read with Sections 60(5) and 61, limiting the judicial review at the time of approval of the plan.

[11] Reference may also be made to **Section 2**; **Section 3.1**; **Section 3.2.1**; **Section 3.3.1**; **Section 3.4.2 (I)**; **Section 3.4.3**; **Section 4.1.4**; & **Section 5** of the **BLRC Report**.

[12] ***B. Himmatlal Agrawal* v. *Competition Commission of India and Ors.*,** 2018 SCC OnLine SC 574 **(see para 8)**, ***Gujarat Urja Vikas Nigam Limited* v. *Solar Semiconductor Power Company (India) Private Limited and Ors.***, (2017) 16 SCC 498 **(see paras 38 & 39)**, ***Peerless Inn v. Fourth Industrial Tribunal and Ors.***, (2017) 2 CALLT 532 (HC) **(see para 22).**

48. Therefore, the Adjudicating Authority's jurisdiction having been expressly limited by the statute, as explained above, it is impermissible for the Adjudicating Authority to traverse beyond the same.

49. The above principles have been recognised and laid down by this Hon'ble Court in the context of the provisions of the Code and the powers of the Adjudicating Authority and the Appellate Authority established thereunder, in ***K. Sashidhar v. Indian Overseas Bank & Ors.***, **Civil Appeal No. 10673 of 2018** wherein this Hon'ble Court has held that,

> "***the legislature has not endowed the adjudicating authority (NCLT) with the jurisdiction or authority to analyse or evaluate the commercial decision of the CoC muchless to enquire into the justness of the rejection of the resolution plan by the dissenting financial creditors*** *and that* ***the commercial wisdom of the CoC has been given paramount status without any judicial intervention, for ensuring completion of the stated processes within the timelines prescribed by the I&B Code.*** This Hon'ble Court has further held that ***the legislature, consciously, has not provided any ground to challenge the "commercial wisdom" of the individual financial creditors or their collective decision before the adjudicating authority. That is made nonjusticiable***. This Hon'ble Court has also noted and upheld the scheme of the Code where ***the discretion of the adjudicating authority (NCLT) is circumscribed by Section 31 limited to scrutiny of the resolution plan "as approved"*** *by the requisite percent of voting share of financial creditors. Even in that enquiry,* ***the grounds on which the adjudicating authority can reject the resolution plan is in reference to matters specified in Section 30(2)****, when the resolution plan does not conform to the stated requirements.* This Court has further held that ***even the jurisdiction of the NCLAT being in continuation of the proceedings would be circumscribed in that regard and more particularly on account of Section 32 of the I&B Code****, which envisages that any appeal from an order approving the resolution plan*

shall be in the manner and on the grounds specified in Section 61(3) of the I&B Code.

50. Additionally, even the framers of the Code have also been emphatic in recommending that the role of the Adjudicating Authority / Appellate Authority is limited to ensure process compliance especially during insolvency resolution and not judicially review matters of commercial prudence. In this respect, the Bankruptcy Law Reforms Committee ("**BLRC**") Report notes as follows:

> "Role of the Adjudicator focused on matters *of procedure: The Committee recommends that the role of the Adjudicator needs to be carefully laid out so as to both minimise undue burden on the judiciary while simultaneously ensure the fairness and efficiency of insolvency resolution. This is done through two sets of recommendations from the Committee.* ***The Committee recommends that the Adjudicator will focus on ensuring that all parties adhere to the process of the Code. For matters of business, the Committee recommends that Adjudicator will delegate the task of assessing viability to a regulated Insolvency Professional*** *(Burman and Roy, 2015). The Adjudicator will be more directly involved in the resolution process once it is determined that the debt is unviable and that the entity or individual is bankrupt."*[13]
>
> *[Emphasis Supplied]*

51. Therefore, the Code, evidently, requires the committee of creditors to take commercial decisions with respect to a resolution plan and limits judicial review by the Adjudicating Authority / Appellate Authority to ensure only compliance with process and compliance with provisions of the Code. The Appellate Authority in the Impugned Judgement has clearly overstepped its jurisdiction by venturing into matters exclusively in the domain of the committee of creditors.

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[13] See BLRC Report, Vol. 13 of the Convenience Compilation @ Pg. 30-31

VIII. DELIBERATE LEGISLATIVE SCHEME TO LEAVE COMMERCIAL DECISIONS TO COC AND LIMITING THE ADJUDICATING AUTHORITY AS PROCESS SUPERVISOR

52. The Bankruptcy Law Reforms Committee in its report (*which formed the basis for the enactment of the Code*) and recognized by this Hon'ble Court in ***Innoventive Industries Limited* v. *ICICI Bank Limited*, Civil Appeal No. 8337-8338 of 2017**, specifically notes the deliberate scheme of the Code, where the law does not prescribe any particular manner of insolvency resolution and leaves this commercial decision to commercial negotiations without the interference of the legislature as well as judiciary. In this respect, the BLRC Report notes as follows:

> *"**No prescriptions on solutions to resolve the insolvency***
>
> ***The choice of the solution to keep the entity as a going concern will be voted on by the creditors committee. There are no constraints on the proposals that the Resolution Professional can present to the creditors committee.** Other than the majority vote of the creditors committee, the Resolution Professional needs to confirm to the Adjudicator that the final solution complies with three additional requirements. The first is that the solution must explicitly require the repayment of any interim finance and costs of the insolvency resolution process will be paid in priority to other payments. Secondly, the plan must explicitly include payment to all creditors not on the creditors committee, within a reasonable period after the solution is implemented. Lastly, the plan should comply with existing laws governing the actions of the entity while implementing the solutions."*[14]
>
> [***Emphasis Supplied***]
>
> "*The Committee believes that there is only one correct forum for evaluating such possibilities, and making a decision: a creditors*

[14] See BLRC Report, Vol. 13 of the Convenience Compilation @ Pg. 75

*committee, where all financial creditors have votes in proportion to the magnitude of debt that they hold**. In the past, laws in India have brought arms of the government (legislature, executive or judiciary) into this question. This has been strictly avoided by the Committee.** The appropriate disposition of a defaulting firm is a business decision, and only the creditors should make it.*"[15]

[***Emphasis Supplied***]

Similarly, Section 5.3.3 of the BLRC Report states as follows[16]:

"*Obtaining the resolution to insolvency in the IRP: The Committee is of the opinion that there should be freedom permitted to the overall market to propose solutions on keeping the entity as a going concern. Since the manner and the type of possible solutions are specific to the time and environment in which the insolvency becomes visible, it is expected to evolve over time, and with the development of the market.* ***The Code will be open to all forms of solutions for keeping the entity going without prejudice, within the rest of the constraints of the IRP. Therefore, how the insolvency is to be resolved will not be prescribed in the Code. There will be no restriction in the Code on possible ways in which the business model of the entity, or its financial model, or both, can be changed so as to keep the entity as a going concern.*** *The Code will not state that the entity is to be revived, or the debt is to be restructured, or the entity is to be liquidated. This decision will come from the deliberations of the creditors committee in response to the solutions proposed by the market.*"

[***Emphasis Supplied***]

53. It is submitted that besides the prescriptive requirements referred above, which have been embodied under Section 30(2) of the Code and extended to the jurisdiction of the Appellate Authority in terms of Section 61(3) of the Code, the manner in which a committee of creditors proposes to resolve the insolvency of the corporate debtor is a commercial decision of the committee and complete freedom has been provided to the committee by the framers of the Code, to decide on the manner in which it proposes to resolve such

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[15] See BLRC Report, Vol. 13 of the Convenience Compilation @ Pg. 12

[16] See BLRC Report, Vol. 13 of the Convenience Compilation @ Pg. 89

insolvency without the interference of the courts. The BLRC Report states as follows:

> *"The key economic question in the bankruptcy process*
>
> *When a firm (referred to as the corporate debtor in the draft law) defaults, the question arises about what is to be done. Many possibilities can be envisioned. One possibility is to take the firm into liquidation. Another possibility is to negotiate a debt restructuring, where the creditors accept a reduction of debt on an NPV basis, and hope that the negotiated value exceeds the liquidation value. Another possibility is to sell the firm as a going concern and use the proceeds to pay creditors. Many hybrid structures of these broad categories can be envisioned.*
>
> ***The Committee believes that there is only one correct forum for evaluating such possibilities, and making a decision: a creditors committee, where all financial creditors have votes in proportion to the magnitude of debt that they hold. In the past, laws in India have brought arms of the Government (legislature, executive or judiciary) into this question. This has been strictly avoided by the Committee. The appropriate disposition of a defaulting firm is a business decision, and only the creditors should make it."***[17]

54. In fact, the principle that commercial decisions being left to the committee of creditors is stated to be one of the principles driving the design of the Code in the following manner in the BLRC in Section 3.4:

> *"Principles driving the design:*
>
> *The Committee chose the following principles to design the new insolvency and bankruptcy resolution framework:*
>
> *I. The Code will facilitate the assessment of viability of the enterprise at a very early stage.*
>
> ***(1) The law must explicitly state that the viability of the enterprise is a matter of business, and that matters of business can only be negotiated between creditors and debtor. While viability is assessed as a negotiation between creditors and debtor, the final decision has to***

[17] See BLRC Report, Vol. 13 of the Convenience Compilation @ Pg. 12

<u>be an agreement among creditors who are the financiers willing to bear the loss in the insolvency.</u>

<u>(2) The legislature and the courts must control the process of resolution, but not be burdened to make business decisions.</u> *...* ***"[18]***

55. The aforesaid scheme of the Code is in line with UNCITRAL Legislative Guide recommended legislative scheme, which states[19]:

"***2. Nature or form of a Plan***

3. The purpose of reorganization is to maximize the possible eventual return to creditors, providing a better result than if the debtor were to be liquidated and to preserve viable businesses as a means of preserving jobs for employees and trade for suppliers. With different constituents involved in reorganization proceedings, each may have different views of how the various objectives can best be achieved. Some creditors, such as major customers or suppliers, may prefer continued business with the debtor to rapid repayment of their debt. Some creditors may favour taking an equity stake in the business, while others will not. Typically, therefore, there is a range of options from which to select in a given case. ***<u>If an insolvency law adopts a prescriptive approach to the range of options available or to the choice to be made in a particular case, it is likely to be too constrictive.</u>*** *It is desirable that the law not restrict reorganization plans to those designed only to fully rehabilitate the debtor; prohibit debt from being written off; restrict the amount that must eventually be paid to creditors by specifying a minimum percentage; or prohibit exchange of debt for equity.* ***<u>A non-intrusive approach that does not prescribe such limitations is likely to provide sufficient flexibility to allow the most suitable of a range of possibilities to be chosen for a particular debtor.</u>***

<u>20. Rather than specifying a wide range of detailed information to be included in a plan, it may be desirable for the insolvency law to identify the minimum content of a plan, focusing upon the key</u>

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[18] See BLRC Report, Vol. 13 of the Convenience Compilation @ Pg. 28

[19] Refer **UNCITRAL Legislative Guide**, Vol. 12 of the Convenience Compilation @ Pg. 223, 224 & 229

> ***objectives of the plan and procedures for implementation***. *For example, the insolvency law may require the plan to detail the classes of creditors and the treatment each is to be accorded in the plan; the terms and conditions of the plan (such as treatment of contracts and the ongoing role of the debtor); and what is required for implementation of the plan (such as sale of assets or parts of the business, extension of maturity dates, changes to capital structure of the business and supervision of implementation).*
>
> [*Emphasis Supplied*]

56. Therefore, it is evident from the aforestated scheme of the Code as interpreted by this Hon'ble Court in ***K. Sashidhar***, and explained in the BLRC Report, that the appellate authority and / or adjudicating authority has limited judicial review in matters of approval of resolution plan and does not have jurisdiction beyond the four corners of Section 31 read with Section 30(2) of the Code to judicially review or sit in appeal or modify/vary the commercial decision of the committee of creditors.

57. It is submitted that a resolution plan is consent based plan proposed by the resolution applicant for a corporate debtor. The counter party to such a resolution plan is the committee of creditors of such corporate debtor which legislatively is required to give a minimum consent of 66% voting share for consensus ad idem on behalf of all stakeholders, which consent is the basis for the Adjudicating Authority to approve the resolution plan for the corporate debtor. Such a resolution plan (*as consented to / approved by minimum of 66% majority of the Committee of Creditors*) once approved by the Adjudicating Authority becomes binding on all stakeholders in terms of Section 31 of the Code. Therefore, any modification of a plan by the Adjudicating Authority and / or Appellate Authority without the consent of the committee of creditors is illegal as there is no legal basis of a resolution plan which is not consented to by the requisite majority of the committee of creditors.

58. Respectfully, as a consequence of the constitutionality of the Code being upheld by this Hon'ble Court in entirety in *Swiss Ribbons*, the doctrine of consent of the resolution applicant and the Committee of Creditors (*by virtue of positive vote of 66%*) is now recognized as the only consent on the basis of which a resolution plan can be ordered as binding upon all stake holders. There is no power conferred upon the Adjudicating Authority and / or the Appellate Authority to impose conditions in a suo-moto exercise and of their own volition without the same being consented to either by the resolution applicant or the committee of creditors.

59. Therefore, any variation / modification introduced by the Adjudicating Authority and / or the Appellate Authority would constitute a new stipulation under the plan, not agreed to or consented to either by the Arcelor or the Committee of Creditors and therefore be completely bereft of legal authority and is void *per-se*.

IX. COMMITTEE OF CREDITORS HAS THE POWER AND JURISDICTION TO DEAL WITH ALL COMMERCIAL ASPECTS OF A RESOLUTION PLAN, INCLUDING DISTRIBUTION OF RESOLUTION PROCEEDS

60. Respectfully, the distribution of proceeds under a resolution plan is a commercial decision within the domain of the committee of creditors subject to compliance with the requirements of Section 30(2) of the Code.

61. Under the scheme of the Code, the committee of creditors has the power and jurisdiction to deal with all commercial aspects of a resolution plan (which includes the distribution of resolution proceeds). While the Code (*and the regulations thereunder*) provides for the *de minimus* prescriptions as to the mandatory contents of a resolution plan, there is no prescription requiring the resolution applicant alone to provide for the exact inter-se distribution of

resolution proceeds within various classes of stakeholders. There is equally no proscription on the committee of creditors from proposing and deciding a method of distribution of resolution proceeds.

62. It is submitted that the distribution of the resolution proceeds is a commercial decision which is a product of deliberations and negotiations between the committee of creditors and the resolution applicant. Therefore, Arcelor empowering the Committee of Creditors to decide upon the *inter se* distribution amongst the secured financial creditors under the terms of the Approved Resolution Plan after having prescribed with the requirements of Section 30(2) of the Code read with Regulation 38(1A) of the CIR Regulations in terms of Section VIII (*Treatment of various stakeholders*) read with Section V *(Summary proposal of the resolution applicant*), whereby the Approved Resolution Plan provides for the payment to each class of stakeholders, is respectfully fully in compliance with the provisions of the Code and the regulations.

63. Respectfully, examining the feasibility and viability of a plan is a statutory duty cast upon the Committee of Creditors by the Code while approving a resolution plan and besides ensuring compliance with Section 30(2) and Regulation 38 of the CIR Regulations. Beyond this the Committee of Creditors has complete authority to examine all the commercial aspects of a resolution plan including but not limited to the projections made by under a resolution plan; the value being ascribed by a resolution applicant to a corporate debtor basis the realisable value of the assets of the corporate debtor and the treatment of all stakeholders in reference to the priorities of the charges on such assets; the steps to be undertaken by a resolution applicant

for the turnaround of a defaulting corporate as well as the distribution of the proceeds under a resolution plan.

64. In fact, while the Appellate Authority itself had upheld the above position of law in ***Darshak Enterprise Private Limited vs. Chhaparia Industries Pvt. Ltd,*** **Company Appeal (AT) (Insolvency) No. 327 of 2017**, however, in a departure from the principles of continuity, certainty and predictability expected of a tribunal by virtue of the law laid down by this Hon'ble Court[20], has completely disregarded its own earlier decision without any reasoning or explanation.

65. Respectfully, the above principle that **the commercial decisions have been entirely left to the committee of creditors** without interference by the courts/tribunals have (as discussed above) been imbibed in the scheme of the Code, recognized under the BLRC Report as well as the UNCITRAL Legislative Guide on Insolvency Law and upheld by this Hon'ble Court in *K. Sashidhar* (*Supra*).

66. Lastly, it may also be noted that even the latest amendment proposed to the Code specifically in reference to Section 30(4), clarifies that the manner of distribution of proceeds under a resolution plan is also within the domain by the committee of creditors.

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[20] See ***Union of India (UOI) and Ors. v. Paras Laminates (P) Limited***, **(1990) 4 SCC 453**.

X. TREATMENT OF OPERATIONAL CREDITORS UNDER A RESOLUTION PLAN

67. As stated above, there is no provision under the Code to treat all financial and operational creditors equally in recognition of the fact that the two classes of creditors are inherently different and un-equal.

68. It is in recognition of the aforestated that this Hon'ble Court in *Swiss Ribbons* has recognized that the financial and operational creditors form two separate classes of creditors, and thus, legislatively have been treated differently to be equitable.

69. In view of the fact that operational crediors do not have voting rights in a commmottee of creditors, the Code provides an inherent safeguard to protect the interests of operational creditors under the Code is to ensure that the operational creditors receive their liquidation value or Minimum Resolution Proceeds. Therefore, the only payment prescription under the Code read with the CIR Regulations is to provide a minimum of liquidation value or Minimum Resolution Proceeds to the operational creditors of a corporate debtor in priority to any other payments being made to the financial creditors and the role of the Appellate Authority and / or the Adjudicating Authority as regards operational creditors are concerned is limited to ensuring that the minimum prescriptions / safeguards prescribed under the Code are met with effectively

70. The said safeguard/minimum payment prescription for operational creditors in the present case was valued at *nil* (*with liquidation value being approximately Rs. 17,180.50 in comparison to an admitted financial debt of Rs. 49,000 Crores itself*) and therefore did not require the resolution plan to provide for an amount under the resolution plan. However, the Approved Resolution Plan ensures that 90.67% of the operational creditors in number

are paid in full, especially the small operational creditors in addition to the amount of ex gratia Rs. 1,000 Crores allocated by the Committee of Creditors at the meeting held on 27 March 2019. Respectfully, there is no infirmity under the Approved Resolution Plan in this respect.

XI. THE SUCCESSFUL RESOLUTION PLAN ADEQUATELY PROVIDES FOR THE TREATMENT OF OPERATIONAL CREDITORS IN TERMS OF THE CODE AND RELEVANT REGULATIONS AND WAS THE BEST RESOLUTION PLAN AMONGST THE ELIGIBLE PLANS

71. Pursuant to the judgement dated 4 October 2018 of the Hon'ble Supreme Court of India in the matter of ***ArcelorMittal India Private Limited* v. *Satish Kumar Gupta***, Civil Appeal No. 9402-9405 of 2018 ("**SC Judgment**"), the only available eligible resolution plan with the Committee of Creditors were that of Arcelor and Vedanta Limited.

72. It is necessary to note that even though the liquidation value payable to the operational creditors in terms of Section 30(2)(b) being ***nil*** in the facts of the case, the Approved Resolution Plan provided for a payment of Rs. 196 Crores ensuring full payment of admitted claims of **1,682 operational creditors of CD ("Operational Creditors") out of a total of 1,855 Operational Creditors** (i.e. 90.67% of the total Operational Creditors in number) in addition to the full payment of the workmen and complete absorption of the workmen to ensure continued employment. Whereas the resolution plan of Vedanta proposed n***il*** payment to the operational creditors.

73. Thus, on account of the Approved Resolution Plan providing for a higher monetary recovery to the operational creditors (*in addition to others factors including feasibility and viability*), the Committee of Creditors approved the

best resolution plan available for its consideration keeping in mind the interests of all stakeholders and the objective of the Code.

XII. RE-CONSIDERATION OF AMOUNTS PAYABLE TO OPERATIONAL CREDITORS UNDER THE APPROVED RESOLUTION PLAN

74. Lastly, without prejudice to each of the above, the Committee of Creditors in its 22nd meeting held pursuant to the directions of the Appellate Authority's order and directions contained in the order dated 20 March 2019[21], has re-considered the aspects of distribution of proceeds payable under the Apprved Resolution Plan, and despite the fact that:

(a) 90.67% of the total operational creditors in number are being repaid their entire admitted debt even when the liquidation value payable in terms of Section 30(2)(b) was ***nil***;

(b) the allocation towards operational creditors has been made by Arcelor;

(c) Arcelor's refusal to increase the payout under the Approved Resolution Plan despite Committee of Creditors making a request to it to re-consider its allocation towards operational creditors;

(d) Payment of a staggering amount of Rs. 55,000 crores to the operational creditors during the 600 days plus of corporate insolvency resolution process carried out under the watchful eye of the Committee of Creditors as opposed to Committee of Creditors loosing out an interest amount of 12,000 crores during 600 days plus of corporate insolvency resolution process*;*

(e) The interests of operational creditors being well protected and served by ensuring that the Corporate Debtor continues as a going concern, at

[21] Refer order of the Appellate Authority dated 20 March 2019, Vol. 9 @ Pg. 1862-1869

> the cost of the sacrifice of the Committee of Creditors in accepting lesser amount in settlement of its dues as against their fair value keeping in mind the value of security available in satisfaction of their debt;

the Committee of Creditors *vide* a majority of 70.73 percent, *ex-gratia* approved the payment of a capped amount of Rs. 1,000 Crores from the resolution proceeds proposed by Arcelor for the secured financial creditors under the Approved Resolution Plan, for payment to the operational creditors of the Corporate Debtor who have not been proposed any payment against their claims under the Approved Resolution Plan.

75. Therefore, post the decision of the Committee of Creditors on 27 March 2019, the 90.67% of operational creditors (*except the workmen and employees*) having claim amount below Rs. 1 crore were being paid 100% of their admitted dues, and the remaining 9.33% of the operational creditors were being paid 20.1% of their admitted dues. This apart, the workmen and employees all along have been proposed to be paid their full admitted amount under the Approved Resolution Plan.

XIII. THE COMMITTEE OF CREDITORS HAS BALANCED THE INTERESTS OF ALL STAKEHOLDERS INCLUDING OPERATIONAL CREDITORS

76. While discharging its statutory function, the committee of creditors, in addition to ensuring compliance of the statutory safeguards provided under the Section 30 (2) of the Code (*including the better safeguard introduced by the Amendment Act*), takes into account various economic and commercial factors while examining acceptability of treatment of operational creditors under a resolution plan including factors such as:

(i) total outstanding debt of the corporate debtor *vis-à-vis* claims of operational creditors;

(ii) the debt liability of a corporate debtor *vis-à-vis* the availability of assets with the corporate debtor;

(iii) the liquidation value[22] of the corporate debtor to assess the current capacity / value of the assets of the corporate debtor to repay the existing liabilities;

(iv) the satisfaction or substantial satisfaction of claims made by operational creditors in numbers (*as against the total amounts);*

(v) payments made to operational creditors during the CIR Process to ensure the running of a corporate debtor as a going concern; and

(vi) the criticality of the nature of goods or services being provided by the operational creditors to ensure continued business existence of the corporate debtor.

(vii) Nature of claims raised by operational creditors including whether the liability is contigent, disputed or undisputed or qua related or unrelated party.

77. During the CIR process of the Corporate Debtor, where the Committee of Creditors has undertaken the present process in utmost good faith and while keeping in mind the interests of each of the concerned stakeholders of the Corporate Debtor. The request for proposal ("**RFP**") issued by the resolution professional of the Corporate Debtor ("**Resolution Professional**") under Section 25(2)(h) of the Code (*as approved by the Committee of Creditors*) pursuant to which the entire CIR Process of the Corporate Debtor has been undertaken had also directed the resolution applicants to separately specify

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[22] "liquidation value" means the estimated realizable value of the assets of the corporate debtor, if the corporate debtor were to be liquidated on the insolvency commencement date

the amounts being made available to each separate class of stakeholders, including, *inter alia*, the operational creditors of the Corporate Debtor.

78. It is submitted that the facts of the present case very well demonstrate how the ecosystem created under the Code, well balances the interest of all stakeholders including the operational creditors and the said factors were duly considered by the Committee of Creditors while approving the resolution plan. In this respect the following ought to be noted and appreciated:

(i) The resolution of the Corporate Debtor involves resolution of approximately Rs. 49,000 crores of admitted financial debt and approximately Rs. 5,000 crores of the admitted operational debt at the time of approval of the Approved Resolution Plan.

(ii) Arcelor after detailed diligence, proposed a resolution plan with different allocations to different stakeholders involved in the resolution plan, as mandated under the Code read with the relevant regulations. As part of the resolution plan of Arcelor (*as approved by the Committee of Creditors*), 90.67% of operational creditors in number are being paid their admitted dues in full (*by payment of Rs. 196 crores allocated by Arcelor for the operational creditors despite their liquidation value being nil*) against their admitted claim of Rs. 5,058 crores as on the date of the approval of the resolution plan of Arcelor by the Committee of Creditors in addition to the amount of *ex gratia* Rs. 1,000 crores allocated by the Committee of Creditors at the meeting held on 27 March 2019. Therefore, resolution applicants themselves looking into the criticality of the nature of goods or services being provided by the operational creditors for ensuring continued business existence of the corporate debtor are required to make a judgement.

(iii) During the period of August 2017 to March 2019 in the CIR Process of the Corporate Debtor (*i.e. approximately 600 days of the 720 days of the CIR Process*), the business of the Corporate Debtor has been running successfully under the supervision and control of the Committee of Creditors, out of which many of the operational creditors who have been paid off to the tune of approximately Rs. 55,000 crores (*being higher than the total admitted debt of the Corporate Debtor as on the date of the approval of the Approved Resolution Plan*) for the goods supplied and services rendered during the aforementioned period of the CIR Process of the Corporate Debtor as evident from the consolidated information provided by the resolution professional of the Corporate Debtor at the meeting of the committee of creditors of the Corporate Debtor on 27 March 2019.

(iv) On the other hand, the secured financial creditors whose admitted debt is about Rs. 49,000 crores are being paid a discounted amount of Rs. 42,000 crores against the fair value of the secured assets which are available as security to them worth approximately Rs. 45,000 crores, while, they have additionally lost about Rs. 17,000 crores of interest in the last three years due to the account of the Corporate Debtor having been classified as a non-performing asset (*out of about Rs. 12,000 crores of interest was not paid during the aforementioned period of the CIR Process*).

(v) During the CIR Process, the financial creditors have not been made any repayment on account of moratorium under Section 14 of the Code, while the performance of the Corporate Debtor has improved and despite positive EBITDA, a large chunk of the available funds have been utilised to make full payments to the operational creditors for the services rendered and goods supplied during the CIR Process period, including

amount paid towards full profit margins, despite contractual arrangements being in place for priority collection by financial creditors which was foregone.

(vi) Evidently, unlike many other insolvency resolution processes being undertaken under the provisions of the Code, the operational creditors of the Corporate Debtor have reaped the benefit of the Corporate Debtor continuing as a going concern and will continue to reap benefits off of the Corporate Debtor continuing as a going concern on the basis of the sacrifice of the financial creditors towards their interest during CIR Process and their haircut under the Approved Resolution Plan even though the fair value of security available to them is far in excess of the payments proposed under the Approved Resolution Plan.

(vii) Lastly, while the operational creditors have been paid their dues for the goods provided and services rendered during the CIR Process, however, the financial creditors have not reaped any benefit like these operational creditors.

79. The above clearly demonstrate that ecosystem created under the Code, adequately protects the interests of the operational creditors, even though the statute only provides for only the minimum payment due to the operational creditors, however, keeping in view the various economic, financial and business factors of each corporate insolvency resolution process, the committee of creditors along with the resolution applicant would need to look into fact specific cases while approving a resolution plan with terms of payments to the operational creditors over and above the minimum prescriptions under the Code as well as the prescriptions under the regulations, if any, formulated by the IBBI with an oversight of the judicial fora in case

the decision is illogical or suffers from procedural impropriety or shocks the conscience of the Court by defying logic or moral standards.

XIV. THE SUB-COMMITTEE HAS BEEN VALIDLY CONSTITUTED WITH THE REQUISITE APPROVAL OF THE COMMITTEE OF CREDITORS AND HAS ONLY FACILITATED THE DECISION MAKING AND IMPLEMENTATION OF THE DECISIONS TAKEN BY THE COMMITTEE OF CREDITORS

80. The Code or regulations thereunder at no juncture restrict the formation of the Sub-Committee. In fact, it is a deliberate scheme of the Code, in as much as the Code does not prescribe any set process, and leaves the flexibility to the committee of creditors within minimal prescriptions.

81. In terms of Section 21(8) of the Code, all decisions by the committee of creditors can be taken with 51% majority vote and there is no proscription on committee of creditors' authority to create a sub-committee to facilitate decision making and/or implementation of its decision as long as the power and authority vested in the committee of creditors to take decisions is not delegated.[23]

82. In the facts of the present case, the Sub-Committee has been duly and validly constituted with the requisite approval of the Committee of Creditors for administrative convenience, and has always acted as per the authority entrusted by the Committee of Creditors and was never objected to by any member of the Committee of Creditors.

83. Lastly, the finding in the Impugned Judgement that powers of the Committee of Creditors were delegated upon the Sub-Committee and the "secret" negotiations by the Sub-Committee have resulted in the infirmity in the

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[23] Refer to ***Pradyat Kumar Bose v. The Hon'ble Chief Justice of the Calcutta High Court***, *(1955) 2 SCR 1331* and ***High Court of Judicature at Bombay through its Registrar vs. Shirish Kumar Rangrao Patil and Ors.***, 1997 (6) SCC 339.

Approved Resolution Plan is contrary to the facts on record for the following reasons:

(a) The Sub-Committee was duly and **validly constituted with the requisite approval** of the Committee of Creditors with overwhelming votes in its favour, much beyond the stipulated voting threshold.

(b) The Sub-Committee's **constitution as well as scope of work/assignment was put to vote** at multiple validly constituted meetings of the Committee of Creditors (*followed by a valid resolution to this effect*) before any task was entrusted to or undertaken by the sub-committee.

(c) **No decision making was delegated to the Sub-committee**, the only tasks delegated to the Sub-committee were either to execute Committee of Creditors decisions (such as filing of pleadings etc.) or facilitating decision making.

(d) **Sub-committee did not at any time, decide or even recommend on the distribution of amounts** payable to secured financial creditors under the Approved Resolution Plan, and it was solely the decision of the Committee of Creditors.

XV. MATERIAL IRREGULARITY AND IMPROPER EXERCISE OF JURISDICTION FOR ADMISSION OF OPERATIONAL CREDITORS' CLAIMS – CREATING LACK OF PREDICTABILITY AND FINALITY

84. The decision of the Appellate Authority to admit various rejected/disputed/estimated claims suffers from material irregularity so far as:

(a) Firstly, neither the Adjudicating Authority and/or the Appellate Authority are permitted under the Code to admit claims (not been admitted by the resolution professional) without due examination of the

proof or the reasoning afforded by the resolution professional for non-admission. Despite that the Adjudicating Authority went ahead and directed "registration" of claims worth Rs. 13, 767 crores without clarifying whether the same needed to be admitted or not.

(b) Secondly, while Section 424 of the Companies Act, 2013 bestow *inter alia* upon the Appellate Authority the power of ordering discovery, inspection etc. However, the Appellate Authority failed to exercise the said power and / or even discuss the reasoning or the basis for admission of various disputed / rejected / partially admitted claims.

(c) Thirdly, the Appellate Authority admitting claims to the tune of more than Rs. 14,000 Crores at this belated stage (*over and above the operational creditor claims of approximately Rs. 5,000 crores admitted by the Resolution Professional as on the date of approval of the Approved Resolution Plan by the Committee of Creditors*) without due application of mind and sound reasoning runs to the principles of predictability and transparency, essential for any insolvency resolution regime.

(d) It is shocking to note that these operational creditors whose claims have been admitted by the Appellate Authority, claimed for a total amount of approximately Rs. 13,175 crores under their respective Form B(s) (*as filed before the Resolution Professional*), however the Appellate Authority admitted a total claim amount of Rs. 14,660 crores against these operational creditors i.e. more than the amount originally claimed by these operational creditors as on insolvency commencement date in accordance with the provisions of the Code.

85. Respectfully, the Appellate Authority has not even thought it fit to record, examine and deal with the reasons for non-admittance of such claims by the resolution professional and the sheer non-application of mind has resulted in blind admittance of operational claims which were disputed by the Corporate Debtor and/or were not considered as payable by the Corporate Debtor in the first place. For example:

(a) out of the total additional operational claims of approximately Rs. 14,000 crores, around Rs. 11, 278 crores worth of claim amount pertain to disputes which are not yet crystallised and are pending at various judicial foras and therefore were admitted by the Resolution Professional at a notional amount of Rs. 1.

(b) The operational claim amount of Dakshin Gujarat Vij Company Limited (of Rs. 5,882 crores approximately as submitted to the Resolution Professional) ("**DGVCL**") was not admitted by the Resolution Professional as the underlying claims were disputed. The claim amount pertaining to cross-subsidy charges under the DGVCL Claim was not admitted by the Resolution Professional as the issue of leviability of cross-subsidy charge in the first place itself has been contested by the Corporate Debtor and the matter is pending before the Hon'ble Gujarat Electricity Regulatory Commission.

(c) Another example can be the operational claim amount of Gujarat Energy Transmission corporation Limited for an amount of Rs. 827.18 crores as submitted to the Resolution Professional for certain transmission/wheeling charges, which was admitted by the Resolution Professional at a notional value of Re. 1 as the matter was pending before this Hon'ble Court. Accordingly, the admittance of such

disputed claims (*pending before various authorities including this Hon'ble Court*) has usurped the jurisdiction of the relevant judicial fora including but not limited to this Hon'ble Court by effectively deciding the dispute inter se the parties and the Corporate Debtor, still pending adjudication.

86. Apart from the above disputed amounts, the Appellate Authority has erroneously on a complete mis-appreciation of facts has admitted operational claim amounts to the tune of approximately Rs. 2,560 crores. For example:

(a) the Appellate Authority has admitted the claim amount of Rs. 813.30 crores of MSTC Limited (who procures iron ore, pellets etc, for the Corporate Debtor on a cash and carry basis) when the said claim pertained to their dues against the Corporate Debtor post the commencement of the CIR process and not pre-CIR dues. It is an admitted fact by MSTC that it had filed a claim under Form B for Rs. 875.88 crores, payment for which was made by the Corporate Debtor and therefore Corporate Debtor was not liable for any pre-CIR dues to MSTC. It is understood by the Appellant herein that apart from a outstanding balance of approximately Rs. 6 crores, all payments (whether pre-CIR or during CIR) have been made to MSTC and considering the deposits made by the Corporate Debtor with MSTC, net amount is liable to be received from MSTC by the Corporate Debtor. Accordingly, the entire amount of Rs. 813.30 crores admitted by the Appellate Authority is on erroneous grounds.

(b) Another example would be the claim amount of Rs. 861.19 crores submitted by Collector of Electricity Duty Energy & Petrochemicals Department, Government of Gujarat, has been admitted by the Appellate Authority, when the Resolution Professional had already

admitted the said amount as operational debt, thereby resulting in double counting of this claim amount of Rs. 861.19 crores.

(c) Similarly, the Appellate Authority on a mis-reading of the facts has sought to admit a claim of Rs. 946.88 crores of Bharat Petroleum Corporation Limited ("**BPCL**"), when the claim filed by BPCL before the Resolution Professional was only Rs. 261.54 crores (admitted at notional amount of Re. 1 on account of dispute). It appears that the additional amount of approximately Rs. 685.34 crores admitted by the Appellate Authority for BPCL, *inter alia*, contains an amount of Rs. 443 crores which has been double counted and another amount of Rs. 181.50 crores which was claimed by BPCL belatedly and possibly for a period post commencement of CIR of the Corporate Debtor and not in the prescribed format in terms of the Code.

87. Evidently, the Appellate Authority has gravely erred in going ahead and admitting a staggering amount of about Rs. 14,000 crores without reference to underlying facts or documents.

XVI. PERMITTING CLAIMS TO BE RAISED OUTSIDE THE CODE AFTER APPROVAL OF RESOLUTION PLAN

88. The Appellate Authority has erroneously permitted several of the disputed claims to be raised oustside the provisions of the Code after the approval of the resolution plan by referring and relying upon Section 60(6) of the Code saving limitation for barred claims.

89. The Appellate Authority has failed to appreciate that if stakeholders are permitted to interfere with and stifle the finality of processes at such belated stages (*after the entire process having culminated into an approved resolution plan*), such interference will defeat the entire object of the Code to attract the

best possible resolution proposals for the corporate debtor, as no serious resolution applicant would come forward with the best possible proposal on account of such uncertainty and open ended liability in respect to such disputed claims permitted to be kept outside the resolution process.

90. In accordance with Section 30(1) of the Code, a resolution applicant is required to prepare and submit a resolution plan in accordance with the information memorandum prepared by the Resolution Professional in accordance with Section 29 of the Code. Section 29 of the Code read with Regulation 36 of the CIR Process Regulations, specifically require an Information Memorandum to contain details of all disputes in relation to the corporate debtor, so that the resolution applicant is put to notice of the same and can deal with the same as part of the resolution plan. Respectfully, a disputed claim of an operational creditor permitted to be pursued outside the resolution process, can be given a superior status than the admitted claims under the Code, which suffer a hair cut.

91. The Impugned Judgement by further allowing claimants of the Corporate Debtor, whose claim have not been dealt with under the Approved Resolution Plan, to agitate their claims subsequent to the resolution applicant taking over the Corporate Debtor defeats the very purpose of insolvency resolution, which is to address all liabilities of the corporate debtor in one go and allow the corporate debtor to re-surface as a viable enterprise with its causes of distress resolved.

XVII. EXTINGUISHMENT OF THE RIGHT OF THE CREDITORS AGAINST GUARANTEES EXTENDED BY THE PROMOTER/PROMOTER GROUP OF THE CORPORATE DEBTOR

92. The Appellate Authority in para 31 of the Impugned Judgement has also erroneously proceeded to hold that upon part satisfaction of the debt by the principal borrower corporate debtor in terms of a resolution plan approved in a CIR process, the guarantee by personal or corporate debtors becomes ineffective. Respectfully, the guarantors to the financial creditors do not stand absolved even when the resolution plan in a corporate insolvency resolution process of the principal borrower is approved, unless the resolution plan so approved makes the full payment of the outstanding debt. Similarly, in para 221 of the Impugned Judgment, proceeding on a similar erroneous assumption, holds that principal borrowers and such other co-obligors shall stand discharged by payment of part-debt by the corporate debtor in its capacity as a guarantor, upon approval of a resolution plan of the corporate debtor.

93. A creditor has a right to proceed against either and/or both the principal borrower and the guarantor and other co-obligors for the payment of the debt due. Therefore, while the part-payment made under a resolution plan upon its requisite approval would absolve the corporate debtor, however, if such payment is lesser than the total admitted debt of such creditor, then the same by no stretch of imagination would settle the entire debt and absolve the gurantor of its liability to pay towards the remaining debt or make the guarantee ineffective, as held by the Appellate Authority.

94. The Appellate Authority infact, failed to appreciate that the mutual understanding between the resolution applicant Arcelor and the Committee of

Creditors was clearly to protect and retain the right of the creditors to proceed against the guarantors for the balance debt after payment of the part debt by the Corporate Debtor. In fact the resolution plan dated 2 April 2018 was specifically amended to this effect post negotiations with the Sub-committee and it was agreed by Arcelor that the assignment of debt against the payment of resolution proceeds shall be without the benefit of guarantees, and thus, the creditors shall continue to be beneficiaries of the same.

95. For instance Mr. Prashant Ruia a promoter director of the Corporate Debtor had given his personal guarantee.[24] Being a promoter director he is presumed to be amongst those responsible for the insolvency of the Corporate Debtor and is also disqualified from being a resolution applicant. Such a promoter guarantor cannot possibly be entitled to any right of subrogation as that would run contrary to the objective of the Code. Section 140 of the Contract Act, 1872 giving a right of subrogation to a guarantor would be inapplicable to CIR process proceedings. This provision is attracted when surety makes a payment when the debt has become due or there is default on the part of principal debtor. In the present case the payment is to be made by the Resolution Applicant in accordance with the resolution plan. Second, the terms of the guarantee executed by Mr Ruia does not reserve the right of subrogation. The Deed of Guarantee clearly provides that the liabilities of the guarantor are unconditional and irrevocable and the same are not discharged in any manner including ***any insolvency or similar proceedings***.

96. Clearly, in terms of the the Deed of Guarantee the guarantor is not released or discharged from his liability under the guarantee on account of the security

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[24] Refer to **Deed of Guarantee dated 28 September 2013** executed by Mr. Prashant Ruia (Volume 15 of the Convenience Compilation at page 169).

of the loan being transferred or relinquished in favour of the Resolution Applicant or on account of the abatement of the right of subrogation available to the Guarantor under the law of contract. The same would be the consequence in view of the approved resolution plan being binding on the Guarantor by virtue of Section 31(1) of the Code. Further, as mentioned above under the Approved Resolution Plan the guarantees by promoters and affiliate groups were kept alive for the benefit of the Secured Financial Creditors and this was specifically and consciously provided for in the modified resolution plan.

97. The above apart, in any case, it is a settled position of law (*as also enumerated in Section 128 of the Indian Contract Act, 1872*) that the liability of a guarantor is co-extensive with that of the principal borrower.[25] Hence, until the entire debt is paid off to the creditor in entirety, the gurantor is not absolved of its joint and several liability to make payment of the amounts outstanding in favour of the creditor. Neither does this absolve or discharge the guarantors of its obligations in terms of Sections 133 to 136 of the Indian Contract Act, 1872, on account of release/discharge/composition or variance of contract with the principal borrower. In terms of Section 31 of the Code, a resolution plan approved by the Adjudicating Authority is binding on all stakeholders including the guarantors, and hence, the release/discharge/ composition or variance of contract with the principal borrower in terms of a resolution plan, is statutorily presumed to be consented to by the guarantors in question. Therefore, approval of a resolution plan, release/discharge or

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[25] ***Bank of Bihar Limited* v. *Damodar Prasad & Ors.***, AIR 1969 SC 297; ***State Bank of India* v. *M/s. Indexport Registered & Ors.***, (1992) 3 SCC 159; ***Industrial Investment Bank of India Ltd.* v. *Biswanath Jhunjhunwala***, (2009) 9 SCC 478.

entering into a composition with the principal borrower cannot discharge the guarantor in any manner whatsoever.

98. It is in fact an established principle of law that discharge of principal borrower on account of bankruptcy does not discharge the liability of a gurantor. This Hon'ble Court in the case of ***Maharashtra State Electricity Board, Bombay* v. *Official Liquidator, High Court, Ernakulam & Ors.*, (1982) 3 SCC 358** (*later followed and reiterated in* ***Punjab National Bank v. State of U.P. and Ors., (2002) 5 SCC 80***) has held that:

> "***The fact that the Company in liquidation i.e. the principal debtor has gone into liquidation also would not have any effect on the liability of the Bank i.e. the guarantor.*** *Under Section 128 of the Indian Contract Act, the liability of the surety is co-extensive with that of the principal debtor unless it is otherwise provided by the contract. A surety is no doubt discharged under Section 134 of the Indian Contract Act by any contract between the creditor and the principal debtor by which the principal debtor is released or by any act or omission of the creditor, the legal consequence of which is the discharge of the principal debtor.* ***But a discharge which the principal debtor may secure by operation of law in bankruptcy (or in liquidation proceedings in the case of a company) does not absolve the surety of his liability*** *...*"
>
> [***Emphasis Supplied***]

99. In fact, the above position of law as laid down by this Hon'ble Court is in recognition of the age old legal position laid down by the courts in United Kingdom that the discharge of the debt of a principal borrower by operation of law, would not absolve the guarantor of its liability as evident from the following:

(a) ***In re Jacobs Ex parte Jacobs*** **[1875] X Law Rep. 211 (Chancery Appeals)**

"*We entirely agree in the decision of the Court of Common Pleas, and in the reasons they have given for it.* ***We think that a discharge of a debtor under a liquidation or a composition is really a discharge in bankruptcy by operation of law. Where a creditor voluntarily agrees to a composition by deed or agreement with the acceptor, it is by his act alone that the acceptor is discharged and the position of the drawer altered.***

On the other hand, if resolutions for liquidation by arrangement or for composition were to contain a reserve of remedies by the creditors against any other person than the debtor, the consequence would be that the debtor would not, either by arrangement or by composition, be completely discharged from any of his debts in respect of which the creditor had a remedy against any other person, which we think would be contrary to the intention of the Act."

[Emphasis Supplied]

(b) ***In re Fitzgeorge Ex parte Robson*** **[1905] 1 K.B. 462**

"I think in this case that the creditor is entitled to prove for the value of the guarantee that the debtor has given. ***It is said that, because the principal debt is gone, therefore the liability under the guarantee to pay the interest on the debenture is also gone. I do not agree with that view. The principal debt is gone no doubt, but not by any act of the creditor. It is gone by operation of law. The principal debt will never be repaid, but in my opinion the obligation of the debtor to pay the interest under his guarantee remains. There must be a declaration that the creditor is entitled to prove for the estimated value of his security, and if necessary there must be a reference to the registrar to ascertain the amount.***"

[Emphasis Supplied]

(c) ***Dane v. The Mortgage Insurance Corporation Limited***, 1894, 1 Q.B. 54 C.A

The contract was upon its true construction one of insurance against a certain event, viz., the bank's default, and, that event having happened, the defendants were liable to pay the sum insured, but would be entitled, the contract being one of indemnity, upon payment to be subrogated to the rights of the plaintiff under the scheme of arrangement.

By Kay, L.J: Whether the contract was one of suretyship or one of insurance, the scheme of arrangement, which operated to discharge the bank under the statute and not by way of accord and satisfaction, did not defeat the right which had vested in the plaintiff under the contract upon the default made by the bank. ***The authorities are clear to the effect that a discharge of the principal debtor by operation of law, as in the case of a bankruptcy or composition under the Bankruptcy Act, does not release the surety: Ex parte Jacobs, In re Jacobs. Such a composition is not equivalent to a voluntary accord and satisfaction at common law: Slater v. Jones This very point was considered in In re London Chartered Bank of Australia by Vaughan Williams, J., who thought that such a scheme of arrangement as this would not discharge sureties.*** *It is clear from condition 2 indorsed on the policy that the parties contemplated the very case that has arisen, and intended that in that case the defendants should pay and take an assignment of the plaintiff's rights under the arrangement.*

At the moment when the money became due, default was made by the principal debtor, and thereupon the right of the plaintiff as against the so-called guarantor or surety under the contract came into existence. ***It happened afterwards that an arrangement was entered into for the winding up and what has been called "reconstitution" of the bank with which the money was deposited; and it is stated that by virtue of a Colonial Act such arrangement is binding on all the creditors of the bank, including the plaintiff. Thereupon the ingenious but, as it seems to me, fallacious argument was put forward by the defendants' counsel that the scheme of arrangement amounted to an accord and satisfaction for the original debt, the effect of which was to discharge the defendants' liability.*** *An answer to that contention may be found in*

the case of Slater v. Jones [6]*, the result of which appears to be clearly to shew that a composition resolution by a meeting of creditors under the bankruptcy laws, by which all creditors are bound, would not operate in the manner suggested by the defendants' counsel.*

[Emphasis Supplied]

100. Therefore, the finding of the Impugned Judgement assuming settlement of the entire debt on account of part-payment under the Approved Resolution Plan is inherently contrary to the legal principles settled by this Hon'ble Court as well as recognized across the globe.

101. The submission of the Appellants herein is further strengthened by this Hon'ble Court's judgement in ***State Bank of India* v. *V. Ramakrishnan & Ors.*, 2018 (9) SCALE 597** wherein this Hon'ble Court has recognized that a guarantor cannot seek a discharge of its liability on account of a resolution plan being approved and the terms of a resolution plan can very well provide for the continuation of the debt of the guarantors and therefore, in terms of Section 31 of the Code, the said terms of a resolution plan are binding on even the guarantors. The following observations of this Hon'ble Court in ***State Bank of India* v. *V. Ramakrishnan & Ors.* (*Supra*)** are being reproduced herein for ready reference:

"*22. Section 31 of the Act was also strongly relied upon by the Respondents. This Section only states that once a Resolution Plan, as approved by the Committee of Creditors, takes effect, it shall be binding on the corporate debtor as well as the guarantor.* ***This is for the reason that otherwise, under Section 133 of the Indian Contract Act, 1872, any change made to the debt owed by the corporate debtor, without the surety's consent, would relieve the guarantor from payment. Section 31(1), in fact, makes it clear that the guarantor cannot escape***

payment as the Resolution Plan, which has been approved, may well include provisions as to payments to be made by such guarantor. *This is perhaps the reason that Annexure VI(e) to Form 6 contained in the Rules and Regulation 36(2) referred to above, require information as to personal guarantees that have been given in relation to the debts of the corporate debtor.*"

[***Emphasis Supplied***]

102. The above apart, even otherwise contractually, in several of the guarantees executed by the guarantors to the Corporate Debtor have themselves waived their right to be discharged on account of any variance of contract and/or release/discharge of the Corporate Dbetor. Such a waiver, is respectfully valid in law as long as the waiver of the advantages offered by law is given in a private capacity. This has been recognized by this Hon'ble Court in the case of ***H.B. Basavaraj (Dead) by LRs. and Anr.* v. *Canara Bank and Ors.*, (2010) 12 SCC 458**, wherein it was held that:

"*5. ...The observations of this Court in Provash Chandra Dalui v. Biswanath Banerjee, AIR 1989 SC 1834 at Para 21 might be useful to recollect at this point of time. It runs as follows:* ***The essential element of waiver is that there must be a voluntary and intentional relinquishment of a known right or such conduct as warrants the inference of the relinquishment of such right. It means the forsaking the assertion of a right at the proper opportunity****.*

6. An examination of the agreement executed between the appellant Basavaraj (since deceased) and the Bank would clearly show it to be one of a continuing guarantee. Section 129 of The Indian Contract Act, 1872 (hereinafter referred to as "the Act") defines a continuing guarantee as "A guarantee which extends to a series of transactions is

called a "continuing guarantee"." Section 130 of the Act says that "A continuing guarantee may at any time be revoked by the surety, as to future transactions, by notice to the creditor." A reading of the agreement clearly shows that the guarantee was to continue to all future transactions except when the guarantor disclaimed from his liability through a written statement. The deed also clearly mentions that while between the guarantor and borrower, the guarantor is only a surety; yet between the bank and the guarantor, the surety is the principal debtor and his liability would be co-extensive to that of the borrower. Accordingly, the guarantor himself waived off his rights under Chapter VIII of the Act which is conferred on a surety. ***This Court is in respectful agreement with the decision of Karnataka High Court in the case of T. Raju Shetty v. Bank of Baroda AIR 1992 Karnataka 108 whereby the High Court held that in surety agreements, the surety can waive his rights available to him under the various provisions of Chapter VIII of the Act. It is in line with long established precedents that anyone has a right to waive the advantages offered by law provided they have been made for the sole benefit of an individual in his private capacity and does not infringe upon the public rights or public policies.*** *This can be inferred from a reading of the Halsbury's Laws of England, Vol 8, 3rd Edn. at page 143 which reads as follows:*

> ***As a general rule, any person can enter into a binding contract to waive the benefits conferred upon him by an Act of Parliament, or, as it is said, can contract himself out of the Act, unless it is shown that such an agreement is in the circumstances of the particular case contrary to public policy.***

This principle was reiterated in Lachoo Mal v. Radhey Shyam, (1971)1 SCC 619."

[***Emphasis Supplied***]

103. Therefore, while keeping in view the above position of law laid down by this Hon'ble Court in *H.B. Basavaraj (Dead) by LRs. and Anr.* v. *Canara Bank and Ors.* (*Supra*), the contractual stipulations waiving the rights of the gurantors, are valid and binding on such guarantors.

104. Without prejudice to the above, it would not be out of place to submit that a promoter having itself contributed towards the insolvency of the Corporate Debtor cannot seek to be benefitted on account of subrogation rights at the expense of the creditors and the Corporate Debtor. Any such findings are in fact in a complete contradiction to Appellate Authority's own judgement (*upheld by this Hon'ble Court*)[26] wherein the Appellate Authority **(a)** rejected the contention of the promoters that a resolution plan containing the stipulation regarding extinguishment of the right of subrogation of personal guarantors is violative of the provisions of the Indian Contract Act; and **(b)** held that the intention of the legislature is not to benefit the personal guarantors by excluding the exercise of legal remedies available in law by the creditors with respect to their recovery of dues by enforcement of guarantees.

XVIII. UTILISATION OF PROFITS OF THE CORPORATE DEBTOR DURING CIR PROCESS

105. It is submitted that the interference of the Appellate Authority as regards the distribution of the profits / excess monies available with the Corporate Debtor in contradiction to the express terms of the request for proposal issued in terms

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[26] ***Lalit Mishra & Ors.* v. *Sharon Bio Medicine Ltd & Ors.***, Company Appeal (AT) (Insolvency) No. 164 of 2018 (***upheld by this Hon'ble Court in Civil Appeal No. 1603 of 2019***)

of Section 25(2)(h) of the Code and consented to between the Committee of Creditors and Arcelor, is without jurisdiction and another instance of vitiation of the consent granted by the Committee of Creditors.

106. Respectfully, it is matter of record that as part of the lending given by the members of the Committee of Creditors to the Corporate Debtor, all present and future assets of the Corporate Debtor, including cash flows of the Corporate Debtor were charged in favour of the secured creditors. Therefore, directing distribution of the same amongst without the consent of the parties is in violation to the principle of consent.

107. The above illegality of the Impugned Judgment becomes even more evident for having not appreciated that while the interests of the operational creditors were duly protected during the CIR Process on account of having been paid a staggering amount of approximately Rs. 55,000 crores during the CIR process run under the supervision and control of the Committee of Creditors, for the good supplied / services rendered by them to the Corporate Debtor during the CIR Process. On the other hand, the members of the Committee of Creditors have lost interest in excess of Rs. 12,000 Crores while ensuring continuity in business operations of the Corporate Debtor and timely payments to operational creditors through continuation of various letters of credit and bill discounting facilities to the Corporate Debtor.

108. Evidently, the Operational Creditors are already reaping the benefit of the CD continuing as a going concern as they have earned full profit margins on the goods and services provided by them during the CIR Process whereas the financial creditors have not received any payments whether towards their interest or principal amounts during CIR process even though **(a)** the profits / excess cash flow of the Corporate Debtor is charged to the financial creditors

and **(b)** the fair value of security available to such financial creditors is far in excess of the payments proposed under the Approved Resolution Plan.

XIX. ARCELOR IS LIABLE TO MAKE PAYMENTS TOWARDS ANY ADDITIONAL LIABILITY TOWARDS THE OPERATIONAL CREDITORS

109. Without prejudice to each of the above, if at all any further payments are to be made to Operational Creditors, Arcelor is be liable to make such additional payments as it is Arcelor which has originally proposed Rs. 196 crores to the Operational Creditors and an upfront payment of Rs. 42,000 crores to the secured financial creditors. The amount of Rs. 42,000 crores available to the secured financial creditors under the Succesful Resolution Plan cannot be reduced in any way whatsoever, as it would alter the very edifice of commercial decision of the CoC and hence, re-open the issue of plan approval *de-novo.*

FILED THROUGH:

SHARDUL S. SHROFF
ADVOCATE FOR THE COMMITTEE OF CREDITORS