



## ERGO

*Analysing developments impacting business*

### THE ESSAR STEEL SAGA: SUPREME COURT BRINGS MUCH NEEDED CLARITY TO IBC

19 November 2019

#### INTRODUCTION

On 15 November 2019, a three judge bench of the Supreme Court delivered its judgment in the much-anticipated matter of *Committee of Creditors of Essar Steel India Limited v. Satish Kumar Gupta and Ors.*, Civil Appeal No. 8766-67 of 2019. The Supreme Court heard appeals against the National Company Law Appellate Tribunal's ("NCLAT") judgment dated 04 July 2019 ("**Judgment**"). The Supreme Court also heard challenges to the Insolvency and Bankruptcy (Amendment) Act 2019 ("**2019 Amendment**") which has introduced key amendments to the Insolvency and Bankruptcy Code 2016 ("**Code**").

The Judgment has been set aside by the Supreme Court and the resolution plan submitted by ArcelorMittal India Ltd. ("**Arcelor**") has been upheld. This has finally paved the way for implementation of Arcelor's plan and ending the insolvency resolution process which has already run for more than 800 days .

The Arcelor plan, amongst other matters required, (i) junior creditors, who did not hold security over project assets, to incur significant losses relative to senior secured creditors (e.g. Standard Chartered Bank stood to recover only INR 59.26 Crores againsts its admitted secured debt of INR 3,487.10 Crores, whereas State Bank of India stood to recover INR 11,871.96 Crores on its admitted secured debt of approx. INR 13,220.91 Crores); and (ii) operational creditors ("**OCs**") with claims in excess of INR 1 Crore to incur substantial write-offs (with nil recovery in most cases), in stark contrast to almost 90% recoveries for senior secured creditors. Such "unequal treatment" of operational and junior creditors, which was approved by the Committee of Creditors ("**CoC**"), was the primary source of litigation.

#### 1. COC DECISION PARAMOUNT

- The Supreme Court has reiterated that it is ultimately the commercial wisdom of the CoC (as upheld in this case) which determines and approves the best resolution plan. This includes the "feasibility and viability" of a resolution plan, considering all aspects including the manner of distribution of funds among the various classes of creditors.
- The Supreme Court did however note that the CoC while exercising its commercial wisdom should consider preserving the business as a going concern, maximising value of assets of the corporate debtor and balancing interests of all stakeholders, including OCs. That said, courts (i.e. the

National Company Law Tribunal and National Company Law Appellate Tribunal) can at best require the CoC to only reconsider a resolution plan which has not considered the above factors. The Code does not confer any power on courts to prescribe the contents of a resolution plan (or the manner of its implementation) apart from those statutorily mandated in the Code.

## 2. MINIMAL INTERFERENCE BY COURTS

- The Supreme Court has held that courts have limited powers of interference with the decision of the CoC. There is no discretionary or equitable jurisdiction, nor can courts examine the supposed question of justness of a resolution plan as long as the interests of each class of creditors has been considered by the resolution applicant.

## 3. UNEQUAL TREATMENT OF CREDITOR CLASSES UPHELD

- The Supreme Court upheld the differential treatment of Financial Creditors ("FC") and OCs, underscoring the principle that equitable treatment is to be accorded only to similarly placed creditors or creditors in the same class. Further, the Court held that the Code does not provide for FCs and OCs to be paid the same amounts or percentages in order for any resolution plan to comply with the Code.
- The Court further held that while OCs are to receive a minimum payment being not less than liquidation value, such is not the case with FCs. The Code itself differentiates between OCs and FCs. In fact, even secured and unsecured creditors do not need to be paid the same since they are treated differently within the Code.

## 4. SUB-COMMITTEE CONSTITUTION UPHELD

- The Court held that in exercising its functions, the CoC is not precluded from appointing sub-committees for the purpose of negotiating with resolution applicants, or for the purpose of performing other ministerial or administrative acts, provided such acts are in the ultimate analysis approved and ratified by the CoC.

## 5. GUARANTOR BOUND & LIABLE

- The Court reiterated its earlier holding that personal guarantors are bound by the terms of the resolution plan and cannot claim the benefit of a moratorium even though they are not parties to the resolution plan. This is on the basis that the Code provides that once a resolution plan is approved by the CoC, it is binding on all stakeholders, including guarantors.
- The Court was also inclined to take a view that the guarantor's right of subrogation (against the corporate debtor) could be extinguished under the terms of a resolution plan.

## 6. CORPORATE DEBTOR - CLEAN SLATE

- The Supreme Court clarified that re-agitation of undecided claims cannot be permitted and that all claims must be submitted to and decided by the resolution professional so that the prospective resolution applicant knows exactly what needs to be paid to take over and run the business. This

provision ensures that the successful resolution applicant starts running the business of the corporate debtor with a "clean slate".

## 7. ROLE OF THE RESOLUTION PROFESSIONAL

- The Supreme Court has clarified that the role of the resolution professional is not adjudicatory but administrative. Under the Code, the resolution professional is only required to collect, collate and admit claims on the basis of which negotiations can take place between the resolution applicant and the CoC.

## 8. 2019 AMENDMENT UPHELD

### **330 day timeline not mandatory:**

- The Supreme Court, in taking note of the judicial adage that time taken in legal proceedings cannot possibly harm a litigant, has held that the corporate insolvency resolution process ("**CIRP**") must be "ordinarily" completed within the outer limit of 330 days from insolvency commencement date unless extended by the court for sufficient cause i.e. primarily delay in disposal of proceedings by courts.

### **Liquidation value as minimum threshold:**

- The Court upheld the amendment stipulating payment of minimum amounts to OCs and dissenting FCs (being the amounts which would be payable to them basis the liquidation value of the corporate debtor, which in the instant case was nil) as a beneficial provision. Further, it has been clarified that courts cannot question the merits of a business decision made by the requisite majority of the CoC.

## 9. ARCELORMITTAL RESOLUTION PLAN

- The Supreme Court held that the CoC does not act in any fiduciary capacity and consequently refused to interfere with the financial allocation by the CoC to Standard Chartered Bank ("**SCB**") based on the value of its security interest, given SCB only had a pledge of shares of Essar Steel Offshore and a corporate guarantee from Essar Steel India Limited (the corporate debtor).
- Similarly, claims by certain other OCs (including government owned entities such as Dakshin Gujarat Vij Co., Sales Tax Officer, Gujarat Energy Transmission Corporation Limited and Indian Oil Corporation Limited) have been rejected and notional allocation of Rupee 1 by the resolution professional has been upheld on account of pending disputes with these entities.

## 10. CONCLUSION

The Supreme Court judgment is an authoritative pronouncement which settles several vexed issues that were affecting the smooth working of the Code. Various aspects of corporate insolvency resolution process including the supremacy of the CoC's decisions, and more critically, limiting the powers of courts to interfere with commercial terms of a resolution plan have now been finally resolved.

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