IN THE HIGH COURT OF JUDICATURE AT MADRAS

W.P. No.29845 of 2022

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Reserved on : 15.09.2023

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CORAM: JUSTICE N.SESHASAYEE

W.P. No.29845 of 2022
and WMP.No.29233 of 2022

The National Sewing Thread Co. Ltd.,
(Post Insolvency Resolution under IBC)
Represented by its Successful Resolution Applicant
Mr.B.Venkatesan
11, Venugopala Pillai Road
Chidambaram - 608 001. ... Petitioner

Vs.

1.The Superintending Engineer
TANGEDCO
Cuddalore Electricity Distribution Circle
Capper Hills, Cuddalore - 607 001.

2.The Assistant Electrical Engineer
TANGEDCO
Anantheeswaran Koil Street
Chidambaram - 608 001. ... Respondents

PRAYER: Writ petition filed under Article 226 of the Constitution of India for a Writ of Certiorarified Mandamus calling for the records of the impugned demand notice dated 19.01.2022 in Lr.No.SE/CEDC/CUD/DFC/AO/REV/ASS.No.384/2022 on the file of the respondents and quash the same as being contrary to law and decisions of the Hon'ble Supreme Court of

India, as such arbitrary, highhanded, illegal, without jurisdiction and direct the respondents to forthwith provide the electricity connection as applied by the petitioner.

For Petitioner : Mr.E.Omprakash, Senior Counsel
Assisted by Mr.Imayavaramban
for M/s.Ramalingam & Associates

For Respondents : Ms.Keerthana R.Shenoi
for Mr.V.Venkata Seshaiya
Standing Counsel for TANGEDCO
[R1 & R2]

ORDER

This petition was filed for a writ of certiorarified mandamus to quash the demand notice of the respondents and to further direct the respondents to provide the electricity connection.

THE FACTS:

2. The case of the petitioner is as below:

a) The petitioner herein is a public limited company, and it is also registered under the MSME Act, 2006. It had availed financial assistance from M/s. Indian Overseas Bank (henceforth IOB). However, it suffered huge business loss owing to which it could not service its loan-liability to the IOB, and as to be expected its loan

was notified as NPA by the lender. Thereafter on 24.03.2017, the IOB assigned the debt of the petitioner-company to M/s. Alchemist Asset Reconstruction Company Ltd., (hereinafter referred to as 'Financial Creditor/FC).

b) The assignee of the loan, as a Financial Creditor moved the NCLT with an application under Sec.7 of the IBC against the petitioner-company for initiating a Corporate Insolvency Resolution Process (henceforth CIRP). The statutorily prescribed course of action commenced, accordingly an Interim Resolution Professional (IRP) was appointed, Committee of Creditors (IOB) was constituted, and it approved the resolution plan and submitted it, and on 06.12.2021 it was approved by the Adjudicating Authority, the NCLT.

c) In terms of the resolution plan, only the financial creditor of the petitioner was partially benefited, since the value of the assets of the petitioner was far short of the value of the liability it faced. So far as Operational Creditors are concerned, the resolution plan directed that they would be paid *pro rata* at 1% of the value of their claim. The petitioner accordingly redeemed itself from the debt-trap it faced.

d) While so, TANGEDCO, to which the petitioner owed arrears of

unpaid electricity charges from June, 2019 to a tune of Rs.32,86,061/- issued a demand notice dated 19.01.2022 for the said sum. The petitioner had replied stating that it had already gone through CIRP and as per the Resolution Plan approved by the NCLT, all the outstanding dues of the company not falling within the purview of the Resolution Plan stood extinguished. And, since the demand of the TANGEDCO was not met, it promptly disconnected the electricity service connection of the petitioner.

e) Thereafter, on 24.2.2022, the petitioner applied for a temporary connection of the LT Energy. TANGEDCO, however, declined to provide the electricity service connection on the ground that the petitioner needs to pay the arrears of electricity consumption charges to it.

f) Contending that the demand of arrears of electricity charges runs counter to the spirit behind the IBC engineered Resolution Process, the claim of the TANGEDCO itself is arbitrary and illegal, the petitioner challenges it in this proceeding.

3. TANGEDCO has filed its counter, wherein it essentially highlighted that, (a) for non-payment of current consumption charges, the electricity

connection provided to the petitioner was disconnected on 08.08.2019, well prior to the commencement of insolvency proceedings; and (b) Regulation 17 of the Electricity Supply Code has made it mandatory for an applicant for fresh electricity service connection to pay the entire arrears of electricity charges.

THE ARGUMENTS

4. Mr.Om Prakash, the learned senior counsel for the petitioner argued that, for the TANGEDCO to sustain any claim against the petitioner, it should have made its claim as an Operational Creditor during the Resolution Process in the CIRP proceedings. It, however, did not choose to make a claim. Now, when once the Resolution Plan is approved by the NCLT on 06.12.2021, all the unclaimed outstanding liability of the petitioner company has extinguished, and the petitioner starts a new innings with the score board reading zero for none. In ***Ghanashyam Mishra & Sons (P) Ltd., Vs Edelweiss Asset Reconstruction Co. Ltd.*** [(2021) 9 SCC 657], the Hon'ble Supreme Court has held that unless any statutory liability which is payable by the corporate debtor to the Central Government or State Government or to any local authority is made part of the resolution plan, it shall stand

extinguished, and hence, no proceedings in respect of such dues for the period prior to the date on which the adjudicating authority grants its approval to the resolution proposal will survive. Reliance was also placed on the ratio in ***Paschimanchal Vidyut Vitran Nigam Ltd. Vs Raman Ispat Private Limited and Others*** [2023 SCC OnLine SC 842], and ***Committee of Creditors of Essar Steel India Limited, through authorised signatory Vs Satish Kumar Gupta and Others*** [(2020) 8 SCC 531].

5.1 Per contra, representing the TANGEDCO, Mr.J.Ravindran, the Additional Advocate General, submitted that it may be that under the scheme of IBC, TANGEDCO might be an operational creditor, but inasmuch as TANGEDCO's activities are governed by the Electricity Act, 2003, and the Electricity Supply Code, it cannot forego its claim. Reliance was placed on the ratio in ***State Tax Officer Vs Rainbow Papers Ltd.,*** [2022 SCC OnLine SC 1162] ; ***K.C.Ninan Vs Kerala State Electricity Board and Others,*** [2023 SCC OnLine SC 663 (para 117, 341)], and ***M/s.Empee Distilleries Limited Vs The Superintending Engineer, Pudukottai, Electricity Distribution Circle, Pudukottai*** [WP(MD) No.14198 of 2022 dated 10.11.2022].

5.2 On the strength of the ratio in ***K.C.Ninan Vs Kerala State Electricity Board and Others,*** [2023 SCC OnLine SC 663], the Additional Advocate General submitted, an owner or an occupier of the premises to which the electricity was provided is liable to pay the entire arrears, and it was not affected by any proceedings initiated under the IBC, nor by any approval to a resolution plan. He also submitted that the ratio in the ***Ghanashyam Mishra case*** has been considered in ***State Tax Officer Vs Rainbow Papers Ltd.,*** [2022 SCC OnLine SC 1162], where the Supreme Court has declared that where the resolution plan presented before the Adjudicating Authority (the NCLT) has ignored certain dues to the instrumentality of the State, then the same is bad. This judgment in the ***Rainbow Papers case*** was followed by a learned Single Judge of this Court in ***M/s.Empee Distilleries Limited Vs The Superintending Engineer, Pudukottai, Electricity Distribution Circle, Pudukottai*** [WP(MD) No.14198 of 2022 dated 10.11.2022].

DISCUSSION & DECISION

(a) Setting the Stage

6.1 Facts are not in controversy. Petitioner is a company and is also registered under the MSME Act, 2006. It had fallen into a debt trap of its own creation

which drew the petitioner before the NCLT to face a CIRP at the instance of its only financial creditor. Necessarily, the Committee of Creditors whose 66% approval is mandatory under Sec.30(4) of the IBC for the NCLT to consider approving any resolution plan, is constituted of a single member financial creditor.

6.2 In view of the fact that the petitioner has been registered under the MSME Act, Sec. 240A of the IBC enabled its existing Board to participate in the resolution process of the CIRP, and hence it made use of the opportunity and came up with its Resolution Plan. And, it was readily approved by the one member CoC, and was also sanctified by the NCLT vide its Order dated 06.11.2021. The Resolution Plan as approved shows that the petitioner would merge one of its units in Chidambaram (in Tamilnadu) with another facility it has at Puducherry, and would sell its non-core assets to pay off its creditors – to be understood essentially as its only financial creditor. And, the petitioner being a MSME, the same promoters or the Board of Directors of the petitioner continued to be in the management of its affairs, but significantly free of all its liability, with its only financial creditor walking away with the chunks, and the operational creditors forced to settle for the crumbs which the IBC regime generously feed them with.

7. The TANGEDCO, a statutory entity, a Generator cum Distribution licensee of electricity in this state, with a claim of around Rs.32.0 lakhs, does not figure anywhere in the scheme of this Resolution Plan, as it has not preferred a claim before the Interim Resolution Professional pursuant to the public notice issued at the instance of the Adjudicating Authority under the IBC (read the same as NCLT). After all, TANGEDCO is only an Operational Creditor within the definition of the term under Sec.5 (21) of the IBC, for whose money and loss the IBC shows scant respect or concern. (But the legislation is still valid). Curiously enough, the petitioner also did not disclose its dues to TANGEDCO in its Resolution Plan.

8. TANGEDCO, very innocently demanded its dues, but the petitioner has a prompt response to it: "*We had one great holy dip in the IBC, and all our sins are washed away. Today, we are a new born, with a clean-slate balance sheet, with all assets and no liability. Hence, we owe TANGEDCO nothing. And if there are any doubts, read* ***Ghanashyam Mishra case****."* And, it does not stop there. It now insists the TANGEDCO to provide it with a new electricity service connection but without payment of arrears of electricity charges. TANGEDCO is plainly uninterested and its response is candid: "*We*

are governed by the Electricity Act and the Supply Code, and we are not bound to provide you, the petitioner, with a fresh electricity connection unless our dues are paid. And, we have our powers intact to realise the arrears as per our governing statute."

(b) A Preludial Statement

9. *Prima facie*, the contentions of the petitioner sound absolutely unconscionable. The petitioner appears to have literally negotiated with its only financial creditor to deny its operational creditors of their dues. This possibility disturbs the consciousness of this court and also disquiets its conscience. However, a *prima facie* perception by itself may not be an ideal material to guide the conscience of this court to a surer decision justifiable in law. As Jerome Frank has stated several decades ago, a 'Judge must forewarn himself of his prejudices', and necessarily any judicial perception that could not be accommodated in law can only pass for the prejudice of the judge.

10. The submissions on either side display an apparent interplay of two statutes, both seeking supremacy over the other, and the issue is entangled in judicial understanding of the scope and extent of the IBC. If the arguments of the petitioner are keenly observed, it appears to be on a firmer ground, since

it is backed by the rule of commercial wisdom of the CoC as well as the Clean Slate Theory (henceforth CST) as evolved by the Supreme Court (which would be discussed in due course). On the pointed issue of the entitlement of TANGEDCO to keep alive its claim against the petitioner is concerned, it does appear that it may well be covered by the dictum in ***Paschimanchal Vidyut Vitran Nigam Ltd., Vs Raman Ispat (P) Ltd., & Others*** [(2023)10 SCC 60].

11.1 Justice has variable content but is in search of a constant - Justice. It aims to find an ideal balance amidst conflicting interests, and it has been its eternal challenge. And, it is best served when it is nurtured with a sense of justice and fairness which occupies, or ought to occupy the judicial consciousness of the Courts. The onus is on the Courts. It is a constitutional obligation which this court can neither reject nor ignore. This obligation is defined by a realization that every citizen in this country is an equal citizen and every ounce of property one possesses in this country is precious. If right to dignified existence in this country has to have any meaning beyond the rhetoric that we are often fed with, then its inalienability to right to property deserves a special recognition. The sense of justice of the Court is summoned every time the individual right to property faces a conflict. It is here the

interest of the operational creditors has drawn the notice of this Court and the possibility for potential misuse of the IBC and the regime it has created has become a source of its concern.

11.2 Pursuit to justice shall not let to be hindered by any attitude that may find appreciation in a School of Mathematics. The existential relevance of Courts as an institution to the citizenry of this country depends on its strength to identify those rights in crisis within the structure of the Rule of Law which the Constitution of this country advocates with pride, and its ability to evolve a solution. The terrain may be plain or may be treacherous. But the Courts should not plea helplessness and shy away from its responsibility to the citizens of this country in evolving a just solution within the contours of our legal system and within the rules of discipline which the Courts follow. This Court therefore, chooses to follow the command of its conscience and to delve deep into this issue.

12. In this endeavour, this Court is conscious that the process of evaluating the sustainability of the defence offered by the TANGEDCO to the plea of the petitioner, in effect invites this Court to judicially review the effect of the resolution plan as approved by the CoC first, and by the Adjudicating

Authority next, without disturbing the finality it had attained in the IBC turf. Much of this Order which would unfold shortly is to ascertain the space available to this Court to sit over the final order of the Adjudicating Authority.

13. Here it has to be stated that in ***Swiss Ribbons Pvt. Ltd., & another Vs Union of India & Others*** [(2019) 4 SCC 17] the Supreme Court while approving the constitutionality of the IBC, has focused more on the legislative competency of the Parliament to enact it, and underscored it as to why the Court should stay off from economic legislations. The case at hand, definitely not the first one in this genre, yet it necessitates a compulsory understanding of the scheme of the IBC one more time, and also the space occupied by the dictum of the Supreme Court in its judgements on the topic (to few of which reference has been generally made already). This course, this Court considers as the convenient point for opening the discussion.

(c) A brief overview of the IBC and its working

14.1 The IBC is a statutory contrivance for consolidating all the statutes that were hitherto in force which dealt with the issue of insolvency – be it an individual or proprietary concern, or a partnership firm, or a registered company, not with an eye to drive the debtors into forced liquidation, but to

salvage them even as their creditors are paid reasonably. Not a novel idea as the theme appears to have been borrowed or lifted from Sick Industrial Companies (Special Provisions) Act,1985 (for convenience, SICA). The principle aim of SICA was to investigate into the cause for the commercial sickness of the debtor-company and to conduct a feasibility study for devising a measure to rehabilitate the company. SICA, however, was repealed in 2004, and one of the reasons behind this move appears to be the rampant misuse of the moratorium provided under Sec.22. One noticeable difference which is instantly visible on a broader comparison of SICA and the IBC is that while SICA was debtor driven, the IBC is financial creditor driven. In effect the soul of the IBC appears to be that which the Parliament has junked vis-à-vis the SICA.

14.2 The IBC aims to settle the corporate creditors with minimal damage to the existential possibilities of a corporate debtor. Surely on paper it appears to provide possibilities of a win-win situation, something which the draftsmen of IBC may elate about. In that sense IBC may be acclaimed as a path breaking legislation, but it is doubtful if it has broken the path without breaking the back of some of the stakeholders – more particularly the Operation creditors. How secured are the operation creditors under the IBC

regime? This requires a dispassionate understanding of the scheme of the IBC and the judicial pronouncements on its working. They are provided below.

15. It commences with a situation where the corporate debtor (which by definition under Sec.3(8) read with 3(7) means a company or a limited liability partnership firm or any other incorporated entity with limited liability but not including any financial service providers) faces an imminent possibility of involving in an insolvency resolution process. The process which IBC provides unfolds as below:

a) Where a corporate debtor commits a default in making payments to its creditors, the stage will be set for invoking the IBC. Here the creditors are classified into two broad categories: (i) Financial Creditors; and (ii) Operational creditors. A combined reading of Sec.5(7) and 5(8) enables a broad understanding of the term '*financial creditors*' as those to whom money is owed by a corporate debtor. Given the context of the case a specific discussion on the term is unnecessary. An Operational creditor, on the other hand are those to whom operational debt is owed, and in terms of the definition provided under Sec. 5(21) of the IBC, it means those to whom payment is due for supply of any goods and services, and,

any dues that "*arises under any law for the time being in force and payable to the Central Government or any State Government or any local body*". Significantly enough the definition does not expressly include any liability payable to any public sector companies and statutory corporations, beneath whose corporate veil lies the public interest and the concern of the citizenry as the principal stakeholder.

b) The IBC enables the financial creditors to initiate proceedings for insolvency resolution under Sec.7, or by the operational creditors under Sec.9, or by the corporate debtor itself under Sec.10 of the IBC.

c) Once the Adjudicating Authority (read it as the NCLT) admits a petition for initiating an insolvency resolution process, three things happen in succession: (i) appointment of an Interim Resolution Professional (IRP) in terms of Sec.16; (ii) issuance of a public notice of the initiation of insolvency proceedings by the NCLT under Sec.13 read with Sec.15, declaring moratorium on all transactions or suits involving the corporate debtor as provided in Sec.14; and (iii) through the said public notice inviting claims from all the creditors of the corporate debtor within a stipulated date (Sec.15).

d) Once an IRP is appointed, he or she replaces the Board of the corporate debtor and the entire managerial responsibility of the corporate debtor vests in the IRP and to this extent the powers of the Board of directors of the corporate debtor will stand suspended (Sec.17).

e) Under Sec.18, the IRP is required to prepare an asset and liability statement of the corporate debtor, and this may include such claims he may have received pursuant to the public notice issued by the NCLT under Sec.13. Now, notwithstanding the suspension of the Board of Directors of the corporate debtor under Sec. 17(1)(b), in terms of Sec.19, the Board of the corporate debtor is still under a statutory obligation to extend its assistance and co-operation to the IRP, and is duty bound to provide all necessary information to him or her. Indeed, on its failure to provide necessary assistance or co-operation, the NCLT has the power to direct the suspended Board of the corporate debtor to provide the same to the IRP.

f) The next significant responsibility of the IRP is to constitute a Committee of Creditors (CoC) once he completes the preparation of the asset and claims statement of the creditors of the corporate debtor. As per Sec.21 of the IBC, only financial creditors will have

the right to be part of the CoC, and the only circumstance when the financial creditor or its representative may be excluded is when they are related to the corporate debtor. The object behind this is obvious as it intends to exclude conflict of interest and possibilities of bias, since the CoC is vested with the exclusive authority to decide on the resolution process as would be seen later.

g) The operational creditor will not be in the loop, and the Parliament has taken a very conscious decision even to limit the voting right of a financial creditor who/which may also figure as an operational creditor only to the extent of its financial debt. [Sec.21(4)]

h) With the constitution of the CoC, the role of the IRP comes to an end. Now the CoC will take over, and it will now appoint the Resolution Professional (RP). He or she may be the IRP or could be a different person and who would be appointed by the Adjudicating Authority subjected to the approval of the Insolvency Bankruptcy Board of India (IBBI). And, on the appointment of the RP, he would assume charge of the affairs of the corporate debtor and is required to continue it as a going concern, but his freedom to manage the affairs of the corporate debtor is largely under the nose and control of the CoC as provided in Sec.28.

i) The RP is also required to initiate the resolution process for which purpose he is vested the power under Sec.25(2) to invite (known as expression of interest) resolution plan from any third parties who might be interested in baling out a stressed company from facing the prospects of becoming an insolvent, for which purpose he also has the power to call for the meeting of the CoC under Sec.24. And, anyone who fails to qualify in terms of Sec.29A cannot be a resolution applicant.

j) The RP is then required to prepare what Sec.29 describes as an Information Memorandum and it is required to provide all necessary information useful for the resolution applicant (either a third party or the financial creditor under Sec.7, or Operation creditor under Sec.8) to formulate a resolution plan and also is required to provide them the access to the information to the extent Sec.29 stipulates. Subject to Sec.29 A, a resolution applicant is required to provide a resolution plan to the RP.

k) Under Sec.30 (2) (b) (introduced vide Act 26/2019 and brought into force on 16.08.2019) the RP is *inter alia* expected to ensure that the proposal for payment to the operational creditor is not less than what they may have obtained in a liquidation proceedings or that

they would have obtained in the order of priority in the liquidation proceedings as provided under Sec 53(1), whichever is higher. But the most significant part of this activity is that the RP is required to ensure in terms of Explanation I of Sec.30(2) that "*distribution in accordance with this clause shall be fair and reasonable to* ***such*** *creditors*", which contextually mean the 'operational creditors'. Some small mercy for the operational creditors, or is it a condescending care that IBC extends?

l) Under Sec.30(4) the CoC is required to approve the resolution plan with a minimum of 66% vote in favour of the said plan. And, under Sec.31 this resolution plan as approved by the CoC is required to be approved by the Adjudicating Authority, the NCLT, after it satisfies itself that the resolution plan has provisions for its effective implementation. This is provided in the Proviso to Sec.31(1). Necessarily it has the power to refuse approval if it is not so satisfied.

16. The legislative intent as conveyed through the body of the IBC highlights three aspects on the right of the operational creditors: (i) The operational creditors has the right to initiate an insolvency proceedings; (ii) it can

participate in the meeting of the CoC; and (iii) it is required to take whatever the CoC grants it with the minimum assurance that it would not be less than the minimum that they would obtain in the eventuality of the corporate debtor going into liquidation. But their inherent right to defend its interest is significantly denied to them as the Parliament embarked on a hitherto unheard of legislative invention of requiring one set of creditors, the financial creditors, to decide on the right of another set of creditors. In that sense IBC has been truly path-breaking. But has not the Parliament unwittingly reduced the operational creditors with lesser insurance against economic uncertainties, to a sacrificial goat to feed the financial creditors, essentially the banking sector, which has greater and better shock-absorbers in-built within its structure against economic turbulences, with the RBI sitting to audit its operational efficiency? This aspect cannot be ignored as the TANGEDCO's grievance will find a slot here.

17. Another striking feature of the IBC which is relevant to the context of this case is that, while a corporate debtor may initiate an insolvency proceeding, in the final leg, it cannot be a resolution applicant and participate in the resolution process except as an observer in the meetings of the CoC. As earlier indicated the solitary exception is a MSME corporate debtor which in

terms of Sec.240A, does not suffer any disqualification under Sec.29A and therefore a MSME corporate debtor can be a resolution applicant. But the statutory concession extended to a MSME stops here. In other words, the scheme of resolution process is the same even if MSME were a resolution applicant.

(d) IBC & Scope for Misuse

18. Is the petitioner liable to pay the arrears of electricity charges which has arisen prior to the commencement of the insolvency proceedings, and will it survive after the successful completion of the resolution process? In trying to shield itself behind the CST, is it on an ambitious overdrive to out manoeuvre the quest for fairness in judicial action?

19. It now throws open a need to understand (i) whether IBC enables a possible collusion or a collaboration between the corporate debtor, financial creditors, and the one who is supposed to be equidistant to both – the IRP and the RP for outsmarting the interests of the operational creditors; and (ii) whether the CST is a panacea for the corporate ills (or is it evils?) of a corporate debtor. In short, the question would be whether the objective behind the IBC could be hijacked by private motives of those in whom the

IBC has invested its trust - the trust the Parliament has invested; the trust the people of this country have invested. And if it could be, does it not impose a responsibility on the legal system of this country of which the courts are the *sentinel on the qui vive* to step in to shape up a just and fair outcome within the framework of law?

20. Having understood the scheme of the IBC, it is now time to navigate through the authoritative pronouncements of the Hon'ble Supreme Court. It is neither about the creation of two broad categories of creditors – the financial creditors and the operational creditors by the IBC, nor about the differential criterion which IBC has employed to define the character of both these categories of creditors, whose alleged inequality of status the Supreme Court has rejected on its way to uphold the constitutionality of the IBC in the ***Swiss Ribbons Case*** [(2019) 4 SCC 17]. It is about the protection and the assurance the IBC offers to the operational creditors and the role of the Adjudicating Authority. This exercise is both inevitable and mandatory since this Court has to ensure that the petitioner, with or without the collaboration of its financial creditor, has not been converted the IBC into mechanism to deny the respondent of their dues by a shrewd manipulation of the process it provides.

(e) Operational Creditors & Right to Property

21. In a free country where every individual citizen is endowed with the fundamental right to do any lawful business under Article 19(1)(g) of the Constitution, all those who engage in different businesses are free to make their commercial decisions. Some succeed and some fail, and hence loss in business is an inevitable consequence attached to the vagaries of commerce. When misfortune strikes like a hurricane it lands some businesses in bankruptcy. And, every time a debtor loses, his or its creditors also lose.

22.1 The object of the IBC evidently is to minimize the loss of various categories of creditors even as it attempts to salvage the corporate debtor from its commercial extinction. Appreciable it is, but it may not be let to gloss over the fact that every claim of the operational creditors involves a right to their property under Article 300 A of the Constitution, which the Supreme Court now reads it as a facet of human right and as integral to the right to life under Article 21 of the Constitution vide the ratio in ***Lalaram Vs Jaipur Development Authority*** [(2016) 11 SCC 31] read alongside the ratio in ***Tukaram Kana Joshi Vs MIDC*** [(2013)1 SCC 353], and approved in ***Vidya Devi Vs State of H.P.***, [(2020)2 SCC 569)]. This is the major premise.

22.2 Every right to property has its adjunct rights shadowing it. ***Kolkata Municipal Corporation Vs Bimal Kumar Shah*** [2024 SCC OnLine SC 968]

> "*26……. The binary reading of the constitutional right to property must give way to more meaningful renditions, where the larger right to property is seen as comprising intersecting sub-rights, each with a distinct character but interconnected to constitute the whole. These sub-rights weave themselves into each other, and as a consequence, State action or the legislation that results in the deprivation of private property must be measured against this constitutional net as a whole, and not just one or many of its strands."*

This necessarily includes the right to enforce or secure the right to property, which we commonly understand as right of action. Ordinarily, a person with a claim has the right of action to enforce the claim before a neutral arbiter, be it the Court or a tribunal, both of which are positioned equidistantly from opposing claims. This is the minor premise.

(f) IBC & Neutral Tribunal

23. It could now be derived that where a substantive right to property is in peril, the right of action before a neutral tribunal springs into action for obtaining justice in the cause. This is fundamental to our Constitutional

jurisprudence. In ***Union of India Vs Madras Bar Association*** [(2010)11 SCC 1], a Constitutional Bench of the Supreme Court has held:

> "*101. Independent judicial tribunals for determination of the rights of citizens, and for adjudication of the disputes and complaints of the citizens, is a necessary concomitant of the rule of law. The rule of law has several facets, one of which is that disputes of citizens will be decided by Judges who are independent and impartial; and that disputes as to legality of acts of the Government will be decided by Judges who are independent of the executive. Another facet of the rule of law is equality before law. The essence of the equality is that it must be capable of being enforced and adjudicated by an independent judicial forum. Judicial independence and separation of judicial power from the executive are part of the common law traditions implicit in a Constitution like ours which is based on the Westminster model.*
>
> *102. The fundamental right to equality before law and equal protection of laws guaranteed by Article 14 of the Constitution, clearly includes a right to have the person's rights, adjudicated by a forum which exercises judicial power in an impartial and independent manner, consistent with the recognised principles of adjudication. Therefore wherever access to courts to enforce such rights is sought to be abridged, altered, modified or substituted by directing him to approach an alternative forum, such legislative Act is open to challenge if it violates the right to adjudication by an*

> *independent forum. Therefore, though the challenge by MBA is on the ground of violation of principles forming part of the basic structure, they are relatable to one or more of the express provisions of the Constitution which gave rise to such principles. Though the validity of the provisions of a legislative Act cannot be challenged on the ground it violates the basic structure of the Constitution, it can be challenged as violative of constitutional provisions which enshrine the principles of the rule of law, separation of powers and independence of the judiciary."*

Indeed, long before the above pronouncement in the ***Madras Bar Association case***, the tone for this idea was set in Article 10 of the Universal Declaration of Human Rights, 1948 which reads:

> "*10. Everyone is entitled to in full equality to a fair and public hearing by an independent and impartial tribunal, in the determination of his rights and obligations and of any criminal charge against him."*

It will be of interest to record that Article 6(1) of the European Convention on Human Rights, 1950 has adopted the same, and it reads:

> "*6.1 In the determination of his civil rights and obligations or of any criminal charge against him, everyone is entitled to a fair and public hearing within a reasonable time by an independent and impartial tribunal established by law."*

Inasmuch as India is a signatory to UDHR, there is a binding obligation on the Parliament of this country to provide a neutral forum for the operational

creditors to present their claim.

24. However, the scheme of IBC provides for a two-tier mechanism for approval of a resolution plan – first by the CoC and next by the Adjudicating Authority. Now, unless the Adjudicating Authority is treated as a neutral tribunal for the operational creditors to defend and secure its right to property which they have in their claims against any perceived unfair and inequitable treatment meted out to them by the CoC, even if the CoC has acted bonafide, there is a lurking danger of IBC straying into the zone of unconstitutionality for breaching the dictum of the Constitution Bench in the ***Madras bar Association case***.

(g) Discussion on the Authorities

25. What then is the role which the Adjudicating Authority is expected to play? This issue, it must be said, is caught in the storm of court room debates, and there is a perception that it has left the role of the Adjudicating Authority on a plane of ambivalence, and it may have to be steered to clarity. And, it may not be discussed in isolation, as its understanding was influenced by the doctrine of commercial wisdom which the Supreme Court has developed in the ***Sashidar Case*** [(2019) 12 SCC 150] and subsequently reinforced vide

ratio in the ***Essar Steel case*** [(2020)8 SCC 531] and the ***Ghanashyam Mishra case***. An understanding about them will be useful to understand the contours of the CST - the Clean Slate Theory. The discussion of these authorities now opens.

25.1 In ***Sashidhar case,*** the Supreme Court was faced with a situation where it was required to decide on the validity of the resolution plan as approved by the majority of the financial creditors of the CoC but with their combined vote-percentage falling short of the percentage which the IBC had fixed for approving a resolution plan and the authority of the Adjudicating Authority to interfere with it, since the latter had rejected the resolution plan. It is in the course of its judgment, the two Judges bench of the Supreme Court has held:

> "*52. The legislature has not endowed the Adjudicating Authority (NCLT) with the jurisdiction or authority to analyse or evaluate the* ***commercial decision*** *of CoC much less to enquire into the justness of the rejection of the resolution plan by the dissenting financial creditors……. Besides, the commercial wisdom of CoC has been given paramount status without any judicial intervention, for ensuring completion of the stated processes within the time lines prescribed by the I & B Code. There is an intrinsic assumption that financial creditors are fully informed about the viability of the corporate debtor and the feasibility of the proposed resolution plan. They*

> *act on the basis of thorough examination of the proposed resolution plan and assessment made by their team of experts.* ***The opinion on the subject matter expressed by them after due deliberations in CoC meetings through voting, as per voting shares, is a collective business decision. 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 non justiciable"****.*

Thus was born the rule of commercial wisdom of the CoC. If the ratio in this case is analysed carefully, the question before the Court has little to do with the rights of the operational creditors or the interest that they are entitled to, to have them protected through a neutral judicial forum.

25.2(a) However, in the ***Essar Steeel case*** [(2020)8 SCC 531], a three Judges bench of the Supreme Court had expanded the scope of the doctrine of commercial wisdom of the CoC and telescoped it into a situation to undo the effect of the interference which the Appellate Authority had when it brought in its perception of equitability and fairness vis-a-vis the approval granted by the Adjudicating Authority to the resolution plan placed before the latter. It may be stated in that case, the CoC constituted sub-committee of creditors (which it named as the core-committee of creditors) which engaged with the

resolution applicant, and tweaked the original resolution plan which was later came to be accepted by the majority of the financial creditors in the CoC. In the process, the CoC voted out the financial creditor which initiated the CIRP and provided nothing significant for operational creditors. This resolution plan found favour with the Adjudicating Authority but not with the Appellate Authority. The Appellate Authority rejected the resolution plan on two scores: (i) that the Code does not provide for delegation of responsibility by the CoC to a sub-committee; and (ii) that there is no equitable treatment given to the operational creditors.

25.2(b) When this matter reached the Supreme Court, it *inter alia* entertained three significant questions of contextual relevance for discussion. They are, (i) whether the Code enables the constitution of a sub-committee by the CoC; (ii) whether the Code envisages identical treatment to different classes of creditors; and (iii) whether the commercial decision of the CoC can be subjected to judicial review. In its decision, the Supreme Court approved the constitution of the core committee and held that inasmuch IBC has employed differential criteria for defining both the financial creditors and the operating creditors they cannot be equated for identical treatment, and these findings led the Supreme Court to emphasis that the commercial wisdom of the CoC

cannot be interfered with by the Adjudicating Authority. It states:

> " *67. ...Thus, it is clear that the limited judicial review available, which can in no circumstance trespass upon a business decision of the majority of the Committee of Creditors, has to be within the four corners of Section 30(2) of the Code, insofar as the Adjudicating Authority is concerned, and Section 32 read with Section 61(3) of the Code, insofar as the Appellate Tribunal is concerned"*

As a byproduct of this judicial thinking, the Clean Slate Theory made its slow and subtle emergence in paragraph 107 of the judgment, when the Supreme Court was dealing with an ancillary issue of extinguishment of guarantee of the promotors of the corporate debtor on the approval of the resolution plan. The Supreme Court states:

> " *107. ... A successful resolution applicant cannot suddenly be faced with "undecided" claims after the resolution plan submitted by him has been accepted as this would amount to a hydra head popping up which would throw into uncertainty amounts payable by a prospective resolution applicant who would successfully take over the business of the corporate debtor. All claims must be submitted to and decided by the resolution professional so that a prospective resolution applicant knows exactly what has to be paid in order that it may then take over and run the business of the corporate debtor. This the successful resolution applicant does on a fresh slate, as has been pointed out by us hereinabove."*

25.3(a). The ratio laid down in the ***Essar Steel*** judgment was followed by another three-Judge bench of the Supreme Court in the case of ***Ghanashyam Mishra and Sons Private Limited Vs Edelweiss Asset Reconstruction Company Limited*** [(2021) 9 SCC 657]. In the said case, the Supreme Court dealt with a batch of appeals wherein the statutory authority attempted to recover the statutory dues from the corporate debtor after a resolution plan had been approved. In the lead case, M/s Orissa Manganese & Minerals Ltd. went through CIRP. There were three resolution applicants who *inter alia* included Ghanashyam Mishra & Sons Private Ltd., and a certain M/s Edelweiss Asset Reconstruction Company Ltd. The plan of Ghanashyam Mishra was approved by the CoC and the plan of Edelweiss was not even admitted by the Resolution professional. Edelweiss challenged the non-admission of its plan before the NCLT. Alongside, the workmen of the corporate debtor also challenged the resolution plan for not making any provision for the payment of their salary and statutory dues. The NCLT rejected both these applications. In appeal, the NCLAT upheld the rejection of Edelweiss's application, but allowed it to enforce the bank guarantee issued by the corporate debtor in an independent proceeding after the expiry of moratorium. It also allowed the workmen to realize their salary and

statutory dues through independent proceedings in the civil courts. In effect the appellate authority had kept alive the dues of the Edelweiss and the workmen despite the approval accorded to the resolution plan. In other cases, the statutory authorities had made a valiant attempt to recover the statutory dues but after the approval of a resolution plan as it did not provide for the payment of such dues.

25.3(b) The issues which confronted the Supreme court are: (i) whether the resolution plan approved by the Adjudicating Authority under Section 31(1) of the Code is binding on the Central Government, State Government, and local authorities; and (ii) whether the Central Government, State Government, and local authorities have any *locus standi* to maintain any action for the recovery for statutory dues after the resolution plan for a corporate concern has been approved by the Adjudicating Authority?

25.3(c) After placing reliance on the rule of commercial wisdom of the CoC developed in ***K. Sashidhar case*** and ***the Essar Steel case*** and placing reliance on Sec.238 of the IBC which has granted supremacy to the provisions of the IBC to override all the other statutes that are inconsistent with them, the Court held that even before amendment of Sec.31(1) (made

vide Act 26/2019 and before the decision in the ***Essar Steel case***) which was to provide the foundation for the Clean Slate Theory to be developed, the statutory intent favoured the extinguishment of those dues owed to the statutory authorities that were not specifically included in the resolution plan. And the CST has been introduced as a reason to explain the legislative intent behind freezing all the claims once the resolution plan is approved. Accordingly, when once the resolution plan is approved, all the statutory dues owed to the Central Government, State Government, and Local Authorities, not claimed and included in the resolution plan, would stand extinguished.

25.3(d) The Court also recognised the limited power of review vested in the Adjudicating Authority to satisfy himself that the resolution plan conforms to Sec.30(2) of the IBC.

26. These authorities of the Supreme Court are now followed by four judgements of the Supreme Court delivered by four different two judges benches. They are: ***State Tax Officer Vs Rainbow Papers Ltd.,*** [(2023) 9 SCC 545], ***Paschimmanchal Vidyut Vitran Nigam Ltd., Vs Raman Ispat Pvt. Ltd., & others*** [(2023) 10 SCC 60] and ***Sanjay Kumar Agarwal Vs State***

Tax Officer & another [(2024) 2 SCC 362] and ***M.K.Rajagopalan Vs Dr.Periasamy Palani Gounder & another*** [(2024) 1 SCC 42]. They are now considered:

a) In the ***Rainbow Papers case***, the facts that visited the Supreme Court was whether the statutory dues which was being litigated between the statutory authority and the corporate debtor and was pending even before the initiation of the CIRP against the corporate debtor is saved when the resolution plan that came to be approved by the CoC does not disclose the statutory dues. The RP defended it on the ground that the statutory authorities did not make a claim pursuant to the public notice. The Court held that the resolution plan is bad in law since the Adjudicating Authority did not ensure that all operational creditors are paid in terms of Sec.30(2) of the IBC. The Court also added that the statutory authority need not prefer a claim as contended by the RP, since this was disclosed in the books of accounts of the corporate debtor. In other words, the decision of the Supreme Court was set to the facts of that case, but more significantly it recognised the fact that the Adjudicating Authority is not a mere rubber stamp for approving whatever resolution plan placed before it while exercising its jurisdiction

under Sec.31 of the IBC.

b) In the ***Paschimanchal Vidyut Vitran case,*** the claim relates to the electricity dues of the corporate debtor for realising which the electricity distribution licensee had approached the Tahasildar and attached the property of the corporate debtor, and during the liquidation proceedings upon the failure of the resolution process, the NCLT would require the Tahasildar to vacate the attachment over the property of the corporate debtor to enable the liquidation of assets of the corporate debtor, and this order came to be challenged and ultimately landed before the Supreme Court. Before the Court, it was argued by the electricity distribution licensee that it was a secured statutory creditor and as it was not included in the resolution plan, it was entitled to the advantage of the ratio in ***Rainbow Papers case.*** And being a secured creditor, even in liquidation proceedings, it was entitled to priority under Sec.53 of the Code. Rejecting the said contention the Supreme Court held that only those dues which are transferred to the consolidated fund of the State are entitled to be termed as statutory dues and hence the electricity dues are not statutory dues and hence the distribution licensee was not entitled to the priority in the waterfall mechanism

provided under Sec.53. It also held that at any rate in terms of Sec.238, the provisions of IBC will prevail over the Electricity Act. And, in its judgement the Supreme Court has distinguished the ***Rainbow Papers case*** on the ground that the latter mentioned case did not take into account the water fall mechanism provided under Sec.53. This case however, neither touches upon the doctrine of commercial wisdom of the CoC or the CST nor on the role of the Adjudicating Authority under Sec.31.

c) What follows next is the ***M.K.Rajagoplan case***. In this case the Court has considerably watered down the concept of the commercial wisdom of the CoC when it held that commercial wisdom of the CoC will have supremacy only when it is formed on the basis of complete disclosure of information. It reads: (Per Dinesh Maheswari J):

> "*160: As noticed hereinbefore, commercial wisdom of CoC is given such a status of primacy that the same is considered rather a matter non-justiciable in any adjudicatory process, be it by the adjudicating authority or even by this Court. However, the commercial wisdom of CoC means a considered decision taken by CoC with reference to the commercial interests and the interest of revival of the corporate debtor and maximisation of value*

of its assets. This wisdom is not a matter of rhetoric but is denoting a well-considered decision by the protagonist of CIRP i.e. CoC. As observed by this Court in K. Sashidhar [K. Sashidhar v. Indian Overseas Bank, (2019) 12 SCC 150 : (2019) 4 SCC (Civ) 222] , the financial creditors forming CoC "act on the basis of thorough examination of the proposed resolution plan and assessment made by their team of experts. The opinion on the subject-matter expressed by them after due deliberations in CoC meetings through voting, as per voting shares, is a collective business decision." This Court also observed in K. Sashidhar [K. Sashidhar v. Indian Overseas Bank, (2019) 12 SCC 150 : (2019) 4 SCC (Civ) 222] that "[t]here is an intrinsic assumption that financial creditors are fully informed about the viability of the corporate debtor and feasibility of the proposed resolution plan.

161. These observations read with the observations in Essar Steel [Essar Steel India Ltd. (CoC) v. Satish Kumar Gupta, (2020) 8 SCC 531 : (2021) 2 SCC (Civ) 443] with reference to the reasons stated in the Report of Bankruptcy Law Reforms Committee of November 2015, make it clear that commercial wisdom of CoC is assigned primacy in CIRP for it represents collective business decision, which is arrived at after thorough examination of the proposed resolution plan and assessment made with involvement of experts by the body of persons who are most vitally interested in rapid and efficient decision making. ***It follows***

> ***as a necessary corollary that to be worth its name, the commercial wisdom of CoC would come into existence and operation only when all the relevant information is available before it*** *and is duly deliberated upon by all its members, who have direct and substantial interest in the survival of corporate debtor and in the entire CIRP."*

d) Next in the line of authorities is the dictum in ***Sanjay Kumar Agarwal case*** [(2024) 2 SCC 362]. In the batch of cases before the Supreme Court, the Court was required to review the dictum in the ***Rainbow Papers*** case based on the observations made in ***Paschimanchal Vidyut Vitran case.*** The Court however, refused to review and affirmed the view in the ***Rainbow Papers case*** vis-a-vis the role of the Adjudicating Authority as declared in that case.

(h) The *M.K.Rajagopalan* Effect

27. An analysis of the aforesaid authorities reveals that though the commercial wisdom of the CoC is usually placed on a golden pedestal, too highly to be touched by the Adjudicating Authority (as propounded in the judgments of ***K. Sashidhar***, ***Essar Steel***, ***Ghanashyam Mishra***), the great run it had was cut short till the sanctity attributed to it was qualified in the ***M.K.Rajagopalan*** case.

28.1 The 'commercial wisdom of CoC' is not a label that the CoC may conveniently paste on a resolution plan and market it to override all other considerations. Nor the dominant or the exclusive role which the CoC enjoys within the scheme of the IBC for giving its approval to a resolution plan places it beyond the judicial reach. Commercial wisdom of the CoC, *strict senso*, may be understood as a knowledge based psychological factor with a subtle blending of intuition of a group of self interested creditors. Until the ***Rainbow Papers case***, it was not adequately brought to focus that unless the commercial wisdom of the CoC in approving a resolution plan conforms to the requirements of Sec.30(2), it may not pass the scrutiny of the Adjudicating Authority under Sec.31, even though the ***Essar Steel case*** has not overlooked this aspect. If Sec.30(2) is scanned for its nature, it imposes restriction on the freedom of the CoC to decide the way their collective wisdom may tempt them to decide, by casting a duty on them – to care for the operational creditors. This aspect will be specifically discussed later.

28.2 Therefore, to reduce an understanding of the phrase 'commercial wisdom of the CoC' – a coinage of the Supreme Court, as a synonym to the collective freedom of the CoC sans the duty which Sec.30(2) imposes will be

a grand misconception. The ***Rajagopalan's case*** insistence to the CoC that its wisdom shall not selectively operate on limited information has ushered in the much needed responsibility to the thought process of the CoC. The rule of commercial wisdom of the CoC should now satisfy the test that in exercising it CoC should help itself with optimum inputs – '*of all the relevant information*'. And, they necessarily include those facts which are essential for the CoC to decide not only for the financial creditors, but also for the operational creditors. Thus through the ***Rajagopalan's case*** the Supreme Court has brought in greater clarity and balance not just to the understanding of the expression 'commercial wisdom of the CoC', but also to the marketability of the concept.

29. An inevitable corollary to the dilution of the supremacy of the commercial wisdom doctrine leaves its imprint on the 'clean slate theory'. CST no more springs as an automatic consequence of an approval which an Adjudicating Authority might accord to a resolution plan, but depends on the quality of the resolution plan to which assent has been accorded. The resolution plan should now satisfy that it has passed the scrutiny of the CoC on complete disclosure of all relevant information. CST ceases to be a password for those who are keen to manipulate the scheme of IBC to the

disadvantage of any of the other stakeholders, more significantly, the operational creditors.

30. It could now be derived that any understanding that the role of the Adjudicating Authority as a mere counter-signatory to the approved plan of the CoC will be misconceived as it has the authority to reject any resolution plan, though approved by the CoC and apparently satisfies the requirements of Sec.30(2), if such approval of CoC is obtained on the basis of half disclosed and hence half-baked information.

(i) Role of the CoC Redefined

31.1 While the ***Rajagopalan dictum*** lays emphasis on the quality of information that ought to pass the scrutiny of the CoC, there is a need to bring in certain clarity to the duty of the CoC to the operational creditors. It has become necessary in the context of the misgivings which are entertained based on the dictum of the ***Essar Steel case*** [(2020)8 SCC 531] where the Supreme Court (at paragraph 146), has held that there is no fiduciary relationship between the CoC and the operational creditors, as if the Court with a backswing of its hand has rejected the need of the CoC to be just, fair and equitable to the operational creditors. What apparently is missed is the

Explanation I to Sec.30(2) which creates a statutory obligation on the CoC to be just, fair and equitable in dealing with the rights of the operational creditors. In the opinion of this Court the declaration of the Supreme Court in the ***Essar Steel case*** on the absence of a fiduciary relationship between the CoC and operational creditors does not operate to undermine the effect of Explanation I to Sec.30(2). It can be explained.

31.2 There cannot be a dispute that there exists no fiduciary relationship between the CoC and the operational creditors, since for a fiduciary relationship to emerge between two persons or entities, there ought to be in existence an equation where they either share a mutual relationship in absolute confidence, or at least one investing all its confidence on the other. Now, given the fact that an operational creditor is as much a creditor as the financial creditor, and since an operational creditor's value for its money is no inferior to that of the financial creditors' (as they constitute right to property in their respective hands), and since both are competing to secure its right to property from the same source, it is inconceivable an operational creditor would have wasted its confidence by investing it on its competitor – read it as the financial creditor, or would have voluntarily outsourced its right to decide on what it may be interested in obtaining from his or its debtor by

forsaking its own commercial wisdom. The IBC has however, placed the interest of the operational creditors on the lap of the CoC and authorized the latter to decide what the operational creditor might get.

31.3 Jurisprudentially, if anyone is either vested with the duty to protect the interest of another, or occupies a position where protecting another's interest becomes inevitable and inescapable, then such person is stated to hold the position of a trustee for the one whose interests he is required to protect. This now provides the jurisprudential basis for Explanation I to Sec.30(2) of the IBC. If it is not so understood, then for the purposes of Sec.30(2)(b), the role of the CoC vis-à-vis the operational creditor will be in a jurisprudential vacuum, which will be an anathema to our understanding of jural relationships within our legal system. It therefore follows that the ***Essar Steel case*** pronouncement cannot hinder the respect which Explanation I to Sec.30(2) imposes on the CoC to be just, fair and equitable to the operational creditors.

31.4 There is another reason to fortify the same conclusion. If the considerable hype created around the expression 'commercial wisdom of the CoC' is kept aside, plainly, can the commercial wisdom of the CoC go

beyond taking care of its own interests? Let it be illustrated. Suppose both the corporate debtor and an operational creditor had borrowed from the same financial creditor. While applying its mind with utmost fairness to the resolution plan made available before it, if the CoC by a majority of 66% or more approves payment of only 10% to an operational creditor, will the same financial creditor, while demanding the loan repayment from the operational creditor grant the latter a rebate of 90% on its loan liability? The answer is an obvious no, for it will be incongruent to its commercial wisdom since a financial creditor is not doing any charity, nor is expected to be charitable in its business. Therefore, the commercial wisdom of the CoC can never extend to the extent of protecting the interest of the operational creditor. It is like expecting a lion to share a slice of his catch with a lesser predator when we all know that it is not even known to share its meal with its own pride. Therefore, unless one understands the role of the CoC for the purposes of Sec.30(2)(b) as a trustee of the operational creditor, fairness of its action cannot be exacted from it in terms of Explanation I to Sec.30(2).

31.5. Now, even if Explanation I to Sec.30(2) is not there in the statute, as long as the CoC functions as the statutory trustee for the operational creditors, its duty to be fair and equitable cannot be forsaken. If viewed

differently, where will the impetus for the operational creditors be to initiate an insolvency proceeding against the corporate debtor under Sec.9 if they are not assured of a fair and equitable treatment? Neither logic, nor life's experience will ever support this proposition.

32. This now necessitates that the plan approved by the CoC should be (a) based on complete disclosure of information; (b) that its treatment of the interest of the operational creditor must be just, fair and equitable; and (c) that its allocation for the operational creditors is not less than that which the operational creditors might have obtained in a liquidation proceedings of the corporate debtor.

33. It could be now derived that any resolution plan, even though approved by the Adjudicating Authority yet if it does not satisfy the triple criteria as enunciated in paragraph 32 above, there will be difficulty in attaching finality to it.

34. Therefore the comfort zone which the petitioner has created for itself on the bed of the ***Ganshyam Misra*** dictum may not provide the kind of coziness which it expects it to provide.

(j) Understanding the "Relevant Information" & sourcing them

(i) Introductory

35.1 CoC's role having been defined, the focus should now shifts to the information which the IRP or the RP is required to make available to the CoC. This is critical to the interests of the operational creditors and integral to the nature of duty cast on the CoC under Sec.30(2)(b). Here there are two sets of creditors: (a) Those who are disclosed in the resolution process, and (b) those who are not disclosed. The challenge is always in negotiating the claim of the undisclosed creditors.

35.2 Hitherto, CST was lavishly used to reject the claim of the undisclosed creditors on the ground that he, who had not responded with his claim pursuant to the public notice under Sec.13 and 15 about the initiation of the insolvency proceedings against the corporate debtor might have to necessarily forfeit his right. This view overlooks two aspects:

a) The right to a claim of the operational creditors, whose loss to them will affect their commercial existence and their right to engage in business under Article 19(1)(g) and the right to life of the promotors and the workmen associated with the operational creditors, an aspect

which did not obtain necessary occasion for an adequate consideration of the Supreme Court. Can it be lost to them merely because they have not responded to a public notice, the publication of which many would not be tracking on a daily basis?

b) Given the duty of the IRP and RP to collect and collate all *relevant information*, which necessarily include such information which the CoC would require in terms of the dictum in the ***Rajagopalan case*** for discharging its duty to the operational creditor, should the failure of the IRP and the RP to gather such information which, they exercising due diligence could have collected, be given a discount?

This is now discussed in greater detail. To remind, the respondent herein was an undisclosed operational creditor (no matter whether it is statutory or not) in the resolution process, and its claim is now hanging perilously from the cliff hanger called the CST.

(ii) Duty of the Suspended Board of the CD

36 The first aspect which now concerns the court is the duty of the suspended board of the corporate debtor. When an IRP is appointed, he replaces the Board of the corporate debtor, but under Sec.19, the suspended Board of the

corporate debtor is still under a statutory obligation to assist and cooperate with the IRP. Contextually, the expression to '*extend all assistance and cooperation*' does not and cannot imply coffee with the IRP, but a subtle way of communicating the legislative intent that the suspended Board shall share all the information which will be useful for the IRP to prepare its assets and liability statement of the corporate debtor. To state it differently, Sec.19 casts a duty to make full and complete disclosure of all the assets and liabilities of the corporate debtor by its suspended Board. Evidently, the Parliament's choice of expression is not happy, but if the expressions that it has used is not interpreted as above, then it would inflict injury on the rights of the creditors and that will derail the objectives of the IBC from its intended course.

(iii) Duty of the IRP & the RP

37. Under the scheme of the IBC, IRP and RP have been enjoined with the statutory duty to prepare the statement of assets and liabilities of the corporate debtor at the preliminary stage of the insolvency proceedings and an Information Memorandum at the final leg of the resolution process, as the case may be. They are but statutory offices temporarily created for each particular case from among the freelancing professionals, sponsored by registered agencies and approved by the IBBI, with no mechanism to

ascertain their professional integrity and ethical fidelity beforehand. Still their role is central to the resolution process, and the commercial wisdom of the CoC of the ***M.K.Rajagopalan dictum*** variety depends chiefly on the quality of the information they provide.

38. It now shifts the spotlight to the Information Memorandum which the RP prepares under Sec.29 of the IBC. The Information Memorandum is critical not only for the CoC but is also for the resolution applicant since it forms the basis for the resolution plan. It therefore, follows that the information so collected and collated shall be a complete disclosure *inter alia* of all the liabilities of the corporate debtor, which in turn will facilitate the application of the clean slate theory to secure the interest of a resolution applicant. Regulation 36 of the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016, details the kind of information which the Memorandum shall contain, and the prominent among them is the list of creditors.

39. What are the possible sources of information to which the Resolution Professional may lay his hands for preparing the Information Memorandum? Very obviously, the blue print will be the statement which the IRP is required

to prepare under Sec.18. This is the first ever statement prepared in the journey of the insolvency proceedings.

40. The next point is how to ascertain the outstanding liabilities of a corporate debtor? Here, neither the IRP nor the RP (in cases where both are different) are blindfolded to travel in a pitch-dark alley but are expected to exercise utmost diligence in accessing every material to which he may lay his hands on as a trained professional.

41.1 Moving further, while ascertaining the list of creditors of the corporate debtor, the IRP or RP may act on the information shared by the suspended Board of the corporate debtor, his own reading of the previous financial statements of the corporate debtor, and also the claims preferred pursuant to the public notice issued by the Adjudicating Authority under Sec.13 read with Sec.15. It may be stated here that merely because a public notice is issued about the admission of an insolvency proceeding against a corporate debtor in couple of newspapers, it cannot be presumed that every creditor, be it operational or financial, will readily read it. And to re-emphasise, the working of the IBC should not ignore or overlook the fact a claim to money of the creditors is their Constitutionally protected right to property under

Art.300A, and hence it cannot be destroyed merely because the creditors have not preferred any claims pursuant to public notice. Seen in the context, a public notice is only a mode for collecting information to aid in the preparation of the data base of the creditors of a corporate debtor, and not the only mode.

41.2. For instance is it difficult for an IRP or a RP to enquire whether the building where the corporate debtor functions or has its factory unit is a rented premises or owned by it, and if it is rented premises whether there are rental arrears, or if there are any litigations for rental arrears. It only requires sheer commonsense. (But sadly, at the field level even this is not seen effectively done by many RPs and the IRPs, who claim themselves to be trained professionals). Similarly, will it be difficult for the IRP or the RP to hold a meeting with the suppliers of goods and services to the corporate debtor to the extent their names are disclosed in the books of accounts? For this purpose is it not necessary that he holds discussions with the auditors of the corporate debtor? Similarly, as regards the issue of statutory liability of any corporate debtor, is it not possible for the IRP or the RP to ascertain: (a) if there are immovable properties, if the property tax payable to the local body and the land tax or the *kist* payable to the Government have been paid;

(b) if there are workers, if ESI contributions and EPF remittances have been made; (c) if there is electricity connection, whether electricity charges have been paid; (d) if any corporate tax is liable to be paid, if the same had been paid. For obtaining these information, should the IRP or the RP require to be graduated from the Harvard Business School or our own IIMs, or possess a Sherlockian intelligence? All it requires is simple curiosity of a common man of ordinary prudence. Hence, if the IRP or the RP still fails even to ascertain them, then it will be a shameless exhibition of their lack of professionalism and clear demonstration of lack of due diligence in preparing their financial statement or the Information memorandum, as the case may be.

41.3 It is time the IRPs and the RPs realized that their office is not an office of comfort, but an onerous one for it is on their diligence and integrity the successful working of the IBC rests. They should not forget that their claim figures first when the resolution plan goes for a shower under the waterfall. Sadly, not many seem to have realized the significance of their duty, and how their abject callousness drowns the operational creditors into poverty, more particularly the MSME operational creditors. Indeed, it is common experience of most courts in this country that they do not even respond to the summons issued by the court in any suits or appeals or other proceedings

involving a corporate debtor. It may be that there may be a moratorium on litigations during the pendency of the resolution process, but it requires to be emphasized that every litigation can give the IRP or the RP some information about the assets and liabilities of the corporate debtor. It could now be derived that due diligence expected of the IRP or the RP makes it mandatory for them to take note of any pending litigations while preparing the statutory documents that they are required to prepare. And, it follows that, if they fail to collect those information, necessarily there is a failure on their part to act with due diligence. (To ensure that the IRP and the RP act with due diligence, it may be necessary to inform the Adjudicating Authority/the NCLT about the pending litigation, which in turn may ensure that the Information Memorandum is a complete document on the information required)

(iv) Transparency As Fairness in action

42. The foregoing discussion significates that the duty to act fairly does not start with the CoC but it commences even when the IRP or the RP prepare their statement or the Information Memorandum, as the case may be. The level of comfort an operational creditor may obtain in his journey through the resolution process is directly proportionate to the extent of fairness with which the CoC treats the former's rights equitably. It is not what the RP or

the CoC consider as fairness that matters to law, but how the operational creditors are treated on an impartial assessment by the Adjudicating Authority that matters.

43. Be it in private law or in public law, fairness is the fulcrum that holds together the societal discipline and administrative order, as the case may be. While transparency in public law echoes often in high amplitude, it is not alien to private law. Do not the parties to a contract owe mutual transparency to ensure fairness in their transaction? It must be remembered that the COC, the IRP and the RP are not purely private actors but are players in a statutory setting. Their respective roles are defined by the statute, and underlying beneath the same is their duty to be transparent. Fairness in action will be acknowledged only where the transparency in action is assured.

44. Therefore, there is a need for the RP to make transparent the correctness of the Information Memorandum he prepares, more critically the valuation reports which he makes available. The operational creditors shall have the same access to information as the CoC, since IBC has only stripped the operational creditors of their right to decide on their right, and not their right to know.

45. Transparency is not just a promoter of fairness but is also a check against collusion and unholy collaboration between the RP, CoC and the corporate debtor from defeating the rights of the operational creditors. It cannot be forsaken.

(k) Duty of the Adjudicating Authority

46. From the ***Essar Steel case*** to the ***Rainbow Papers case*** and other decisions, the Adjudicating Authority has been told that its duty is limited to satisfying itself of the due compliance of Sec.30(2) requirement by the CoC when the latter approved the resolution plan. The ***Essar Steel*** in particular has held that the Adjudicating Authority shall not substitute its sense of fairness and equity to replace the commercial wisdom of the CoC. The ***Rajagopalan*** effect**,** it must be stated, does not stop with bringing in clarity in understanding the expression 'commercial wisdom' of the CoC, but also has interfered to realign the understanding of the duty of the Adjudicating Authority. Therefore, even though the Adjudicating Authority may not sit in appeal over the commercial wisdom of the CoC, still it is required to exercise a jurisdiction, akin to a revisional jurisdiction, to ascertain the correctness of what has been done before and by the CoC. And, this may have to be

appreciated in the backdrop of the Constitutional need to constitute the Adjudicating Authority as a neutral tribunal to save IBC from facing embarrassing moments in view of the law declared in the ***Madras bar Association case***. Set on this plane and based on the discussion hereinabove made, it could be now derived that the Adjudicating Authority may refuse to give his approval to a resolution plan as approved by the CoC in the following circumstances:

a) if the information which forms the basis for the CoC for according its assent to a resolution plan is incomplete and exhibits lack of due diligence on the part of the RP to collect and collate information. This includes failure of the suspended Board of the Corporate debtor to make full disclosure of its affairs, which the IRP or the RP could have discovered with due diligence;

b) where there is lack of transparency vis-a vis the correctness of the information to the knowledge of the operational creditors;

c) where the CoC does not provide for the minimum payment which the operational creditors would have received in case of liquidation of the corporate debtor;

d) where despite providing for the minimum, the operational creditors are not fairly and equitably treated in terms of Explanation I to

Sec.30(2), such as where fairness and equity might have permitted payments above the minimum. To repeat, the Adjudicating Authority may not substitute the commercial wisdom of the CoC with its sense of equity and fairness, but can always refuse his assent to a resolution plan for breach of Explanation I to Sec.30(2) of the IBC.

(l) Finality of the Resolution Plan & the CST

47. Here the creditors of the corporate debtor, both financial and operational, form themselves into two classes: (a) Disclosed creditors, who had the opportunity to participate in the resolution process; and (b) the undisclosed creditors whose existence the IRP and the RP with due diligence could have found.

48. In the case of disclosed creditors, CST will definitely apply, if any of the aggrieved creditors did not opt to challenge the resolution plan as approved under Sec.31 before the Appellate Authority, the NCLAT. So far as the undisclosed creditors are concerned if CST is applied, they become instant victims of the callousness of the IRP and the RP as well as the deliberate silence of the suspended board in not revealing them.

49.1 Here, the corporate debtors themselves must be classified into two: The MSME corporate debtor who had the opportunity to participate in the resolution process effectively to the extent of presenting a resolution plan; and (b) non MSME corporate debtor.

49.2 In ascertaining how CST will apply vis-à-vis an undisclosed creditor is concerned, irrespective of whether the corporate debtor is a MSME or not, its suspended Board has an obligation to make a complete disclosure. See paragraph 36 above. This will now produce two consequences:

a) If after a successful completion of a resolution process, the same promoters or substantially the same set of directors of the corporate debtor continue to be in the management, then CST will not apply to forfeit the rights of the undisclosed creditors when the suspended Board had an opportunity to disclose all its creditors during the resolution process. One who owes a duty to disclose cannot take advantage of one's own suppression of information.

b) If after a successful resolution process, a third party-resolution applicant takes over the corporate debtor, then CST will apply to

extinguish the rights of the undisclosed creditors but only against the successful resolution applicant or its successors-in-interest, and not against the promoters or the suspended board of directors of the corporate debtor. It should not be forgotten that CST is a judicial coinage to protect the third party-successful resolution-applicant from the uncertainties of future claims, and not invented to protect the fraud and suppression of the suspended board of the corporate debtor.

49.3 In all the cases, where the undisclosed creditors' rights are kept alive against the erstwhile promoters or board of directors of the corporate debtor, as indicated in paragraph 49.2(b) above, the following aspects go with it as a backup measure to ensure its working:

a) The immediate consequence is that each of the promoters or the directors in the suspended board of the corporate debtor shall be personally liable, jointly and severally, to the undisclosed creditors – both financial and operational, and they can be proceeded against both for civil and criminal liability. And, none of them shall be let go anywhere near the shelter which Sec.32-A of the IBC provides, for the extinguishment of criminal liability contemplated under the said

provision is not intended for those who conspire to defeat the intent of the IBC, play on fraud on the statute, and abuse its process. Indeed even Sec.32-A is intended to operate only "*if the resolution plan results in change in the management or control of the corporate debtor*" and to protect a third party resolution applicant who is unrelated to the erstwhile managers of the corporate debtor.

b) None in the suspended board of the corporate debtor shall be granted a sanctuary behind the jurisprudential principle of corporate personality. After all, when the corporate debtor was in crisis and was one step short of going into liquidation when it was facing a resolution process, the jurisprudential difference between the company and its shareholders shall necessarily melt to pave the way for enthroning justice for the undisclosed creditors. Corporate veil is not an impregnable iron curtain to interfere with the court's power to lift it when motivated acts of fraud or unfairness attempt to hide behind it, more so, when such acts prejudice the interests of the innocent third parties.

(m) What the Petitioner may anticipate

50. Is the writing on the wall for the petitioner? Obviously yes, as it cannot

now resile from its obligation to pay the TANGEDCO. The reasons are twofold:

- First, it is a MSME corporate debtor, which participated in the resolution process, came up with a successful resolution plan and chose not to disclose its liability to the TANGEDCO. And, today the same promoters continue in the management. They fit in perfectly with a situation contemplated in paragraph 48.2(a) above.
- Second aspect is about a lurking suspicion, to which this court did not intend to invest more time, of a collusion between the corporate debtor and its only financial creditor. This is explained as below:
  - Let the facts be examined closely again: Here is a MSME in debt-trap. It has one secured financial creditor, and God knows how many operational creditors it had. At least TANGEDCO was not one of its disclosed operational creditor. If the aim of the IBC is to preserve the assets of the MSME as a going concern even as it struggles to find a way out of it, and if the only financial creditor had shared this concern and had chosen not to liquidate the MSME, then it could have easily invoked the SARFAESI Act, more particularly Sec.13(4)(b) and could have taken over the

management of the MSME. This would have ensured that not only the MSME is saved, but the interests of the operational creditors are also preserved intact. This must also be appreciated in the context of the nature of solution that had eventually developed in the resolution plan offered and accepted: The MSME petitioner offered to sell its non-core assets for paying off its debts to its only financial creditor. This still could have been achieved without a CIRP under the IBC regime, as it only required that the MSME petitioner and its only financial creditor shared due consensus. But the charm and the temptation in invoking the IBC is that, unlike the regime it has created, SARFAESI does not have a clean slate theory inbuilt in its statutory scheme nor has the advantage of any judicial pronouncements to bring it out, with the result the MSME debtor will still be under an obligation to pay the liability to all its other creditors.

- Why should the financial creditor invoke IBC even though it has an option to invoke, and what has it achieved when it was only offered a promise to repay the debts by the sale of the non-core assets of the MSME petitioner? The point is not

about the financial creditor's choice of remedy- either under the SARFAESI Act or under the IBC, or its right to invoke them, but about the intent behind exercising its option.

Has fraud or collusion ever paraded with a placard proclaiming them to be one such? Fraud has to be unearthed through inferences from attending circumstances. It is hence, mandatory not to eschew the attending circumstances from judicial purview while evaluating the bonafides of a resolution plan, more significantly the fairness expected of it as there is an obligation on the CoC to protect the interests of the operational creditors.

51. Another aspect which is intriguing is that when the IBC contemplates a Committee of Creditors, it uses a plural and a not singular, and hence is it permissible within the scheme of IBC to recognize one member CoC? This requires examination but may have to be tested in another case.

POINTS TO PONDER

52.1 This is for the Parliament. Before winding up, this Court intends to persuade the Parliament to evaluate the working efficiency of the IBC. Here it would be apposite to refer to the candid review of the IBC by Shri.V.Ramasubramanian J., (former Judge of the Supreme Court of India),

and it reads: [1]

> "*An impact assessment study of IBC has now become necessary, for more reasons than one. Of late, cases of misuse of the provisions of the Code by all stakeholders such as (i) debtors (ii) creditors (iii) resolution professionals and (iv) resolution applicants, have started attracting the attention of courts. For instance, NCLAT highlighted in a case very recently, that large business houses with multiple business arms cannot be allowed to disrupt small businesses.*
>
> *Cases of (i) misconduct on the part of the Resolution Professionals (ii) highhandedness on the part of some of the creditors (iii) abuse of the Code by debtors, through collusive CIRPs and (iv) vultures eyeing for takeover of healthy companies are actually on the rise. The percentage of hair cuts have increased to such an extent that in some cases, they appear as close shave.*
>
> *Therefore, it will be worthwhile to have a thorough study conducted at the earliest so that there is a timely cure. Otherwise,* ***we may land up in a situation where IBC itself may need a resolution plan****."*

Shri. Anant Merathia's book titled "*Defaulter's Paradise Lost*" also makes a poignant reading on the functioning of the IBC.

1Justice V. Ramasubramanian, in his introduction to the book titled "*Corporate Insolvency Resolution Process and Liquidation under the Insolvency and Bankruptcy Code, 2016*," authored by Justice L Nageswara Rao and Avinash Krishnan Ravi, Lexis Nexis, 2023.

52.2 In the context of attempts to avoid the dues to TANGEDCO by the corporate debtor, it is relevant to refer to the following passage from judgement of the Supreme Court in ***K.C. Ninan Vs Kerala State Electricity Board and Ors.*, 2023 SCC Online SC 663** (a case not on IBC). Speaking for the bench, the Hon'ble Chief Justice has observed:

> *"117….the failure or inability to recover outstanding electricity dues would negatively impact the functioning of the public utilities and licencees…. In the larger public interest, conditions are incorporated in subordinate legislation whereby Electric Utilities can recoup electricity arrears. Recoupment of electricity arrears is necessary to provide funding and investment in laying down new infra structure and maintaining the existing infrastructure. In the absence of such a provision, electric utilities would be left without any recourse and would be compelled to grant fresh electricity connection, even when huge arrears of electricity or outstanding. Besides impacting the financial health of the utilities, this would impact the wider body of consumers."*

It will be appreciable if the Parliament considers the views of Supreme Court in ***K.C.Ninan's case*** in all seriousness for protecting the statutory dues and other commercial dues payable to Government run companies or corporations which has the potential of adding to the financial burden of the common man.

It is not about what constitutes a statutory liability that concerns this Court, but why should there be a social distribution of the liability of the corporate debtor, when in the best of times the latter hardly may have shared its profit with the society, except perhaps to the extent mandated by law through Corporate Social Responsibility. For instance, if electricity-distribution-licensees suffer loss in the water-fall mechanism because of their classification as operational creditors, this loss will eventually be spread socially on other consumers.

52.3 While the legislative intent to save the corporate debtor as a going concern may be appreciable, should it be at the cost of others, more so when IBC offers adequate space for engineering manipulation? The larger question therefore, is why should the Parliament bend backwards to protect one corporate debtor at the risk of exposing the public interest to peril? The present case, a case-study merely, illustrates how IBC could be manipulated to defeat the interests of the undisclosed creditors of the corporate debtor. Some points for the Parliament to ponder, and some legislative correction for it to make, lest the long term impact of the IBC could be disastrous, if not counter productive. Incidentally, has the Parliament taken note of the percentage of recovery generally achieved out of a successful resolution

process of the corporate debtor?

CONCLUSION

53. In the result, this petition is dismissed and given the nature of questions it raised, there will no order as to costs. And the connected miscellaneous petition stands closed.

Note:

After going through the papers in this case and the authorities and other literature on the topic, it became an imperative necessity for this Court to find an internal balance in the working of the IBC to ensure that the statute does not sap the confidence of the operational creditors, nor it becomes a tool in the hands of a few to profit out of a situation unduly, who include some IRPs and the RPs lacking in professional integrity (till at least the Parliament decides to review the functioning of the IBC). And the decision to this case is well wrapped in this endeavour. It therefore, required some intimate moments with the issue, requiring deeper contemplation and took a longer time to prepare this order.

07.06.2024

Index : Yes / No
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N.SESHASAYEE.J.,

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Pre-delivery order in
W.P.No.29845 of 2022

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