



Essar Insolvency Case

Why in News

The Supreme Court has recently given its judgement in the **Essar Insolvency case**. The Judgement has paved the way for ArcelorMittal and Nippon Steel to take over debt-laden Essar Steel.

Takeover troubles

The SC on Friday paved the way for ArcelorMittal's takeover of Essar Steel. A brief timeline of how the bid unfolded:

October 4, 2018: SC uses extraordinary powers under Article 142 to give ArcelorMittal and Numetal a chance to pay off the NPAs of corporate debtors as a pre-condition to buy Essar Steel

Oct. 18: Arcelor informs resolution professional it has paid off the debts

Oct. 19: Arcelor



re-submits resolution plan for Essar

Oct. 25: Essar's committee of creditors' (CoC) approves Arcelor's final negotiated resolution plan

March 8, 2019: NCLT says financial and operational creditors

should get equal treatment

July 4: NCLAT holds that in a resolution plan, there can be no difference between a financial creditor and an operational creditor in the payment of dues. CoC moves SC in appeal

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Background

- In March 2019, [National Company Law Tribunal \(NCLT\)](#) approved global steel-giant ArcelorMittal's bid for Essar Steel.
- The **Committee of Creditors (CoC)** approved the resolution plan offered by the ArcelorMittal. Under the resolution plan, ArcelorMittal offered an advance cash payment of about ₹42,000 crore to the financial creditors and capital infusion of ₹8,000 in the next few years. However, the offer did not have much for operational creditors to Essar Steel.
- In 2019, the [National Company Law Appellate Tribunal \(NCLAT\)](#) cleared the CoC's plan but **changed the financial distribution plan by ordering an equal recovery plan** for all creditors, including financial and operational creditors.

Highlights of the Judgement

- **Wisdom of CoC:** It is the commercial wisdom of the requisite majority (66%) of the CoC under



the [Insolvency and Bankruptcy Code \(IBC\)](#) to negotiate and accept a resolution plan, which may involve **differential payment** to different classes of creditors.

- **Principle of Equality:** The Court held that the equality principle cannot be stretched to treating unequals equally. This will destroy the very objective of the IBC to resolve stressed assets. **Equitable treatment is to be accorded to each creditor depending upon the class to which it belongs:** secured or unsecured, financial or operational.
- **Restriction on Tribunals:** Tribunals have no “**residual equity jurisdiction**” to interfere in the merits of a business decision taken by the CoC. This implies that the NCLT and NCLAT **cannot interfere** with the commercial decisions taken by the CoC.
- **Financial vs Operational Creditors:** The Court upheld the **primacy of financial creditors** over operational creditors in the distribution of funds received under the corporate insolvency scheme.
 - The Court explained that financial creditors are capital-providers for companies, i.e. help companies to purchase assets and run business operations.
 - Operational creditors, in a way, are beneficiaries of amounts lent by financial creditors.
- **Relaxation of Resolution Deadline:** The Supreme Court has **done away with the 330-day mandatory deadline** for the resolution of insolvency and bankruptcy cases after which liquidation is invoked. The bench allowed a bit of flexibility by allowing exceptions where the resolution plan is on the verge of being finalised.
 - The 330-day mark is **violation of Article 14** (right to equal treatment) of the Constitution **and Article 19(1)(g)** (Right to carry any business) of the Constitution.

Likely Impact of the Judgement

- **Impact on Banks:** Banks will recover Rs. 42,000 crore against admitted debts of Rs. 49,473 crore- a recovery of about 85% compared to the average recovery of 53% in other resolution cases. This would help banks in boosting their capital adequacy.
- **Speedy Resolution:** The verdict is likely to reduce legal wrangling between financial and operational creditors and accelerate resolution process.
- **Foreign Investment:** It will attract investors who were getting wary of the nation’s bankruptcy process.
 - India is trying to attract foreign capital to its bad loan cleanup, as it battles the **worst nonperforming loan ratio** among the world’s major economies.
- **Upheld the Spirit of IBC:** The removal of mandatory 330-day deadline will facilitate resolution, the ultimate objective of the IBC.

Insolvency Resolution Process in India

- **Eligibility:** Under IBC, companies (both private and public limited company) and Limited Liability Partnerships (LLP) can be considered as defaulting corporate debtors.
 - A **corporate debtor** is any **corporate** organization which owes a debt to any person.
- **Default Amount:** The Insolvency and Bankruptcy Code can be triggered if there is a **minimum default of Rs 1 lakh**. This process can be triggered by way of filing an application before the National Company Law Tribunal (NCLT).
- **Resolution Initiation:** The process can be initiated by two classes of creditors which would include financial creditors and operational creditors.
 - **Creditors:** A Creditor means any person to whom a debt is owed and includes a financial creditor, an operational creditor, etc.
 - **Financial Creditors:** The financial creditor in simple terms is the institution that provided money to the corporate entity in the form of loans, bonds etc. E.g. banks.
 - **Operational Creditors:** An operational creditor is the entity who has a claim for providing any of the four categories to the defaulted corporate- goods, services, employment and Government dues (central govt, state or local bodies).
- **Appointment of Interim Resolution Professional:** As soon as the matter is admitted by the NCLT, the NCLT proceeds with the appointment of an Interim Resolution Professional (IRP) who

takes over the management of the defaulting debtor.

- **Committee of Creditors (CoC):** A committee consisting only of the financial creditors i.e. the CoC is formed by the IRP.
 - Only operational creditors having aggregate dues of at least 10% of the total debt are invited into the meeting of CoC (**Operational creditors are not a member of CoC**). The operational creditors don't have any voting power.
- **Corporate Insolvency Resolution Process (CIRP):** It includes necessary steps to revive the company such as raising fresh funds for operation, looking for new buyer to sell the company as going concern, etc.
 - The CoC takes a decision regarding the future of the outstanding debt owed to it. The resolution plan can be implemented only if it has been approved by 66% of the creditors in the CoC
- **Liquidation Proceedings:** In the event a resolution plan is not submitted or not approved by the committee of creditors (COC), the CIRP process is deemed to have failed. In such a situation the liquidation proceedings commences subject to the order of the tribunal.

[Source: TH](#)

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