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# UPDATE

*11 August 2022*

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# The Hon'ble Supreme Court's ruling on the preponderance of the commercial wisdom of the Committee of Creditors in withdrawal of insolvency proceedings.

## *A. Setting the context*

The preamble of the Insolvency and Bankruptcy Code, 2016 (the "**Code**") makes the objective of the Code clear and unambiguous, by seeking to achieve reorganisation and insolvency resolution of corporate persons, partnership firms and individuals for, maximization of value of assets, promoting entrepreneurship; greater availability of credit and; balancing the interests of all the stakeholders, albeit in a time bound manner. Each provision of the Code was drafted keeping these principles in mind, and the introduction of this legislation was done with the aim of replacing the existing framework for insolvency which was visibly inadequate, ineffective and wrought with delays.

The Ministry of Corporate Affairs (the "**MCA**") constituted the Insolvency Law Committee (the "**Committee**") to conduct a detailed review of the Code in consultation with key stakeholders. The Committee through its recommendation, was of the view that, in order to fulfil the stated objective of the Code i.e. to promote resolution, it is necessary to re-calibrate the voting threshold for various decisions of the committee of creditors. Consequently, the Committee unanimously agreed that with regard to withdrawal of Corporate Insolvency Resolution Process ("**CIRP**") pursuant to settlement, "*relevant rules may be amended to provide for withdrawal post admission if the CoC approves of such action by a voting share of ninety per cent*"[1]. It is pertinent to note here that, prior to this, under the CIRP Rules[2], the NCLT may permit withdrawal of the application on a request by the applicant before its admission, and there was no provision in the Code or the CIRP Rules in relation to permissibility of withdrawal post admission of a CIRP application. The Committee was of the view that once the CIRP is initiated, it is no longer a proceeding only between the applicant creditor and the corporate debtor but is envisaged to be a proceeding involving all creditors of the debtor i.e. a proceeding in rem. The intent of the Code is to discourage individual actions for enforcement and settlement to the exclusion of the general benefit of all creditors.

In Vallal RCK vs M/s Siva Industries & Anr,[3] the Hon'ble Supreme Court of India ("**Hon'ble SC**") has given precedence to the commercial wisdom of the Committee of Creditors ("**CoC**") where the short question that falls for consideration was as to whether the adjudicating authority i.e., the NCLT or the appellate authority i.e., the NCLAT can sit in an appeal over the commercial wisdom of the CoC.

## *B. Factual Background*

IDBI Bank Limited had filed an application[4] for initiation of CIRP in respect of the Corporate Debtor, M/s Siva Industries and Holdings Limited. The Ld. NCLT, vide its order dated 4th July 2019, admitted the said

[1] Para 29.2, Report of Insolvency Law Committee Report, 2018
[2] R 8, The Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016
[3] Civil Appeal Nos. 1811-1812 of 2022 decided on 03 June, 2022
[4] S 7, The Insolvency and Bankruptcy Code, 2016

application, thereby initiating the CIRP, in respect of the Corporate Debtor. The Resolution Professional ("**RP**") had presented a Resolution Plan before the CoC, submitted by one M/s Royal Partners Investment Fund Limited. However, since the said Plan received only 60.90% votes of the CoC and could not meet the statutory requirement of receiving 66% votes[5], the said Plan could not be approved.

Thereafter the RP filed an application for the initiation of liquidation process of the Corporate Debtor. The appellant, who is the promoter of the Corporate Debtor, filed a settlement application before the Ld. NCLT, showing his willingness to offer one-time settlement plan. Deliberations took place in the said meetings with regard to the said Settlement Plan and the final settlement proposal which was submitted by the appellant came to be considered by the CoC in its 16th meeting. Initially, the said Settlement Plan received only 70.63% votes. However subsequently, one of the Financial Creditors viz. International Assets Reconstruction Co. Ltd. having voting share of 23.60 %, decided to approve the said Settlement Plan and intimated the RP about the same and the said Settlement Plan stood approved by more than 90% voting share. Consequently, the 17th CoC meeting was convened, wherein the said Settlement Plan was approved with a voting majority of 94.23%. Accordingly, the RP filed an application before the Ld. NCLT seeking withdrawal of CIRP initiated against the Corporate Debtor in view of the approval of the said Settlement Plan by CoC. The Ld. NCLT, vide its order dated 12th August 2021, holding that the said Settlement Plan was not a settlement *simpliciter* under S 12A of the IBC but a "Business Restructuring Plan", rejected the application for withdrawal of CIRP and approval of the Settlement Plan. Vide another order, the Ld. NCLT initiated liquidation process of the Corporate Debtor. Being aggrieved thereby, the appellant preferred two appeals before the Ld. NCLAT. However, the Ld. NCLAT vide its judgment dated 28th January 2022, dismissed the same. Hence, the appeals were preferred by the Appellant before the Hon'ble SC.

## C. *The Verdict*

Earlier, the Hon'ble SC and the Ld. NCLTs/NCLAT were allowing settlement between creditors and debtors on an ad-hoc basis. Therefore, the Insolvency Law Committee suggested introduction of an amendment to allow withdrawal of insolvency proceedings subject to approval of 90% of the CoC. The Hon'ble SC, while citing the legislative history, analyzed the object and intent of S12A of the Code and Regulation 30A of the CIRP Regulations[6] to hold that approval of a settlement plan by the CoC is a product of the commercial wisdom of the CoC which is paramount. Therefore, the NCLTs/NCLAT cannot intervene with such a decision of the CoC. Consequently, the Hon'ble SC allowed the appeal and quashed the orders of Ld. NCLT and the Ld. NCLAT. Referring to an earlier judgment, the Hon'ble SC stated that only if a CoC rejects a just settlement arbitrarily, can the Ld. NCLT set aside such a decision of the CoC.

## D. *Endnote*

It could be seen that S 12A of the IBC was brought in the statute book on the basis of the said Committee's Report. It could be noticed that though by the amendment of the Code in 2018, the voting share of 75% of CoC for approval of the Resolution Plan was brought down to 66%, S 12A of the Code which was brought in the statute book by the same amendment, requires the voting share of 90% of CoC for approval of withdrawal of CIRP. It could thus, clearly be seen that a more stringent provision has been made insofar as withdrawal of CIRP is concerned.

In the case of *Swiss Ribbons Private Limited and Another v. Union of India and Others*[7], it was held that the main thrust against the provision of S 12A is the fact that 90% of the CoC has to allow withdrawal. This high threshold has been explained in the Committee report as all financial creditors have to put their heads together to allow such withdrawal as, ordinarily, an omnibus settlement involving all creditors ought, ideally, be entered into. This explains why 90%, which is substantially all the financial creditors, have to grant their approval to an individual withdrawal or settlement. However, in any case, the figure of 90%, in the absence of anything further to show that it is arbitrary, must pertain to the domain of legislative policy. Hence, the preponderance of the wisdom of the CoC is the right step forward and consequently, the need for judicial intervention or innovation from NCLT and NCLAT should be kept at its bare minimum and should not disturb

[5] Sub-section (4) of S 30, The Insolvency and Bankruptcy Code, 2016.
[6] Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016
[7] Para 83, (2019) 4 SCC 17

the foundational principles of the IBC. The Hon'ble SC, further held that, "*The interference would be warranted only when the adjudicating authority or the appellate authority finds the decision of the CoC to be wholly capricious, arbitrary, irrational and de hors the provisions of the statute or the Rules*"[8].

Having said that, the basic tenet of the IBC, among other things, is the insolvency resolution of in a time bound manner and increased availability of credit. In the instant case, the Ld. NCLT rejected the application for withdrawal of CIRP and approval of the Settlement Plan on the ground that the Settlement Plan was not a settlement *simpliciter* under S 12A of the Code but a "Business Restructuring Plan". While the legislation has provided a procedure for withdrawal of Application under S 7, 9 or 10 of the Code, in the case on hand, the CoC had voted under S 12A of the Code without even getting a single sum from the promoter of the Corporate Debtor, in respect of the withdrawal of the CIRP pertaining to the Corporate Debtor. As a matter of fact, the Ld. NCLT had in its order, categorically observed that the 'Settlement Proposal' is not a 'Settlement *Simpliciter'* but it is a business restructuring plan. Further, the well settled legal principle is that the CoC ought not to approve the Resolution Plan where the Resolution Applicant is ineligible under S 29A of the Code. It is in alignment with the Code, had the CoC voted for the Settlement Proposal only in the event of receipt of money in entirety in terms of the Settlement Proposal of the Promoter of the Corporate Debtor. In such an event there was no scope of contemplating a default of the promoter of the Corporate Debtor. The primordial fact being that, as no amount was paid to the Financial Creditors of the Corporate Debtor, in case of any default committed on the part of the promoters of the Corporate Debtor, there will be no clarity with regard to the manner in which one is to proceed further, especially the Corporate Debtor being out of the CIRP, and thus entering a limbo, without any resolution.

In light of the above, it needs to be seen that whether allowing such a practice, the promoters may take course of protracted proceedings which consequently is likely to lead to substantial wastage of time and resources. It appears that in case the promoter fails to honour the commitment as approved in the Settlement Plan, then the CIRP proceeding may have to be re-initiated and the progress so made thus far shall be a mere nugatory. Therefore, the judiciary should take a pedantic approach in allowing such settlement plans which should be under exceptional circumstances and not the norm.

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[8] Para 24, ibid sl.no. 4.