



**Protection of Dissenting Financial Creditors vis-à-vis
Resolution Plan: Fair or Extravagant**

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Introduction

The Insolvency and Bankruptcy Code, 2016 (“**the Code**”) legislated with an aim of timely insolvency resolution of corporate persons, partnership firms and individuals; ensures asset value maximization while balancing the interest of all the stakeholders. When a corporate person statutorily defined as corporate debtor defaults, a financial creditor, an operational creditor or the corporate debtor itself may initiate Corporate Insolvency Resolution Process (“**CIRP**”) under the Code. The Code not only stipulates different procedures to be adopted for initiation of CIRP in each category of creditor but also confers different treatment to each such category. As per Section 21 of the Code, the Committee of Creditors (“**CoC**”) shall comprise of all the financial creditors. The CoC since its inception till the completion of CIRP propels the entire process by taking all the decisions in its commercial wisdom. The most pivotal of all such decisions is the approval of resolution plan put forth by a resolution applicant for the insolvency resolution of the corporate debtor. The legal framework mandates approval of resolution plan by a vote of atleast 66% voting share of the financial creditors. However, there may be cases where certain financial creditors either vote against the resolution plan or abstain from voting for the resolution plan, as approved by the CoC, such financial creditors are generally referred to as dissenting financial creditors.

Minimum Entitlement to Dissenting Financial Creditors under a Resolution Plan

The Insolvency and Bankruptcy Code (Amendment) Act, 2019, amended section 30(2)(b) of the Code to provide a minimum entitlement to the dissenting financial creditor. The said section guarantees a minimum payment to dissenting financial creditors, which shall not be less than the amount to be paid to such creditors in accordance with waterfall mechanism in the event of a liquidation of the corporate debtor. Further, regulation 38(1)(b) of the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 (“**CIRP Regulations**”), mandates that dissenting financial creditor shall be paid in priority over financial creditors who voted in favour of the resolution plan.

Therefore, as per the current position under the Code/CIRP Regulations, the following dual benefits flow to dissenting financial creditors in a resolution plan –

- Guaranteed payment of minimum liquidation value as per waterfall mechanism; and
- Payment in priority to assenting financial creditors.

One of the primary objectives of the Insolvency and Bankruptcy Code (Amendment) Act, 2019 was to ensure that all creditors are treated fairly, without unduly burdening the Adjudicating Authority whose role is to ensure that the resolution plan complies with the provisions of the Code. Although, the purpose of entitling a minimum amount to the dissenting financial creditors was to protect them and to balance the interests of all the creditors but this has led to certain issues. The afore-mentioned dual benefits, may sometimes incentivize the financial creditors to vote against the resolution plan.

Protection of Dissenting Financial Creditors

Financial creditors may consciously choose to vote against a resolution plan (even if the resolution plan is compliant of the provisions of the Code and CIRP Regulations) in anticipation of higher amount ensuant to the amended provisions of section 30(2)(b). This may happen in a situation where the realisable value under the plan is less than the liquidation value of the corporate debtor. This may act as a deterrent for financial creditors from approving resolution plans which offer less value than the liquidation value. The Hon'ble Supreme Court in the case of Committee of Creditors of Essar Steel India Limited Vs. Satish Kumar Gupta & Ors¹, also observed that section 30(2)(b) is a beneficial provision in favour of dissenting financial creditors as they are now to be paid a certain minimum amount.

The National Company Law Appellate Tribunal in the matter of DBS Bank Ltd., Singapore Vs. Mr. Shailendra Ajmera & Anr², has rightly observed that, *"no 'Financial Creditor' including a 'secured creditor' can dissent on the ground that if it dissents against the 'resolution plan', inspite of plan being feasible and viable and in accordance with Section 30(2), just to get the more amount than the other 'secured creditor' such 'dissenting secured financial creditor' cannot take advantage of amended Section 30(2)(b)(ii)"*

Securing Payment based on Liquidation Value

While Section 30(2)(b) of the Code, ensures a minimum entitlement to dissenting financial creditors, but the basis for calculating such guaranteed payment is dependent on an estimation i.e., liquidation value. Regulation 2(1)(k) of the CIRP Regulations spells out the definition of liquidation value to mean the estimated realizable value of the assets of the corporate debtor, if the corporate debtor were to be liquidated on the insolvency commencement date. Albeit, Section 12 of the Code necessitates that CIRP in respect of a corporate debtor should be completed within 330 days, nonetheless, this timeline is often stretched through extension or exclusion of time consumed in legal proceedings surrounding insolvency resolution of the corporate debtor. Such prolonged process often causes value erosion due to the depleting assets of the corporate debtor, thus, the liquidation value as on the insolvency commencement date, in some cases, could be higher than the actual realizable value to the creditors under the approved resolution plan.

According to the statistics reported in the Quarterly Newsletter of the Insolvency and Bankruptcy Board of India (October-December, 2022), as per the timeline of the ongoing CIRPs, 64% of the cases have already crossed the 270 days threshold limit. Furthermore, as per the data, in a total of seven CIRPs out of a total twenty-eight cases yielding resolution plan during the reporting quarter, the realisable value was less than the liquidation value of the corporate debtor, which is almost twenty-five percent of the total cases. It is noteworthy that the average number of days consumed in conclusion of the aforesaid seven cases is approximately 907 days. Although, the realisable value is contingent upon several market driven factors, the enduring insolvency resolution process also greatly affects the realisable value under a resolution plan due to value erosion of assets of the corporate debtor in the course of time.

Protection of Dissenting Financial Creditors

Therefore, in a case where the liquidation value is higher than the realisable value, the financial creditors may tend to dissent in order to secure higher payments over and above the assenting creditors. This may sometimes even result in death of the corporate debtor if it is ultimately pushed into liquidation.

Conclusion

To pre-empt any deliberate or undue rejection of the resolution plan, CIRP Regulations would have to be revisited to provide clarity on the methodology, term and type of payment, be it monetary / non-monetary. The insolvency law regulator, Insolvency and Bankruptcy Board of India, in one of its discussion papers titled **“Changes in the corporate insolvency resolution process to reduce delays and improve the resolution value”**, released in the month of June, 2022, also acknowledged that when liquidation value is higher than the actual realization, this may create a perverse incentive for creditors to dissent to a resolution plan and receive a higher value and militate against the objective of resolution. Suitable amendments were proposed to link the minimum entitlement to the dissenting financial creditors to the realisable amount in the event of liquidation when the resolution plan has been approved. Despite the fact that this issue was recognized by the Regulator, the proposed amendment is yet to transpire.

The Courts have time and again reiterated that the Code is not a recovery mechanism, but it acts as a cradle for the corporate debtor enabling its timely resolution and value maximization. Ergo, while protecting the interest of the minority dissenting financial creditors, it is important to ensure that individual interest does not partake the larger goal of insolvency resolution of the ailing corporate debtor.

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¹Civil Appeal No. 8766-67 of 2019

²CA(AT)(Ins) No. 788 of 2019

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