

SHOT IN THE ARM: ON SC UPHOLDING INSOLVENCY AND BANKRUPTCY CODE

Relevant for: Indian Economy | Topic: Issues relating to Growth & Development - Banking, NPAs and RBI

Last week's [Supreme Court judgment upholding the validity of the Insolvency and Bankruptcy Code](#) 2016 (IBC) in its "entirety" could have a major impact on the country's economic landscape. The fledgling IBC has been severely tested in the two years since its enactment, with the Centre being forced to amend a couple of its provisions in order to plug some loopholes that enabled defaulting borrowers to challenge the legislation. Any law of this nature that takes over businesses and assets from defaulters and empowers lenders to change the management is bound to face legal challenges. Borrowers were never going to take the IBC lying down, and that is exactly what happened; over the last two years, they have challenged various aspects of the law in tribunals and courts. In the event, the apex court's stamp of approval on the entire Code is a strong signal to borrowers and banks even as it brings a sense of relief to the Centre, which has been watching one of its better economic initiatives being stifled by vested interests.

One of the major challenges mounted against the IBC was by operational creditors, who are owed money by the company in the normal course of operations for supply of goods and services. In the payment waterfall prescribed under Section 53 of the IBC in the event of liquidation of the company or its sale to another entity, their dues rank below those of financial creditors, workmen and employees. This was challenged by the operational creditors, who wanted equal treatment with financial creditors in the waterfall mechanism. Several landmark cases that were referred to the National Company Law Tribunal under the IBC remain stuck there, including that of the high-profile Essar Steel, as a result of its operational creditors seeking equal treatment. With the Supreme Court now ruling that there are "intelligible differentia" between operational and financial creditors, an avenue that defaulters used to stymie proceedings has been closed. Repayment of financial debt by borrowers infuses capital into the economy as lenders can on-lend the money that has been repaid to other entrepreneurs, thus aiding economic activity, the judges observed. The apex court has also clarified that a mere relationship with an ineligible person cannot disqualify someone from becoming a bidder for a troubled asset. It has to be proved that such a person is "connected" with the business activity of the resolution applicant. The court used strong words: "...[T]he experiment conducted in enacting the Code is proving to be largely successful. The defaulter's paradise is lost." This constitutes a clear signal of its backing for the IBC which, despite all the challenges that it has faced, has been successful in sending a message to recalcitrant defaulters that there can be no more business-as-usual when they default.

The Meghalaya government must urgently ensure that all illegal mines are shut down

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