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RAMAN ISPAT: SUPREME COURT CONFINES APPLICABILITY OF RAINBOW PAPERS

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On 17 July 2023, the Hon'ble Supreme Court delivered its judgement in *Paschimanchal Vidyut Vitran Nigam Ltd. v. Rarman Ispat Private Limited & Ors.*, 2023 SCC OnLine SC 842 (**Raman Ispat**). The specific issue of whether Paschimanchal Vidyut Vitran Nigam Ltd. (**Appellant**) could enforce a security interest created over the assets of Raman Ispat Private Limited (**Corporate Debtor**) outside of the liquidation proceedings under the Insolvency and Bankruptcy Code, 2016 (**Code**) was settled in the negative. More importantly, the Hon'ble Supreme Court confined the applicability of *State Tax Officer v. Rainbow Papers Ltd.*, 2022 SCC OnLine SC 1162 (*Rainbow Papers*) to its own factual circumstances, effectively quarantining *Rainbow Papers* from the jurisprudence on treatment of government dues under the Code and allied regulations.

Background

The Appellant, a statutory company distributing electricity, assailed an order of the National Company Law Appellate Tribunal (**NCLAT**) before the Supreme Court, as the NCLAT directed District Collector and Tehsildar to release the Corporate Debtor's assets which had been attached in the course of recovery proceedings under electricity laws. The charge on the Corporate Debtor's properties was created by the operation of a clause in an electricity supply agreement of 2010 between the Appellant and the Corporate Debtor. The clause enabled the Appellant to create a "charge on the assets of the company" pursuant to outstanding dues. Upon the Corporate Debtor's default in payment of electricity dues, the Tehsildar attached the Corporate Debtor's properties in furtherance of enforcement. Subsequently, in the liquidation proceedings before the National Company Law Tribunal, Allahabad (**NCLT**), the Liquidator applied to NCLT to direct the Tehsildar to release the attached properties in favour of the Liquidator. NCLT directed the Tehsildar to release the attached properties in favour of the Liquidator in 2018. The Appellant filed an appeal from NCLT's order which was dismissed in 2019, leading to a second appeal before the Supreme Court.

Submissions of the Appellant

The Appellant relied upon the definition of "secured creditor" and "transfer" under the Code to classify the outstanding electricity dues as security interests, and further cited *Rainbow Papers* to buttress its position as a secured operational creditor able to realise its dues outside the liquidation proceedings. Relying upon the non-obstante clause included in the Electricity Act, 2003, along with the special nature of the legislation –

the Appellant asserted the primacy of the electricity dues recovery proceedings prescribed under electricity laws over the Code and allied regulations.

Submissions of the Liquidator

The Liquidator relied upon *The West Bengal State Electricity Distribution Company Limited v. Sri Vasavi Industries Limited and Anr.*, 2022 SCC OnLine Cal 1918 to establish that electricity dues do not enjoy any special priority. While the existence of a security interest is a matter of fact that needs to be established, no such requirement exists in the electricity laws, reducing it to a mere recovery mechanism for arrears of outstanding electricity dues. Per contra, Section 52 (3) of the Code requires a liquidator to verify the existence of a security interest before it can be enforced outside the liquidation proceedings in accordance with the Code. Further, the Liquidator invoked *generalia specialibus non derogant* in favour of the Code's mechanism for enforcement of security interest, highlighting the special nature of the Code, its later enactment relative to the Electricity Act, 2023, and Section 238 of the Code which gives effect to the Code's overriding mandate when in conflict with other legislations. The Liquidator also attempted to classify the electricity dues as "government dues" under Section 53(1)(e)(i) of the Code.

Issue

Whether the Appellant can enforce its security interest over the Corporate Debtor's assets through the procedure prescribed under electricity laws, as opposed to opting for the stand-out procedure prescribed under Section 52 of the Code?

Findings and Observations of the Supreme Court

The Court affirmed the validity of the security interest created in favour of the Appellant and clarified that the dues payable to statutory corporations like the Appellant (and not to the Central Government or State Government) are to be classified as financial debt or operational debt, depending upon the nature of the transaction entered upon with the Corporate Debtor. However, such dues do not fall under the ambit of dues owed to the Central Government or State Government under Section 53 (1) (e)(i) of the Code.

Rainbow Papers was distinguished on facts as the corporate debtor in that case was undergoing insolvency resolution proceedings as opposed to the Corporate Debtor in the present case which is undergoing liquidation. Further, the Court observed that *Rainbow Papers* did not consider the waterfall mechanism under Section 53 of the Code, consequently treating the state government as a "secured creditor". The Court emphasised upon the inclusion of "government dues" in the scheme of Section 53 of the Code, highlighting the intention of the Parliament to treat dues owed to the government as distinct from dues owed to a secured creditor.

The Court further observed that Section 52 of the Code gives an option to a secured creditor to stand outside the liquidation proceedings if the secured creditor chooses not to relinquish its security in favour of the liquidation estate. The Code and allied regulations lay down a procedure and a timeline for a secured creditor to exercise this option and require such a secured creditor to make payment of insolvency and liquidation costs from the recoveries made pursuant to enforcement.

Comment

Through this decision, the Supreme Court has reiterated the primacy of IBC over other laws in the context of liquidation proceedings. More importantly, the applicability of *Rainbow Papers* has been confined to its own factual circumstances, effectively

isolating it from the jurisprudence on treatment of government dues under the Code and allied regulations.

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