

ARTICLES

APARTMENT BUYERS AS FINANCIAL CREDITORS:
PUSHING THE CONCEPTUAL LIMITS OF THE INDIAN
INSOLVENCY REGIME

M P Ram Mohan & Vishakha Raj***

A unique feature of the Indian insolvency regime is its classification of debt into “operational” and “financial” debt. In Swiss Ribbons v. Union of India, the Supreme Court of India tenaciously upheld the difference between operational and financial creditors and declared this classification constitutionally valid. In 2018, the Insolvency and Bankruptcy Code, 2016 (IBC) was amended to include amounts raised from allottees (persons to whom an apartment or plot in a real estate project has been allotted) within the definition of “financial debt,” thus making allottees financial creditors. Though the amendment was passed to empower allottees in India’s real estate sector, it revived a more general discussion on the characteristics of operational and financial creditors.

This paper posits that the amendment was enacted at the cost of stretching the definition of “financial creditor” beyond its conceptual limit and interfering with the IBC’s insolvency resolution mechanism. We use the United States’ and the United Kingdom’s insolvency regimes as a point of reference for ascertaining the role of creditors in insolvency proceedings and whether operationalizing the insolvency regime to solve problems in a particular sector is justified.

* Associate Professor, Indian Institute of Management Ahmedabad and Member, Misra Centre for Financial Markets and Economy at IIMA (mprmoan@iima.ac.in).

** Researcher, Business Policy Area, Indian Institute of Management Ahmedabad. We are thankful to the participants of the IIMA Conference on “Financial Distress, Bankruptcy and Corporate Finance” during August 9–10, 2019. Authors gratefully acknowledge the funding support of IIMA, and the detailed comments from Pratik Datta, Raj Rani Bhala and Praachi Misra. We also thank the editorial members of the *Columbia Journal of Asian Law* for their support. Errors are authors’ alone.

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I. INTRODUCTION

In 2014, the Ministry of Finance, Government of India set up the Bankruptcy Law Reforms Committee (“BLRC”) to study the legal framework for bankruptcy in India.¹ The BLRC submitted its final report in 2015 which contained the rationale and design of the Insolvency and Bankruptcy Code, 2016² (“IBC”) which went in to effect on August 5, 2016.³ The IBC overhauled the Indian insolvency regime by consolidating existing insolvency laws,⁴ introducing a new process for insolvency resolution, and altering liquidation priorities in case the resolution process failed. Notably, the IBC puts creditors at the helm of the insolvency resolution process. The BLRC report explained that the decision of what must be done with a financially distressed firm was ultimately a business decision.⁵ Accordingly, the BLRC report suggested that a

¹ Ministry of Finance, The Report of the Bankruptcy Law Reforms Committee, Volume I: Rationale and Design, 148 (November 2015), https://ibbi.gov.in/BLRCReportVol1_04112015.pdf.

² Insolvency and Bankruptcy Code, 2016, No. 31, Acts of Parliament, 2016 (India) [henceforth “IBC”].

³ Ministry of Corporate Affairs Notification, S.O.2618(E) (Aug. 5, 2016), <https://ibbi.gov.in/webadmin/pdf/legalframwork/2017/Jul/Notificationdated05.08.2016.pdf>.

⁴ Namely, the Presidency Towns Insolvency Act, 1909, the Provincial Insolvency Act, 1920, the Sick Industrial Companies (Special Provisions) Act, 1985, and parts relating to the winding up and liquidation of companies under the Companies Act, 2013. Presidency Towns Insolvency Act, 1909, No. 3, Acts of Parliament, 1909 (India); Provincial Insolvency Act, 1920, No. 5, Acts of Parliament, 1920 (India); Sick Industrial Companies (Special Provisions) Act, 1985, No. 1, Acts of Parliament, 1986 (India); Companies Act, 2013, No. 18, Acts of Parliament, 2013 (India).

⁵ The Report of the Bankruptcy Law Reforms Committee, Volume I: Rationale and Design, *supra* note 1.

“Committee of Creditors” comprising the “financial creditors” of the debtor was in the best position to make this decision.⁶

The BLRC report (and the IBC) describes two types of creditors: financial creditors and operational creditors.⁷ Financial creditors may be secured or unsecured.⁸ The BLRC report describes financial creditors as those who have a *solely* financial relationship with the debtor.⁹ Financial creditors include entities such as banks with charges over the assets of the debtor (secured creditors) and bond holders who do not have any security for the money lent by them.¹⁰ Creditors are characterized as “operational creditors” on the basis of the underlying transaction which lead to the creation of the debt.¹¹ Debts created by a contract for the provisions of goods or services (such as employment) are classified as operational debt.¹² Both financial creditors and operational creditors can trigger the insolvency resolution process under the IBC against a debtor, however, the circumstances under which operational creditors can trigger the IBC are more restricted.¹³ Importantly, operational creditors do not form a part of the Committee of Creditors which decides how a corporate debtor’s business is to be reorganized and whether it should be liquidated.¹⁴

On August 17, 2018 the Parliament of India amended the IBC by passing the Insolvency and Bankruptcy (Second Amendment) Act, 2018 (“2018 Amendment”). The 2018 Amendment used a deeming fiction to bring “allottees” under a real estate project within the scope of the definition of “financial creditor.”¹⁵ This was done by inserting an “Explanation” under clause (f) of sub-Section (8) of Section 5 which defines “financial debt.”¹⁶ Since “financial creditors” are defined as persons to whom

⁶ *Id.* at 12.

⁷ *Id.* at 54

⁸ *Id.*

⁹ *Id.* at 77. See IBC, *supra* note 2, § 5(8).

¹⁰ The Report of the Bankruptcy Law Reforms Committee, Volume I: Rationale and Design, *supra* note 1, at 54.

¹¹ *Id.* at 77.

¹² *Id.*

¹³ See *infra* section II.A. “Role of Financial and Operational Creditors in India.”

¹⁴ IBC, *supra* note 2, § 21(2).

¹⁵ *Id.* § 3.

¹⁶ *Id.* § 5(8)(f). In full:

[I]n clause (8), in sub-clause (f), the following Explanation shall be inserted, namely: — ‘Explanation. —For the purposes of this sub-clause,—

a “financial debt” is owed, the 2018 Amendment gives an allottee within a construction project the status of a financial creditor under the IBC. The 2018 Amendment makes other changes to the IBC as well which, however, are outside of the scope of this paper.

An “allottee” has been defined under Section 2(d) of the Real Estate (Regulation and Development) Act, 2016 (“RERA”) as any person to whom an apartment or plot in a real estate project has been allotted or sold.¹⁷ An “apartment” refers to a separate and self-contained part of any immovable property meant for commercial or residential use.¹⁸ An apartment, *inter alia*, includes a shop, dwelling unit, office, and showroom.¹⁹ The 2018 Amendment was based on the Insolvency Law Committee’s Report of March 2018 (“ILC report”) which highlighted how real-estate projects in India were often delayed and that this was a sector-wide concern across the country.²⁰ The ILC Report noted that out of 782 real estate projects in India, 215 of them had undergone delays ranging from 1 month to 261 months.²¹ Allottees had attempted to trigger insolvency proceedings against their real-estate developers to remedy such delays with varying results.²² The insertion of the term “allottee” as defined under RERA into the IBC was recommended by the ILC report to put them in a better position *vis-à-vis* the real estate developer.²³

The 2018 Amendment was unsuccessfully challenged by real estate developers before the Supreme Court of India in *Pioneer Urban Land and Infrastructure Ltd. v. Union of India*.²⁴ One of the grounds of the challenge by the real estate developers was that “allottees” and “other financial creditors” did not belong to the same

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- (i) any amount raised from an allottee under a real estate project shall be deemed to be an amount having the commercial effect of a borrowing; and
 - (ii) the expressions, "allottee" and "real estate project" shall have the meanings respectively assigned to them in clauses (d) and (zn) of section 2 of the Real Estate (Regulation and Development) Act, 2016.

¹⁷ Real Estate (Regulation and Development) Act, 2016, No. 16, Acts of Parliament, 2016 (India), § 2(d).

¹⁸ *Id.* § 2(e).

¹⁹ *Id.* § 2(e).

²⁰ Ministry of Corporate Affairs, Report of the Insolvency Law Committee, ¶ 1.3 (Mar. 2018), http://www.mca.gov.in/Ministry/pdf/ReportInsolvencyLawCommittee_12042019.pdf.

²¹ *Id.*

²² *Id.* ¶¶ 1.1, 1.2, 1.9.

²³ *Id.* ¶ 1.9.

²⁴ (2019) 8 SCC 416.

category, and that treating the two equally would violate the right to equality provided in Article 14 of the Constitution of India.²⁵ The petitioners likened “allottees” to “operational creditors.” When allottees are classified as “financial creditors” instead of “operational creditors,” the real-estate developers lose valuable defenses against allottees.²⁶ The Court rejected these arguments by stating, *inter alia*, that allottees were in a unique position, given that they financed the construction of their own apartments.²⁷ *Pioneer’s* differentiation of allottees from other operational creditors renewed the discussion on the characteristics of financial and operational creditors, and the need to clearly distinguish between the two.²⁸

Classifying creditors based on the characteristics of the debts they own is not a novel phenomenon in insolvency law. For instance, the United States Bankruptcy Code gives specific rights to trade creditors during the insolvency process by allowing them to stop deliveries and reclaim goods under State law.²⁹ But the Indian approach which uses the classification of “financial” and “operational” creditors is unique. This paper evaluates the Indian Government’s approach to protecting allottees by classifying them as financial creditors and the Supreme Court’s reasoning in *Pioneer* through three sections: Sections II-IV. Section II examines the working of insolvency law in India, the United States of America, and the United Kingdom, with a specific focus on the roles assigned to different types of creditors. The paper uses this context to explain the importance of a clear differentiation between financial and operational creditors to the working of India’s insolvency regime.

²⁵ The Supreme Court has interpreted Article 14 of the Indian Constitution to include the right against arbitrary treatment. See *Chiranjit Lal Choudhuri v. Union of India*, AIR 1951 SC 41, ¶ 86, 91; *E.P. Royappa v. State of Tamil Nadu*, AIR 1974 SC 555, ¶ 85; *Committee of Creditors of Essar Steel India Ltd. v. Satish Kumar Gupta* 2019 SCC OnLine SC 1478, ¶ 108.

²⁶ See *infra* section II.A. “Role of Financial and Operational Creditors in India.”

²⁷ *Pioneer Urban Land and Infrastructure Ltd.*, (2019) 8 SCC 416, ¶ 42.

²⁸ Anjali Sharma, *Jaypee: Consumer Angle in IBC Play*, THE HINDU (Sept. 17, 2017), www.thehindu.com/business/Industry/jaypee-consumer-angle-in-ibc-play/article19704254.ece; Sikha Bansal, *Home-buyers Provisions in IBC: Putting Square Pegs in Rounds Holes?*, VINOD KOTHARI CONSULTANTS (Aug. 11, 2019), vinodkothari.com/2019/08/home-buyers-provisions-in-ibc/; Abhilash Pillai & Tarun Agarwal, *Home Buyers = Financial Creditors: Supreme Court Reigns*, INDIA CORP. L. (Aug. 14, 2019), corporate.cyrilamarchandblogs.com/2019/08/home-buyers-equivalent-financial-creditors-supreme-court-rules/.

²⁹ 11 U.S.C. § 546(c) (2018). See Daniel A. Lowenthal, *Tough Choices Confront Trade Creditors When a Retailer Faces Bankruptcy*, MONDAQ (Oct. 09, 2014), <https://www.mondaq.com/unitedstates/InsolvencyBankruptcyRestructuring/345390/Tough-Choices-Confront-Trade-Creditors-When-A-Retailer-Faces-Bankruptcy>.

Section III looks at the 2018 Amendment in detail. It examines prior decisions of the adjudicating authority³⁰ under the IBC (“Adjudicating Authority”) to determine the most suitable classification of allottees’ debts (financial or operational) and uses this as a foundation to critically analyze the *Pioneer* case. Section IV of the paper highlights practical consequences of the 2018 Amendment which may not have been foreseen by the Government and the Supreme Court of India. Section IV also explains the alternatives that were available to the Indian Government based on the experiences of the US and the UK.

II. THE ROLE OF CREDITORS IN CORPORATE REORGANIZATIONS UNDER INSOLVENCY REGIMES

A. ROLE OF FINANCIAL AND OPERATIONAL CREDITORS IN INDIA

The objectives of the IBC are contained in its Preamble. While the main objective of the IBC is to rehabilitate the debtor,³¹ the scheme of the IBC reveals that the debtor’s rehabilitation is not prioritized as a benefit in and of itself. Even in the Preamble, the IBC is set up as a regime to maximize the value of distressed debtors’ assets for the benefit of all their stakeholders. The provisions of the IBC make it clear that it is the wisdom of the creditors (specifically, “financial creditors”) which will be deferred to when deciding whether a corporate debtor should be rehabilitated.³²

The IBC gives the Committee of Creditors (“CoC”), comprising the corporate debtor’s financial creditors, a period of 180 days (which can be extended by the Adjudicating Authority by a maximum of 90 days) to approve a resolution plan; this would require a 66 percent majority from the members of the CoC.³³ Each financial creditor’s vote is calculated based on their share in the total debt.³⁴ Once a resolution plan is approved by the CoC, the Adjudicating Authority has only limited grounds based on which it can reject the plan (such as the contravention of other laws or non-

³⁰ The National Company Law Tribunal (NCLT) is the Adjudicating Authority under the IBC. IBC, *supra* note 2, § 5(1). Appeals against decisions of the NCLT lie with the National Company Law Appellate Tribunal (NCLAT), and appeals against the NCLAT’s decisions lie with the Supreme Court of India. *See* Companies Act, 2013, No. 18, Acts of Parliament, 2013 (India), § 423.

³¹ *Swiss Ribbons v. Union of India*, (2019) 4 SCC 17, ¶ 27.

³² *Committee of Creditors of Essar Steel India Ltd. v. Satish Kumar Gupta*, (2019) SCC OnLine SC 1478, ¶ 33; *see* Report of the Insolvency Law Committee, *supra* note 20, ¶ 11.3.

³³ IBC, *supra* note 2, §30(4).

³⁴ *Id.* § 5(28).

payment of insolvency costs).³⁵ If the CoC does not approve a resolution plan within the prescribed time, then the corporate debtor goes into liquidation.

Section 7 of the IBC allows a financial creditor to trigger insolvency proceedings against the corporate debtor. Operational creditors can also trigger insolvency proceedings against the corporate debtor.³⁶ However, a corporate debtor has more defenses against operational creditors than financial creditors. For instance, operational creditors have to give the debtor an opportunity to pay them their dues.³⁷ Debtors can also effectively stop an operational creditor from triggering insolvency proceedings under the IBC if they show that the claim of the operational creditor is disputed.³⁸ The financial creditor, however, is neither obliged to give the debtor any opportunity to pay the due amount nor can their petition be rejected by the Adjudicating Authority because a dispute in respect of their claim exists.³⁹ So, whether the creditor is owed a financial debt or an operational debt significantly alters the relationship between the creditor and the debtor. It also affects the extent to which the creditor has a say in the debtor's future (through voting in the CoC). Evidently, financial creditors play a crucial and more decisive role than operational creditors in the mechanism of India's insolvency regime. The differences between these two classes of creditors is significant for the analysis that follows and will be discussed in greater detail in subsequent sections.

B. ROLE OF CREDITORS IN THE INSOLVENCY REGIMES OF THE US AND THE UK

This section studies the classification and role of creditors under the US and UK insolvency regimes. The US and UK insolvency regimes are considerably different from each other, and a nuanced examination of each of them is beyond the scope of this paper. The purpose of this section is limited to exploring the role assigned to creditors by the insolvency regimes in both jurisdictions during a corporate debtor's reorganization. Legislative developments in the US and the UK have often guided Indian law makers and jurists.⁴⁰ Given that these jurisdictions' insolvency

³⁵ *Id.* §§ 30–31.

³⁶ *Id.* § 9.

³⁷ *Id.* § 8.

³⁸ *Id.* § 8(2)(a) read with §9.

³⁹ *Innovative Industries Ltd. v. ICICI Bank & Anr.*, (2018) 1 SCC 407, ¶ 30.

⁴⁰ Gautam Sundaresh, *In Whose Interests Should a Company Run? Fiduciary Duties of Directors During Corporate Failure in India: Looking West for*

regimes also deal with consumer prepayments and deposits, it would be valuable to see how they have included consumer interests within their insolvency regimes. In India, the US, and the UK, liquidation priorities of creditors are based on whether their claims are secured or unsecured debts. Since the liquidation waterfall in all three jurisdictions is largely similar in this regard, this section will not explore it in detail.

1. Reorganization of Companies Under the US Bankruptcy Code

The US Bankruptcy Code is contained in Title 11 of the United States Code (“USC”)⁴¹ and was enacted by the Bankruptcy Reform Act, 1978.⁴² A company that is unable to meet its obligations may be reorganized under Chapter 11 or liquidated under Chapter 7 of Title 11. A petition for Chapter 11 reorganization can be filed by the company itself (in which case it is voluntary) or by three or more persons who have an aggregate claim against the company which is at least 10,000 USD (in which case it is involuntary).⁴³ “Claims” have been given a broad definition under Section 101(5) of Title 11. A claim is a right to payment or an equitable right to remedy for a breach of performance irrespective of whether it is secured or unsecured.⁴⁴ Unlike the case under the IBC, there is no distinction between the types of creditors who can initiate proceedings under Chapter 11 (and 7) of Title 11.

After initiating proceedings under Chapter 11, a plan needs to be presented and accepted by the creditors of the debtor.⁴⁵ The entire proceedings are supervised by the bankruptcy court which may appoint a trustee.⁴⁶ Anyone can submit a plan for reorganization including the creditors, trustee, and the debtor.⁴⁷ In order for any plan to come into effect, it must be approved by the creditors through the process of voting.⁴⁸ For the purpose of voting to accept a plan, Chapter 11 requires the classification of different types of creditors into separate groups. Section 1122(a) requires that all the creditors’ claims be divided into classes with other claims that are substantially

Answers, 8 MICH. BUS. & ENTREPRENEURIAL L. REV. 291, 297 (2019) (discussing India’s use of U.S. and U.K. jurisprudence for guidance in drafting statutes and resolving complex legal issues).

⁴¹ 11 U.S.C. §§ 101–1501 (2018).

⁴² *Id.*

⁴³ *Id.* §§ 301–303.

⁴⁴ *Id.* § 101(5).

⁴⁵ *Id.* §§ 1126, 1129.

⁴⁶ *Id.* § 1104.

⁴⁷ *Id.* § 1121.

⁴⁸ *Id.* § 1126.

similar.⁴⁹ The same section also allows for the classification of all unsecured claims below a certain amount (as approved by the court) as one class of claims for the purpose of administrative convenience.⁵⁰ Notably, while the US Bankruptcy Code (Title 11) requires the division of creditors' claims into different classes, it does not specify the characteristics of each class and has effectively allowed this to be decided on a case by case basis.⁵¹

Each of these classes of claims needs to approve the plan before a court can confirm it and make it binding upon all parties.⁵² A plan is approved by a class of claims if a majority of creditors representing two-thirds of the amount of debt within that class and one half of the number of claims in that class have voted in favor of the plan.⁵³ Creditors whose claims are being paid to the extent they have been allowed are deemed to have approved the plan.⁵⁴ Creditors who are not being paid to the full extent of their allowed claims are said to have impaired claims.⁵⁵ In the event that the plan has created impaired classes of claims (claims which are not paid in full), such classes of creditors also need to approve the plan.⁵⁶

Thus, the court *inter alia* needs the plan to be approved by all classes of creditors (through a two-thirds majority) and ensure that impaired creditors are not worse off than they would be in the event of a Chapter 7 liquidation; only then can a court confirm the plan.⁵⁷ However, the US Bankruptcy Code carves out certain instances which allow the court to confirm the plan without the approval of impaired classes of creditors.⁵⁸ These provisions are commonly referred to as "cramdown provisions."⁵⁹ The cramdown provisions cannot be used to bind creditors (secured or unsecured) to unfair and inequitable treatment under a plan.⁶⁰ There is a

⁴⁹ *Id.* § 1122(a).

⁵⁰ *Id.* § 1122(b).

⁵¹ Stefan A. Riesenfeld, *Classification of Claims and Interests in Chapter 11 and 13 Cases*, 75 CALIF. L. REV. 391, 393 (1987).

⁵² 11 U.S.C. § 1129 (2018).

⁵³ *Id.* § 1126(c)–(d).

⁵⁴ *Id.* § 1126(f).

⁵⁵ *Id.* § 1124.

⁵⁶ *Id.* §§ 1126–1129.

⁵⁷ *Id.* § 1129(a).

⁵⁸ *Id.* § 1129(b).

⁵⁹ *RadLAX Gateway Hotel, LLC v. Amalgamated Bank*, 132 S. Ct. 2065, 2069–70 (2012); Brian P. Hanley, *Preserving the Secured Creditor's Bargain in Chapter 11 Cramdown Scenarios*, 8 BROOK. J. CORP. FIN. & COM. L. 494 (2014).

⁶⁰ 11 U.S.C. § 1129(b); Richard F. Broude, *Cramdown and Chapter 11 of the Bankruptcy Code: The Settlement Imperative*, 39 BUS. LAW. 441, 451 (1984) (discussing how the requirements of fair and equitable treatment apply to treatment of the dissenting class of creditors and not to the plan as a whole).

continuing obligation to treat creditors in a fair and equitable manner and to prevent any unfair discrimination. Cramdown provisions ensure that secured creditors interests are protected in the event that they are a part of the class upon whom the plan is being forced. This is done by requiring that secured creditors either retain their security interest in the plan or are given an “indubitably” equivalent value in lieu of this.⁶¹

The use of cramdown provisions is contingent on at least one class of impaired creditors approving the plan under Section 1126 (c) of Title 11.⁶² Classification, thus, plays an important role in determining whether or not a plan is approved. Bankruptcy courts have the ability to set aside plans which have classifications only to manufacture a consenting impaired class of creditors.⁶³ Courts have likened the practice of classifying claims in such a manner to “gerrymandering” and have called these classifications “artificial”.⁶⁴ While decisions regarding classifications are made on a case by case basis, the need for placing claims with those that are substantially similar will prevent some types of claims from being combined. For instance, it is impermissible to classify secured and unsecured claims so that their owners vote as a part of the same class.⁶⁵ This is different from the scheme of the IBC which allows secured and unsecured creditors to vote as one class – financial creditors.

2. Reorganization Under the UK Insolvency Act

The UK Insolvency Act, 1986 as amended by the Enterprise Act, 2002, contains the insolvency machinery of the UK.⁶⁶ There are three procedures provided by the Insolvency Act for the rescue and reorganization of a financially distressed company, namely, receivership, administration, and company voluntary agreements.⁶⁷ Out of these, receivership is the least relevant after the Enterprise Act, since the process can now only be used in limited circumstances and by those whose floating charges were created prior to September

⁶¹ 11 U.S.C. §1129(b)(2)(A).

⁶² *Id.* §§1126(c), 1129(a)(10).

⁶³ Bruce A. Markell, *Clueless on Classification: Toward Removing Artificial Limits on Chapter 11 Claim Classification*, 11 BANKR. DEV. J. 1, 18 (1995) (discussing US courts’ reluctance to allow the artificial classifications of claims).

⁶⁴ *Id.* at 3 (discussing the relevance of classifications under §1122 of the US Bankruptcy Code).

⁶⁵ *Id.*

⁶⁶ Insolvency Act 1986, c. 45 (UK).

⁶⁷ VANESSA FINCH, *CORPORATE INSOLVENCY LAW – PERSPECTIVES AND PRINCIPLES* 328 (2d ed. 2009).

2003.⁶⁸ Floating charge holders who have a charge over all or substantially all of the company's property can appoint administrative receivers to take legal control of the company.⁶⁹ It is common for debenture instruments to give debenture holders the right to appoint receivers under certain circumstances, for instance, the company's failure to pay interest, presentation of a winding up petition, passing a resolution for voluntary liquidation, or failure to meet any other obligations set out in the debenture.⁷⁰

The administrative receiver's primary duty is to satisfy the debt of the appointer and the administrative receiver can dispose of the assets of the company in order to do so. The powers and duties of an administrative receiver, though broad, are far from settled. However, due to the reduced relevance of receivership and administrative receivers after the Enterprise Act,⁷¹ these issues will not be examined here.

The process of administration can be initiated by the directors of a company, its members, or its creditors.⁷² The provisions governing administration are contained under Schedule B1 of the Insolvency Act.⁷³ An application for the appointment of an administrator can be made (to the court) only by the company, its directors, one or more of its creditors, a designated officer for a magistrate's court, or a combination of these persons.⁷⁴ Floating charge holders not only have a right to appoint an administrator, but also have a right to intervene in applications to appoint administrators before the court. A court is required to grant the application of the intervening floating charge holder unless it believes that there is a justification to refuse the application in the specific circumstances of the case before it.⁷⁵ The right of a floating charge holder to appoint a receiver has effectively been converted into a right to appoint an administrator.

An administrator is required to perform their functions keeping in mind one of the three objectives: rescuing the company as a going concern, or achieving a better result for the company's creditors as a whole than they would have gotten if the company had been wound up without going through the process of administration, or realizing the property of the company in order to make a

⁶⁸ Enterprise Act 2002, c. 40, § 250 (UK); FINCH, *supra* note 67, at 328.

⁶⁹ FINCH, *supra* note 67, at 331.

⁷⁰ *Id.* at 332.

⁷¹ *Id.* at 327.

⁷² Insolvency Act 1986, c. 45, sch. B1, ¶12 (UK).

⁷³ *Id.* sch. B1.

⁷⁴ *Id.* ¶12.

⁷⁵ *Id.* ¶36.

distribution to one or more secured or preferential creditors.⁷⁶ In order to achieve these objectives, the administrator makes proposals which need to be approved by creditors, with or without modification. This is the rough equivalent of proposing reorganization plans under the IBC and the US Bankruptcy Code. For a proposal to bind the creditors of a company, it must be approved by a simple majority of them, calculated based on the value of the debt owed to them.⁷⁷ During the process of administration, officers of the company cannot exercise any powers which would interfere with the administrator's powers and functions.⁷⁸

All creditors who are entitled to vote can challenge the conduct of an administrator based on misfeasance or if they believe that the administrator has unfairly harmed their interests.⁷⁹ Decisions of the administrator are commercial in nature and the courts will normally refrain from interfering with these decisions unless it can be shown that there has been differential treatment of similarly placed creditors or if assets have been undervalued and sold to the detriment of the creditors as a whole.⁸⁰

Finally, an important means of reorganizing a financially distressed corporation is a Company Voluntary Arrangement ("CVA") which is covered by Sections 1-7 of the Insolvency Act.⁸¹ A CVA may be proposed by the director of a company to its creditors unless it is undergoing administration or being wound up, in which case the CVA may be proposed by the administrator or liquidator respectively.⁸² CVAs can be used to restructure the debt of the company; they are essentially a compromise between the company and its creditors. Unlike the proposals of an administrator, a proposal for a CVA needs to be reported to the court before it is considered by a company's creditors.⁸³ For a CVA to be approved by the company's creditors, it must be approved by a two-thirds majority

⁷⁶ *Id.* ¶3.

⁷⁷ The Insolvency (England and Wales) Rules 2016, No. 1024, rule 15.34 (requisite majorities for Administration proposals and CVAs).

⁷⁸ Insolvency Act 1986, c. 45, sch B1, ¶ 64.

⁷⁹ Insolvency Act 1986, c. 45, sch. B1, ¶75 (UK); FINCH, *supra* note 67, at 439.

⁸⁰ *Re Meem, Goel & Anr. v. Grant & Anr.*, [2017] EWHC 2688; Serena McAllister, *UK: High Court Refuses To Interfere With Administrators' Decision To Auction Causes of Action*, MONDAQ, (Feb. 5, 2018), <http://www.mondaq.com/uk/x/670586/Insolvency+Bankruptcy/High+Court+Refuses+To+Interfere+With+Administrators+Decision+To+Auction+Causes+Of+Action>.

⁸¹ Insolvency Act 1986, c. 45, § 1-7.

⁸² *Id.* § 1.

⁸³ *Id.* sch. B1, ¶ 80. See FINCH, *supra* note 67, at 489.

of the creditors (calculated based on the value of debt).⁸⁴ CVAs that affect the rights of secured creditors or alter the order of preference of creditors cannot be approved by the meeting of creditors except with the concurrence of the affected creditors (secured and preferential creditors).⁸⁵

An important distinction between the US and UK insolvency regimes from the perspective of reorganization is the organization of creditors before they vote. The US allows for the creation of classes of creditors for the calculation of their votes (on a case by case basis) and the UK allows all creditors to vote for proposals of administrators and CVAs. India falls somewhere in the middle of these two regimes. On the one hand, it allows secured and unsecured creditors to vote in the same class (something that would not meet the test under Section 1122 of the US Bankruptcy Code). On the other, it imposes a statutory restriction on the type of creditors who can vote on a reorganization plan, thus differing from the UK's approach that allows all creditors to vote in the creditor's meeting to the extent of the debt they own.

The rationale behind classifications of claims in the US is that there is some common interest shared by the creditors so classified.⁸⁶ This is why it is acceptable to dispense with a unanimous vote by allowing a majority of creditors to bind dissenting ones. The existence of a common interest thus becomes an important rationale for the classification of debts.⁸⁷ In the absence of classifying debts on the basis of common interest, one might simply opt for the model of the UK where all creditors vote on plans proportionate to the debt they own. The BLRC report and the IBC do not explicitly state the "common interest" of financial creditors as a justification for making them the only voting class in an insolvency resolution process, but there are some indications that this distinction was rooted in some common characteristics of these financial creditors. It would be fair to infer that the BLRC report attributed some commonality to creditors who are financial creditors in terms of their ability and suitability to decide on the future of a financially distressed firm. The Indian Supreme Court has attempted to build on these common characteristics and interests of financial creditors while differentiating them from operational creditors.

⁸⁴ The Insolvency (England and Wales) Rules 2016, No. 1024, rule 15.34 (requisite majorities for Administration proposals and CVAs).

⁸⁵ Insolvency Act 1986, c. 45, §§ 4(3), 4(4).

⁸⁶ Markell, *supra* note 63, at 12–13 (discussing the relevance of classifications under § 1122 of the US Bankruptcy Code).

⁸⁷ *Id.*

C. DIFFERENTIATING BETWEEN FINANCIAL AND OPERATIONAL CREDITORS: *SWISS RIBBONS V. UNION OF INDIA*

The differentiation between financial and operational creditors under the IBC is largely based on the underlying function of the transaction (operational creditors trace their claims to contracts for the provision of goods and services). While the IBC defines financial debt as having specific characteristics (consideration of time value for money, etc.),⁸⁸ the approach employed by Indian courts and tribunals to differentiate between financial and operational debts has heavily relied on the purpose or intention with which the debt was created.

The case of *Swiss Ribbons v. Union of India*,⁸⁹ which was decided shortly before the *Pioneer* case but after the 2018 Amendment, needs to be discussed when debating the characteristics of a financial creditor under the IBC. Though *Swiss Ribbons* was decided after the 2018 Amendment, it did not specifically address the subject of allottees as financial creditors, as this question was not being contested by the parties. In *Swiss Ribbons*, the differential treatment accorded to financial and operational creditors under the IBC was challenged on the grounds of being arbitrary. If found to be arbitrary, the differentiation would be in violation of Article 14 of the Indian Constitution which guarantees the right to equality and eschews arbitrariness.⁹⁰ Upholding the constitutional validity of the differentiation between operational and financial creditors, the Supreme Court used the case as an opportunity to articulate the differences between the two categories of creditors. Though the judgment largely dealt with the characteristics of financial creditors who were not individuals (such as banks) it did not excuse individual lenders from meeting the criteria the IBC sets out for being called a financial creditor.⁹¹ The only manner in which individual financial creditors differed from other financial creditors was that they would be represented by an insolvency professional because they tended to be numerous.⁹²

It is significant to note that when referring to individual financial creditors, the Indian Supreme Court referred to individuals such as debenture holders and deposit holders. In one instance, the

⁸⁸ IBC, *supra* note 2, § 5(8)(f).

⁸⁹ (2019) 4 SCC 17.

⁹⁰ *Id.* ¶ 38.

⁹¹ *Id.* ¶¶ 42, 49–51.

⁹² Insolvency and Bankruptcy Board of India (Insolvency Resolution for Corporate Persons) Regulations, 2016 IBB/2016-17/GN/REG004, Regulation 16A read with Regulation 12.

Court also referred to persons with home loans. However, the Court did not refer to allottees of real estate projects in its decision (except when directly quoting Section 5(8)(f)). Even when quoting parts of the ILC report that referenced individual financial creditors, which include apartment buyers, the Court emphasized deposit holders and debenture holders and did not refer to apartment buyers.⁹³ It is unclear why the Court chose to emphasize persons with home loans over other apartment buyers. As already mentioned, the Court may have refrained from delving into the issue of including all apartment buyers/allottees in the definition of “financial creditor” because it was not being contested in *Swiss Ribbons*. The issue before the Court in *Swiss Ribbons* was in relation to the general characteristics of financial and operational creditors, to which it spoke in unequivocal terms as explained below.

Swiss Ribbons identified characteristics of financial creditors that help maintain the distinction between them and operational creditors. Financial creditors tend to have fixed repayment schedules, making it easier to ascertain a default (which is a ground for triggering the insolvency resolution process under Section 7). Operational creditors’ claims are more likely to be disputed and require adjudication before it can be ascertained if a default has occurred.⁹⁴ For instance, the goods supplied by the operational creditor may be of substandard quality, in which case reduced payment would not necessarily amount to a default.⁹⁵ Financial creditors normally lend money on a term loan or for working capital that enables a company to set up and operate a business. Operational creditors normally only participate in the operation of a business and not its set-up. Another important characteristic of a financial creditor is that they are involved in assessing the long-term viability of a corporate debtor. Thus, they will be able to restructure their loans and enable the corporate debtor to remain a working business.⁹⁶ For all these reasons, the Supreme Court in *Swiss Ribbons* held that there exists a difference (“intelligible differentia”)⁹⁷ between financial and operational creditors, making the different treatment accorded to both classes constitutional under Article 14.

⁹³ *Swiss Ribbons*, (2019) 4 SCC 17, ¶¶ 27, 46.

⁹⁴ *Id.* ¶ 50.

⁹⁵ Sale of Goods Act, No. 3, Acts of Parliament, 1930 § 59 (India).

⁹⁶ *Swiss Ribbons*, (2019) 4 SCC 17, ¶¶ 27, 51.

⁹⁷ Intelligible differentia refers to an intelligible distinction between a group of persons/things included within a classification and those excluded from it. This standard allows classification for the purpose of legislation but requires that it is not done on an arbitrary basis. See *State of West Bengal v. Anwar Ali Sarkar*, (1952) SCR 284, ¶ 55; *Navtej Singh Johar & Ors. v. Union of India*, (2018) 10 SCC 1, ¶¶ 256, 408.

This common purpose of financial credit as identified in *Swiss Ribbon* might be the Indian substitute to a “common interest” as the basis for classifying debt. However, because this class has been statutorily prescribed in India, its constituents cannot be easily altered (as under Chapter 11 of the US Bankruptcy Code). The statutory enumeration of the characteristics of financial and operational debts in the IBC makes it difficult to accommodate new types of debt that have different characteristics. The ambiguity in deciding the position of prepaying consumers (specifically, allottees) can be attributed to this prescription – the purpose of these prepayments did not clearly fit within those described by the IBC. The next part examines the definition of financial debt and financial creditors in detail and explains why allottees do not conceptually fit within this framework both before and after the 2018 Amendment.

III. ALLOTTEES UNDER THE INSOLVENCY AND BANKRUPTCY CODE BEFORE THE 2018 AMENDMENT

This section examines the treatment of allottees under the IBC as it has evolved through the decisions of the IBC’s Adjudicating Authorities and the Indian Supreme Court. The National Company Law Tribunal (“NCLT”) is the designated Adjudicating Authority concerning corporate debtors under the IBC.⁹⁸ Appeals from the NCLT lie with the National Company Law Appellate Tribunal (NCLAT), and appeals from the NCLAT lie with the Apex Court of the India, i.e., the Supreme Court.⁹⁹ This section also explains how the decisions of the NCLT/NCLAT (collectively referred to as the “company law tribunals”) and the Supreme Court influenced the ILC report and whether the ILC’s understanding of these decisions was correct.

A. TREATMENT OF ALLOTTEES BY THE SUPREME COURT AND COMPANY LAW TRIBUNALS

While the 2018 Amendment specifically identified “allottees” to be financial creditors, the genesis of this concern for all allottees can largely be attributed to the treatment of a specific type of allottee – the apartment buyer. Apartment buyers who approached the Supreme Court and the NCLT in the past seeking initiation of insolvency proceedings against real-estate developers had a common grievance – developers were delaying the completion

⁹⁸ IBC, *supra* note 2, § 5(1).

⁹⁹ Companies Act, 2013, No. 18, Acts of Parliament, 2013 (India), § 423.

of construction despite apartment buyers having paid their installments on time.

For instance, the Supreme Court had dealt with the question of protecting apartment buyers' interests under the IBC prior to the 2018 Amendment in the case of *Bikram Chatterji v. Union of India*.¹⁰⁰ In that case, real estate developers had created charges on all the land and buildings of the project in order to raise finances, leaving nothing for apartment buyers in the event of a liquidation. To protect the interests of the apartment buyers, the Supreme Court ordered that the flats of the apartment buyers could not be sold to pay the banks/authorities, and that other projects of the group would have to be sold in order to realize these sums.

1. Apartment Buyers as Operational Creditors

In two recent cases before the company law tribunals, apartment buyers contended that they were operational creditors.¹⁰¹ Both these cases had petitioners who obtained orders from the State Consumer Disputes Resolution Commission (“SCDRC”) directing the real estate developer to pay compensation for delayed construction. SCDRCs or “State Commissions” were established under the Consumer Protection Act, 1986, and they function as adjudicatory fora for complaints under the Consumer Protection Act.¹⁰² The Consumer Protection Act, 1986 has since been replaced by the Consumer Protection Act, 2019 under which SCDRCs continue to retain their functions but with an enhanced pecuniary jurisdiction between INR 10,000,000 – 100,000,000.¹⁰³

The petitions in the two cases being discussed were filed under Section 9 of the IBC¹⁰⁴ when the real estate developer did not pay the compensation as directed by the respective orders of the SCDRC. Thus, the basis on which the petitioners were considered operational creditors were amounts due under the orders of the SCDRC, and not the initial amounts paid to the real estate developer. These cases were eventually settled between the parties and there was no need for a detailed order by the NCLT. The NCLT did not explain why it considered unpaid compensation (as ordered by

¹⁰⁰ (2019) SCC OnLine SC 901.

¹⁰¹ See, e.g., *Kadiri Narasimha Reddy v. Aliens Developers*, (2017) SCC OnLine NCLT 11673; *Shakeel Ahmed v. Aliens Developers*, (2017) SCC OnLine NCLT 11679.

¹⁰² Consumer Protection Act, No. 68, Acts of Parliament, 1986 (India), § 9.

¹⁰³ Consumer Protection Act, No. 35, Acts of Parliament, 2019 (India), § 47.

¹⁰⁴ IBC, *supra* note 2, § 9.

SCDRCs) to be operational debt. It simply referred to the petitioners in these cases as operational creditors.¹⁰⁵

In cases where the apartment buyers approached the NCLT claiming that they were “operational creditors” based on the advances they had made to real-estate developers, the NCLT had rejected the petitions, stating that apartment buyers were not operational creditors under the IBC.¹⁰⁶ The NCLT reasoned that “operational creditors” were those who supplied goods or services and needed to receive payments for the same.¹⁰⁷ Apartment buyers did not supply any good or service.¹⁰⁸ The NCLT held that their grievance was related to the delayed delivery of the possession of a property and hence they could not be considered as operational creditors under the IBC.¹⁰⁹

On the specific question of whether receivers of goods and services can be considered operational creditors, the NCLAT, in *Overseas Infrastructure Alliance (India) Pvt. Ltd. v. Kay Bouvet Engineering Ltd.*¹¹⁰ answered in the affirmative. The NCLAT held that receivers of good and services who have made advance payments can be considered operational creditors. In *Overseas Infrastructure*, the appellant was awarded a contract to construct a sugar plant in Sudan. The entire project was to be financed by the Government of India through a line of credit from the Indian Export-Import Bank. The appellant engaged the services of the respondent as a sub-contractor to construct the sugar plant. Accordingly, a tripartite agreement was entered into by all the parties. The appellant made an advance payment to the respondent for the construction of the plant, however, when the Export-Import Bank did not release the second tranche of payment the tripartite agreement came to an end. When the respondent refused to refund the sums advanced by the appellant, the appellant approached the NCLT to trigger insolvency proceedings against the respondent as its operational creditor.

The NCLT dismissed the application by citing the existence of a dispute (thus barring an operational creditor from triggering the

¹⁰⁵ *Kadiri Narasimha Reddy*, (2017) SCC OnLine NCLT 11673, ¶ 2; *Shakeel Ahmed*, (2017) SCC OnLine NCLT 11679, ¶ 2.

¹⁰⁶ *Col. Vinod Awasthy v. AMR Infrastructures Ltd.*, (2017) C.P. No. (IB)-10(PB)/2017, [http://164.100.158.181/Publication/Principal_Bench/2017/Others/Col.%20Vinod%20Awasthy%20\(Final\).pdf](http://164.100.158.181/Publication/Principal_Bench/2017/Others/Col.%20Vinod%20Awasthy%20(Final).pdf); *Pawan Dubey & Anr. v. J.B.K. Developers & Pvt. Ltd.*, (2017) SCC OnLine NCLT 520.

¹⁰⁷ *Col. Vinod Awasthy*, (2017) C.P. No. (IB)-10(PB)/2017, ¶ 8; *Pawan Dubey & Anr.*, (2017) SCC OnLine NCLT 520, ¶ 6.

¹⁰⁸ *Col. Vinod Awasthy*, (2017) C.P. No. (IB)-10(PB)/2017, ¶ 8.

¹⁰⁹ *Id. See Pawan Dubey & Anr.*, (2017) SCC OnLine NCLT 520, ¶ 6.

¹¹⁰ (2018) SCC OnLine NCLAT 873.

IBC).¹¹¹ The NCLAT found that there was no dispute regarding the operational debt.¹¹² It held that the definition of “operational debt” could be interpreted to cover instances where the goods/services have been provided by the debtor as well. While the situation in *Overseas Infrastructure* is analogous to that of apartment buyers (who also pay for the service of construction), the NCLAT reached different conclusions in *Overseas Infrastructure* and the apartment buyers cases decided by the NCLT and NCLAT.¹¹³ When considering the case of apartment buyers, the NCLT and NCLAT had rejected arguments which stated that apartment buyers were operational creditors. In the apartment buyers cases, the company law tribunals explained that operational creditors are only those who provide goods or services (such as employment) to the corporate debtor.¹¹⁴ These decisions have also held that simply because someone is not a financial creditor, they would not automatically fall under the category of operational creditors.¹¹⁵

However, the decision of the NCLAT in *Overseas Infrastructure* came after the NCLAT pronouncements which stated that apartment buyers are not operational creditors. Significantly, there is nothing to distinguish apartment buyers from the type of operational creditor described in *Overseas Infrastructure*. The NCLAT’s decision in *Overseas Infrastructure* appears to overlook the precedents set by its previous decisions which refused to classify apartment buyers as operational creditors. This is significant given that in both cases, money was advanced for a construction project. But the debt was classified as operational only in *Overseas Infrastructure*.

2. “Financial Creditor” and “Time Value For Money” as Understood by the Company Law Tribunals Before the 2018 Amendment

Prior to the 2018 Amendment, the NCLT and NCLAT had decided that apartment buyers/allottees were financial creditors under the IBC only under specific circumstances. The NCLAT

¹¹¹ IBC, *supra* note 2, § 9.

¹¹² *Overseas Infrastructure (India) Pvt. Ltd. v. Kay Bouwet Engineering*, (2018) SCC OnLine NCLAT 873, ¶ 15.

¹¹³ Col. Vinod Awasthy, (2017) C.P. No. (IB)-10(PB)/2017; *Nikhil Mehta & Sons (HUF) v. AMR Infrastructures Limited*, (2017) SCC OnLine NCLT 219; *Nikhil Mehta & Sons (HUF) v. AMR Infrastructures Limited*, (2017) SCC OnLine NCLAT 377; *Pawan Dubey & Anr.*, (2017) SCC OnLine NCLT 520.

¹¹⁴ *Pawan Dubey & Anr.*, (2017) SCC OnLine NCLT 520, ¶¶ 6–7.

¹¹⁵ *Id.* at ¶ 6. See *Col. Vinod Awasthy*, (2017) C.P. No. (IB)-10(PB)/2017, ¶ 8.

decision in *Nikhil Mehta & Sons v. AMR Infrastructures Ltd.*¹¹⁶ is significant because it was the first to case to recognize apartment buyers as financial creditors and allow them to trigger the IBC against the corporate debtor (real estate developer). The NCLAT reached this decision by reversing an NCLT decision on appeal.¹¹⁷

The facts of *Nikhil Mehta* were that a real estate developer (AMR Infrastructure) entered into a contract with the applicants to construct residential and commercial units for them. As a part of this contract, the applicants would pay most of the consideration in advance to AMR Infrastructures (respondent). The contract also stipulated that the respondent would pay the applicants committed returns until the possession of the apartments were handed over to them. For some time after entering into the contract, the respondent had been paying the committed returns erratically. When the payment of these committed returns (or “assured returns” as it has been called) stopped entirely, the applicants filed an application under Section 7 (default in payments towards *financial creditors*) against the respondent.

The NCLT began its inquiry into the issue of apartment buyers under the IBC from the definition of “financial debt.” While Section 5(8) of the IBC is an inclusive sub-section, it qualifies the types of transactions which may be included within it. This qualification is categorical and not inclusive; Section 5(8) states that a financial debt *means* any sum of money disbursed for the “consideration for time value of money.”¹¹⁸ This means that notwithstanding the inclusive nature of the definition, the IBC requires disbursements to be made against the consideration of “time value of money” in order they qualify as financial debts.¹¹⁹

The NCLT decision noted that the requirement of consideration for time value for money was unique to Indian law. The UK Insolvency Act of 1986 and rules, for example, do not contain such a requirement in their definition of a debt. The NCLT referenced Black’s Law Dictionary’s definition of “time value,” which is “price associated with the length of time that an investor must wait before an investment matures or the related income is earned.”¹²⁰ NCLT’s rationale was that money earned in the future is discounted, thus the investor/lender is being compensated for parting with money and deferring its use to some later point (when it is paid

¹¹⁶ (2017) SCC OnLine NCLAT 377.

¹¹⁷ *Id.*; *Nikhil Mehta & Sons (HUF)*, (2017) SCC OnLine NCLT 219.

¹¹⁸ *Nikhil Mehta & Sons (HUF)*, (2017) SCC OnLine NCLT 219.

¹¹⁹ *Id.* ¶12. See also *Pioneer Urban Land and Infrastructure Ltd.*, (2019) 8 SCC 416, ¶ 71.

¹²⁰ *Nikhil Mehta & Sons (HUF)*, (2017) SCC OnLine NCLT 219, ¶ 12 (citing Time Value Definition, *Black’s Law Dictionary* (9th ed. 2009), available at Westlaw).

back or when it matures). This can also be understood as a compensation for the opportunity cost incurred by the investor/lender. From this analysis of the NCLT decision, it appears that the consideration for time value of money would flow from the debtor to the creditor (in the context of the real estate sector this would mean that it would flow from the developer to the financial creditor) since “financial debt” is defined as a disbursement against the consideration for the time value of money.¹²¹ Accordingly, the consideration can be most reasonably interpreted to flow from the person to whom the money is disbursed (debtor) to the person who is disbursing the money (financial creditor).

Given the importance of “consideration for time value of money” to the definition of financial debt, the NCLT made attempts to identify such a consideration in the transaction between the apartment buyers and the real estate developer. The NCLT noted that not all cases have a very clear relationship demarcating what the consideration for the money disbursed is and how it is paid. Such instances can arise under Section 5(8)(f) of the IBC which includes amounts raised under other transactions (such as forward sale agreements) having the effect of a commercial borrowing. This clause recognizes that money can be raised using various means including sales, and simply because a transaction is structured as an agreement of sale, it does not mean that it cannot be commercial borrowing.¹²² However, not all money raised through a “forward sale agreement”¹²³ can be considered a financial debt. Even these agreements must have some “consideration for the time value of money” as it is mandated by the definition for financial debt under Section 5(8) of the IBC. The requirement that financial debts have “consideration for time value of money” has not been questioned by any court, however, what comprises such consideration has been subject to varied interpretations.¹²⁴ To summarize, the NCLT held that a simple agreement to sell something would not comprise a “financial debt” even if a payment for this has been made in advance. The NCLT decision in *Nikhil Mehta* completely ruled out the possibility of calling apartment buyers/allottees who have made advances towards real-estate developers “financial creditors” in the absence of a committed returns scheme.

The NCLT then considered whether the existence of a committed returns scheme would change the nature of the transaction between the allottee and real estate developer from a

¹²¹ IBC, *supra* note 2, § 5(8).

¹²² *Id.* § 5(8)(f).

¹²³ *Id.*; see Report of the Insolvency Law Committee, *supra* note 20, ¶ 1.6.

¹²⁴ See *infra* section III.B. “The Pioneer Case.”

simple agreement to sell to one creating a financial debt. The NCLT noted that though there was money flowing from the real-estate developer (alleged corporate debtor) to the allottees (alleged financial creditor), the purpose of these committed returns was connected to the delivery of property.¹²⁵ There was no indication that the committed returns were calculated to serve as a consideration for the time value of money.¹²⁶ Thus, the NCLT held that applicants were not “financial creditors” capable of triggering the IBC through Section 7.

The applicants appealed against the NCLT’s decision before the NCLAT. The NCLAT agreed with the NCLT’s characterization regarding what comprised a financial debt under Section 5(8)(f) – that there must be a consideration for time value of money.¹²⁷ However, the NCLAT disagreed with the NCLT’s application of the definition of “financial debt” to the present case. The NCLAT held that committed returns were a consideration for time value of money as these payments were being made until possession was handed over to the applicants.¹²⁸ However, this line of reasoning of the NCLAT does little to clarify why committed returns could be “consideration for the time value of money.”

To supplement its reasoning, the NCLAT made note of various other characteristics of “committed returns.” The NCLAT pointed out that the applicants did not have to do anything other than make advance payments for the apartments in order to receive committed returns.¹²⁹ This supported the argument that the payment of committed returns was consideration for the applicants’ disbursement of money as advance payments. The committed returns scheme allowed the respondent to raise finances without having to provide any collateral, thus making a case for the scheme of committed returns being a tool to raise money (which would bring it within the definition under Section 5(8)(f)). The NCLT followed this precedent when adjudicating cases where transactions between real estate developers and apartment buyers involved the payment of committed returns.¹³⁰

There were two additional facts which were brought out in the appeal before the NCLAT by the appellants in *Nikhil Mehta*.

¹²⁵ *Nikhil Mehta & Sons (HUF)*, (2017) SCC OnLine NCLT 219, ¶ 13.

¹²⁶ *Id.*

¹²⁷ *Nikhil Mehta & Sons (HUF)*, (2017) SCC OnLine NCLAT 377, ¶ 24.

¹²⁸ *Id.* ¶ 25.

¹²⁹ *Id.* ¶ 7.

¹³⁰ *See, e.g., Anubhuti Aggarwal v. DPL Builders Pvt. Ltd.*, (2017) SCC Online NCLT 12672, ¶¶ 8–9; *Neelam Singh v. Megasoft Infrastructure*, (2017) SCC Online NCLT 10612, ¶¶ 5, 15, 16; *Pawan Dubey*, (2018) SCC Online NCLT 794, ¶¶ 23, 26, 29.

First, the committed returns payable to the applicants were put under the heading of “financial costs” in the accounts of the respondent (the real estate developer). Second, a reference was made to a decision of the Securities and Exchange Board of India (“SEBI”) which stated that in cases where real-estate developers offer committed returns, the transaction would satisfy the ingredients of a “collective investment scheme.”¹³¹ All of these factors contributed to the NCLAT holding that while the transaction between allottees and developers was one to construct and sell property, it also had aspects of a commercial borrowing because of the way in which it was designed.

The key takeaway from the discussions in this section is that neither the Supreme Court nor the NCLT/NCLAT concluded that the definition of “financial creditor” under the IBC extended to allottees (except in limited cases as mentioned above). While the ILC based its recommendations on the company law tribunals’ decisions relating to apartment buyers such as *Nikhil Mehta*,¹³² it reaches a different conclusion on the issue. The next section will examine the ILC report and its reasons for recommending that all allottees be made financial creditors under the IBC.

3. *The Insolvency Law Committee Report*

The Insolvency Law Committee was set up by the Ministry of Corporate Affairs (Government of India) to conduct a thorough review of the IBC and help India improve its “World Bank Doing Business” ranking.¹³³ The ILC report was cognizant of the manner in which the company law tribunals and Supreme Court had dealt with claims of apartment buyers against real estate developers under the insolvency regime for delayed construction and defaults in payments of committed returns.¹³⁴ They saw the prevailing situation as one of confusion which required the legislature to clarify the position of home-buyers/allottees under the IBC. In this context, the ILC recommended that the amounts raised under the real estate project from allottees be considered under entry (f) of Section 5(8) of the IBC, thus categorizing them as financial creditors.¹³⁵

¹³¹ In the Matter of MVL Limited, Order dated December 19, 2014 (Securities and Exchange Board of India), at 20, https://www.sebi.gov.in/sebi_data/attachdocs/1418979855194.pdf.

¹³² Report of the Insolvency Law Committee, *supra* note 20, ¶¶ 1.2, 1.6–1.7, 1.9

¹³³ *Id.* at 4.

¹³⁴ *Id.* ¶ 1.7.

¹³⁵ Report of the Insolvency Law Committee, *supra* note 20, ¶ 1.6.

The ILC report articulated two reasons to substantiate its recommendation. They first dealt with the legal appropriateness of including apartment buyers in the definition of “financial creditor” under the IBC.¹³⁶ A financial creditor is defined under the IBC as any person to whom a financial debt is due under Section 5(8) of the IBC.¹³⁷ Section 5(8) states that a financial debt is any debt “along with interest, if any, which is disbursed against the consideration for the time value of money,” the sub-section then lists types of transactions which would be considered as financial debts. The ILC recommended that Section 5(8)(f) be amended to include allottees within its ambit.¹³⁸ The ILC thought that this would be appropriate given that the definition of “financial debt” is an inclusive one. Further, Section 5(8)(f) already states that forward sale or purchase agreements which have the commercial effect of a borrowing can create financial debts. Payments made by allottees often finance large parts of real estate projects. These payments are essentially tools of raising finance as the payments directly contribute to constructing the apartment.¹³⁹ Thus, the ILC opined that allottees were analogous to financial creditors under Section 5(8)(f).

The second reason identified by the ILC for making allottees financial creditors under the IBC was a pragmatic one. The ILC was conscious of how allottees were often victims of a callous real estate sector which often delayed projects for years.¹⁴⁰ Thus, there was a need to safeguard the interests of allottees and to secure and clarify their position in the event of a liquidation under Section 53 of the IBC.¹⁴¹ In 2016, two years before the 2018 Amendment, the Insolvency and Bankruptcy Board of India (“IBBI”) amended the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 to introduce the term “other creditors.”¹⁴² Per these regulations, allottees were neither operational nor financial creditors; consequently, they ranked below both these types of creditors in the event of a liquidation. The IBBI clarified that allottees (the clarification specifically referred to apartment buyers)

¹³⁶ IBC, *supra* note 2, § 5(8)(f).

¹³⁷ *Id.* § 5(8).

¹³⁸ Report of the Insolvency Law Committee, *supra* note 20, ¶ 1.9.

¹³⁹ *Id.* ¶ 1.6.

¹⁴⁰ *Id.* ¶¶ 1.3, 1.7.

¹⁴¹ IBC, *supra* note 2, § 53; Report of the Insolvency Law Committee, *supra* note 20, ¶ 1.9.

¹⁴² Notification No. IBBI/2017-18/ GN/ REG013 (Aug. 16, 2017), Insolvency and Bankruptcy Board of India.

were not on par with financial and operational creditors through a press note dated August 18, 2017.¹⁴³

To summarize, the NCLT and the NCLAT agreed that an advance payment to a real estate developer for the construction and sale of a house would not fall within the definition of “financial debt.”¹⁴⁴ Both the NCLT and the NCLAT were looking for the “consideration for time value of money” (which was missing in ordinary advance payments made by allottees) before categorizing allottees as financial creditors. Even in the NCLAT’s decision in the case of *Nikhil Mehta*, the existence of committed returns was crucial in determining the nature of the transaction.¹⁴⁵ This aspect of the NCLAT’s decision is significant as it shows a conceptual boundary to categorizing transactions as financial debts (the existence of consideration for the time value of money). In light of the company law tribunals’ analysis, neither the ILC’s report nor the 2018 Amendment seem to provide an adequate conceptual justification for expanding the definition of financial creditors to *all* allottees notwithstanding the existence of committed returns schemes. The ILC report does not explain why a payment advanced by an apartment buyer (when there is no committed returns scheme in place) would satisfy the condition of being disbursed in consideration for “time value of money” as explained in *Nikhil Mehta*. The approach of the NCLT and NCLAT to classifying allottees as financial creditors only in specific situations appears to be more deliberate and consistent with the text of the IBC. The next section of the paper will examine the Indian Supreme Court’s decision *Pioneer* and evaluate whether it was able to identify a conceptual justification for the 2018 Amendment.

B. THE *PIONEER* CASE

As soon as the 2018 Amendment came into force, several real estate developers challenged the constitutional validity of the amendment before the Supreme Court.¹⁴⁶ The challenge was

¹⁴³ Insolvency and Bankruptcy Board of India, *Regarding News Item – Insolvency Regulator Empowers Property Buyers, Puts Them on Par with Financial Creditors*, INSOLVENCY AND BANKRUPTCY BOARD OF INDIA (Aug. 18, 2017), <http://www.ibbi.gov.in/media/press-releases?page=5>.

¹⁴⁴ *Nikhil Mehta & Sons (HUF)*, (2017) SCC OnLine NCLT 219; *Nikhil Mehta & Sons (HUF)*, (2017) SCC OnLine NCLAT 377.

¹⁴⁵ *Nikhil Mehta & Sons (HUF)*, (2017) SCC OnLine NCLAT 377; see *Anubhuti Agarwal v. DPL Builders Pvt. Ltd.*, (2017) SCC OnLine NCLT 12672, ¶¶ 8, 10.

¹⁴⁶ These challenges were filed through writ petitions under Article 32 of the Constitution of India. The Supreme Court has original jurisdiction over writ

launched on a number of grounds, of which two important ones were the arbitrary discrimination against real-estate developers (thus violating article 14 of the Constitution),¹⁴⁷ and the effect the 2018 Amendment had on eroding the distinction between financial and operational creditors. The petitioners also urged that allottees already had a sector-specific remedy under the RERA, which provides a mechanism for adjudicating disputes between the developer and allottees. There were also arguments made about how allottees could blackmail real estate developers by threatening to trigger the IBC and force developers to divert funds from other projects to benefit the allottees.¹⁴⁸ However, such problems are not unique to the present case. Even financial creditors who easily fit within the definition under section 5(8) can misuse insolvency proceedings to blackmail corporate debtors. This warrants a more general discussion for making the insolvency regime more alert to misuse, which is outside the scope of this paper. Accordingly, the rest of this section considers and contends with the legal concepts in the *Pioneer* judgment which were used by the court to decide on the inclusion of apartment buyers under Section 5(8)(f).

1. Discrimination Between Real-Estate Developers and Other Operational Debtors

In *Pioneer*, the petitioners argued that real-estate developers were closer to the class of “operational creditors” under the IBC than they were to financial creditors.¹⁴⁹ By treating allottees as financial creditors *vis-à-vis* real estate developers (and treating developers as financial debtors), the petitioners claimed that the 2018 Amendment violated Article 14 of the Constitution.¹⁵⁰ It was argued that real estate developers were operational debtors and that the amendment treated real estate developers differently from other members of their class. The petitioners urged that the classification of real estate developers as operational debtors was under-inclusive as it excluded other similarly placed operational debtors.

The Supreme Court responded to the argument on classifications by referring to the latitude which is normally allowed to the legislature when deciding the constitutional validity of economic legislations. In doing so, it referred to previous Supreme

petitions filed under Article 32 of the Constitution. See *Pioneer Urban Land and Infrastructure Ltd.*, (2019) 8 SCC 416, ¶ 1.

¹⁴⁷ *Id.* ¶¶ 5–6.

¹⁴⁸ *Id.* ¶ 5.

¹⁴⁹ *Id.* ¶¶ 5, 11.

¹⁵⁰ *Id.* ¶ 33.

Court judgments which held that an economic legislation does not violate Article 14 only because it does not contain or make a perfect classification while giving effect to a policy.¹⁵¹ Given that economic problems can be complex and require equally complex solutions, the legislature must be allowed to solve these problems through economic experimentation.¹⁵² Economic legislation might affect only one person or a specific class of persons and there may also be situations in which economic legislations affect some members of a class more harshly than others.¹⁵³ However, if a classification is made to promote a general public interest and the legislature can cite special circumstances which set some members of a class apart from others, then a legislation cannot be struck down as unconstitutional simply because it suffers from under-inclusion.¹⁵⁴ In the case of real estate developers, the special circumstances were the delays and mismanagement plaguing the real estate sector, which had resulted in the frustration of large investments made by allottees.¹⁵⁵ In addition to citing the latitude normally accorded to economic legislation, the Supreme Court also distinguished real estate developers from other operational debtors. This was done as a response to the petitioner's contention that the 2018 Amendment led to the creation of a class which was under-inclusive. If it is shown that apartment buyers were different from other operational creditors, this would satisfy the requirement of "intelligible differentia" under Article 14.¹⁵⁶ The 2018 Amendment would not be arbitrary for its exclusion of other operational creditors if substantial differences between them and apartment buyers are established.

2. Blurring the Distinction Between Financial and Operational Creditors

By examining the difference between real estate developers and *other* operational debtors, the Court has implicitly stated that real estate developers fall within the class of operational debtors but deserve differential treatment because of how they differ from other members of this class. This sets a precedent according to which operational debtors can be classified as financial debtors because

¹⁵¹ *Id.* ¶¶ 36–40. See *Ram Krishna Dalmia v. S.R. Tendolkar*, (1959) SCR 279; *State of Gujarat v. Shri Ambica Mills Ltd.*, (1974) 4 SCC 656; *Swiss Ribbons*, (2019) 4 SCC 17.

¹⁵² *Pioneer Urban Land and Infrastructure Ltd.*, (2019) 8 SCC 416, ¶ 36.

¹⁵³ *Id.* ¶ 39.

¹⁵⁴ *Id.* ¶ 36.

¹⁵⁵ *Id.* ¶¶ 39–40.

¹⁵⁶ *Id.* ¶¶ 5, 42.

they differ from other operational debtors, and not necessarily because they fit into the category of financial debtors.

The Court identified three unique characteristics of real estate developers (identified below) which warranted their status as a financial debtor. But these characteristics are not as unique to real estate developers as the Court was led to believe. Hence, their use as a distinguishing feature blurs the line between operational and financial creditors. We argue that the inclusion of real estate developers within the term “financial debtors” based on the characteristics identified by the court effectively broadens the scope of the definition of financial debtors.

The first distinguishing characteristic identified by the Court related to the nature of the transaction between real-estate developers and apartment buyers.¹⁵⁷ In most cases, consideration for goods and services flows (or ought to flow) from an operational debtor to an operational creditor.¹⁵⁸ Thus, if an entity supplies goods or services to a company, it becomes the operational creditor of that company. The relationship is reversed in the case of allottees and real estate developers, allottees are the ones who pay for the service (construction of an apartment) rendered by the real estate developer.¹⁵⁹

This reasoning seems unpersuasive because it ignores other instances wherein the supplier of goods and services may be considered a corporate debtor. The Supreme Court stated that other projects for which advance payments were made such as “turnkey projects” and “capital goods” would not be analogous to real estate projects because the advance payments were made for the purpose of specific customization required by the buyer.¹⁶⁰ While this might be true, it would be hard to defend that there are no projects which are financed partly or entirely by the buyers (as noted by the Court, apartment buyers finance between 50 percent – 100 percent of the real estate projects).¹⁶¹ The transaction in the case of *Overseas Infrastructure* shows that there are other transactions which are analogous to those between real-estate developers and allottees, for instance, projects for building equipment (customized or otherwise) and home-improvement projects. The Court also stated that such “turnkey projects” lacked the essential ingredient of “consideration for time value of money” which was required in a financial debt.¹⁶²

¹⁵⁷ *Id.* ¶ 42.

¹⁵⁸ *Id.*

¹⁵⁹ *Id.*

¹⁶⁰ *Id.*

¹⁶¹ *Id.* ¶ 61.

¹⁶² *Id.* ¶ 42.

The consideration for time value of money was the second distinguishing characteristic identified by the Court.¹⁶³ The respondents argued that “time value of money” was present in the transaction between real estate developer and the allottees.¹⁶⁴ It was present for the allottees because they gained the benefit of acquiring an apartment at a cheaper price than they would have had to pay once it was already constructed.¹⁶⁵ Thus, the respondents argued that the allottees gained the “time value of money” by saving money because of their early investment in the apartment. Time value of money was also present for the real estate developers as they received money for the construction of the apartment with every investment that was paid.¹⁶⁶ The Court agreed with this reasoning and reiterated the respondent’s arguments to conclude that there was a “consideration for the time value of money” in the transaction between allottees and real estate developers.¹⁶⁷ A charitable reading of this part of the Court’s judgment would suggest that the allottees gain the difference between the price they would have had to pay for an already constructed apartment and the total price paid through instalments to construct the apartment.¹⁶⁸ This difference is the time value of money gained by the allottees.

Such a construction of “consideration for time value of money” does not sit well with how the term has been defined by the orders of the company law tribunals, including the ones cited by the Supreme Court in its decision.¹⁶⁹ As explained above, time value of money refers to the price associated with having to defer the spending of that money to a later time. Examples of this include waiting for an investment to mature or for a loan to be paid back. However, in the case of real estate developers, the use of the money itself is to purchase the apartment. Thus, there is no deferment of enjoyment of that money, or in being able to use it. No opportunity cost is incurred by the allottee as they are not waiting for the money to be returned. Time value of money cannot be characterized as the ability to save money on an investment or transaction. By this logic, a company which pays to have its tools/machinery manufactured rather than buy them once they are put up for sale would also be gaining the time value of money. Even the NCLAT decision in *Nikhil Mehta* differentiated forward sale agreements and advance

¹⁶³ *Pioneer Urban Land and Infrastructure Ltd.*, (2019) 8 SCC 416, ¶ 42.

¹⁶⁴ *Id.* ¶ 12.

¹⁶⁵ *Id.*

¹⁶⁶ *Id.*

¹⁶⁷ *Id.* ¶ 40.

¹⁶⁸ *Id.*

¹⁶⁹ *Id.* ¶¶ 70–71.

payments from transactions which created a financial debt.¹⁷⁰ They required an additional element which made the sale a mere tool to raise finance, and identified the “committed returns” as meeting this requirement.¹⁷¹ However, the *Pioneer* case and the 2018 Amendment deem all allottees as financial creditors irrespective of the existence of “committed returns.”¹⁷² Thus, the analysis of the NCLT and NCLAT on the existence of “consideration for time value of money” appears to be more persuasive simply because its identification of such consideration is closer to the definition of what comprises “time value of money.”

The third distinguishing factor identified by the Supreme Court is that, unlike most operational creditors, allottees are vitally concerned with the financial health of the real-estate developer given that the completion of the project will be jeopardized if they are not financially viable.¹⁷³ This was explained as the reason for why allottees would vote in the CoC keeping in mind the same interests as other financial creditors. While it is true that allottees are interested in ensuring that the real estate developers complete their projects, this does not address the concern raised by the petitioners regarding the position from which allottees participate in CoC meetings. While allottees may have an interest in the long-term viability of a real estate developer, this concern only exists to the extent that the allottees are able to secure their one-time investment.¹⁷⁴ This is different from other financial creditors such as banks and debenture holders which are interested in the long term sustainability of the developer notwithstanding whether some projects are delayed/terminated.¹⁷⁵ Thus, in a situation where the financial viability of a developer is at odds with its ability to complete all projects, it is unlikely that allottees would acquiesce to suspending a project of the developer in which they have an interest (even if it means that their investments will be refunded).¹⁷⁶ This is because the interest of allottees is not purely financial. For instance, in *Chitra Sharma v. Union of India*,¹⁷⁷ the Supreme Court dealt with petitions of over six hundred home buyers filed against a real estate developer that delayed the completion of its construction project.¹⁷⁸ Only 8 percent of the allottees wanted refunds and the rest wanted

¹⁷⁰ *Nikhil Mehta & Sons (HUF)*, (2017) SCC OnLine NCLAT 377, ¶¶17, 24.

¹⁷¹ *Id.* ¶¶ 24–26.

¹⁷² IBC, *supra* note 2, § 5(8)(f)(ii).

¹⁷³ *Pioneer Urban Land and Infrastructure Ltd.*, (2019) 8 SCC 416, ¶ 42.

¹⁷⁴ *Id.* ¶ 48.

¹⁷⁵ *Id.*

¹⁷⁶ *Id.*

¹⁷⁷ (2018) 18 SCC 575.

¹⁷⁸ *Id.* ¶ 6.

possession of their flats.¹⁷⁹ Further, as noted by the Supreme Court, allottees have often invested large sums of their hard-earned money; in such cases it would be all the more difficult for them to restructure their investment or condone delays in order to allow the developer to continue running its business.

As discussed above, allottees are more likely to prioritize the completion of those projects of the corporate debtor of which they are a part. They tend to be interested in the viability of the real estate developer only to the extent that it allows for the construction of their apartments. The inappropriateness of categorizing allottees as financial creditors becomes stark when reading the *Swiss Ribbons* judgment.¹⁸⁰ While the judgment acknowledges the existence of financial creditors who are individuals, the term is still restricted to persons who have made an investment/loaned money to the debtor with the expectation of getting money in return (deposit holders/debenture holders/banks).

The judgment in *Pioneer* drives around the characteristics of financial creditors as discussed in *Swiss Ribbons* by differentiating between other operational creditors and real estate developers and emphasizing the interest of the allottees in the long-term viability of the real-estate developer. However, the difference between the nature of long-term interests that financial creditors normally have and the interests of allottees is not adequately addressed in *Pioneer*. The next part of the paper examines the unintended consequences of categorizing allottees as financial creditors. Some of these consequences are independent of the conceptual correctness of the 2018 Amendment's classification of apartment buyers as financial creditors. The next part also attempts to ground the discussions so far in practical outcomes and emphasize the need for conceptual consistency within the Indian insolvency regime.

IV. IMPLICATIONS AND UNINTENDED CONSEQUENCES OF THE 2018 AMENDMENT AND *PIONEER* JUDGMENT

The 2018 Amendment grants allottees the rights to trigger the IBC as “financial creditors” and participate in CoC meetings, both of which would affect the real estate developer and their other

¹⁷⁹ *Id.* ¶ 48.2.

¹⁸⁰ *Swiss Ribbons*, (2019) 4 SCC 17, ¶¶ 50–51 (In *Swiss Ribbons* the Supreme Court had to decide whether the classification between financial and operational creditors under the IBC was arbitrary, thus violating Article 14 of the Constitution. The Court upheld this classification; in doing so it highlighted important differences between financial and operational creditors. The Court emphasized on a financial creditor's ability to restructure loans for the corporate debtor).

creditors during the insolvency resolution process.¹⁸¹ However, the 2018 Amendment does not significantly alter the position of allottees in case of a liquidation. In the *Pioneer* judgment, the Court stated that allottees were unsecured creditors.¹⁸² Section 53 of IBC gives first priority to claims relating to the costs of the insolvency proceedings and liquidation proceedings; second priority is given to workers' dues and debts owed secured creditors (ranked equally); the third priority is given to employees' dues; the fourth to debts of financial unsecured creditors; government dues (such as taxes, money owed to the Consolidated Fund of India etc.) and any remaining amount owed to secured creditors are ranked equally and paid fifth; other dues and claims (such as those of "other creditors") are paid sixth; and the seventh and eighth to be paid are the preference and equity shareholders respectively.¹⁸³ Thus, the liquidation waterfall does not differentiate between financial and operational creditors. It is only concerned with whether a creditor is secured or unsecured. The 2018 Amendment effectively moves an allottee from being the sixth priority to being the fourth priority in the liquidation waterfall. The remainder of this section will discuss some effects of the 2018 Amendment which Parliament may not have foreseen or intended.

A. ALLOTTEES' POSITION IN INSOLVENCY RESOLUTION PLANS

As far as the insolvency resolution plan is concerned, after the 2018 Amendment, allottees can use their votes in the CoC to keep the real-estate developer a going concern.¹⁸⁴ However, it is unclear why the other financial creditors would be ill-equipped to make this decision when necessary and viable. An allottee's right to refund would have been protected even if they were operational creditors. Resolution plans are required to prioritize payments to operational creditors over payments to financial creditors (including payments to allottees).¹⁸⁵ This means that operational creditors will receive at least as much as they would have in case of a liquidation in any resolution plan. The position of operational creditors can be loosely compared to the position of impaired creditors in under the US Bankruptcy Code – neither can receive lesser from a reorganization than they could have in the event of liquidation under the IBC or US Bankruptcy Code respectively.

¹⁸¹ IBC, *supra* note 2, §§ 7, 21.

¹⁸² *Pioneer Urban Land and Infrastructure Ltd.*, (2019) 8 SCC 416, ¶ 61.

¹⁸³ IBC, *supra* note 2, §§ 53(1)(g)–53(1)(h).

¹⁸⁴ *Id.* § 30(4).

¹⁸⁵ *Id.* § 30(2)(b).

In *Swiss Ribbons*, it was noted that out of the 80 cases which had been resolved since the IBC came into force, operational creditors have not only been paid before financial creditors in resolution plans but also recovered slightly more than the financial creditors.¹⁸⁶ While predicting the type of impact allottees would have on CoC meetings is outside the scope of this paper, it would be reasonable to say that most allottees (especially apartment buyers) will be dependent on other financial creditors to adjust their loans or commit extra funds to keep a real estate developer alive as a going concern. This is because allottees are less likely to have access to more funds (unlike banks). And unlike other financial creditors, allottees may not prefer to be monetarily compensated at some later time through debt restructuring as their primary interest is to possess a completed apartment.

B. USE OF THE IBC INSTEAD OF ALTERNATE REMEDIES

In the *Pioneer* judgment the Supreme Court had maintained that RERA and the Consumer Protection Act 1986¹⁸⁷ (now replaced by the Consumer Protection Act, 2019)¹⁸⁸ would continue to exist as remedies for the allottees. The Court also held that the RERA was the appropriate forum to approach in case construction was delayed or in case allottees wanted compensation.¹⁸⁹ The IBC, according to the Supreme Court, would be triggered by allottees only when they wanted a change in management.¹⁹⁰ While this is the only reasonable (and ideal) situation under which allottees should trigger the IBC, there is nothing in the IBC nor the *Pioneer* decision which ensures such a prudent use of the insolvency process by allottees. For instance, in *Chitra Sharma* and many of the cases brought before the company law tribunals prior to the 2018 Amendment, allottees (mainly home buyers) either wanted to expedite construction or they wanted a refund of their payments.¹⁹¹ The IBC has a more coercive effect on the real estate developer than RERA and the Consumer Protection Act. This is because real estate developers are affected by RERA and the Consumer Protection Act only after the court's adjudication of the claims before it. The IBC subjects real estate developers to the insolvency process from the very beginning (once

¹⁸⁶ *Swiss Ribbons*, (2019) 4 SCC 17, ¶ 10.

¹⁸⁷ Consumer Protection Act, 1986, No. 68, Acts of Parliament, 1986 (India).

¹⁸⁸ Consumer Protection Act, 2019, No. 35, Acts of Parliament, 2019 (India).

¹⁸⁹ *Pioneer Urban Land and Infrastructure Ltd.*, (2019) 8 SCC 416, ¶ 30.

¹⁹⁰ *Id.*

¹⁹¹ *Chitra Sharma v. Union of India*, (2018) 18 SCC 575, ¶ 48.2; *Nikhil Mehta & Sons (HUF)*, (2017) SCC OnLine NCLAT 377, ¶¶ 4–5, 8.

a default is shown); this is something which real estate developers wish to avoid. Thus, allottees may choose to trigger the IBC even when faced with grievances that can be addressed by other laws and past experiences (*Chitra Sharma, Nikhil Mehta, etc.*) are evidence of this tendency.¹⁹²

Recent developments have shown that the government has already started grappling with this particular consequence of the 2018 Amendment.¹⁹³ In Mumbai, India's financial capital, half the cases brought before the NCLT by allottees (specifically apartment buyers) are against real estate developers.¹⁹⁴ These cases could disrupt the functioning of otherwise properly operating companies. In December 2019, the IBC was further amended to require a minimum of 100 allottees or 10 percent of the allottees in a real estate project (whichever is lesser) to file an application for triggering the insolvency process.¹⁹⁵ Allottees did not welcome this amendment and have challenged it before the Supreme Court.¹⁹⁶ Even if this amendment were to be upheld by the Supreme Court, the interests of allottees as examined in this paper which make them ill-placed to trigger the IBC would continue to skew the purpose of the insolvency resolution process.

C. DETERMINATION OF DEFAULTS

Section 7 of the IBC allows financial creditors to trigger insolvency proceedings in case of a "default."¹⁹⁷ In the context of financial creditors, it is easy to determine what amounts to a default. Defaults refer to instances of not repaying a debt in a timely fashion and information regarding defaults can be found with information utilities.¹⁹⁸ Section 214 of the IBC states that the core function of an

¹⁹² Deepak Mondal, *IBC Code: Are Speculative Homebuyers Misusing Insolvency Law?*, BUSINESS TODAY (Oct. 2, 2019), <https://www.businesstoday.in/current/corporate/ibc-code-are-speculative-homebuyers-misusing-insolvency-law/story/382538.html>.

¹⁹³ Asit Ranjan Mishra, *Govt Moves to Prevent Misuse of IBC Provision*, LIVEMINT (Oct. 1, 2019), <https://www.livemint.com/politics/policy/govt-moves-to-prevent-misuse-of-ibc-provision11569947831546.html>

¹⁹⁴ See *supra* note 158.

¹⁹⁵ Ministry of Law and Justice, *The Insolvency and Bankruptcy Code (Amendment) Ordinance, 2019 (India) § 7*, <https://ibbi.gov.in/uploads/legalframwork/d6b171ec9b9ea5c54f7423bc36f92977.pdf>.

¹⁹⁶ Renu Yadav, *Homebuyers Move SC Against the IBC Amendment Introducing Minimum Threshold*, LIVEMINT (Jan. 8, 2020), <https://www.livemint.com/money/personal-finance/homebuyers-move-sc-against-the-ibc-amendment-introducing-minimum-threshold-11578453198183.html>.

¹⁹⁷ IBC, *supra* note 2, § 7.

¹⁹⁸ *Innovative Industries v. ICICI Bank*, (2018) 1 SCC 407, ¶ 30.

information utility is to maintain a data base of financial information in an accessible format.¹⁹⁹ Financial information refers to records of the debts, liabilities, assets (with or without charges on them), and balance sheet and cash flow information of a person.²⁰⁰ For allottees who are a part of committed returns schemes, a default occurs when the committed returns are not paid or when a check issued to pay them has been dishonored.

The determination of the occurrence of a default becomes tricky when considering the interests of allottees who are not a part of a committed returns scheme. Seeing as many allottees are aggrieved by delayed construction, a relevant question would be whether such delay would amount to a default. Given that the decision in *Pioneer* interpreted receiving possession of a constructed house as “consideration for the time value of money” it would seem fair to consider a delay in such delivery of possession as a default. However, in *Pawan Dubey v. J.B.K. Developers*,²⁰¹ the NCLT refused to consider a “delay” as a default and stated that allottees could only seek relief as financial creditors if there was a failure in the timely payment of committed returns by the developer.²⁰² Though allottees have been brought within the ambit of the IBC, the definition of default remains unchanged and the *Pioneer* case does not provide any guidance in this regard. Accordingly, *Pawan Dubey* may still apply to allottees effectively denying them the right to trigger the IBC in case of a delay (despite the 2018 Amendment).

The issue of determining defaults becomes even more important when considering the fact that the NCLT must only be satisfied that a default exists with respect to financial creditors and cannot go into the merits of the case even if the default is disputed.²⁰³ Construction contracts often excuse delays that occur due to circumstances that the real-estate developer cannot control. It would seem unfair to begin insolvency proceedings against real estate-developers in such cases but the NCLT’s hands would be tied if delays are characterized as defaults.

One might say that the 2018 Amendment may be read down to only apply to allottees who are a part of committed returns schemes (thus allowing the NCLT to determine default by checking

¹⁹⁹ IBC, *supra* note 2, § 214.

²⁰⁰ *Id.* § 3(13).

²⁰¹ (2018) SCC Online NCLT 794. The tribunal distinguished the facts of this case from those of *Nikhil Mehta* by stating that there was not default in repayments in a committed returns scheme. The tribunal in *Pawan Dubey* held that a delay in construction in and of itself would not be a ground for allottees to trigger the IBC under Section 7.

²⁰² *Id.* ¶ 29.

²⁰³ *Innovative Industries*, (2018) 1 SCC 407, ¶ 28.

if the real estate developer has not been paying the committed returns). However, the Court in *Pioneer* unequivocally stated that the 2018 Amendment must not be read down.²⁰⁴ It would also seem puzzling if the courts and tribunals (through interpretation) restricted the 2018 Amendment to allottees who are a part of a committed returns scheme. The Supreme Court and the ILC report both stressed on the hardships faced by allottees on account of delays in construction notwithstanding membership to a committed returns scheme.²⁰⁵

Allottees can not only trigger the IBC for defaults in payments due to them but also defaults in payments due to other financial creditors.²⁰⁶ This would mean that in case there has been a default on a loan provided by a bank and the bank is willing to restructure the loan without triggering the IBC, the allottee could still trigger the IBC. The ability to trigger the IBC so easily is dangerous as it could jeopardize the otherwise smooth functioning of a company. For instance, when the IBC was triggered against one of the petitioners in *Pioneer* by the buyers of 14 out of 19,062 units sold the by the real estate developer, the Infrastructure Finance Development Company prematurely invoked a letter of credit to recover the entire amount (one billion rupees) due to them from the real estate developer. Granted that there may be divergences of interests between other financial creditors as well, their bottom line remains the same because all of them have a purely monetary interest in the corporate debtor. They are thus in a better position than allottees to decide when (and whether) to trigger the IBC.

D. NATURE OF PRECEDENT SET

A deeming fiction can be used to serve multiple functions by Parliament. It can be used to include the impossible with the meaning of a word or phrase, thus moving the meaning of a word away from what would normally be attributed to it. A deeming fiction can also simply be used to clarify an interpretation of a provision by making express what is already implied. The Supreme Court in *Pioneer* took pains to explain why the deeming fiction used by the 2018 Amendment to make allottees financial creditors was only clarificatory in nature.²⁰⁷ This meant that the text of the existing Section 5(8)(f) already subsumed allottees and the 2018 Amendment only made express what was already implied. However, a perusal of

²⁰⁴ *Pioneer Urban Land and Infrastructure Ltd.*, (2019) 8 SCC 416, ¶ 64.

²⁰⁵ *Id.* ¶¶ 18, 41; Report of the Insolvency Law Committee, *supra* note 20, ¶¶ 1.3, 1.7.

²⁰⁶ IBC, *supra* note 2, § 7(1).

²⁰⁷ *Pioneer Urban Land and Infrastructure Ltd.*, (2019) 8 SCC 416, ¶ 79.

the wording of the relevant provision and the manner in which it has been interpreted by the company law tribunals does not support the Supreme Court's conclusion regarding clarificatory the nature of the deeming fiction.

Cases where the company law tribunals discussed Section 5(8)(f) have already been analyzed.²⁰⁸ In none of these decisions did the company law tribunals conclude that Section 5(8)(f) would include all allottees, rather they reached the opposite conclusion and held that only some allottees (those who were a part of committed returns schemes) would fall within the definition.²⁰⁹ Further, the IBBI amendment to its Regulations in August 2017 and the press note that followed showed that the IBBI believed that apartment buyers were neither operational creditors nor financial creditors, which is why they were put under the category of "other creditors." Press notes are issued in public interest; though they do not bind the ministry issuing them, they are issued with expectation that readers will act according to the information contained in them.

The ability for a legislature to use a deeming fiction to amend a legislation cannot be questioned. As noted by the Supreme Court in *Pioneer*, the text of the legislation binds only the courts and not the legislature.²¹⁰ This means that the legislature has more freedom when amending the legislation than the court does while interpreting it. However, we argue that the legislature's use of a deeming fiction to amend the IBC has undesirable implications even though it is not illegal. The 2018 Amendment has blurred the distinction between financial and operational creditors. Even if the Supreme Court's distinction (in *Pioneer*) between real estate developers and "other" operational debtors is considered to be persuasive, it is very fact-specific (the nature of contracts between real-estate developer and allottees). There is no guidance provided to investors and entrepreneurs on what would warrant classifying other "operational debtors" as "financial debtors." While attempting to distinguish between real estate developers and other operational debtors in *Pioneer*, the Supreme Court did not set out general criteria for when operational debtors may be classified as financial debtors.

E. BLURRING THE LINE BETWEEN FINANCIAL AND OPERATIONAL CREDITORS

²⁰⁸ See *supra* section III.A. "Treatment of Allottees by the Supreme Court and Company Law Tribunals."

²⁰⁹ *Nikhil Mehta & Sons (HUF)*, (2017) SCC OnLine NCLAT 377; *Anubhuti Agarwal v. DPL Builders Pvt. Ltd.*, (2017) SCC OnLine NCLT 12672.

²¹⁰ *Pioneer Urban Land and Infrastructure Ltd.*, (2019) 8 SCC 416, ¶ 83.

The distinction between financial creditors and operational creditors is unique to India²¹¹ and has been discussed in previous sections.²¹² The retention of this distinction between the two types of creditors (and debtors) is something that Parliament and the courts must tend to seriously because it affects the rights given to creditors (within the CoC) and those of debtors when disputing a creditors' claim.²¹³ This is because there are no other standards which the business community can fall back on to ascertain where they stand; they are wholly reliant on the signaling of the legislature and judiciary for this. It is thus vital that the legislature refrains from using deeming fictions as it did in the 2018 Amendment because it eats away at the objectives of separating financial and operational creditors (and consequently financial and operational debtors).

In *Swiss Ribbons*, the Solicitor General of India articulated reasons for the legislative policy enshrined in the IBC, i.e., the maintenance of predictability and certainty, protection of the interests of the corporate debtor, ensuring that liquidation is the last resort.²¹⁴ The 2018 Amendment militates against the first two policy objectives of the Code. The amendment makes the debtor vulnerable to a larger number of insolvency proceedings being initiated against it, more importantly, it reduces the predictability with which different businesses can assess their positions *vis-à-vis* the insolvency regime. As already mentioned, the "unique" relationship between allottees and real estate developers, where the debtor supplies the goods/services is actually quite common. This might arise in cases where any entity commissions the services of another to build or provide something and partly finances the same.

The insurance sector is another example where a financial creditor-financial debtor relationship may exist: policy holders often invest large sums of money over their lifetimes to secure themselves against hazards such as fires and accidents. They too contribute to the pool which helps finance pay-outs made to them. Based on the *Pioneer* judgment, one could even make a case for policy holders to be considered as "financial creditors." After the enactment of the 2018 Amendment, the IBC has moved closer the UK's insolvency regime where all creditors are allowed to vote during insolvency resolution proceedings. If this is the direction in which Parliament intends to proceed, then it is unclear why a specific type of operational creditor (trade creditors) ought to be excluded from voting in the CoC.

²¹¹ *Swiss Ribbons*, (2019) 4 SCC 17, ¶ 44.

²¹² See *supra* section II. "The Role of Creditors in Corporate Reorganizations Under Insolvency Regimes."

²¹³ IBC, *supra* note 2, §§ 9, 21(2), 30(4).

²¹⁴ *Swiss Ribbons*, (2019) 4 SCC 17, ¶ 64.

The real estate sector has come to a point where allottees are increasingly becoming victims of mismanagement. This is beyond dispute. The number and duration of delays is alarming and something which requires urgent action. Further, it cannot be ignored that allottees are affected by insolvency proceedings against the real-estate developer. However, the solution to these issues should not have been sought through the IBC. The mandate of the IBC has already been discussed and it is clear.²¹⁵ It is meant for the maximization of the value of the debtors' assets so as to allow creditors to decide whether to keep it as a going concern or liquidate it. In either scenario, the IBC serves the greater economic goal of ensuring that credit is efficiently allocated within the economy. The use of insolvency law as a tool to fix problems which plague a sector is inappropriate, especially when there are other alternatives which may have been pursued to protect the interest of allottees.

F. ALTERNATIVE MEASURES TO PROTECT ALLOTTEES UNDER THE IBC

Ideally, Parliament should protect consumer pre-payments in general when the entity to which such pre-payments were made is subject to insolvency proceedings. While a minimum amount to be paid by the consumer may be set in order for this protection to take effect, consumer pre-payments should be protected when a resolution plan is drafted and when the debtor goes into liquidation.

In the US and the UK, it would be difficult to confer the advantages of one type of creditor onto the other. This is because classification of creditors is either contingent on a substantial similarity of claims (US) or is non-existent and one's ability to influence reorganization is based on the amount of debt they own (UK). Even preferential debt (in the UK) is only protected to the extent that it gets a priority during liquidation and it cannot be altered by other creditors during reorganization.²¹⁶ However, owning preferential debt does not confer any special or different voting rights.

Accordingly, discussions on the protection of consumer prepayments in the US and the UK is centered around strengthening consumers' pre-insolvency contract rights or clearly giving them a preference in the liquidation hierarchy. In India, the artificial distinction between financial and operational creditors gives law

²¹⁵ See *supra* section II.A. "Role of Financial and Operational Creditors in India."

²¹⁶ Insolvency Act 1986, c. 45, sch VI, § 386 (UK).

makes the option to change the nature of the debt at a much more significant scale (which this paper has cautioned against).²¹⁷

There are other methods to protect consumer prepayments which are less disruptive of the insolvency process and involve fewer interpretational feats. While the regulations governing the real estate sector in India, UK, and the US are different, all three jurisdictions allow apartments to be sold prior to their construction.²¹⁸ The money collected from these sales is often used to finance the construction of these apartments. For instance, the state of Florida allows ninety percent of buyers' escrow deposits to be used for construction purposes.²¹⁹ Further, it is also acknowledged that such a model for financing construction is riskier but offers buyers more favorable prices than ones they would have to pay for buying an apartment that is already constructed.²²⁰ Thus, even in the US and the UK, apartment buyers bear the risk of incomplete construction and delays when they decide to purchase prior to construction.²²¹ What might set India apart from the US and the UK is the sheer scale of the delays and their numerosity.

1. Treatment of Consumer Prepayments Under US and UK Insolvency Regimes

Under the US Bankruptcy Code, consumers (including apartment buyers)²²² will be treated as unsecured creditors because they have a claim against the debtor for the provisions of a good or service (for which they have paid).²²³ Consumers are most likely to

²¹⁷ See *supra* section IV.E. “Blurring the Line Between Financial and Operational Creditors.”

²¹⁸ Editors, *Condominium Regulation: Beyond Disclosure*, 123 U. PA. L. REV. 639, 643–44 (1975) (discussing the risks of investing in preconstruction condominiums in the US); LAW COMMISSION, CONSUMER PREPAYMENTS ON RETAILER INSOLVENCY, 2016 Law Com. No. 368 at ¶ 3.21.

²¹⁹ Fla. Stat. § 501.1375 (2019). See Amy Gunderson, *When You Buy Before Its Built*, N.Y. TIMES, (Apr. 4, 2007), <https://www.nytimes.com/2007/04/04/realestate/greathomes/04GH-home.html>; Martha Brannigan, *New Condo Financing Model Has Merit*, MIAMI HERALD, (Sept. 3, 2012), <https://www.miamiherald.com/latest-news/article1942428.html>.

²²⁰ *Id.*

²²¹ *Id.*

²²² See *supra* note 218.

²²³ 11 U.S.C. § 101(5) (2018); Phillip G Schrag & Bruce C. Ratner, *Caveat Emptor – Empty Coffers: The Bankruptcy Law Has Nothing to Offer*, 72 COLUM. L. REV. 1147, 1147–48 (1972); Tibor Tajti, *Unprotected Consumers in the Digital Age: The Consumer Creditors of Bankrupt, Abandoned, Defunct and of Zombie Companies*, 24 TILBURG L. REV. 3, 4 (2019) (discussing the inadequacies of current bankruptcy systems in protecting consumers and how this is attributed to their positioning in the liquidation waterfall).

be unsecured creditors given that their prepayments normally do not create a charge over the assets of the company. In 1970, when Shield International Corporation filed for reorganization under Chapter 11, they listed 4616 purchasers of books who had paid in full and not received their orders as unsecured creditors.²²⁴ Multiple purchasers of books from Shield International Corporation had their claims listed as those of unsecured creditors.²²⁵ It would be reasonable to assume that prepayments made towards real estate development projects would also be considered unsecured credit for the purposes of the US Bankruptcy Code.

Under UK insolvency law, consumers who have made prepayments are unsecured creditors.²²⁶ While it is permissible for administrators to invite claims from consumers and repay them or make good on the promised delivery of goods, administrators cannot favor one class of creditors (such as consumers) over others.²²⁷ Thus, administrators are likely to repay consumer prepayments or honor contracts only if they decide that the company should continue trading while in administration and if honoring prepayments would help achieve a better result for the company's creditors in general.²²⁸ Given that the required votes to approve a proposal and bind other creditors a simple majority and the quorum for meetings of creditors is one creditor, consumers would have to be vigilant and represent a substantial portion of the debt owed in order to make a difference in the outcome of an administration.²²⁹ The position of consumers as unsecured creditors and the limitations they face in changing the outcome of any reorganization through a CVA are similar to their position in the event of a company undergoing administration.²³⁰

In both the US and the UK, liquidation preference is given to secured creditors and administrative expenses incurred during the insolvency proceedings.²³¹ Unsecured creditors (consumers) are

²²⁴ Schrag & Ratner, *supra* note 223, at 1147–48.

²²⁵ *Id.*

²²⁶ LAW COMMISSION, CONSUMER PREPAYMENTS ON RETAILER INSOLVENCY, 2016 Law Com. No. 368 (UK), ¶ 1.2.

²²⁷ *Id.* ¶ 2.14.

²²⁸ *Id.* ¶ 2.16.

²²⁹ The Insolvency (England and Wales) Rules 2016, No. 1024, rules 15.20, 15.34 (quorum for meeting of creditors, and requisite majorities for Administration proposals and CVAs respectively).

²³⁰ *Id.*

²³¹ 11 U.S.C. §§ 724, 507; Insolvency Act 1986, c. 45, §§ 175, 176ZA, 386, sch. 6.

among the last to be paid out the liquidation estate but are paid before shareholders of the liquidated entity.²³²

2. Strengthening Pre-insolvency Protections

One way of protecting the consumer without giving them additional rights in the process of a reorganization of a financially distressed firm is through the creation of a trust. Recommendations for protecting consumer prepayments were made in the UK's Law Commission Report on Consumer Prepayments ("ULC report").²³³ The ULC report noted that consumers suffer losses when companies enter the insolvency process. These losses range from simple gift vouchers to investments in home improvements to the purchase of new homes. The ULC report also recommended that consumers whose claims meet certain criteria may be given priority in payments from the bankrupt's estate.²³⁴ In the US, it is common for escrow accounts to be created for deposits to secure real estate transactions. But if the escrow account is not closed prior to the developer going filing for bankruptcy under Chapter 11, it may become a part of the bankruptcy estate.²³⁵ Accordingly, the creation of trusts with clearly delineated rights has been advocated as a method of protect consumer deposits from becoming a part of the insolvency estate in the US as well.²³⁶ Since bankruptcy courts have clear rules for the treatment of properties held as a trust, this structure would be preferable to an escrow.²³⁷ There needs to be some means by which consumer credit is returned to the consumer before other distributions for liquidation begin.²³⁸

Requiring that a trust be created with allottees' deposits instead of an escrow account would be an effective method of

²³² *In re Nortel* [2013] UKSC 52, ¶ 39; *What Happens When Public Companies Go Bankrupt?*, SECURITIES AND EXCHANGE COMMISSION, <https://www.sec.gov/reportspubs/investor-publications/investorpubsbankrupthtm.html> (last visited May 18, 2020).

²³³ LAW COMMISSION, CONSUMER PREPAYMENTS ON RETAILER INSOLVENCY, 2016 Law Com. No. 368, 115–17.

²³⁴ *Id.* ¶¶ 8.92, 8.106–8.109.

²³⁵ Thomas M. Byrne, *Escrows and Bankruptcy*, 48 THE BUS. LAW. 761, 776 (1993) (discussing the enforceability of escrow arrangements after a bankruptcy petition has been filed).

²³⁶ Schrag & Ranter, *supra* note 223, at 1151 (juxtaposing how simple it would be to return consumer credit during bankruptcy if it was considered to be held in trust by the retailer with how difficult it is to establish that a trust has been created for the consumer credit).

²³⁷ Byrne, *supra* note 235, at 777.

²³⁸ Schrag & Ranter, *supra* note 223, at 1188 (discussing the substantial reforms required to empower consumers during retailer bankruptcy).

protecting allottees in India as well. Assets held in trusts or for any third party are left out of the liquidation estate under the IBC.²³⁹ In *Bikram Chatterji*,²⁴⁰ the Supreme Court seemed to employ this strategy when it ordered that the buildings and lands allotted to apartment buyers be left out of the insolvency estate, thus preventing creditors from using these assets to recover their debts. Such measures would be easy to enforce given that RERA already requires 70 percent of the allottees' payments to be put into an escrow account (which can be only be used for the purpose of construction).²⁴¹

Another means of protecting consumer pre-payments is to give them a place in the hierarchy of payments during liquidation and prioritize their payments along with those of operational creditors (as was also recommended by the ULC report). The benefit of these alternatives is that they take a more consistent and systemic approach to the problem without disrupting the insolvency regime where it is not necessary. For instance, giving a preference to consumers in the insolvency hierarchy would not substantially change their ability to affect a company's reorganization. Compared to this, characterizing a consumer (allottee) as a financial creditor under the IBC gives them a right they would not have otherwise had as an operational creditor. The Indian insolvency regime cannot be expected to solve the problems (though persistent) of specific sectors. However, it can prioritize the interests of stakeholders based on how society perceives them and how equipped they are to bear the costs of insolvency (as is already done in the case of employees' dues payable by the corporate debtor).²⁴²

V. CONCLUSION

The IBC's provisions and Preamble show that its main purpose is to maximize the value of the debtor's assets for all stakeholders and improve credit markets and the ease of doing business in India.²⁴³ There is little room for equity within the scheme of the IBC, which is demonstrated by the clearly circumscribed role of the NCLT.²⁴⁴ However, an insolvency regime cannot be divorced from the realities which surround it. The IBC is cognizant of the socio-economic circumstances which surround it and it has taken

²³⁹ IBC, *supra* note 2, § 36.

²⁴⁰ (2019) SCC OnLine SC 901.

²⁴¹ Real Estate (Regulation and Development) Act, No. 16, Acts of Parliament, 2016 § 4 (India).

²⁴² IBC, *supra* note 2, § 53; *see* FINCH, *supra* note 67, at 609–11.

²⁴³ IBC, *supra* note 2.

²⁴⁴ *Id.* §§ 30–31.

steps to address them. For instance, in the liquidation waterfall, the IBC prioritizes employees' and workers' dues. This is a reflection not just of a societal reality (the vulnerability of workers and employees) but also of a societal prioritization. While the IBC is capable of accommodating societal concerns and urgencies, it should not do so in an unfettered manner. The treatment of employees and workers shows that to give a class of persons a priority in payments, they need not be given other rights (such as those flowing from being a financial creditor).

One might ask whether apartment buyers/allottees would have been included in the insolvency regime if the real-estate sector was not in its current deplorable state. Given the extent to which the flaws in the real estate sector have been cited by those who have suggested, enacted and upheld the 2018 Amendment, the answer to this question would most reasonably be in the negative. In addition to setting a dangerous precedent, the 2018 Amendment strikes at the conceptual consistency of the IBC. One of the biggest strengths of the IBC is the certainty with which financial creditors can trigger it and use it as an opportunity to change the management of their corporate debtor and reorganize its debt. The expediency and efficiency of such a process may tempt Parliament to use it as a tool to remedy other issues or sectors. However, Parliament must be cautious not to misallocate the efficiency of its insolvency regime as this may risk compromising it all together.