IBC DOSSIER

Bulletin on Landmark Judgments under IBC, 2016

M/S TATA STEEL LTD.
Vs.
VARSHA & ANR.

Brief Facts

Prior to the Corporate Insolvency Resolution Process (CIRP) of Bhushan Steel Limited (BSL), Respondent No.1-Varsha had instituted a civil recovery suit against BSL for Rs. 38,89,674.14 with interest, while Intervenor-Masyc had initiated six arbitral references for goods supplied to BSL. When CIRP commenced at the instance of State Bank of India, both submitted claims as Operational Creditors, which the Resolution Professional admitted only at a notional value of Re. 1 each in the Interim List of Creditors dated 17th January 2018, with a note recording that the claims were sub-judice and liability was subject to the outcome of pending proceedings.

Tata Steel Ltd. (Appellant-SRA) submitted its Resolution Plan on 3rd February 2018. Since the claims of financial creditors exceeded the liquidation value, Operational Creditors were entitled to NIL payment; nevertheless, the Plan voluntarily earmarked an Operational Creditors Settlement Amount of Rs. 1,200 crore, of which Rs. 1,000 crore was for essential and critical creditors and the remaining Rs. 200 crore for pro-rata distribution among other admitted Operational Creditors within twelve months of the closing date. In the Final List of Creditors dated 20th March 2018, the claims of Varsha and Masyc continued to be valued at Re. 1 each, but the earlier note stating that liability was subject to pending proceedings was omitted.

The Committee of Creditors approved the Resolution Plan on 20th March 2018, and the NCLT sanctioned it on 15th May 2018; the NCLAT dismissed appeals against it, and Masyc's separate challenge was dismissed as withdrawn. Tata Steel thereafter sought dismissal of Varsha's civil suit and termination of Masyc's arbitration on the ground that all pre-CIRP claims stood extinguished. Both the Trial Court and the Sole Arbitrator declined to do so, and the Bombay High Court, Nagpur Bench, dismissed Tata Steel's writ petition and review application, permitting the suit to continue notwithstanding approval of the Resolution Plan. Tata Steel accordingly appealed to the Supreme Court, and Masyc was permitted to intervene on the limited question of whether Operational Creditors could enforce past dues through civil suit or arbitration after approval of a Resolution Plan.

Decision

The Supreme Court allowed the appeals, holding that once a Resolution Plan is approved under Section 31(1) of the IBC, all claims provided for therein stand frozen and binding on all stakeholders, while claims not incorporated in the Plan stand extinguished, consistent with the 'clean slate' doctrine. The Court held that the Final List of Operational Creditors, never having been challenged by Varsha, had attained finality, and that the change from Note 3 (recording claims as sub-judice) to Note 2 in the Final List reflected that the Re. 1 valuation had become a quantified, final figure rather than a placeholder pending adjudication.

The Court further held that only Rs. 200 crore of the settlement pool was earmarked for pro-rata distribution among Operational Creditors with claims crystallised as on 20th March 2018, and that permitting uncertain or unquantified claims to resurface years later would be 'akin to a hydra-headed recurrence', defeating the finality contemplated under the Code. It rejected the argument that Clauses 8.7.3(i) and 8.2.4 of the Resolution Plan carved out an exception preserving sub-judice claims, finding instead that the Plan, read as a whole, extinguished all such claims save for the amounts payable under the Operational Creditors Settlement Amount. The principles of contra proferentem and the 'face value reservation mechanism' urged by the creditors were held inapplicable in the absence of any ambiguity in the Plan.

Accordingly, the Court set aside the Bombay High Court's orders and the Trial Court's order, and dismissed both Varsha's recovery suit and Masyc's arbitration proceedings. In an afterword, the Court observed that the Code, while a marked improvement over the erstwhile Sick Industrial Companies (Special Provisions) Act regime, does not adequately protect small operational creditors such as MSMEs, who are placed at the bottom of the repayment waterfall, and urged the Law Commission and Legislature to examine a fairer repayment mechanism for such creditors.

Link of the Order

https://ibbi.gov.in/uploads/order/11487cc8fdf860689d07fd02e7677b95.pdf