"Ineligible Resolution Applicants" - Supreme Court on Section 29A(h) of IBC

For the first time since its introduction, Section 29A(h) of the IBC came up for interpretation before the Supreme Court (SC) in the case of Bank of Baroda Vs MBL Infrastructures Ltd (2019). On perusal of facts of the case and the law involved, the SC held that the resolution applicant, a Personal Guarantor to the Corporate Debtor, was barred by provisions of Section 29A(h) of IBC from submitting a resolution plan. This judgement is exceptional because, although the SC concluded that the resolution applicant was not allowed to submit a resolution plan, yet, on peculiar facts of the case, the implementation of resolution plan was allowed to continue in the overall interests of the Corporate Debtor. ***Read on to know more…***

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1. Introduction

Section 29A of the Insolvency and Bankruptcy Code, 2016 (IBC) is one of the most adversarial (qua the promoters/their related parties/connected persons) and talked about provisions, that has thrown a spanner in the world of corporate planning and restructuring vis-à-vis resolution of companies, who are undergoing through financial stress. This provision bars and restricts the entities and persons, who defaulted on payment of debts to creditors, from attempting to reclaim their business entity, although, the doors of Section 12A are open to them for withdrawal of CIRP.

Introducing the Section 29 A in the Parliament, the Government said, "Concerns have been raised that the persons who, with their misconduct contributed to defaults of companies or are otherwise undesirable, may misuse this situation due to lack of prohibition or restrictions to participate in the resolution or liquidation process, and gain or regain control of the Corporate Debtor (CD). This may undermine the processes laid down in the Code as the unscrupulous person would be seen to be rewarded at the expense of the creditors. In addition, in order to check that the undesirable persons who may have submitted their resolution plans in the absence of such a

provision, responsibility is also being entrusted on the committee of creditors to give a reasonable period to repay overdue amounts and become eligible,". The plain reading of this quoted text gives a clear picture about the intent and purpose of the legislature in formulating and introducing Section 29A in the IBC, although a little later after the enactment of IBC in the year 2016. At time of introduction of IBC, there was general perception amongst public that the errant promoters, who defaulted on payments to banks and other creditors, will definitely try to retain the ownership and control of their enterprise in one way or another. There were expectations in financial and corporate circles that there will, possibly, be some extraordinary corporate and financial structuring exercises, which would be undertaken by business entities, in order to ensure that the ultimate ownership and control of the enterprise was not taken away from the present promoters.

The legislature, too, in its wisdom, was conscious of the possibility of such efforts that may be undertaken by erring entities. The law makers realized that there was no provision in the IBC to prevent defaulters of creditors from submitting resolution plans for CD. So much so, there was, also, no deterrent in the IBC, which could come to the aid of the judiciary, to interpret any provision against such mischief. This was the genesis for introduction of Section 29A in the IBC in year 2017, which was subsequently amended in year 2018, to enhance its scope and effectiveness.

One particular provision relating to Personal Guarantors (PG) to CD was included as sub-Section (h) of Section 29A of IBC. This sub-Section was to ensure ineligibility of 'person', who provide personal guarantees to creditors and bars them from becoming a resolution applicant once their personal guarantee is invoked by such creditor.

2. Judicial Scrutiny of Section 29A

Bank of Baroda (BOB) Vs. MBL Infrastructures Ltd[1]. (2022) is the first case, wherein the SC analyzed the provisions of Section 29A(h) of IBC in detail and delivered its judgement on January 18, 2022. The fact of the case is as follows:

a) This case brought up an issue before the SC with regard to interpretation of provisions of Section 29(A)(h) of IBC. This Section of IBC provides an express bar on a person from becoming a resolution applicant, who has executed a guarantee in favour of a creditor in respect of a CD, against whom an application for initiating resolution process has been made by such creditor and such a guarantee, when invoked by the creditor, has remained unpaid in full or in part.

b) Two resolution plans were received by RP out of which, one resolution plan was submitted by a person, who was a PG to the CD with the creditor that had initiated CIRP of CD.

c) Section 29A of IBC was introduced in IBC with effect from November 23, 2017. Section 29A(h), specifically, after its introduction, was amended on January 18, 2018, and again on June 06, 2018.

"NCLT held that the PG to CD was not disqualified as the guarantee given by him had not been invoked by the particular creditor, that had initiated the resolution process of CD."

d) On an application moved by RP before AA, the AA, vide its order on December 18, 2017, held that the PG to CD was not disqualified from submitting a resolution plan as the personal guarantee given by him "had not been invoked by the particular creditor, who had initiated the resolution process of CD".

e) On appeal, the NCLAT also decided in favour of the guarantor and held that the guarantor did not suffer from the ineligibility provided under Section 29A(h) of IBC. However, the interpretation on the question of law was left open and unanswered.

f) Meanwhile, the resolution plan submitted by the guarantor of CD was accepted by CoC on the basis of its techno-commercial feasibility and viability and the CoC voted in favour of this resolution plan with more than 75% voting share.

g) On appeal before the SC, the appellant (BOB) submitted that as per provisions of Section 29A of IBC, the guarantor of CD, being a promoter, could not have submitted a resolution plan for the CD as the personal guarantee given by him in

[1] *Bank of Baroda Vs. MBL Infrastructures Ltd* (https://main.sci.gov.in/supremecourt/2019/36841/36841_2019_36_1501_32

favour of various other lenders (financial creditors/banks) had been invoked prior to commencement of resolution process.

h) In response, the respondent submitted before the SC that the personal guarantee had not been invoked by the creditor, who had filed the application before AA for resolution of CD and "the invocation of guarantee by other creditors, who had not invoked the jurisdiction of AA, could not be a ground for ineligibility of resolution applicant".

i) It was further contended by the respondents that the CD was now a Going Concern (GC) and the successful resolution applicant had infused substantial funds and resources in the CD post completion of resolution process. Thus, it would be a travesty to disturb the smooth implementation of the resolution plan at this stage.

3. Statutory Interpretation by the SC

a. While deep diving into the realm of interpretation of statutes, the SC quoted extensively from previous judgements of the SC as well as other International Courts. Citing from a previous judgement in the matter of *RBI Vs Peerless General Finance*[2] by the SC "The information must depend on the text and colour. If the text is the texture, context is what gives the color. Neither can be ignored…. No part of a statute and no word of a statute can be construed in isolation…."

b. The principle laid down by such decisions became the basis of judgements pronounced by SC in the CIRP matters related to Arcelor Mittal[3], Phoenix Arc[4], Jindal Steel & Power ltd[5], Swiss Ribbons[6] and Essar Steels[7].

4. General Observations of SC on IBC

The Supreme Court observed that -

a) The IBC recognizes a way to rehabilitate and revive the corporate debtor and it recognizes two principal players in this respect – CoC and CD.

b) All other persons and parties, like IRP, RP, Liquidator, AA, etc. are facilitators. They just facilitate the process of resolution, but it is the CoC, which makes the final call with regard to commercial and viable resolution of a CD, and it is the CD that ultimately benefits from the whole resolution process.

"As and when CoC takes a decision in favour of a resolution plan in the overall interest of CD, the facilitators need to ensure that such a decision finally receives approval of authorities, observed the SC."

c) While the facilitators play a major role in putting the CD on the path of recovery by ensuring that the most suitable resolution plan is brought before the CoC in order to help CoC to take a commercially viable decision, it is also ensured that the same is done efficiently and transparently. As and when CoC takes a decision in favour of a resolution plan in the overall interest of CD, the facilitators ensure that such a decision finally receives approval of authorities.

d) All decisions taken by the facilitators of resolution process are aimed at maximization of value of the CD so as to ensure that the CoC has the most suitable resolution plans to consider and decide upon. All these processes go a long way in acting as a catalyst in the overall revival and rehabilitation of the CD.

5. Specific Observations of SC with regard to Section 29A(h) of IBC

a) The main intent behind introduction of Section 29A of IBC was to avoid unwarranted and unscrupulous elements from getting into the resolution process in order to protect their personal interests. The involvement of such elements, that were expressly disqualified under Section 29A of IBC, would take away the

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[1] *Reserve Bank of India Vs. Peerless General Finance and Investment Company Limited,* (1987) 1 SCC 424.

[2] *Arcellor Mittal India Pvt. Ltd. Vs. Satish Kumar Gupta,* (2019) 2 SCC 1

[4] *Phoenix Arc (P) Ltd. Vs. Spade Financial Services Ltd.,* (2021) 3 SCC 475

[5] *Arun Kumar Jagatramka Vs..Jindal Steel & Power Limited,* (2021) 7 SCC 474.

[6] *Swiss Ribbons (P) Ltd. Vs. Union of India,* (2019) 4 SCC 17

[7] *Committee of Creditors, Essar Steel India Ltd. Vs. Satish Kumar Gupta* (2020) 8 SCC 531.2611_Judgement_18-Jan-2022.pdf)

credibility of the entire resolution process.

b) The word "person" used in Section 29A(h) of IBC includes a promoter and/or a director of the CD and there is no exclusion provided in any provision of IBC to these persons. Therefore, the persons mentioned in Section 29A alone were not eligible to be resolution applicants. No other person was barred from becoming a resolution applicant under IBC.

c) If a person executes a personal guarantee in favour of any creditor in respect of a CD and the creditor initiates CIRP against such CD and invokes the personal guarantee issued by such a guarantor, then the bar provided under Section 29A(h) of IBC will come into play, if the amount remains unpaid.

d) If there are more than one creditor, who are part of resolution process initiated against the CD, then invocation of personal guarantee by any one creditor will be sufficient to act as a bar against the guarantor under Section 29A(h) of IBC.

e) It is not necessary that each and every creditor should have invoked the personal guarantee given by the guarantor as the proceedings of CIRP are in rem. Therefore, all creditors, falling under the same class (financial creditors), will have the same rights, which are at par with such other creditors.

f) There could be a case, where an application is filed under Section 7 of IBC by one creditor, who also invokes the personal guarantee, while there could be other creditors in the same class, who did not file such application, but they became part of the resolution process on constitution of CoC. The SC observed that it could not be said that the rights of creditors, who became members of CoC at a later stage, were in anyway, inferior to the rights of the creditor, who had filed the application under Section 7 of IBC and/or invoked the personal guarantee given by the guarantor.

g) The ineligibility of the "person", who may submit a resolution plan, has to be seen from the point of view of the resolution process. It can never be said that there can be ineligibility vis-à-vis one creditor as against others. The ineligibility operates with regard to the "person", who is to submit the resolution plan, and not in relation to the creditors.

h) There can never be any other interest than that of the CoC and the CD. If there is a bar under Section 29A of IBC as on the date of submission of the resolution plan, then the resolution plan cannot be submitted by such a person. Even if such a bar under Section 29A of IBC becomes applicable at a later date before the resolution plan is accepted by CoC, then also the bar is applicable against such person and the CoC cannot accept such a resolution plan.

"The submission of resolution plan by a person does not create any right in his favour and no right gets extinguished, if the resolution plan is not accepted."

i) The submission of resolution plan by a person does not create any right in his favour and no right gets extinguished, if the resolution plan is not accepted. The resolution applicant is considered as a facilitator in the entire resolution process, the main pillars of resolution process being the CoC and CD.

j) It cannot be said that if the resolution applicant was not barred on day one of the CIRP, then he cannot be barred at a later date. The entire resolution process revolves around the interests of CoC, and CD and all decisions are to be taken as per law to safeguard their interests solely.

6. Conclusion of the SC with regard to Section 29A(h)

The SC concluded as follows:

a) In this case, the personal guarantee given to three financial creditors were invoked by them, even prior to filing of application for initiating CIRP. Therefore, the rigors of Section 29A(h) were attracted in such a case. Due to this reason alone, the ineligibility of resolution applicant was applicable with respect to all creditors (and not only to three creditors) in the same class. Ineligibility has to be seen from the point of view of the resolution process. It can never be said that there can be ineligibility qua one creditor as

against others. Rather, the ineligibility is to be seen in relation to the participation of a person in the resolution process of the CD.

b) Although the application under Section 7 of IBC was filed by one creditor, while the personal guarantee was invoked by other creditors, yet the bar under Section 29A(h) was squarely applicable in this case and the resolution applicant could not have submitted the resolution plan for the CD.

c) The AA and NCLAT were not correct in rejecting the contention of the appellants on the ground that the issue with regard to eligibility could not be raised for second time as all earlier appeals on this matter had been withdrawn.

d) Although the resolution plan submitted by the resolution applicant was ineligible, yet lot of time had gone by, when the matter came up before the SC, and the resolution applicant had already taken significant steps to provide funds for the CD and had also executed several projects of national importance and the CD was now a Going Concern.

e) It was also expected that the interests of all dissenting financial creditors had been addressed and no prejudice had been caused to them under the resolution plan as they would receive, at least, the liquidation value of their credit limits under the resolution plan approved by CoC.

f) The CoC had accepted the resolution plan by requisite majority and the AA has approved such resolution plan. Only the question relating to ineligibility of the resolution applicant was pending for final decision of the SC.

g) Considering the overall objective of IBC that being to put the business of CD back on track and in the light of significant steps taken by the resolution applicant to implement the resolution plan and ensuring that the CD remains a going concern, it was held that the resolution plan should not be disturbed at this stage and should be allowed to proceed further.

h) The SC specifically mentioned that such a decision was being made, considering the peculiar set of circumstances in this particular case, although as per the provision of Section 29A(h) of IBC, the resolution plan could not have been accepted by the CoC as the resolution applicant was ineligible.

7. Author's Views

The provisions of Section 29A of IBC have served as a big roadblock in the way of promoters, who had the keen desire to retain ownership and control of their enterprise even after defaulting on payments to creditors which resulted in initiation of resolution process against the enterprise. Many judgements pronounced by SC have dealt with this issue on multiple occasions wherein the waters were tested by "related parties" and/or "connected persons", who were desirous of becoming resolution applicants of CD.

"In this case, the SC pronounced an exceptional judgement to bring out the real intent and purpose of the amendments made in Section 29A(h) of IBC."

In this case, the SC pronounced an exceptional judgement to bring out the real intent and purpose of the amendments made in Section 29A(h) of IBC. Such elaborate consideration of all issues, which are related to the invocation of personal guarantee given by the guarantors to the creditors of CD, gives much needed guidance on this contentious issue. The effect of invocation of personal guarantee by any creditor in the same class and ineligibility of the guarantor of the CD from becoming a resolution applicant has been explained in great detail.

Although the resolution applicant did succeed, basis peculiar circumstances of this case, when the SC held that the resolution plan should not be disturbed at an advanced stage of implementation, yet this judgement will serve as a guiding light in all such cases, where the resolution applicants, specially the personal guarantors of CD whose guarantees have been invoked and they remain unpaid, suffer from inherent ineligibility right on day one of the resolution process or any time during the resolution process. It is expected that all the facilitators of resolution process will follow the guidelines laid down by the SC in this judgement whenever they are called upon to decide on Ineligible Resolution Applicant/s.