SC Judgement on Essar Steel Case

Why in news?

In a major judgement, the Supreme Court has paved the way for global steel giant ArcelorMittal to take over Essar Steel.

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What are the different types of creditors?

- The Companies Act, 2013 merely introduced the term 'creditor', without any classification thereof.
- The Insolvency and Bankruptcy Code (IBC) has introduced new concepts of 'Financial Creditor' and 'Operational Creditor' as opposed to the above.
- **Operational Creditor** is a person to whom an operational debt is owed and includes any person to whom such debt has been legally assigned or transferred.
- In other words, vendors and suppliers of raw materials, etc are the operational creditors.
- In Essar case, these were Dakshin Gujarat, Gujarat Energy, Bharat Petroleum, Indian Oil, GAIL, ONGC, and the NTPC.
- **Financial creditor** is any person to whom a financial debt is owed and includes a person to whom such debt has been legally assigned or transferred to.
- In simple terms, they are those who provide long-term capital in the form of loans.
- Public-sector lenders are Essar Steel's primary financial creditors.

What is the dispute?

- Essar Steel owes around Rs 54,500 crore to its creditors - financial creditors and operational creditors combined.
- The company had been put on the block under IBC to recover the unpaid dues.
- The Ahmedabad bench of National Company Law Tribunal (NCLT) had in March 2019 approved global steel-giant ArcelorMittal’s bid for Essar Steel.
- ArcelorMittal had offered an upfront cash payment of about Rs. 42,000 crore to the financial creditors and capital infusion of Rs. 8,000 in the next few

years.
- The operational creditors had opposed the bid on the basis that they were getting notional payment while 92.5% of the financial creditors' dues were being paid.
- **NCLAT Order** - The National Company Law Appellate Tribunal (NCLAT), in July 2019, had ordered equal distribution of funds among all classes of creditors.
- It ruled that operational creditors should be treated on a par with financial creditors for distribution of funds from ArcelorMittal's bid in the Essar Steel insolvency case.
- NCLAT had said all operational creditors including employees with claims below Rs. 1 crore were to recover 100% of their dues.
- Financial and operational lenders having claims above Rs. 1 crore were allowed to recover 60.7% of their total dues.
- As of July 2019, total debt in the Essar Steel case had inflated to around Rs. 69,000 crore following fresh claims by some operational creditors.
- The Committee of Creditors (CoC) had filed petitions against NCLAT's judgment. [The CoC includes all financial creditors.]
- [A consortium of banks (financial creditors) led by the SBI had moved the Supreme Court against the NCLAT order in the case.]
- The CoC challenged that it should recover more than operational creditors in the bankruptcy resolution process.

What is the SC judgement?

- The Supreme Court decision overrules NCLAT's July 2019 judgment.
- The verdict paves the way for ArcelorMittal's takeover of the bankrupt Essar Steel.
- The court said that the CoC will have a final say in the resolution plans under the Insolvency and Bankruptcy Code (IBC).
- The NCLT and NCLAT cannot interfere with the commercial decisions taken by the CoC.

Why is the judgement so significant?

- **Bankruptcy cases** - The insolvency and bankruptcy process is still young in India.
- There is a long way to go yet, especially in the matter of recovery percentages.
- Moreover, significant capital is locked up in bankrupt companies.
- Given these, these clarifications made in the judgement could help in quickening a number of other cases that are stuck in the insolvency courts.
- **Primacy** - The apex court has upheld the primacy of financial creditors over

operational creditors in the repayments process.

- [It is the financial creditors who provide capital to an enterprise and their interests are secured in the form of collaterals on the firm's assets.
- Operational creditors are unsecured creditors and they cannot claim equality or precedence over financial creditors.]
- The ruling clarifies that the CoC is supreme when it comes to deciding on commercial issues, including the repayment waterfall, in an insolvency resolution.
- [A waterfall payment is a repayment system by which senior lenders receive principal and interest payments from a borrower first, and subordinate lenders after.]
- **Time limit** - The apex court has also held that the 330-day limit for resolution is not sacrosanct.
- This will ensure that creditors are not pressured to accept a below-par deal due to paucity of time.
- **Banks** - With the go-ahead given to the sale of Essar Steel, banks could recover over 90% of the over Rs. 40,000 crore that the company owes them.
- Operational creditors are set to receive close to Rs. 1,200 crore.
- This should clearly help improve the financial position of weak public sector banks and boost profitability.

Source: The Hindu, Economic Times, Livemint

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