

TERMINATION OF CONTRACTS DURING THE MORATORIUM: LOOKING BEYOND THE ‘GOING CONCERN’ STATUS

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The resolution of distressed companies on a going concern basis is a cornerstone of the corporate insolvency resolution process (“CIRP”) introduced under the Insolvency and Bankruptcy Code, 2016 (“IBC”). This is critical to maintain the viability of the company, maximise the value of its assets and improve the likelihood of insolvency resolution. Section 14 of the IBC furthers this intent by instituting a moratorium from the date of commencement of the CIRP, until its conclusion. The moratorium prohibits persons in rem from undertaking certain actions against the corporate debtor, including the recovery of any property held by the corporate debtor and cessation of supply of goods and services critical for its operations.

The moratorium does not per se prohibit third parties from terminating contracts entered with the corporate debtor. However, insolvency tribunals have set aside the termination of lease agreements, supply contracts and other pre-existing arrangements with the corporate debtor, where termination would have the effect of breaching the moratorium or jeopardising the corporate debtor’s going concern status.

This paper examines judicial and legislative developments in the IBC in connection with termination of contracts from critical and comparative perspectives. The paper first examines the ambiguities in the scope of the moratorium provisions; and second, highlights that the IBC’s focus on the maintenance of the corporate debtor as a going concern often discounts hardships faced by contractual counterparties to the corporate debtor. Through a comparative study, the paper considers measures instituted in the United Kingdom and United States to balance the interests of such counterparties, while giving due regard to the overarching goal of insolvency resolution.

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I. INTRODUCTION

As businesses struggle with the impact of the COVID-19 crisis on their operations and revenue streams, there has been renewed focus on assessing the risk of financial distress and insolvency. The risk of insolvency is, however, neither a novel concept nor a remote one in the business world. To safeguard against this risk, parties to a contract typically incorporate *ipso facto* clauses in the agreement. These clauses allow a contracting party to terminate the agreement, suspend further credit or enforce other contractual remedies if the counterparty is faced with insolvency or other similar proceedings.

However, the right to suspend or terminate the contract may not be available to a contracting party, even if it is contractually stipulated through an *ipso facto* clause, where the counterparty is admitted into the corporate insolvency resolution process (“**CIRP**”) under Insolvency and Bankruptcy Code, 2016 (“**IBC**”). This is pursuant to the moratorium provision set out under Section 14 of the IBC, which bars third parties from *inter alia*, (a) recovering any property occupied by or in possession of the debtor company (called the “**corporate debtor**”);⁸⁹⁵ and (b) terminating, interrupting or suspending supply of critical goods and services to the corporate debtor, during the CIRP.⁸⁹⁶ These restrictions facilitate a key objective of the IBC – to maintain the corporate debtor as a going concern during the CIRP, in order to maximise the value of its assets⁸⁹⁷ and obtain better realisation from interested buyers.

⁸⁹⁵ Insolvency and Bankruptcy Code 2016 (IBC), s 14(1)(d).

⁸⁹⁶ IBC, ss 14(2) and 14(2A).

⁸⁹⁷ IBC, Preamble.

Notably, the moratorium provisions do not expressly bar the termination of contracts, which suggests that third parties may terminate contracts with debtors during the moratorium.⁸⁹⁸ However, where termination of the contract has the *effect* of either triggering the moratorium provisions mentioned above or preventing the corporate debtor from continuing as a going concern, insolvency tribunals have set aside the termination of contracts.⁸⁹⁹ In the fast-evolving landscape of the IBC, the moratorium has posed a variety of challenges. While third parties have sought to limit their exposure to companies admitted into CIRP, insolvency resolution professionals (“**RP**”)⁹⁰⁰ have sought to ensure that the corporate debtor has the requisite assets, goods and services to continue its operations.

This paper attempts to examine recent judicial and legislative developments under the IBC in this domain from a critical and comparative lens.⁹⁰¹ From a critical perspective, the paper *first*, examines the ambiguities in the scope of the moratorium provisions. *Second*, the paper argues that the narrow focus on the maintenance of the corporate debtor as a going concern under the IBC, both in legislation and judicial interpretation, discounts the hardships faced by contractual counterparties to the corporate debtor. Through a comparative study, the paper draws on measures instituted in the United Kingdom (“**UK**”) and the United States of America (“**United States**”) to balance the interests of such counterparties, without diminishing the overarching goal of insolvency resolution.

Redressal of these lacunae in the IBC is crucial, more so in the COVID-19 era, where economic data signals a steep contraction of the Indian economy.⁹⁰² In these extraordinary times, compelling cash-strapped businesses to perform contracts with companies under CIRP can have lasting detrimental effects on commercial operations – especially for small businesses. This makes an exploration of statutory safeguards for protection of such contractual counterparties a worthwhile endeavour. Added to this is the IBC’s aspiration to balance the interests of *all* stakeholders in the insolvency resolution process, which further fuels the spirit of this venture.⁹⁰³

⁸⁹⁸ See, for instance, *In the matter of Gujrat NRE Coke Limited* CP (IB) No 326/KB/2017 (NCLT Kolkata, 22 August 2017) where the insolvency tribunal allowed the termination of a contract for maintenance of certain windmills during the moratorium, due to failure of the corporate debtor to pay outstanding dues under the contract.

⁸⁹⁹ See, for instance, *Pepsico India Holdings Pvt Ltd v. Mr V Nagarajan* CP/564 (IB)/CB/2017 (NCLT Chennai, 28 May 2019); *Srei Infrastructure Finance Ltd v. Sundresh Bhatt* Company Appeal (AT) (Insolvency) No 781 of 2018 (NCLAT, 31 July 2019).

⁹⁰⁰ The resolution professional is a qualified insolvency professional appointed by the ‘committee of creditors’ constituted under the IBC. The resolution professional administers the CIRP and manages the operations of the corporate debtor until the CIRP is concluded.

⁹⁰¹ The scope of this paper has been limited to examination of contracts executed between the corporate debtor and non-government counterparties. Contracts with central/state governments or government authorities have not been discussed.

⁹⁰² National Statistical Office, Ministry of Statistics & Programme Implementation, ‘Press Note On Second Advance Estimates Of National Income 2020-21 And Quarterly Estimates Of Gross Domestic Product For The Third Quarter (Q3) Of 2020-21’ (2021) paras 5-8 <http://mospi.nic.in/sites/default/files/press_release/PRESS%20NOTE%20SAE%2026-02-2021.pdf> accessed 15 March 2021.

⁹⁰³ IBC, Preamble.

In this setting, section II of the paper undertakes a critical review of key caselaw dealing with termination of different kinds of contracts during the CIRP, including lease agreements and supply contracts. Section III deals with the introduction of Section 14(2A) in the IBC, which has empowered RPs to prevent termination of supply of goods and services which are in their view, “critical” to manage the operations of the corporate debtor as a going concern. Section IV comments on the recent trend in judicial decision-making, where courts and tribunals have prohibited the termination of contracts relying on the preamble and overarching goal of the IBC, rather than the express moratorium provisions. In each of these sections, the paper argues that the IBC moves in the right direction by protecting the interests of the corporate debtor, but falls short of addressing concerns of contractual counterparties to the corporate debtor. Section V briefly discusses jurisprudence on the payment of dues to counterparties compelled to continue contracts during CIRP and the section VI concludes the paper.

II. THE BAR ON RECOVERY OF PROPERTY

Section 14(1)(d) of the IBC prohibits the “*recovery of any property by an owner or lessor where such property is occupied by or in the possession of the corporate debtor.*” The provision is aimed at preventing owners and lessors from recovering “any property” from the corporate debtor from the date of commencement of CIRP until its formal conclusion. This includes both immovable property like land and building as well as moveable property like goods and equipment. Given the wide breadth of this provision, third parties have faced resistance from both RPs and insolvency tribunals where the termination of a contract is intertwined with the recovery of property held by the corporate debtor.

This section focuses on key caselaw under the IBC on the termination of three types of contracts during the moratorium: (a) contracts dealing with immovable property, (b) contracts vesting a license or right in respect of property in the corporate debtor, and (c) contracts dealing with moveable property. Through this discussion, the paper seeks to achieve a two-fold objective. *First*, an examination of this caselaw gives insight into judicial trends under the IBC in this domain and offers a review of evolving literature. *Second* and more crucially, the paper relies on the caselaw to critically examine Section 14(1)(d) of the IBC. To this end, sub-sections A and B examine judicial interpretation of Section 14(1)(d) and discuss the implications of a significant Supreme Court ruling on this provision. Sub-section C highlights that the current form of Section 14(1)(d) suffers from certain critical lacunae, much to the detriment of contractual counterparties to the corporate debtor.

A. Immoveable assets

The express language of Section 14(1)(d) prohibits the recovery of any property in the possession of the corporate debtor by a “lessor”. Given the express bar on recovery by lessors, insolvency tribunals have unwaveringly barred the termination of lease agreements executed

with the corporate debtor – holding such termination to be in clear violation of the moratorium.⁹⁰⁴

Outside of lease agreements, the Supreme Court has discussed the scope of Section 14(1)(d) in the context of immovable property in *Rajendra Bhutta*.⁹⁰⁵ Here, the court was dealing with the termination of a land development agreement, pursuant to which the Maharashtra Housing and Area Development Authority (“MHADA”) had granted the corporate debtor license to undertake development of certain land owned by the MHADA. The termination of this agreement during the moratorium was challenged by the RP. He argued that the termination would have the effect of allowing recovery of the MHADA property granted to the corporate debtor for development activities, in direct violation of the bar on such recovery under Section 14(1)(d). The Supreme Court allowed this appeal and clarified the scope and application of Section 14(1)(d) of the IBC.

It observed that in order to give proper effect to the language of Section 14(1)(d), the word “owner” must be read in conjunction with the expression “occupied by”, which refers to property which is *physically* occupied by the corporate debtor. In contrast, the word “lessor” should be read in conjunction with “in possession of”. This connotes *legal possession* being held by the corporate debtor and includes both actual possession and constructive possession⁹⁰⁶. Thus interpreted, Section 14(1)(d) bars an “owner” from recovering property when the corporate debtor is in physical occupation of such property, whereas “lessors” are barred from recovering property regardless of whether the debtor has physical or constructive possession under the lease agreement.

This view suggests that where a contract pertains to ownership of moveable property (such as goods and equipment) or immovable property outside the context of a lease, the court would simply examine whether the corporate debtor is in physical occupation of such property. In contrast, where the termination pertains to a lease agreement, the court will test whether the corporate debtor would be deprived of actual possession over the property, or constructive possession vested in it pursuant to the lease agreement.⁹⁰⁷ In the case before the Supreme Court, the development agreement was not in the nature of a lease. The court held that agreement vested the corporate debtor with a license to enter upon the property with a view to develop the property and undertake all actions thereon, and after such entry, the property had been physically occupied by it. Hence, the restriction under Section 14(1)(d) was attracted and MHADA was not entitled to terminate the development agreement.

⁹⁰⁴ *Navbharat Castings LLP v. Moser Baer India Ltd & Anr* Company Appeal (AT) (Insolvency) No 323 of 2018 (NCLAT, 30 July 2018); *Raj Builders v. Raj Oil Mills Limited Company Appeal* (AT) (Insolvency) No 304 of 2018 (NCLAT, 8 August 2018); *Srei Infrastructure Finance Ltd* (n 6).

⁹⁰⁵ *Rajendra K Bhutta v. Maharashtra Housing and Area Development Authority and Anr* Civil Appeal No 12248 of 2018 (Supreme Court, 19 February 2020).

⁹⁰⁶ Where, for instance, the right to exclusive possession has been granted contractually but has not been exercised.

⁹⁰⁷ See also, *Embassy Property Developments Pvt Ltd v. State of Karnataka & Ors* Civil Appeal No 9170 of 2019 (Supreme Court, 3 December 2019) where the Supreme Court observed that Section 14(1)(d) will not be applicable to the termination of a mining lease which granted the corporate debtor the right to mine, excavate and recover iron ore over certain area of land, but did not grant exclusive possession over said land.

B. Licenses and Contractual Rights in Property

The decision of the Supreme Court in *Rajendra Bhutta* appears to settle another hotly contested issue under the IBC – the reliance on Section 14(1)(d) to prevent the termination of licenses and usage rights which are vested in the corporate debtor in respect of a property. Notably, the IBC gives a non-exhaustive definition to the term “property” and includes within its scope both tangible property such as money, land and moveable property, as well as intangible “interest” arising in or incidental to any such property.⁹⁰⁸ Given this definition, National Company Law Tribunals (“NCLTs”) have held that the bar on recovery of “property” under Section 14(1)(d) will also prohibit third parties from depriving the corporate debtor of intangible interest granted to it in the form of licenses or usage rights in relation to a property.⁹⁰⁹

In *Rajendra Bhutta*, the court was presented with the argument that the license to enter the property created an “interest” in the land in favour of the corporate debtor, which would be covered within the ambit of “property” under Section 14(1)(d). The termination of the development agreement would therefore deprive the corporate debtor of “property” currently in its possession. However, the Supreme Court considered the question of grant of any “interest” in the property irrelevant to the facts of the case. It reiterated that Section 14(1)(d) speaks of recovery of property which is “occupied” by the corporate debtor i.e., property in physical possession of the corporate debtor and does not refer to any “right or interest” in the property.

While the court did not elaborate on this issue, the court’s reasoning suggests that the wide definition of the term “property” under the IBC is curtailed by the context in which the term is used in Section 14(1)(d). Since the provision only refers to property which is “occupied” by the corporate debtor or is in its “possession” pursuant to a lease, parties cannot rely on Section 14(1)(d) to argue against deprivation of intangible “interest” in a property.⁹¹⁰ It therefore stands to reason that third parties are *not* barred from terminating licenses or agreements granting specific rights in respect of a particular property to the corporate debtor during the moratorium. This view does not however apply to licenses or rights granted by government authorities, which are separately dealt with under the IBC⁹¹¹ and fall outside the scope of this paper.

⁹⁰⁸ IBC, s 3(27).

⁹⁰⁹ *Vasudevan v. State of Karnataka and Others* CP/39/2018 (NCLT Chennai, 3 May 2019) where the tribunal set aside the termination of a mining lease for iron ore, since the sole business of the corporate debtor was the right granted to mine iron ore; *Pepsico India Holdings* (n 6) where the termination of an exclusive manufacturing agreement with the corporate debtor by Pepsico India was set aside *inter alia*, on the ground that the termination would deprive the corporate debtor of “interest” granted to it over trademarks and designs of Pepsico India; *Vijaykumar V Iyer v. Union of India* CP (IB)-298/(MB)/2018 (NCLT Mumbai, 27 November 2019) where it was held that the Department of Telecommunication cannot terminate the telecom license granted to Aircel Limited during the CIRP, since the license is intrinsic to Aircel’s telecommunication business and its recovery would be in violation of the moratorium under Section 14(1)(d).

⁹¹⁰ Except in case of interest granted by way of constructive possession under a lease agreement since the Supreme Court has included constructive possession within the scope of “possession” under Section 14(1)(d).

⁹¹¹ See, explanation to Section 14(1) of the IBC which prohibits the central, state and local government, and any other authority constituted under law from terminating licenses, permissions, grants and other rights granted to a corporate debtor on the ground of its insolvency, provided that the corporate debtor has made requisite payments in respect of such rights during the moratorium.

C. Moveable Assets

The contours of the moratorium under Section 14(1)(d) as set out in the *Rajendra Bhutta* decision are equally applicable to moveable property. However, prior to the *Rajendra Bhutta* decision, NCLTs have taken conflicting views in relation to the recovery of moveable assets like raw material and equipment from the corporate debtor, during the moratorium. The following paragraphs discuss two decisions, i.e., the orders of NCLT, Chennai in *Pepsico*⁹¹² and NCLT, Chandigarh in *Weather Makers*⁹¹³ to illustrate this conflict. Though this discussion, the paper identifies key lacunae in Section 14(1)(d) and considers feasible recommendations to address these shortcomings.

In *Pepsico*, the NCLT dealt with the termination of a manufacturing contract and recovery of certain equipment provided to the corporate debtor by Pepsico India Holdings Private Limited (“**Pepsico**”). Incidentally, the sole business of the corporate debtor was manufacturing, processing and packaging of goods for Pepsico, which were further distributed under certain trademarks licensed by Pepsico to the corporate debtor. The tribunal noted that the legislative notes to Section 14 explain that the moratorium is instituted to ensure that the corporate debtor is able to operate as a going concern during the CIRP and therefore, any action which frustrates the resolution process is prohibited under the IBC. Thus, Section 14 will require “*a contextual and purposive interpretation*” to give effect to the legislative intent. Since the business of the corporate debtor had an intrinsic link with the manufacturing contract terminated by Pepsico, the termination of the contract would effectively frustrate the CIRP since no buyers would submit a resolution plan to rescue the company.⁹¹⁴ Pepsico was barred from terminating the contract and recovering the equipment supplied to the corporate debtor. On appeal, the National Company Law Appellate Tribunal (“**NCLAT**”) reaffirmed this view.⁹¹⁵ The NCLAT order however warrants a separate examination and has been analysed in greater depth in section IV.

In contrast to *Pepsico*,⁹¹⁶ NCLT Chandigarh allowed suppliers to recover certain raw material and equipment in *Weather Makers*,⁹¹⁷ by carving out an exception to Section 14(1)(d). The NCLT examined the breadth of Section 18(f) of the IBC, which *inter alia* requires the interim RP⁹¹⁸ to take control and custody of assets *owned* by the corporate debtor. Notably, the explanation to the provision states that the term “assets” excludes assets which are owned by a third party, but are in possession of the corporate debtor under trust or contractual arrangements. The NCLT held that there was a “*fine distinction*” between the areas of operation of Sections 14 and 18 of the IBC – while the moratorium provision under Section 14(1)(d) covered a wide range of “property” and provided for the general rule barring recovery from the

⁹¹² *Pepsico India Holdings* (n 6).

⁹¹³ *Weather Makers Pvt Ltd and Ors v. Parabolic Drugs Ltd and Ors* CP (IB) No 102/Chd/CHD/2018 (NCLT Chandigarh, 26 April 2019, 26 July 2019 and 11 September 2019).

⁹¹⁴ See also, *Vasudevan* (n 16); *Vijaykumar V Iyer* (n 16).

⁹¹⁵ *Pepsico India Holdings Pvt Ltd v. V Nagarajan, Resolution Professional of Oceanic Tropical Fruits Pvt. Ltd.* Company Appeal (AT) Insolvency No. 686 of 2019 (NCLAT, 13 November 2019).

⁹¹⁶ *Ibid.*

⁹¹⁷ *Weather Makers Pvt Ltd* (n 20).

⁹¹⁸ The interim RP is the insolvency professional appointed by the NCLT upon the commencement of CIRP to manage the operations of the corporate debtor and the CIRP. The interim RP forms the committee of creditors, which replaces the interim RP with the RP.

corporate debtor, a narrower exception to this rule was later carved out in the explanation to Section 18, with the effect that the RP does not have control over assets held by the corporate debtor under trust or contractual arrangements. These assets are therefore exempt from the moratorium provision. Since both the raw material and the equipment were not owned by the corporate debtor but were provided to it under contractual arrangements, they would fall within the exception to the moratorium carved out under Section 18 of the IBC. This decision was reaffirmed by the NCLAT.⁹¹⁹

The approach adopted by the NCLT in *Weather Makers*⁹²⁰ highlights that as Section 14(1)(d) currently stands, there is no exception to the bar on recovery of assets within the provision itself. While the NCLT's attempt to carve out an exception is laudable, the exception itself runs afoul of the language of the provision and the goal of the moratorium. To begin with, though the NCLT considered the applicability of Section 18 to be "*more appropriate*" to the issue, Section 18 deals with the *duties of the interim RP* and provides the series of actions which the interim RP is required to take upon the initiation of CIRP. Among other actions, the provision requires the RP to collect information regarding assets of the corporate debtor to assess its financial health. Since the assets held by the corporate debtor under trust or contractual arrangements will not be considered in valuing the corporate debtor, the provision provides for a specific exclusion of such assets by the RP. Section 18 thus deals with the assets of the corporate debtor, whereas Section 14(1)(d) deals with assets owned by third parties, which are held by the corporate debtor. Further, neither Section 18 nor the definition of "*assets*" therein makes any reference to the moratorium under Section 14 – calling to question the connection drawn by the NCLT between these provisions. The inapplicability of Section 18 to the moratorium was also highlighted by the Supreme Court in *Rajendra Bhutta*, where it observed that Section 14(1)(d) does not pertain to assets of the corporate debtor and therefore, a reference to Section 18 of the IBC is "*wholly unnecessary*" in deciding the scope of Section 14(1)(d). This view of the Supreme Court would preclude third parties from placing reliance on the rationale in *Weather Makers* to seek recovery of their assets during CIRP.

The second criticism to the exception in *Weather Makers* stems from the language of Section 14, which bars "*recovery of any property by an owner or lessor*". A plain reading suggests that the provision seeks to prevent owners and lessors, i.e., third parties, from recovering property held by the corporate debtor during the moratorium. Since corporate debtors will usually hold property belonging to a third party under trust or contractual arrangements, the exclusion of such arrangements from the purview of the moratorium renders the exception as wide as the rule itself. Third, the purpose of the moratorium is two-fold – to give the corporate debtor a breathing spell from its troubles by imposing a statutory *status quo* and to facilitate its operation as a going concern.⁹²¹ The bar on recovery of assets which are held under contractual arrangements is crucial to achieve this, since the loss of key assets will disrupt the operations of the corporate debtor and plunge its value.

⁹¹⁹ *Orbit Lifesciences Private Limited v. Raj Ralhan, PwC professional Services LLP Company Appeal (AT) (Insolvency) No 846 of 2019 (NCLAT, 4 February 2020).*

⁹²⁰ *Ibid.*

⁹²¹ Insolvency and Bankruptcy Code Bill, 2015, Notes on Clauses, p. 118, <https://www.prsindia.org/sites/default/files/bill_files/Insolvency_and_Bankruptcy_code,_2015.pdf> accessed 15 March 2021.

Yet, there is merit to the argument that there should be exceptions to the rule barring recovery, albeit not as wide as the exception carved out in *Weather Makers*. At present, Section 14 does not empower the RP to surrender any third party property held by the corporate debtor, even if such property is not required for the operations of the corporate debtor – for instance, where the operations have been downscaled or where the asset is perishable and has no foreseeable use. For third parties, this issue is compounded by the fact that the IBC does not impose any specific obligations on the RP to preserve the assets of third parties and there may be little incentive for the RP to incur incremental expenses in the CIRP for ensuring such maintenance.

Viewed from this perspective, a sweeping ban on the recovery of assets during the moratorium may not always be necessary and instead, may be harmful to owners and lessors. Carving out a suitable exception to the rule under Section 14(1)(d) is critical to ensure that the IBC accounts for interests of such third parties.

Illustratively, the moratorium provisions applicable to administrations⁹²² in the UK allow for recovery of assets with: (a) the consent of the insolvency representative,⁹²³ or (b) the permission of the court.⁹²⁴ Similarly, bankruptcy law in the United States prevents the insolvency representative from continuing a contract unless defaults in the underlying contract (including payment defaults) are cured or adequate assurance to this end is provided by the insolvency representative.⁹²⁵ These measures have ensured that third parties have some form of recourse to seek recovery of their assets, or otherwise minimise risk through payment of outstanding dues and performance of contractual obligations by the corporate debtor.

In the Indian context, the model followed in the United States appears less feasible. It will require RPs to cure all defects in the contract in order to seek its continuation. This is a difficult feat to achieve since RPs will *first*, need to raise interim finance from banks or other lenders to cure any payment defaults subsisting under the contract. This will also result in the corporate debtor making out-of-turn payments to select operational creditors with whom it seeks to continue contracts – a significant departure from the current framework under the IBC where all operational creditors receive pay-outs only once the CIRP, or alternatively liquidation, has concluded. *Second*, the RP will need to have suitable manpower, expertise and tools to cure any other non-performance under the contract, such as a breach in the manufacture of contractually stipulated quantities under a production contract.

Instead, the legislative framework in the UK appears more aligned with the Indian regime. In adopting this, the IBC can empower RPs to give consent for recovery of assets, where such recovery would have little bearing on the corporate turnaround. Illustratively, the RP may allow termination of an agreement for lease of equipment where the equipment is neither utilised for

⁹²² The administration process in the UK is akin to CIRP under the IBC and involves placing the debtor company under the control of an insolvency practitioner to enable revival as a going concern, or liquidation where the sale of the company's assets would achieve better realisation.

⁹²³ In this paper, insolvency representative refers to the insolvency practitioner (including one appointed on an interim basis) who supervises the debtor company's activities and is authorised to administer the reorganisation of the debtor in the referenced jurisdiction. The insolvency representative is akin to the RP under IBC.

⁹²⁴ Insolvency Act 1986, Schedule B1, Paragraph 43.

⁹²⁵ 11 U.S.C, Title 11, Bankruptcy Code, s 365(b)(1).

the ongoing operations of the corporate debtor nor critical to maximise its value. Alongside, the IBC can provide judicial recourse to third parties, where: (a) the RP is hesitant to permit recovery of a particular asset without the blessing of the insolvency tribunal; or (b) exceptional circumstances support the recovery of property, such as concerns regarding maintenance of the asset or a threat of significant depletion in its value. This will allow insolvency tribunals to give due regard to the interests of the counterparties to the corporate debtor.

III. SUPPLY OF CRITICAL GOODS AND SERVICES

In addition to the prohibition on the recovery of property under Section 14(1)(d), third parties are prohibited from terminating, suspending and interrupting the supply of “essential goods and services”⁹²⁶ to the corporate debtor under Section 14(2) of the IBC. The expression “essential goods and services” has been defined narrowly under the Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations 2016 (“**CIRP Regulations**”) and refers only to four supplies, namely electricity, water, telecommunication services and information technology services.⁹²⁷ The four supplies are considered basic requirements for any corporate debtor to remain a going concern and are not meant to be supplied in large quantities to make a commercial profit.⁹²⁸

In practice, NCLTs have not only restored the supply of these items to the corporate debtor, but have gone beyond the scope of this provision to order continuation of other supplies which were considered critical to the operations of the corporate debtor.⁹²⁹ In a report examining issues in implementation of the IBC⁹³⁰ (“**February Report**”), the Insolvency Law Committee (“**ILC**”)⁹³¹ noted that insolvency tribunals were being approached by RPs to seek continuation of various goods and services on a case-by-case basis. The ILC concluded that the four specified supplies may not be sufficient to run the corporate debtor as a going concern and other “critical” supplies, such as input supplies, may be required.⁹³² It also noted that private negotiations with suppliers to continue existing contracts during the CIRP were not always successful, especially where supplies are not easily replaceable and existing suppliers demand “ransom payments” to keep up supply.⁹³³

The ILC suggested that the IBC be amended to provide flexibility in determination of which goods and services may be considered essential to the operations of the corporate debtor.⁹³⁴ The introduction Section 14(2A) to the IBC gives legislative effect to this view and allows RPs

⁹²⁶ IBC, s 14(2).

⁹²⁷ To the extent that such supplies are not a direct input to the output produced by the corporate debtor.

⁹²⁸ Insolvency and Bankruptcy Board of India, *Discussion Paper on Corporate Insolvency Resolution Process*, p. 2 <<https://ibbi.gov.in/uploads/whatsnew/b6be2f41ed8a1b8f4ac1ed2838ac9fcc.pdf>> accessed 15 March 2021.

⁹²⁹ For instance, the supply of printing ink, printing plates, printing blankets and solvents has been included in “essential goods and services” where the company was in the business of print media (*Canara Bank v. Deccan Chronicle Holdings Limited* CP No IB/41/7/HDB/2017 (NCLT Hyderabad, 19 July 2017)).

⁹³⁰ Ministry of Corporate Affairs, *Report of the Insolvency Law Committee* <http://www.mca.gov.in/Ministry/pdf/ICLReport_05032020.pdf> accessed 15 March 2021.

⁹³¹ The ILC is a standing committee of experts in the field of insolvency law, appointed by the Ministry of Corporate Affairs, Government of India to act as an advisory body in connection with issues pertaining to the implementation of the IBC.

⁹³² *Ibid* 38.

⁹³³ *Ibid*.

⁹³⁴ *Report of the Insolvency Law Committee* (n 37) 40; *Discussion Paper* (n 35) 4.

to prevent the termination of supply of goods and services, which they consider “critical to protect and preserve the value of the corporate debtor and manage the operations of such corporate debtor as a going concern”. However, suppliers need not continue to supply to the corporate debtor if the debtor fails to pay for supply during the moratorium period.⁹³⁵ While more clarity on the implementation of this amendment is awaited, a recent discussion paper suggests that where the RP considers a particular supply to be critical, she will be required to submit an application to the relevant NCLT for this purpose and obtain a declaration that a particular good or service is essential and should continue during the moratorium period.⁹³⁶

A. Ambiguities in the Amendment

Neither the IBC nor the proposed amendments to the CIRP Regulations provide any guidance to determine which supplies would be considered “critical”. Illustratively, will critical supplies be limited to aircrafts and fuel in the airlines business? Or will they also extend to maintenance and ground staff services? Will the supply be “critical” if the corporate debtor can arrange engage alternate suppliers? What if engagement of alternative supply is not time efficient? Different stakeholders may construe the scope of the term “critical” differently. The ILC has recommended that RPs should consider factors such as whether the supplies have a significant and direct relationship with keeping the corporate debtor operational, and whether the supplies may be replaced easily. However, these yardsticks have not been incorporated into the amended law. This has rendered the scope of critical supplies ambiguous and its interpretation, subject to judicial discretion.

While an exhaustive list of critical supplies would defeat the goal of the amendment, clear legislative yardsticks to assess the scope of critical supplies are still required. Such guidance will allow suppliers and resolution professionals to *inter se*, determine whether a particular supply can be terminated and avoid formal adjudication mechanisms. This will save time and costs in the resolution process and ease the caseload on insolvency tribunals. Where parties approach insolvency tribunals for a formal decision, such yardsticks can introduce uniformity and predictability in adjudication.

B. Absence of assurance of payment

As means of protection to critical suppliers, Section 14(2A) requires the corporate debtor to make payments for goods and services received during the CIRP. In case the corporate debtor fails to make due payments, suppliers are entitled to terminate supply. While this provides a remedy *after* a default in payment has occurred, suppliers are not provided any formal assurance of payment to keep up supplies. Critical suppliers therefore have no option but to carry the daunting risk of default by the corporate debtor, much like the Sword of Damocles. This risk is compounded where the contract contemplates payment of goods after completion of delivery of goods or performance of service, or where payments are made in specific time cycles rather than on a current basis.⁹³⁷

⁹³⁵ IBC, s 14(2A).

⁹³⁶ Ibid.

⁹³⁷ United Nations Commission on International Trade Law, *Legislative Guide on Insolvency Law* (2005) 127 <https://uncitral.un.org/sites/uncitral.un.org/files/media-documents/uncitral/en/05-80722_ebook.pdf> accessed 15 March 2021.

Other jurisdictions offer more concrete protections to critical suppliers, such as assurance of payment in the form of guarantees or other agreed means⁹³⁸ and personal liability of the insolvency representative for payment of supplies.⁹³⁹ These features ensure that critical suppliers are guaranteed payment despite the insolvency of the corporate debtor, and protects them from economic loss in case the corporate debtor suffers commercial or operational setbacks during the resolution process. The UNCITRAL Legislative Guide on Insolvency Law (“**UNCITRAL Guide**”) also supports the inclusion of statutory protection for critical suppliers. It mentions that a policy in this regard should weigh a number of factors, including the importance of the contract to the proceedings, the cost to the proceedings for providing the necessary protections, whether the debtor will be able to perform the obligations under a continued contract and the impact of forcing the counterparty to assume the risk of non-payment.⁹⁴⁰

In the Indian context, incorporation of protections for critical suppliers can not only offer requisite comfort to such suppliers, but also encourage non-critical suppliers to continue “business as usual”, enhancing the value and viability of the corporate debtor. From a legislative perspective, it may be worthwhile to consider leveraging the IBC’s creditor-driven framework to seek assurance of payment. Where the committee of creditors (“**COC**”) constituted to spearhead the CIRP considers the corporate debtor to be a viable enterprise, a financial creditor in the COC can provide assurance in the form of a bank guarantee, letter of credit or other agreeable means on behalf of the corporate debtor. The financial creditor need not bear this liability alone – the COC members may *inter-se* bear the cost of such assurance, proportionate to their voting rights.⁹⁴¹ Any expenses incurred upon invocation of such payment assurance can be recouped as part of “insolvency resolution process costs” (“**IRP Costs**”), which are regarded as senior debt and paid in priority to all other dues of the corporate debtor.⁹⁴²

First, this mechanism will ensure that dues payable to critical suppliers for provision of goods and services during the moratorium are not impacted due to the CIRP. *Second*, in case the bank guarantee, letter of credit or other assurance provided by a financial creditor is invoked, such amount can be justifiably included in IRP Costs, since it would correspond to costs duly incurred towards procurement of critical supplies for the operations of the corporate debtor.

Notably, this mechanism may be more feasible for a COC comprising of banks and financial institutions. For a small company where there are few to no financial creditors on the COC, it may be difficult to arrange for such assurance to keep up supply. Therefore, for cases where formal means of assurance of payment are not viable, the IBC may consider other statutory protections, such as a requirement for advance payment for procurement of critical supplies. The aforementioned suggestions are however drawn from a comparative study and

⁹³⁸ 11 U.S.C, Title 11, Bankruptcy Code, s 365(b).

⁹³⁹ Insolvency Act 1986, s 233 (UK).

⁹⁴⁰ *Legislative Guide on Insolvency Law* (n 44) 127.

⁹⁴¹ See for instance, *Newgrowth Credit Private Limited v. Resolution Professional, Bhaskar Marine Services Private Limited & Ors.* Company Appeal (AT) (Insolvency) No. 1053 of 2020 (NCLAT, 10 December 2020) where the NCLAT directed a financial creditor on the COC to bear its share of the IRP Costs as agreed by the COC.

⁹⁴² See, section V below for further discussion on IRP Costs.

seek to conceptualise the statutory protections which may be feasible in the Indian insolvency framework. Any imposition of financial liability as part of the insolvency resolution process would naturally require careful deliberation.

C. Exceptions to Continuation of Supply

In some instances, continuing the supply of goods and services to the corporate debtor may not be commercially feasible for suppliers, especially small businesses. For instance, if the terms of payment were negotiated at a discount relying on future projections (such as an annual increase in purchase volumes by the corporate debtor), such projections may no longer hold true. The supplier will need to revisit the contract to ensure that continuation of supply at discounted rates will not impact its own commercial viability. A similar assessment may also be required if the supplier faces some other hardship, for instance, due to the impact of the COVID-19 pandemic on its business. The IBC, however, does not create any exceptions to the mandate for continuation of critical supply. By forcing performance, it exposes critical suppliers to insolvency risk. As recourse, it may be open to suppliers to renegotiate key terms of the contract with the RP, since renegotiations of existing contracts is not barred under the IBC. This, however, is merely a contractual remedy and such negotiations will remain at the discretion of the RP.

This emphasises the need for legislative measures allowing for suspension or termination of critical supplies in exceptional circumstances. To this end, the IBC may empower insolvency tribunals to suspend or terminate a critical supply or pass other appropriate directions, where the supplier is able to establish that continuation of supply would cause hardship. The insolvency framework in the UK follows this approach.⁹⁴³ This ensures that there is a balancing of interests between the maintenance of the corporate debtor as a going concern and the hardship faced by the counterparty to further this goal. The IBC is yet to account for these contingencies or undertake a balancing of interests of this nature.

There is no doubt that the introduction of Section 14(2A) in the IBC will aid corporate debtors in obtaining a continuous supply of goods and services from key suppliers. However, ambiguities in the language of the amendment and the absence of adequate protection for critical suppliers warrants further legislative reforms.

IV. EXPANDING THE SCOPE OF THE MORATORIUM

The discussion above suggests that as a general rule, courts and tribunals assess the validity of a contract terminated during the moratorium in light of the language and scope of Section 14 of the IBC. Outside of Section 14, the IBC does not contain express provisions that bar third parties from undertaking actions against the corporate debtor. More recent judicial development, however, highlights a second, more discretionary approach adopted by tribunals while dealing with termination of contracts. In at least four instances,⁹⁴⁴ tribunals have set aside

⁹⁴³ Insolvency Act 1986, s 233A(4).

⁹⁴⁴ *Pepsico India Holdings* (n 6); *Yes Bank Limited v. Gujarat Urja Vikas Nigam Ltd* CP (IB) No. HI/07/HDB/2017 (NCLT Hyderabad, 6 May 2020); *Astonfield Solar (Gujarat) Private Limited v. Gujarat Urja Vikas Nigam* CP. No. (IB)-940(ND)/2018 (NCLT Delhi, 29 August 2019); *Tata Consultancy Services v. Vishal Ghisulal Jain Company* Appeal (AT) Insolvency No. 237 of 2020 (NCLAT, 24 June 2020) upholding the order of NCLT

the termination of a contract by placing reliance on the overarching goal of the IBC – the maintenance of the corporate debtor as a going concern. This trend raises concerns of judicial activism, especially since these decisions were not grounded under any express provisions of the IBC. In fact, two of these decisions are in the context of liquidation,⁹⁴⁵ where the moratorium is far narrower than Section 14 and only bars the initiation of suits or legal proceedings by or against the corporate debtor.⁹⁴⁶

At the heart of this trend is the *Astonfield*⁹⁴⁷ case, where a dispute regarding the validity of termination of a power purchase agreement (“PPA”) during the moratorium reached the Supreme Court. The discussion below dissects the developments in this domain and examines the implications of the Supreme Court’s ruling.

A. Saving critical contracts

In *Astonfield*,⁹⁴⁸ the corporate debtor (Astonfield Solar (Gujarat) Private Limited) was solely engaged in the business of generation of power for Gujarat Urja Vikas Nigam Limited (“GUVNL”) under the terms of a PPA. The PPA embodied an *ipso facto* clause which provided that the initiation of insolvency proceedings against the corporate debtor would constitute an event of default under the PPA. If such default was not cured within 30 days from the delivery of notice of default, GUVNL would be entitled to terminate the PPA. Relying on this provision, GUVNL issued a default notice to the corporate debtor upon initiation of its CIRP and thereafter terminated the agreement.

The RP challenged this termination before NCLT, Delhi which set aside the default notices and the termination of the PPA on two grounds. *First*, the tribunal noted that GUVNL was the sole purchaser of the power generated by the corporate debtor. Termination of its singular purchase contract would cause serious prejudice to the maintenance of the corporate debtor as a going concern and jeopardise its resolution, since no resolution applicants would submit a resolution plan without the assurance of a subsisting PPA to generate future revenue. *Second*, the NCLT observed that the *ipso facto* clause under the PPA compelled the corporate debtor to exit the CIRP within 30 days of issue of the notice of default, or otherwise face termination of the PPA. The IBC however statutorily provides a period of 330 days for completion of resolution. Given the conflict between the terms of the PPA and the IBC, the NCLT held that the IBC would prevail over the PPA by virtue of Section 238 of the IBC, which grants overriding effect to the IBC over such agreements. Therefore, the *ipso facto* clause under the PPA was not available to GUVNL to terminate the PPA. On appeal, the NCLAT reaffirmed this view, emphasising that there had been no default in the supply of the electricity to GUVNL by the corporate debtor and the PPA could not be terminated *solely* on the basis of initiation of CIRP.⁹⁴⁹ A further appeal was filed before the Supreme Court. Before venturing into the

Mumbai in *BMW India Financial Services Private Limited v. SK Wheels Private Limited* CP. (IB) 4301/2018 (NCLT Mumbai, 18 December 2019).

⁹⁴⁵ See, IBC, s 33(5).

⁹⁴⁶ While this paper is focused on the termination of contracts during the moratorium, these cases are relevant to establish the judicial trend which places reliance on the overarching goal of the IBC to bar termination of contracts.

⁹⁴⁷ *Astonfield* (n 51).

⁹⁴⁸ *Ibid.*

⁹⁴⁹ *Gujarat Urja Vikas Nigam Ltd v. Mr. Amit Gupta* Company Appeal (AT) Insolvency No. 1045 of 2019 (NCLAT, 15 October 2019).

Supreme Court's ruling on this issue, it is useful to briefly discuss the *Yes Bank*⁹⁵⁰ case – another instance where the termination of a PPA by GUVNL was set aside, this time in the context of liquidation.

The *Yes Bank* case involved a PPA executed between the corporate debtor (Lanco Infratech Limited) and GUVNL for supply of power to GUVNL. When the corporate debtor entered into liquidation, GUVNL issued a notice of default under the PPA solely on this ground and thereafter terminated the PPA. The corporate debtor's power plant had been built by availing financial assistance from Yes Bank Limited to the extent of INR 63.5 crores, which was secured by a charge over all moveable and immovable assets of the power plant. Yes Bank challenged the termination of the PPA relying on the preamble to the IBC and argued that the termination would prevent the maximisation of value of the assets of the corporate debtor, since the plant would be rendered unviable for sale as a going concern without a subsisting PPA. The NCLT was persuaded by this argument. It noted that the termination of the PPA directly affected the security interest of Yes Bank, in that it would not be able to realise the maximum value from the secured assets. The NCLT therefore set aside the termination of the PPA, observing that the tribunal "*has to see the object of the Code, which is maximisation of value of the asset.*" In October 2020, the NCLAT reaffirmed this decision.⁹⁵¹ This ruling is unusual since, as mentioned above, the moratorium under the liquidation process only bars the initiation of suits or legal proceedings by or against the corporate debtor.⁹⁵² No prohibition on the termination of contracts is expressly or impliedly imposed at this stage.

Both the *Astonfield* and *Yes Bank* decisions barred the termination of PPAs, *inter alia*, on the ground that the corporate debtor *should* be maintained as a going concern to ensure resolution under the IBC. A similar view was also taken in respect of another PPA by NCLT, Kolkata and subsequently reaffirmed by the NCLAT.⁹⁵³ The PPA, however, is in the nature of a contract for supply of power *by* the corporate debtor to a third party to generate income. It is neither barred under the moratorium imposed under Section 14 of the IBC (which deals with supplies *to* the corporate debtor), nor under liquidation provisions of the IBC. By placing reliance on the preamble to the IBC and its overarching goal, the aforementioned decisions concretise the view that tribunals will prohibit termination of contracts where it can be proved that the contract is critical to attempt a successful resolution.

⁹⁵⁰ *Yes Bank* (n 51).

⁹⁵¹ *Gujarat Urja Vikas Nigam Ltd v. Yes Bank Limited*, Company Appeal (AT) (Insolvency) No. 601 of 2020 (NCLAT, 20 October 2020).

⁹⁵² See, IBC, s 33(5).

⁹⁵³ *Hemant Khaitan v. Alex Green Energy Private Limited CP (IB)* No. 1439/KB/2018 (NCLT Kolkata, 14 October 2019); *GRIDCO Limited v. Surya Kanta Satapathy and Ors* Company Appeal (AT) (Insolvency) No. 1271 of 2019 (NCLAT, 14 July 2020) where both NCLT, Kolkata and the NCLAT held the termination of a PPA to be in contravention of Section 14(1) of the IBC, without specific analysis of the provisions. The NCLAT decision can be distinguished from *Astonfield* above, since the ruling was largely based on the invalidity of the termination notices and the lack of objection by GRIDCO Limited (the terminating party) to finalisation of a resolution plan premised on the subsistence of the PPA. The decisions however highlight that tribunals did not specifically examine *how* the termination of the PPA contravened Section 14 of the IBC.

However, it is a settled position of law that the preamble to a legislation or its legislative intent can neither be relied upon to override the express provisions of the legislation,⁹⁵⁴ nor to give new meaning to the plain words of the statute.⁹⁵⁵ The Indian Supreme Court has categorically held that the preamble cannot be the starting point for construing the provisions of the legislation and should be resorted to only if the language of the legislation is unclear.⁹⁵⁶ An examination of contracts on a case-by-case basis in light of the preamble thus contravenes an established principle of interpretation of statutes. It also instils considerable unpredictability in the law and diminishes the sanctity of contractual bargains – especially for counterparties seeking to assess whether contractual remedies agreed under the contract are available to them. If greater flexibility to tribunals is to be granted, clear legislative amendments to the moratorium provisions of the IBC should be made.

This view also finds support in the Supreme Court decision in *Astonfield*.⁹⁵⁷ In its ruling, the court gave regard to the fact that the PPA was of “enormous significance” for the success of the corporate debtor’s insolvency resolution.⁹⁵⁸ At the same time, the court took cognizance of rolling effects of judicial intervention in setting aside commercial agreements. *First*, reaffirming the decision of the NCLT to set aside the PPA would open floodgates for intervention by insolvency tribunals in negotiated commercial contracts. In the absence of any statutory basis, this would undermine foundational principles of contract law and the sanctity of commercial bargains. *Second*, there was no express embargo under the IBC against the enforcement of *ipso facto* clauses in commercial agreements. Section 14 of the IBC only stays their operation in case of: (a) licenses, permits and legal rights granted by Central, state or local governments or other government authorities;⁹⁵⁹ and (b) the supply of critical goods and services.⁹⁶⁰

The court noted that in the absence of clear legislative guidance on the enforceability of *ipso facto* clauses in the Indian insolvency regime, its intervention would need to be guided by legislative intent – derived from the provisions of the IBC. The court reiterated that the moratorium provisions under the IBC are intended to preserve the corporate debtor as a going concern. It also observed that the legislature had amended Section 14 on several occasions to ensure that the going concern status of the corporate debtor was not impeded by circumstances which were not contemplated during the introduction of the IBC. Thus noting, it held that the NCLT’s intervention in the matter was justified bearing in mind the goal of preservation of the corporate debtor during the CIRP. However, there needed to be a “textual hook” for the NCLT to have exercised its jurisdiction – mere spirit or overarching objective of the IBC would not suffice.

⁹⁵⁴ *Burrakur Coal Co. Ltd v. The Union of India and Others* AIR 1961 SC 954; *Motipur Zamindari Co. (Private) Limited v. State of Bihar* AIR 1962 SC 660; *Arnit Das v. State of Bihar* (2000) 5 SCC488; *Union of India v. Elphinstone Spinning and Weaving Co. Ltd.* (2001) 4 SCC 139; *State of Rajasthan and Ors v. Basant Nahata* (2005) 12 SCC 77.

⁹⁵⁵ *Ibid*, *Motipur Zamindari Co. (Private) Limited*.

⁹⁵⁶ *Ibid*, (*Burrakur Coal Co.*).

⁹⁵⁷ *Gujarat Urja Vikas Nigam Limited v. Mr. Amit Gupta & Ors* Civil Appeal No. 9241 of 2019 (Supreme Court, 8 March 2021).

⁹⁵⁸ *Ibid*.

⁹⁵⁹ IBC, explanation to s 14(1).

⁹⁶⁰ IBC, explanation to ss 14(2), 14(2A).

Recognising the gap in the NCLT's ruling, the court placed reliance on Section 60(5)(c) of the IBC. This provision vests the NCLT with wide residuary powers to adjudicate on any question of law or fact "arising out of or in relation to" the insolvency resolution process, notwithstanding anything to the contrary contained in any other law in force. Since the PPA was terminated solely on account of the insolvency of the corporate debtor, the matter arose out of the insolvency of the corporate debtor and was connected with it. It would therefore squarely fall within the jurisdiction of the NCLT under Section 60(5)(c). Thus, on both jurisdiction and merit, the court found the NCLT's decision to set aside the termination of the PPA valid. Notably, the appellants had strongly contended that Section 14 of the IBC clearly established the scope of the moratorium and there was no statutory basis for the NCLT to adjudicate on the validity of the PPA's termination. Dismissing this contention, Supreme Court observed that "*residuary jurisdiction under Section 60(5)(c) would be rendered otiose if Section 14 is held to be the exhaustive of the grounds of judicial intervention contemplated under the IBC in matters of preserving the value of the corporate debtor and its status as a going concern.*"⁹⁶¹

The Supreme Court's ruling is pragmatic, having stitched together a quick fix to resolve a gaping void in the moratorium provisions of the IBC. There is no doubt that some degree of flexibility is required under the IBC to deal with contracts which are critical to the corporate debtor, but are not covered within the ambit of the moratorium under Section 14. However, contrary to recent judicial trend, reliance on the overarching objective of the IBC to maintain the corporate debtor as a going concern is unfounded in law. The Supreme Court ruling recognises the absence of a legal basis for the NCLT's intervention. In effect, the ruling provides NCLTs with statutory grounds for adjudicating on such matters, so long as the termination is connected with the insolvency of the corporate debtor. To RPs, it gives the option to seek a stay on the termination of contracts critical for the revival of the corporate debtor, where the moratorium under Section 14 would not come to their aid.

At the same time, the ruling recognises that such judicial recourse could open a Pandora's box – allowing NCLTs to rely on residuary powers to exercise complete judicial discretion in dealing with the termination of contracts. It therefore casts clear restrictions on the exercise of judicial intervention under Section 60(5)(c) in this regard. *First*, the termination of a contract must have nexus with the insolvency of the corporate debtor. Such nexus would be established, for instance, where a contract is terminated based on an *ipso facto* clause, pursuant to initiation of CIRP of the corporate debtor.⁹⁶² Without a nexus between the termination of the contract and the insolvency of the corporate debtor, the NCLT cannot rely on its residuary jurisdiction.⁹⁶³ This will allow counterparties to validly terminate the contract where the corporate debtor is in breach of contract, irrespective of whether or not the contract is critical to the going concern status of the corporate debtor. *Second*, the termination of the contract *must* lead to certain 'corporate death' of the corporate debtor, i.e. the contract should be critical for resolution of its insolvency. This is a high threshold to satisfy. In fact, the ruling expressly

⁹⁶¹ *Astonfield, Supreme Court* (n 64).

⁹⁶² *Ibid* 132.

⁹⁶³ *Ibid*.

mentions that where termination of the contract would merely lead to dilution of the value of the corporate debtor, intervention by the NCLT will not be justified. This means that insolvency tribunals cannot set aside the termination of a contract for value maximisation of the corporate debtor, contrary to judicial trend.⁹⁶⁴

Thus, as the law currently stands, contractual counterparties to the corporate debtor will now need to assess legal risks associated with termination of contracts in a two-step process. At the outset, they will need to assess whether the termination of the contract would trigger the moratorium under Section 14. If the termination is not barred by the express moratorium provisions, parties will need to assess whether: (a) the termination has a nexus with the insolvency of the corporate debtor; and (b) the contract is critical for the survival of the corporate debtor. If the answer to both these prongs is in the affirmative, there may be likelihood of a challenge to the termination of the contract.

B. What about liquidation?

In the concluding paragraphs of the judgement in *Astonfield*,⁹⁶⁵ the Supreme Court mentions that it would not adjudicate on the question of whether the termination of the PPA would have been valid in case the corporate debtor was in liquidation. It considered this question purely academic since the corporate debtor was under CIRP.⁹⁶⁶ Yet, more clarity on this issue would have helped interpret discretionary rulings by tribunals in cases where contracts are terminated during liquidation.

For instance, in the *Yes Bank*⁹⁶⁷ case discussed in sub-section A above, the NCLAT set aside the termination of the PPA in order to maximise the value of the corporate debtor and protect the interests of its financial creditor, Yes Bank. In the *Pepsico*⁹⁶⁸ case as well, the NCLAT set aside the termination of a manufacturing and supply agreement during the liquidation of the corporate debtor. Similar to the PPAs discussed in sub-section A above, this was the sole customer contract of the corporate debtor. Here, the tribunal grounded its decision in the NCLAT's decision of *Shivram Prasad*,⁹⁶⁹ noting that even during the liquidation process, the liquidator "is to ensure" that the corporate debtor remains a going concern. Failing such sale, the liquidator would be forced to sell the assets of the corporate debtor piecemeal. Only at this stage would Pepsico be entitled to terminate the contract and recover its equipment.

However, unlike Section 14, there is no provision in respect of the liquidation process under the IBC which is focussed on the preservation of the corporate debtor as going concern during liquidation. Further, neither the Supreme Court in *Astonfield* nor the NCLAT ruling in *Shivram Prasad* manifest this intent. In *Shivram Prasad*, the NCLAT had held that the liquidator *should*

⁹⁶⁴ See, *Yes Bank* (n 51); *BMW India Financial Services* (n 51); *Tata Consultancy Services* (n 51) where the NCLAT set aside the termination of an agreement for provision of certain services to Tata Consultancy Services Limited to ensure "smooth functioning" of the corporate debtor, to further its operation as a going concern and preserve the value of its assets. Note that this NCLAT decision is pending in appeal before the Supreme Court (*Tata Consultancy Services Limited v. Vishal Ghisulal Jain* Civil Appeal No 3045/2020).

⁹⁶⁵ *Gujarat Urja Vikas Nigam, Supreme Court* (n 64).

⁹⁶⁶ *Ibid* 135.

⁹⁶⁷ *Yes Bank, NCLAT* (n 58).

⁹⁶⁸ *Pepsico India Holdings, NCLAT* (n 22).

⁹⁶⁹ *Y Shivram Prasad v. S Dhanpal & Ors, Company Appeal (AT) (Insolvency) No. 224 of 2018 (NCLAT, 27 February 2019)*.

take steps to revive the corporate debtor even at the liquidation stage, first by attempting to enter into a scheme of arrangement under Section 230 of the Companies Act, 2013 and failing so, attempting to sell the corporate debtor as a going concern. If both these attempts to revive the corporate debtor fail, the assets of the corporate debtor may be liquidated.⁹⁷⁰ While the decision encourages revival of the corporate debtor during liquidation, it does not make it an *obligation* on the liquidator to ensure that the corporate debtor remains a going concern.

In fact, the ILC specifically deliberated whether NCLTs should mandate liquidators to conduct a going concern sale in the February Report and noted that this may not be feasible in some situations, for instance where the business of the corporate debtor is found to be economically unviable or there is lack of funds to continue operations.⁹⁷¹ It concluded that the choice to proceed with a going concern sale of the business of the corporate debtor should vest with the liquidator, in consultation with the committee of creditors and other stakeholders.⁹⁷² Thus, the active facilitation of preservation of a debtor's going concern status by insolvency tribunals has the potential to cause more harm than good, especially to counterparties compelled to continue contracts with an unviable corporate debtor. Notably, GUVNL has filed an appeal against the NCLAT decision in the *Yes Bank* case, which is currently pending adjudication before the Supreme Court.⁹⁷³ This ruling will perhaps shed light on the validity of termination of contracts during the liquidation process, providing much needed clarity in this domain.

V. PAYMENT OF DUES ARISING DURING THE MORATORIUM

This section of the paper briefly reflects on the legislative framework and evolving jurisprudence on the payment of dues to contractual counterparties for performance of contracts during the moratorium. Recognising that third parties are critical in keeping the corporate debtor afloat during the CIRP, the IBC classifies the costs incurred by the RP in making payments to such third parties as IRP Costs. IRP Costs are regarded as senior debt and are paid in priority to all other dues of the corporate debtor upon the successful conclusion of the CIRP⁹⁷⁴ and failing resolution, during the liquidation.⁹⁷⁵ The CIRP Regulations expressly include the amounts due to: (a) persons who are prejudicially affected due to the bar under Section 14(1)(d); and (b) suppliers of essential goods and services, within IRP Costs.⁹⁷⁶ Further, a residuary provision has been incorporated to cover "any costs" incurred by the RP in running the corporate debtor within the purview of IRP Costs,⁹⁷⁷ thus including any amounts paid by the corporate debtor for other critical supplies, or amounts which are which are not expressly covered within (a) or (b) above.

⁹⁷⁰ This view has been incorporated into law under Regulation 2B and Regulation 32 of the Insolvency and Bankruptcy Board of India (Liquidation Process) Regulations 2016.

⁹⁷¹ *Report of the Insolvency Law Committee* (n 37), 72-73.

⁹⁷² *Ibid.*

⁹⁷³ *Gujarat Urja Vikas Nigam Limited v. Yes Bank Limited & Anr* Civil Appeal No. 3956/2020.

⁹⁷⁴ IBC, s 30(2)(a).

⁹⁷⁵ IBC, ss 52(8), 53(1)(a).

⁹⁷⁶ CIRP Regulations, regulation 31.

⁹⁷⁷ *Ibid.*

Typically, the RP makes payments to lessors, suppliers and other contractual counterparties on a current basis during the moratorium period. Insolvency tribunals have followed this approach and directed RPs to make payments accrued to suppliers during the moratorium, where such payments were not being made.⁹⁷⁸ The NCLAT has also gone a step further and allowed suppliers to terminate essential supplies such as electricity, where the RP is unable to pay the dues accruing during the moratorium on a current basis.⁹⁷⁹ The absence of funds for essential supplies indicates that the corporate debtor is so far in debt that there is little hope of rescue. The developing caselaw under the IBC thus suggests that insolvency tribunals will stand in favour to termination of contracts for critical supplies, if the corporate debtor is unable to pay dues on a current basis.

It is also worth noting that unlike the bankruptcy process followed in the United States, there is no obligation on the RP to make payments for outstanding sums before continuing with a contract during the moratorium. The arrears of payments due to lessors and suppliers for the period *prior* to the commencement of CIRP are not considered a part of IRP Costs. Rather, these dues must be filed as claims with the RP, along with other creditors of the corporate debtor.⁹⁸⁰ This rule has been applied by tribunals strictly, with NCLAT decisions holding that suppliers cannot apply payments received from the RP during the moratorium towards satisfaction of dues outstanding for the period prior to insolvency.⁹⁸¹ This means that suppliers cannot negotiate any out-of-turn payments with the RP, as consideration for continuation of supply under the IBC.

Given the discussion above, contractual counterparties to the corporate debtor can draw comfort from the fact that the IBC requires that at the very least, the dues payable for provision of services during the CIRP are paid to them on an on-going basis. In case the corporate debtor defaults in making such payments, insolvency tribunals have permitted third parties to terminate the underlying agreements.

VI. CONCLUSION

The moratorium provisions under the IBC play a key role in protecting the corporate debtor and facilitating a successful resolution. While this can pose significant obstacles for third

⁹⁷⁸ *Innoventive Industries Ltd v. Maharashtra State Electricity Distribution Co. Ltd* Company Appeal (AT) (Insolvency) No 156 of 2017 (NCLAT, 6 October 2017); *Uttarakhand Power Corporation Ltd v. ANG Industries Ltd* Company Appeal (AT) (Insolvency) No 298 of 2017 (NCLAT, 24 January 2018); *Dakshin Gujarat Vij Co Ltd v. ABG Shipyard Ltd* Company Appeal (AT) (Insolvency) No. 334 of 2017 (NCLAT, 8 February 2018); *JAS Telecom (P) Ltd v. Eolane Electronics Bangalore (P) Ltd* Company Appeal (AT) (Insolvency) No. 37 of 2018 (NCLAT, 21 March 2018); *In the matter of Rave Scans Pvt Ltd* (IB)-01(PB)-2017 (NCLT Principal Bench, 17 October 2018); *Asset Reconstruction Company (India) Ltd v. R Venkatakrishnan and Ors* Company Appeal (AT) (Insolvency) No. 232 of 2019 (NCLAT, 23 July 2019).

⁹⁷⁹ *Uttarakhand Power Corporation Ltd* (n 85); *Innoventive Industries* (n 85) where the NCLAT allowed the electricity board to take 'appropriate steps' in case of failure of the RP to make payments on a current basis.

⁹⁸⁰ *Andhra Bank v. Oracle Home Textile Ltd* CP(IB)-1842/(MB)/2018 (NCLT Mumbai, 7 May 2019); *JAS Telecom (P) Ltd; Innoventive Industries* (n 85).

⁹⁸¹ *Indian Overseas Bank v. Dinkar T. Venkatsubramaniam Resolution Professional for Amtek Auto Ltd* Company Appeal (AT) (Insol) No. 267 of 2017 (NCLAT, 15 November 2017); *MSTC Limited and Ors v. Adhunik Metalliks Ltd* Company Appeal (AT) (Insol) No. 519 of 2018 (NCLAT, 15 March 2019); *Asset Reconstruction Company (India) Ltd* (n 85); *JSW Steel Ltd and Ors v. Mahender Kumar Khandelwal and Ors* Company Appeal (AT) (Insol) Nos 957 of 2019 (NCLAT, 17 February 2020); *Vijay Kumar V Iyer v. Bharti Airtel Ltd* Company Appeal (AT) (Insol) No.530 & 700 of 2019 (NCLAT, 30 July 2020).

parties, it is encouraging to see that the jurisprudence on Section 14 is evolving to take the concerns faced by third parties into account. There is still however a need for re-evaluation of these provisions. The current language of Section 14(1)(d) does not provide exceptions to the bar on recovery of property. Similarly, Section 14(2A) does not clarify the scope of which goods and services would be considered “critical” to the corporate debtor and does not provide adequate statutory protections to critical suppliers, despite compelling them to keep up supplies. These issues have been compounded by the recent trend in judicial decision-making, where tribunals have set aside the termination of contracts by relying on the overarching goals of the IBC rather than the express moratorium provisions. The Supreme Court decision in *Astonfield* offers some respite to third parties in this regard.

While the success of a law is greatly enhanced by its efficiency and predictability, these ambiguities in the moratorium provisions often render the termination of contracts during CIRP subject to the views of insolvency tribunals, decided on a case-to-case basis. It is important therefore, to empower the RP to deal with the assets of third parties as may be feasible, and to build in protections for third parties continuing contracts with the corporate debtor. The need for these legislative changes also finds support of the UNCITRAL Guide, which recommends that insolvency laws should define the scope of powers granted to the insolvency representative to deal with on-going contracts of the debtor and should identify the types of contract that should be excepted from the exercise of these powers.⁹⁸² Incorporation of these nuances in the IBC will go a long way to truly balance the interests of “all stakeholders” in the insolvency process.

⁹⁸² *Legislative Guide on Insolvency Law* (n 44) 132.