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Noida is an Operational Creditor, as the Supreme Court differentiates between nature of Creditors under IBC

New Okhla Industrial Development Authority v. Anand Sonbhadra

Citation	Civil Appeal No. 2222/2021
Date	17 May 2022
Court	Supreme Court of India
Coram	Hon'ble Mr. Justice K.M. Joseph, Hon'ble Mr. Justice Hrishikesh Roy

1. FACTUAL MATRIX AND PROCEDURAL HISTORY:

- 1.1 A contract was entered into between NOIDA (**“Appellant”**) and the Corporate Debtor (**“Respondent”**) vide which a bid was floated and a lease for a plot was granted for a period of 90 years. It was the Appellant’s position that it shall be considered to be a financial creditor under the scope of Insolvency & Bankruptcy Code, 2016 (**“IBC”**) even though it was undisputed that it had not classified the lease with the Respondent as a financial lease.
- 1.2 A Corporate Insolvency Resolution Process (**“CIRP”**) was initiated against the corporate debtor in lieu of the amount due to the Appellant. A claim was filed in National Company Law Tribunal (**“NCLT”**) via Form-B as an Operational Creditor. Subsequently, NOIDA filed its claim in Form-C alleging to be a Financial Creditor in hopes for getting a seat in the committee of creditor and sought a voting share.
- 1.3 The Hon’ble adjudicating Authority, National Company Law Appellate Tribunal (**“NCLAT”**) found that the lease deed did not have any clause relating to the transfer of ownership. There was an underlying transfer of right to sub lease but ownership of the land per se was not transferred and thus the disputed lease cannot be termed as a financial lease as per the Indian Accounting standards and hence the appellant cannot be termed as a financial creditor.

2. ISSUE:

- 2.1 Whether the appellant is entitled to be treated as a financial creditor within the meaning of the IBC?

3. CONTENTIONS OF APPELLANT:

- 3.1 The Appellants contended that there was a substantial transfer of the risks and rewards incidental to ownership from the lessor to the lessee owing to the lessee’s discretion to fix any amount of consideration it deems fit from the buyer which is an element of paramount importance that existed when determining the existence of a financial lease.
- 3.2 The Respondent was given an option of upfront payment of premium along with interest and deed was financial in nature hence the dues constituted a financial debt u/s 5(8) of the IBC.
- 3.3 Lease also involved “deemed disbursement” by virtue of a financial facility thus giving a commercial effect of a borrowing u/s 5(8)(f) of the IBC.
- 3.4 The Appellant has a statutory duty to carry out planned development and group housing and thus has to regulate activities in order to ensure construction is being carried out in accordance with the laws. Also the appellant being a statutory authority has a responsibility towards the public as well.
- 3.5 The Financial creditors play a dominant role in the decision making of Committee of Creditors (**“CoC”**) that is responsible for the formation of the resolution plan thereby making it responsible for the destiny of all financial and operational creditors. Since the CoC is filled with homebuyers it is likely that the issues of the appellant would not be addressed and it would be unfair for it to be treated as an outsider when such a huge claim is at stake.

4. CONTENTIONS OF THE RESPONDENT:

- 4.1 The Respondent submitted that the appellant has never demarcated the said lease as a financial lease in its books since the date of commencement. The classification is mandatory as per objectives of Indian Accounting Standards 116 and u/s 133 of the Companies Act which provides for penalty on non-compliance.
- 4.2 The terms of the lease were unilateral and titled in favour of the lessor, as it does not take into consideration the interest of the lessee and deprives it of rewards it is entitled to as lessee is not permitted to assign leasehold interest, there is restrictive shareholding, no possibility of renewal of lease, no option for the respondent to opt out/terminate the contract, in terms of mortgage any increase value of the property would be at the disposal of the lessor in terms of unearned profits.

5. JUDGEMENT OF THE SUPREME COURT:

- 5.1 In this landmark judgement, the Supreme Court held that NOIDA isn't a financial creditor as a lease agreement with restrictive clauses cannot be determined as a financial lease leasing of a plot with a restrictive clause didn't amount to finance lease relied on *Asea Brown Boveri Ltd v. Industrial finance Corporation of India and Others*¹ and definitions under *Lease Financing & Hire Purchase by Dr. JC Verma*². Recourse shall be taken to section 5(8)(d) of IBC and Rule 62 & 65 of Indian Accounting standards to determine what shall be deemed as a financial lease. As a liability should be arising from the said lease.
- 5.2 Reliance has also been placed on case of *Phoenix Arc Pvt Ltd. V. Ketulbhai Ramubhai Patel*³ where it was argued that when there is absence of disbursement which is a primary element of the Section 5(8)(f) reliance cannot be placed on the same.
- 5.3 Case of *Pioneer Urban Land and Infrastructure Limited v. Union of India*⁴ it was argued that when there is absence of disbursement which is a primary element of the Section 5(8)(f) reliance cannot be placed on the same and elaborates on the principle that a claim for unliquidated damages cannot be concluded as a debt unless damages and liabilities are adjudicated by a court of law.
- 5.4 The appellant would be considered an operational creditor due non-existence of transaction that has commercial underpinning. As per Rule 63 of the Indian accounting standards said that a lease would be given a financial status if its terms are for the major portion of economic life of the underlying assets, transfer of title not being a pre-requisite. As between the lessor and lessee and the underlying would be the plot of land. Appellant's position in this case is very peculiar as their primary argument is rejected in view of Section 5(8)(f) of the IBC as the premium paid cannot be considered to be money raised by the lessee. The appeal was therefore dismissed.

6. PSL Opinion:

- 6.1 The Insolvency & Bankruptcy Code, 2016 still being in its infancy stage is prone to misinterpretations. The dire need to be treated as a financial creditor and become a part of the CoC, interferes with the rightful claims of other stakeholders under the guise of Section 5(8)(f). But this judgement leaves the ball in court of the stakeholders of such real estate projects who have smaller though substantial claims to take

¹ *Asea Brown Boveri Ltd v. Industrial finance Corporation of India and Others*, (2004) 12 SCC 570.

² *Lease Financing & Hire Purchase*, 4th Edn., 1999 at p. 33.

³ *Phoenix Arc Pvt Ltd. V. Ketulbhai Ramubhai Patel*, (2021) 2 SCC 799.

⁴ *Pioneer Urban Land and Infrastructure Limited v. Union of India*, (2019) 8 SCC 416.

decisions in the CoC leaving behind authorities like Noida from patronizing and having the need of influencing and/or channelizing the CIRP unfairly. If Leases were started to be treated as amount raised by the lessee instead of simple rentals or premium, half of the population in the country would be debt ridden. The crux and scope of a contract cannot be changed as per the convenience of the parties.

- 6.2 It is pertinent to note that NCLT and NCLAT were right in their judgement of pronouncing NOIDA as an operational creditor as they fail to fall within the ambit of Financial Creditor under section 5(7) of IBC.