

IBC: A decade of exclusion

The treatment of operational creditors defies constitutional principle, economic logic, and global practice

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The Bankruptcy Law Reforms Committee (BLRC), legislature, and judiciary have consistently reinforced a singular proposition: The corporate insolvency resolution process (CIRP), under the Insolvency and Bankruptcy Code (IBC), 2016, belongs to financial creditors (FCs). Their commercial wisdom is paramount and largely beyond challenge. Operational creditors (OCs) appear in the Code largely as subjects of exclusion. A decade of implementation reveals the consequences: FCs recovered 38 per cent of admitted claims exclusive of realisations from avoidance transactions and personal guarantors, compared with 10 per cent for OCs in 2024-25.

OCs are not a homogeneous class. They include governments, workmen, employees, and trade vendors, most of which are micro, small and medium enterprises (MSMEs). In liquidation, MSMEs stand at the bottom of the waterfall. While disaggregated recovery data is unavailable, recoveries for trade creditors appear negligible.

This outcome was not inevitable. In *Swiss Ribbons* (2019), the Supreme Court noted that in percentage terms, OCs had actually recovered slightly more than FCs did, and that tribunals had consistently ensured comparable treatment. The position changed after the July 2019 amendment placed the distribution of resolution proceeds within the purview of the committee of creditors' (CoCs) commercial wisdom. Upholding the amendment later that year, the Supreme Court effectively insulated differential payments of creditor classes from meaningful review. Since then, recoveries for suppliers have fallen from parity to statistical irrelevance.

A basic principle of game theory separates the power to divide a pie from the power to choose a slice. The IBC collapses the two. It empowers FCs to decide how the resolution proceeds are shared, including their own

share, while denying OCs both the vote and a remedy against an adverse allocation. Commercial wisdom may justify business decisions, not self-allocation of value. This is a textbook conflict of interest: The party deciding the distribution is its principal beneficiary.

The asymmetry is reinforced by procedural barriers. Since 2020, the default threshold to initiate the CIRP has been ₹1 crore. While most FCs easily clear this bar, many MSMEs do not. Even where they do, OCs must first issue a demand notice, which can be easily thwarted by a claim of "pre-existing dispute", however tenuous. They are also excluded from initiating the pre-packaged and creditor-initiated insolvency processes.



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The law vests authority in a CoC composed solely of FCs. The constitutional justification is weak. Article 14 permits classification only where it rests on an intelligible differentia, and that differentia must bear a rational nexus to the object of the law. The FC-OC divide struggles on both counts.

The IBC rests on the premise that financial debt embodies the time value of money while operational debt does not. This distinction is difficult to sustain as an intelligible differentia. Every business understands that a rupee today is worth more than a rupee tomorrow. A supplier that charges a higher price for credit sales than for cash sales prices time value no less than a lender charging interest on a loan. The economic substance is identical. Only the contractual form differs.

The nexus requirement fares no better. The BLRC and subsequent jurisprudence justify FC primacy on the grounds that they are best-positioned to rescue distressed firms. This misreads the object of the law. The IBC is not a rescue statute. Its objective is the resolution of insolvency, whether through a resolution plan or through liquidation, whichever is efficient.

Nor is it evident why the FC-OC distinction advances that objective. Resolution requires assessing enterprise value, operational viability, market prospects, and stakeholder interests. Suppliers routinely make such assessment in the ordinary course of business. They extend trade credit, evaluate counterparties, monitor performance, and bear commercial risk. Commercial wisdom is more likely to reside in OCs, active participants in commerce, than in many FCs, which merely hold financial claims.

The nexus argument fares no better even if one accepts the mistaken premise that rescue is the objective. Two assumptions are commonly invoked. First, FCs are said to possess superior commercial wisdom. The evidence is unpersuasive. More than half the companies admitted into the CIRP end up in liquidation, mostly because no resolution plan is received. More tellingly, a significant proportion of companies sent to liquidation later survive through going-concern sales or restructuring, suggesting that viability assessments are far from being infallible. The outcomes hardly support the claim that lenders possess a unique ability to identify firms worth saving.

Secondly, FCs are said to be uniquely capable of deferring recovery in the larger interests of rescuing a business, whereas OCs would press for immediate payment. The evidence points the other way. Approved resolution plans overwhelmingly provide FCs immediate cash exits rather than long-term participation in the revived enterprise. If rescue requires sacrificing present recovery for future value, lenders have demonstrated no special commitment to that objective.

The FC-OC classification, therefore, fails twice over. The distinction lacks a convincing economic basis, and, even if accepted, it bears no rational nexus either to the true objective of the Code, resolution, or to the narrower objective of rescue invoked in its defence.

The IBC's organising axis is unusual. Insolvency regimes worldwide recognise the priority of secured creditors, but few make the financial-operational divide the centrepiece of the process. In the United States, OCs often dominate the trade creditors' committee and vote on reorganisation plans. In the United Kingdom and under the Legislative Guide of the United Nations Commission on International Trade Law, the distinction is between secured and unsecured claims, not between lenders and suppliers. In these jurisdictions OCs have a voice. Under the IBC, they are largely voiceless.

The inconsistency is striking. The IBC's individual insolvency framework does not mandate a committee composed exclusively of FCs, proving that the FC-OC divide is a policy choice rather than an operational necessity.

Secured creditors deserve priority, but priority is not supremacy. The IBC has evolved into a regime where FCs not only dominate the process but also determine how the insolvency estate is divided, including the share they receive. Few areas of law permit such a convergence of power and self-interest. The time has come to ask whether lender control has gone too far, and whether a value-maximising process remains legitimate when those most affected are denied a meaningful voice.

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