
POWER WITHOUT PRIORITY: RETHINKING DISCOM'S POSITION AS OPERATIONAL CREDITORS UNDER THE INSOLVENCY AND BANKRUPTCY CODE

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ABSTRACT

Electricity Distribution Companies, commonly referred to as DISCOMs, play a crucial role in facilitating domestic, industrial, and commercial activities by providing essential services that underpin market operations. However, despite their critical role, DISCOMs are situated near the bottom of the liquidation priority hierarchy, as specified in Section 53 of the Insolvency and Bankruptcy Code (IBC) of 2016. This classification raises serious concerns about the low recovery rates that DISCOMs experience and the significant financial challenges they face. This paper presents a comprehensive critical analysis of the tensions between the statutory obligations imposed on DISCOMs requiring them to deliver uninterrupted services and the limited priority granted to them under Section 53 of the IBC, where they are categorised as operational creditors. Additionally, it aims to clarify the legal standing of DISCOMs within the structure of the National Company Law Tribunal (NCLT) and the broader IBC framework. This exploration will involve a detailed review of pertinent statutes and the evolving judicial interpretations that have emerged over time, illuminating their impact on DISCOM operations. Furthermore, this paper aims to propose practical reforms designed to establish a more balanced framework. Such reforms would seek to reconfigure the statutory obligations placed on DISCOMs, ensuring they are designed to effectively address and balance the pressing recovery needs of these entities. Through this dual approach of analysis and reform, the paper strives to contribute meaningfully to the ongoing discourse regarding the financial sustainability of DISCOMs in India.

Keywords: DISCOMs, Insolvency and Bankruptcy Code, 2016, NCLAT, Electricity Act, 2003, CIRP

INTRODUCTION:

Electricity is an essential pillar of modern life, intricately integrated into our daily routines. From the moment we wake and prepare our first meal to the last light we switch off at night, our dependence on this resource is undeniable¹. It illuminates our homes, powers our cooling systems, preserves our food through refrigeration, and drives the countless electronics and machinery that enhance our activities.

As the backbone of a robust economy, electricity fuels industries, supports healthcare facilities, and provides comfort in households. At the centre of this complex supply chain are Distribution Companies, or DISCOMs, which serve as the critical final link, ensuring electricity reaches every corner of society. While predominantly state-owned, with some private operators, it also plays a crucial role in shouldering the responsibilities of electricity distribution, network management, billing, and customer service. However, the electricity sector is not without its challenges. DISCOMs face a range of ongoing issues that lead to significant financial losses, impacting not only their operations but also casting a long shadow over the energy landscape and affecting the availability and reliability of electricity for millions across the nation.²

When scrutinizing the details of the Insolvency and Bankruptcy Code, it becomes clear that Distribution Companies (DISCOMs) are regarded on equal terms with any other trade creditor. This situation introduces a significant challenge, particularly as the state requires these companies to continue supplying essential services, such as electricity, regardless of the uncertainty surrounding payments. Unfortunately, the protections afforded to DISCOMs under insolvency law are minimal in cases of default. This leads to a crucial question: Should entities that provide vital public goods like electricity be deprioritised in their recovery efforts simply because they are classified as unsecured creditors? This issue highlights the complex dynamics between regulatory obligations and the essential need for a consistent power supply.

Therefore, this research aims to investigate whether the existing insolvency regime truly supports the financial stability of the DISCOMs. Additionally, the study will explore ways to reconcile the conflicts of laws and priorities through doctrinal clarity, judicial interpretation, or legislative reform. It will outline a comprehensive framework for reassessing the status of

¹ Bahman Zohuri, *Electricity, an Essential Necessity in Our Life*, 1 SPRINGER PUB. CO. 17, 17-33 (2016).

² Vishal Singh Patyal, Ravi Kumar, Kuldeep Lamba, Sunil Maheshwari, *Performance evaluation of India electricity distribution companies: An integrated DEA-IRP-TOPSIS approach*, 124 ELSEVIER 1, 1-2 (2023)

DISCOMs under the Insolvency and Bankruptcy Code (IBC), acknowledging their vital economic role while ensuring their protection.

LEGAL POSITION OF DISCOMs IN NCLT: THE JUDICIAL APPROACH:

Under the Insolvency and Bankruptcy Code (IBC), Distribution Companies (DISCOMs) are categorized as operational creditors, as outlined in Section 5 (20)³ of the Act. When a company undergoes the winding-up process, it initiates a liquidation phase governed by the IBC. At the core of this process is Section 53⁴, which establishes a waterfall mechanism for asset distribution during liquidation. This mechanism specifies a hierarchy among creditors, positioning DISCOMs beneath not only secured creditors but also the dues owed to workmen. Consequently, DISCOMs find themselves in a precarious situation, particularly in financial distress scenarios.

In sharp contrast, the Electricity Act imposes a crucial obligation on DISCOMs through Sections 43⁵ and 44⁶, mandating them to provide a continuous supply of electricity. This requirement creates a complex dilemma, as the conflicting mandates of both statutes leave these distribution companies in a state of uncertainty. Despite routinely facing payment defaults from consumers and businesses, DISCOMs are still required to fulfil their supply obligations due to stringent regulatory demands. This dual burden places them in an inequitable position, forcing them to navigate the challenges of financial instability while ensuring reliable access to electricity for consumers.

Court and tribunals, through various precedents, have consistently upheld the classification of DISCOMs as operational creditors without any relief given; those precedents include:

1. Paschimanchal Vidyut Vitran Nigam Ltd. v. Raman Ispat Private Limited⁷:

This landmark precedent primarily addresses the priority of claims during liquidation proceedings. PVVNL, a state-owned electricity distribution company, had an agreement with RIPL for the supply of electricity. However, when RIPL entered

³ The Insolvency and Bankruptcy Code, 2016, § 5 (20).

⁴ The Insolvency and Bankruptcy Code, 2016, § 53.

⁵ The Electricity Act, 2003, § 43.

⁶ The Electricity Act, 2003, § 44.

⁷ Paschimanchal Vidyut Vitran Nigam Ltd. v. Raman Ispat Private Limited, 2023 SCC OnLine SC 842 (2023) (India)

insolvency proceedings, PVVNL sought to assert its claims as a creditor for the unpaid electricity bills.

In this case, the Supreme Court affirmed that Section 238⁸ of the Insolvency and Bankruptcy Code (IBC), which outlines the Code's overriding effect, takes precedence over the Electricity Act of 2003, even though the latter is considered a special Act. PVVNL claimed the status of a secured creditor based on a clause in its electricity supply agreement. The court acknowledged that such a clause could create a charge, thereby qualifying PVVNL as a secured creditor. Nevertheless, even as a secured creditor, PVVNL was obligated to file its claim during the liquidation process under the IBC, which it failed to do. Consequently, PVVNL can no longer demand priority or seek recovery outside the framework of the IBC.

2. Uttarakhand Power Corporation Limited v. ANG Industries Ltd.⁹:

Uttarakhand Power Corporation Limited (UPCL), the electricity provider for ANG Industries Limited, took the decisive step to disconnect the power supply due to the company's failure to settle its outstanding dues. In response to this action, ANG Industries sought relief by filing for insolvency proceedings under the Insolvency and Bankruptcy Code (IBC). The National Company Law Tribunal (NCLT) reviewed the application, admitted it, and subsequently imposed a moratorium, effectively halting any unilateral enforcement actions by creditors. This moratorium was instituted to allow the corporate debtor to stabilize its operations amid financial distress.

As a result, the moratorium precluded UPCL from pursuing the recovery of any pre-CIRP dues outside the designated insolvency proceedings. However, the power corporation retained the right to submit a formal claim to the Resolution Professional (RP) for these outstanding amounts. The NCLT took proactive measures to ensure that electricity supply remained uninterrupted, thereby allowing ANG Industries to continue its operations without the disruption of power disconnection. Nevertheless, it mandated that all outstanding dues be resolved strictly within the framework established by the

⁸ The Insolvency and Bankruptcy Code, 2016, § 238.

⁹ Uttarakhand Power Corporation Limited v. ANG Industries Ltd., 2018 SCC OnLine NCLAT 53 (2018) (India).

IBC.

3. Punjab State Power Corporation Ltd. v. Akums Lifesciences Ltd.¹⁰

Akums Lifesciences Ltd. entered the Corporate Insolvency Resolution Process (CIRP) in 2018. During this process, the Punjab State Power Corporation Limited (PSPCL) attempted to deny the restoration of electricity services unless the pre-CIRP dues were settled. They argued that under Section 56¹¹ of the Electricity Act, the Successful Resolution Applicant (SRA) is required to clear all outstanding dues prior to restoration.

However, the National Company Law Appellate Tribunal (NCLAT) noted that Section 238 of the Insolvency and Bankruptcy Code (IBC) supersedes the Electricity Act, indicating that any inconsistencies should be resolved in favor of the provisions of the IBC. Consequently, matters related to insolvency, including electricity arrears, should be addressed under the insolvency framework rather than through the provisions of the electricity law. PSPCL did not submit any claims during the CIRP, and the approved resolution plan did not include any provisions for pre-CIRP electricity dues. Thus, the tribunal determined that such claims are extinguished once the resolution plan is sanctioned, and the SRA cannot be compelled to pay them afterwards.

An examination of the judicial standings of the NCLT reveals that while the Electricity Act imposes statutory obligations on DISCOMs to ensure a consistent electricity supply, the IBC places these entities at a significant disadvantage during insolvency proceedings. Despite their critical role, DISCOMs are classified as operational creditors under the IBC, which means they only receive recovery after secured creditors, workmen, and government dues have been settled. Furthermore, even during the liquidation process, the framework of the IBC takes precedence over the Electricity Act, complicating the recovery of pre-CIRP dues for DISCOMs. This inability to enforce such claims severely affects the financial liquidity of DISCOMs, particularly when facing large industrial consumers that are themselves undergoing insolvency.

¹⁰ Punjab State Power Corporation Ltd. v. Akums Lifesciences Ltd., 2023 SCC OnLine NCLAT 650 (2023) (India).

¹¹ The Electricity Act, 2003, § 56.

FINANCIAL FALLOUT: THE IMPACT ON DISCOMS:

The marginal treatment of DISCOMs under the IBC framework is not solely a legal issue; it has significant financial implications as well. DISCOMs across India are already weighed down by structural inefficiencies and high-power purchase costs. On top of this, the challenge of low recovery rates from commercial consumers facing insolvency exacerbates their instability. Pre-CIRP dues, amounting to 100s of crores, are routinely written off due to DISCOMs' low priority status. Cases such as *UPCL v. ANG Industries*¹² and *PSPCL v. Akums Lifesciences*¹³ show how DISCOMs often recover only a fraction of their claims during the liquidation, which not only leads to revenue losses but also erodes their long-term financial planning capacity.

Between 2017 and 2023, Distribution Companies (DISCOMs) have experienced substantial losses, accumulating to over ₹ 3 lakh crore. These financial setbacks are often exacerbated by delayed payments, resulting in higher debt levels¹⁴. A significant portion of this debt originates from commercial and industrial users who have entered insolvency proceedings under the Insolvency and Bankruptcy Code (IBC). The following surveys highlight the situation:

- The Ujjwal DISCOM Assurance Yojana (UDAY) Dashboard, published by the Ministry of Power, reported that as of March 2022, the losses of state DISCOMs exceeded approximately five lakh crore rupees¹⁵.
- The 2022 Report on the Performance of State Power Utilities, released by Power Finance Corporation Ltd., indicates that DISCOMs incurred total losses exceeding 90,000 crore rupees in just one year¹⁶.

¹² *Uttarakhand Power Corporation Limited v. ANG Industries Ltd.*, 2018 SCC OnLine NCLAT 53 (2018) (India).

¹³ *Punjab State Power Corporation Ltd. v. Akums Lifesciences Ltd.*, 2023 SCC OnLine NCLAT 650 (2023) (India).

¹⁴ Tanvi Vipra, *What is Fuelling Power Sector Losses?*, PRS Legislative Research (May 10, 2024), <https://prsindia.org/theprsblog/what-is-fuelling-power-sector-losses>

¹⁵ Aditya Kumar, *Policy Brief Impact of Ujwal Discom Assurance Yojana (UDAY)*, PRS Legislative Research (December 9, 2021), <https://prsindia.org/policy/discussion-papers/impact-of-ujwal-discom-assurance-yojana-uday>

¹⁶ *The Performance of State Power Utilities for the years 2011-12 to 2013-14*, Power Finance Corporation Ltd. (July, 2015),

https://www.pfcindia.co.in/ensite/DocumentRepository/ckfinder/files/Operations/Performance_Reports_of_State_Power_Utilities/Report%20Database%202022-23%20-%20updated%20up%20to%20April%202024EntityApr.pdf

- A study by NITI Aayog titled “Reforms in Electricity Distribution Sector” acknowledges that the liquidity crisis faced by DISCOMs has worsened due to their inability to recover dues from the Corporate Insolvency Resolution Process (CIRP) through the waterfall mechanism¹⁷.

Moreover, because the IBC's approach to DISCOMs does not account for public service considerations, there are no compensatory frameworks in place. Consequently, the financial challenges confronting DISCOMs are not solely the result of inefficiencies and regulatory delays; however, these issues are significantly intensified by the current system.

COMPARATIVE ANALYSIS OF THE INSOLVENCY LAWS OF INDIA AND UK

The Indian Insolvency and Bankruptcy Code of 2016 distinctly places operational creditors at a disadvantage when it comes to recovering their dues, a situation that is particularly problematic for critical service providers like Distribution Companies (DISCOMs). In stark contrast, the United Kingdom's insolvency framework, established under the Insolvency Act of 1986, although it also favours secured creditors, offers a more nuanced approach when it comes to recognizing the importance of essential operational creditors.

Sections 233¹⁸ and 233A¹⁹ The UK Insolvency Act 1986 serve to protect crucial suppliers from the risks of having their contracts abruptly terminated or being forced to settle pre-insolvency debts as a prerequisite for continued supply. This provision introduces the vital concept of critical suppliers, ensuring that those who provide essential services are duly recognized for their systematic importance. This protection not only promotes continuity of business operations but also enhances the assurance of timely payments. Additionally, in the UK framework, certain operational creditors have the opportunity to negotiate priority charges, granting them elevated treatment within restructuring plans that receive approval under the Corporate Insolvency and Governance Act of 2020. Such mechanisms actively shape the outcomes of insolvency proceedings, rather than relegating these creditors to a passive role within rigid liquidation hierarchies.

¹⁷ Diagnostic study of the power distribution sector, Niti Aayog (April 2019), https://niti.gov.in/sites/default/files/2019-08/Final%20Report%20of%20the%20Research%20Study%20on%20Diagnostic%20Study%20for%20power%20Distribution_CRISIL_Mumbai.pdf

¹⁸ The UK Insolvency Act, 1986, § 233.

¹⁹ The UK Insolvency Act, 1986, § 233A.

Furthermore, innovative models from other countries, such as Singapore, exemplified by their Insolvency, Restructuring and Dissolution Act of 2018, offer valuable insights. This legislation empowers courts to ring-fence essential services, allowing for the restructuring of obligations by conferring super priority status to rescue financing and debts owed to crucial service providers, thereby guaranteeing the continuity of vital operations.

This international landscape underscores the need for India to consider targeted reforms to the IBC. Potential strategies could involve elevating the priority of DISCOMs or instituting statutory exemptions that safeguard their receivables during corporate insolvency and liquidation processes. While the IBC has indeed strengthened the rights of creditors in general, it nevertheless falls short in recognizing that not all operational creditors are interchangeable or fungible. This oversight can have significant implications for the stability and reliability of essential services that underpin the broader economic framework.

POSSIBLE RECOMMENDATIONS:

The marginalization of Distribution companies, it can be seen that the current IBC framework has a structural flaw, with consequences for the financial viability of these entities. Therefore, to correct the imbalances, a set of targeted reforms are necessary which can aim to recalibrate the treatment of DISCOMs under the Code, some suggestions follow:

1. Incorporating a new sub-category as “essential services providers”:

Building international models such as those of the UK and Singapore, we could incorporate a new sub-category for essential services, including electricity supply, with higher priority in the liquidation hierarchy, preferably ranked after the secured creditors and the workmen dues. This initiative would acknowledge the systematic importance of the Distribution Companies and encourage timely recovery of their dues.

2. Recognition of the Pre-CIRP Dues as priority:

Pre-CIRP electricity dues which are currently subsumed under the general operational debts should be treated differently and be given priority. At present, many Resolution Plans either disregard or reduce pre-CIRP arrears, a practice which undermines the financial viability of the DISCOMs. Therefore, certain recommendations are provided as a suggestion.

CONCLUSION:

The intersection of infrastructure and financial insolvency regulation in India is currently at a pivotal juncture. Electricity Distribution Companies (DISCOMs) serve as essential facilitators of electrical supply, yet they remain among the most vulnerable stakeholders within the framework of the Insolvency and Bankruptcy Code (IBC). Despite their indispensable role in providing an uninterrupted power supply even to corporate debtors in default DISCOMs are classified as operational creditors. This classification inherently positions them at a structural disadvantage within the creditor hierarchy, compelling them to endure the financial losses incurred during insolvency and liquidation proceedings.

This research exposes a persistent and deeply ingrained conflict: the disparity between the statutory obligations imposed on DISCOMs and the protections available to them under financial legislation. Although the IBC was designed to streamline debt resolution processes and optimize asset value, it inadequately accounts for the public utility nature of DISCOMs, whose services are neither optional nor easily substitutable or deferred. The lack of recognition for, and prioritization of, their dues notably those categorized as pre-CIRP claims detrimentally impacts their financial stability, disrupts revenue recovery efforts, and undermines the operational efficacy of the power sector as a whole.

Moreover, a comparative legal analysis indicates that India falls short relative to jurisdictions such as the United Kingdom and Singapore, where utilities are afforded more robust protections, including payment prioritization, statutory assurances, and specific classifications. The absence of similar mechanisms within the Indian context has exacerbated the burdens placed on DISCOMs, amplifying their fiscal challenges against a backdrop of increasing sectoral debts and ongoing operational losses.

This situation transcends mere financial entitlement; it raises significant concerns regarding policy consistency and infrastructural sustainability. For electricity to retain its status as a universally accessible public good, the regulatory framework governing its provision must align with the economic and legal realities confronting those who deliver it. DISCOMs should not be expected to fulfil their public service obligations without concurrent legal protections in insolvency contexts.

In light of these findings, this paper underscores the urgent need for reform. Recognizing pre-

CIRP dues, reclassifying DISCOMs within the creditor hierarchy, harmonising the IBC with the Electricity Act, and introducing statutory protections for utility creditors are not merely desirable reforms they are imperative. A contemporary insolvency framework must regard DISCOMs as central agents of the economy rather than as peripheral entities.