
FROM PERIPHERY TO RECOGNITION: OPERATIONAL CREDITORS IN LIGHT OF THE SWISS RIBBONS RULING

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ABSTRACT

The Insolvency and Bankruptcy Code (IBC), 2016 introduced major reforms to India's insolvency framework by establishing a structured, time-bound resolution mechanism and distinguishing between financial and operational creditors. However, this creditor classification has sparked significant debate over the unequal treatment of operational creditors during the Corporate Insolvency Resolution Process (CIRP). While financial creditors hold voting rights within the Committee of Creditors (CoC), operational creditors are largely excluded from essential decision-making, raising concerns over equity and procedural fairness.

This paper critically assesses whether the unequal treatment of operational creditors under the IBC aligns with constitutional principles, is economically rational, and can withstand legal scrutiny. It delves into judicial interpretations, with a particular focus on the Supreme Court's ruling in *Swiss Ribbons v. Union of India*, to understand the reasoning behind such differentiation. The paper further examines whether the current legal framework offers sufficient safeguards to operational creditors and identifies potential reforms to promote a more equitable insolvency process.

By employing doctrinal analysis, incorporating views from key stakeholders, and reviewing relevant case law and policy materials, this study seeks to enrich the broader discourse surrounding creditor rights and the ongoing reform of insolvency law in India.

Keywords: Insolvency and Bankruptcy Code 2016, Operational Creditors, Financial Creditors, Committee of Creditors.

CHAPTER 1: INTRODUCTION

The core of the insolvency framework is rooted in the relationship between creditors and debtors. The Insolvency and Bankruptcy Code (IBC), 2016, aims to reinforce this relationship by promoting the prompt resolution of insolvency cases and preserving the value of a company's assets.¹ The Code empowers creditors by providing mechanisms such as the Corporate Insolvency Resolution Process (CIRP) or liquidation to recover dues from defaulting debtor entities. Insolvency proceedings can be initiated against any company upon a minimum default of ₹1 lakh, with creditors filing an application before the designated adjudicating authority.²

Under the IBC, creditors are mainly classified into two categories: financial and operational. Financial creditors are those whose relationship with the debtor is purely monetary in nature, whereas operational creditors are entities that supply goods or services to the debtor, including employees and government bodies. Over time, operational creditors have raised concerns about unequal treatment in several areas, such as limitations in initiating insolvency proceedings, lack of voting rights in the Committee of Creditors, the role and authority of the Resolution Professional, and the distribution priorities outlined in Section 53 of the Code.³

Supporters of this differential approach contend that including operational creditors in the resolution process is challenging due to the time-consuming nature of verifying varied claims and interests. For example, the concerns of a one-time supplier differ significantly from those of employees, homebuyers, or government agencies

“Secondly, the operational creditors tend to have a strong anti-liquidation bias, had a potential threat to the efficient resolution of the dispute,⁴ therefore they are excluded from the insolvency process. In the year 2019, in the case of Swiss Ribbons, the Hon'ble Supreme Court has tried to answer the same”.

“The court in the said judgment has tried to a certain extent justify the differential treatment and upheld the opinion that differential enunciated between the operational and financial

¹ Abhay Chandalia, Getting your Dues: Procedure for Creditors to file under IBC, <https://economictimes.indiatimes.com/small-biz/legal/procedure-for-creditors-to-file-under-ibc-insolvency-and-bankruptcy-code/articleshow/70920647.cms?from=md>

² Ibid

³ Supra Note 1

⁴ Ibid

creditor will streamline the speedy resolution of the insolvency, as envisioned by the Drafters of the Code”.

“This article will be extensively discussing the role of the operational creditor in the resolution of the insolvency of any company. The process adopted by them for initiating the resolution of insolvency and the legislative limitation on the operational creditors. It will also point out the four major ground whose constitutional validity is challenged before the court of law and the reasoning put forward by the court to justify the differentiation”.

Definition of Financial and Operational Creditors

The financial Creditor is defined **5(7) of IBC which states**

“Financial creditor means any person to whom a financial debt is owed and includes a person to whom such debt has been legally assigned or transferred to. Financial debt means a debt along with interest, if any, which is disbursed against the consideration for the time value of money and includes—

- a) money borrowed against the payment of interest;
- b) any amount raised by acceptance under any acceptance credit facility or its dematerialized equivalent;
- c) any amount raised pursuant to any note purchase facility or the issue of bonds, notes, debentures, loan stock or any similar instrument;
- d) the amount of any liability in respect of any lease or hire purchase contract which is deemed as a finance or capital lease under the Indian Accounting Standards or such other accounting standards as may be prescribed;
- e) receivables sold or discounted other than any receivables sold on non-recourse basis;
- f) any amount raised under any other transaction, including any forward sale or purchase agreement, having the commercial effect of a borrowing; Explanation.—For the purposes of this subclause—

- i. any amount raised from an allottee under a real estate project shall be deemed to be an amount having the commercial effect of a borrowing; and
- ii. the expressions, —allottee and —real estate project shall have the meanings respectively assigned to them in clauses (d) and (zn) of Section 2 of the Real Estate (Regulation and Development) Act, 2016 (16 of 2016)
- g) any derivative transaction entered into in connection with protection against or benefit from fluctuation in any rate or price and for calculating the value of any derivative transaction, only the market value of such transaction shall be taken into account;
- h) any counter-indemnity obligation in respect of a guarantee, indemnity, bond, documentary letter of credit or any other instrument issued by a bank or financial institution;
- i) the amount of any liability in respect of any of the guarantee or indemnity for any of the items referred to in sub-clauses (a) to (h) of this clause.”⁵

Section 5(20) defines —Operational creditor as follows

“In this Part, unless the context otherwise requires an Operational creditor means a person to whom an operational debt is owed and includes any person to whom such debt has been legally assigned or transferred”.⁶

Distinction Between Operational Creditor and Financial Creditor

Bankruptcy code enunciates the distinction between the financial creditor and operational creditor while retaining the distinction between the secured and unsecured creditor. The distinction between the two is based on the recommendation of BLRC which states “The Committee deliberated on who should be on the creditor's committee, given the power of the creditor's committee to ultimately keep the entity as a going concern or liquidate it. The Committee reasoned that members of the creditor's committee have to be creditors both with the capability to assess viability, as well as to be willing to modify terms of existing liabilities

⁵ The Insolvency and Bankruptcy Code 2016, No. 31 of 2016,
<https://www.mca.gov.in/Ministry/pdf/TheInsolvencyandBankruptcyofIndia.pdf>

⁶Supra 1

in negotiations. Typically, operational creditors are neither able to decide on matters regarding the insolvency of the entity nor willing to take the risk of postponing payments for better future prospects for the entity. The Committee concluded that, for the process to be rapid and efficient, the Code will provide that the creditor's committee should be restricted to only the financial creditors".⁷

The committee considers only the capacity of the financial creditors to assess the viability and their potential to modify the terms of existing liability in the negotiation so as to place them over the financial creditors. Moreover, operational creditors are not expected to bear the burden of postponing the payments. Consequently, keeping in view the above said reasons financial creditors are placed above the operational creditors.

CHAPTER 2: PROCESS OF INITIATION OF RESOLUTION OF INSOLVENCY BY THE OPERATIONAL CREDITORS

"The insolvency and Bankruptcy code has dramatically changed the process of insolvency resolution unlike old legislation namely, The Sick Industrial Companies(Special Provisions) Act, 1985. In the earlier enactment, the accumulated losses were the sole criteria for the invocation of the insolvency resolution whereas in the said code the financial and operational creditors are given the flexibility to initiate the insolvency resolution process against the companies which have defaulted in making payment of Rs.1,00,000 or more against the legitimate dues of the financial and operational creditors".⁸

The process of invocation of insolvency resolution by the operational creditor is slightly different in the case of the operational creditor, unlike the financial creditors.

STEP 1: FILING OF APPLICATION BEFORE THE ADJUDICATORY AUTHORITY

The operational creditor can invoke the insolvency resolution process only when there is the default by the operational debtor in payment of goods supplied or services rendered by the operational creditor. In the cases wherein there is the default is made the operational creditor

⁷ The Report of Bankruptcy; Law Reform Committee, Vol. 1 Research and Design, https://ibbi.gov.in/BLRCReportVol1_04112015.pdf

⁸ Sharad Tyagi, Saloni Sharma and Yukti Makan, India: Insolvency and Bankruptcy Code, Insolvency resolution ProcessbyOperationalCreditor/Tradecreditor,<http://www.mondaq.com/india/x/711678/Insolvency+Bankruptcy/Insolvency+and+Bankruptcy+Code+Insolvency+Resolution+Process+by+Operational+Creditor+Trade+Creditor>

is required to serve upon the creditor a demand notice(Form-3) requiring the debtor to make defaulted payment within a period of 10 days or to send the operational creditor the notice of default.⁹

If the debtor fails to make any payment or send notice of default within the requisite time period i.e 10 days, the operational creditor has as a matter of his Right can initiate the insolvency process by filing an application (Form 5) for the purpose before the requisite adjudicatory authority i.e NCLT having jurisdiction over that place.¹⁰

The operational creditor is required to submit to the adjudicatory authority the following document along with the applications. “They are

1. The proof of delivery demand notice or copy of the invoice demanding payment. (Form 3)
2. An affidavit as to declare that no notice of dispute regarding unpaid operational creditor debt has been given by the corporate debtor.
3. A certificate from the bank in which the account of the operational creditor is maintained confirming that there is no receipt of the payment due to the corporate debtors along with bank account statements where credits are normally received by the operational creditor confirming non-receipt of the payment due to the corporate debtor. (In Re: **Macquarie Bank Limited Vs. Shilpi Cable Technologies Ltd.** [*AIR 2018 SC 498*], the Hon'ble Supreme Court of India held that the requirement of the bank certificate is a directory in nature)¹¹.

Further, even after the invocation of resolution many times it has been seen that the resolution is not entertained by NCLT due to failure on their part to show the existence of a dispute. The dispute is defined in Section 5(6) of the Code as dispute includes a suit or arbitration proceeding relating to¹²

1. Existence of the amount of debt;

⁹ Ibid

¹⁰ Supra Note 8

¹¹ Ibid

¹² Supra Note 8

2. The quality of goods or services; or
3. The breach of a representation or warranty.

Section 5 (6) of the Code defines the term "dispute"-“ A dispute includes a suit or arbitration proceedings relating to

- (a) the existence of the amount of debt;
- (b) the quality of goods or service; or
- (c) the breach of a representation or warranty”¹³

“Now, it is imperative to understand what will construe as an 'existence of dispute'. Will mere sending of the notice of dispute by the corporate debtor be construed as the existence of a dispute or should there be some genuine dispute”¹⁴

Further, “*the dispute will be said to have existed only when on filing of the application of a complete application before the adjudicatory authority which is otherwise complete and the adjudicatory authority has rejected the application on the grounds of receipt of notice of default by the operational creditor or there is a record of dispute in the information utility. Such notice shall be deemed to bring to the notice of operational creditor the existence of a dispute or the fact that a suit or arbitration proceeding relating to the dispute is pending between the parties. Therefore, all that the adjudicating authority is to see at this stage is whether there is a plausible contention that requires further investigation and that the "dispute" is not a patently feeble legal argument or an assertion of fact unsupported by evidence. It is important to separate the grain from the chaff and to reject a spurious defense which is mere bluster. However, in doing so, the Court does not need to be satisfied that the defense is likely to succeed. The Court does not at this stage examine the merits of the dispute except to the extent indicated above. So long as a dispute truly exists in fact and is not spurious, hypothetical or illusory, the adjudicating authority has to reject the application*”.¹⁵

¹³ Supra Note 8

¹⁴ Ibid

¹⁵ Mobilox Innovations Private limited V. Kirusa Software Private Limited, Civil Appeal No. 9405 of 2017, <http://vinodkothari.com/wp-content/uploads/2019/06/Booklet-IBC-Final.pdf>

Thus it is clear from the above judgment that the term dispute is not exhaustive, it is not solely restricted to the suit or an arbitration proceeding and that NCLT, before admitting the application once need to examine and look into the matter to an extent required to ascertain whether the actual dispute existed or not. They have also tried to ascertain whether it is merely used as a tool to avoid the resolution and the genuineness of the dispute.

STEP 2: Conditions for the acceptance of the application

“When the application has been filled by the operational creditor it is subject to acceptance of the NCLT on the fulfillment of the following conditions¹⁶

1. The application as filed should be **complete** in all respects.
2. There must **not be any repayment** of the operational debt.
3. The **notice for the payment of the debt** has been duly delivered by the operational creditor.
4. There is **no notice of dispute** which has been received by the operational creditor or there is **no record of a dispute** with the information utility (*if applicable*).
5. There are **no disciplinary proceedings** pending against the proposed interim resolution professional (*To be complied with if the name of the interim resolution professional is mentioned in the application*)”.¹⁷

STEP 3: DECLARATION OF MORATORIUM PERIOD

“When the application is accepted by the NCLT, the adjudicatory authority will declare the moratorium period, a period wherein no judicial proceeding for recovery, enforcement of security interest, sale or transfer of assets or termination of essential contracts can be instituted or continued against the corporate debtor, of 180 days and state the commencement date of the insolvency and confirm the appointment of Interim Resolution Professional. The Interim resolution professional for inviting the claims from the creditors”.¹⁸

¹⁷ Supra Note 8

¹⁸ Ibid

STEP 4: CONSTITUTION OF COMMITTEE OF CREDITORS

The interim resolution professional upon the receipt of the claims of the creditors shall formulate the Committee of Creditors for the process of insolvency. The process shall include preparation of information memorandum, the appointment of resolution professional, discussing the relevant agenda of the Committee of creditors.¹⁹

After the receipt of the claims the insolvency resolution Professional shall constitute a committee of creditors and conduct the meeting for taking actions for insolvency process such as preparation of information memorandum, appointment of resolution professional and discussions on the other related issues of the insolvency.²⁰

STEP 5: STEPS BY THE RESOLUTION PROFESSIONAL

“Resolution professional shall thereafter take such steps which will be conducive for the revival of the corporate debtor in accordance with the Code. Such a process involves the preparation of the information memorandum, invitation of expressions of interest for a resolution plan, convening meetings of the COC as and when required, etc.”²¹

In the event, no resolution plan is agreed upon in the meeting of the COC and also approved by the Hon'ble NCLT within the aforesaid moratorium period of 180 (One Hundred and Eighty) days (which is extendable by another 90 (Ninety) days on the discretion of the Hon'ble NCLT), the Hon'ble NCLT may allow commencement of the liquidation process in relation to such corporate debtor”.²²

CHAPTER 3: WHETHER THE OPERATIONAL CREDITOR ARE GIVEN COLD SHOULDER IN THE RESOLUTION OF THE DISPUTES IN THE IBC REGIME.

“There are various instances, Benami Transaction case, wherein it is alleged that the operational creditor is given cold shoulder in the insolvency process. As once the insolvency process is initiated the interim Resolution professional collects and verifies the claims of

¹⁹ Supra Note 8

²⁰ Ibid

²¹ Supra Note 8

²² Ibid

various debtors and constitutes a committee of Creditors.²³ This committee of Creditors is centrally responsible for the insolvency resolution initiated by the creditors. COC solely comprises of the financial creditors and representation of operational creditors in the cases wherein the aggregate dues are not less than 10% of the total debt, as per Section 24(3)(c) of the Code.²⁴ In the meeting of the Coc, the operational creditors are not entitled to vote even though he or she is representing a class of creditors whose proportion of the total debt is not less than 10% of total debt”.²⁵

However, the condition becomes questionable when the extremely opposite treatment is provided to the financial creditors. All the financial creditors are entitled to have the Right to vote at the Committee of Creditors and they enjoy the voting Rights, provided under Section 5(28) of Code, equivalent to their proportion of the financial debt owned by them against the financial debtors

Thus, the financial creditor will retain their Right to vote even in the condition of proportion of their debt less than 1% of the total amount due amount.

“It is important to remember that financial creditors are not neutral parties who have no personal interest. The aim of every financial creditor being a commercial entity is to ensure that the maximum dues are recovered qua their debts and the dues of operational creditors are a secondary concern at best. This problem is compounded by the lack of safeguards under the Insolvency and Bankruptcy Court, 2016 to protect the rights of the operational creditors. The only safeguard that is available to operational creditors is under Section 30 (2) (b) of the Code, which provides that a resolution plan has to ensure that the operational creditor receives at least the amount which would have been paid to the operational creditors if the corporate debtor had been liquidated i.e. the operational creditors must at least receive the liquidation value”²⁶.

“Regulation 35 of the Insolvency Resolution Process for Corporate Persons Regulations, 2016 defines liquidation value as the estimated realizable value of the assets of the corporate debtor if the corporate debtor were to be liquidated on the insolvency commencement date. However,

²³ Swaroop George, Corporate Resolution Insolvency Process: Are Operational Creditor being Given Cold shoulder?, <https://www.barandbench.com/columns/corporate-insolvency-resolution-operational-creditors-cold-shoulder>

²⁴ Ibid

²⁵ Supra Note 23

²⁶ Ibid

there may be a huge difference between the actual value of the assets of a corporate debtor and its liquidation value. This is why the Insolvency and Bankruptcy Board of India had passed the Insolvency Resolution Process for Corporate Person) (Amendment) Regulation, 2018 whereby it had become mandatory for the fair value of the assets of the corporate debtor also to be determined in addition to the liquidation value”²⁷.

“The fair value of the assets of the corporate debtor as per the amendment, is defined as the estimated realizable value of the assets of the corporate debtor, if they were to be exchanged on the insolvency commencement date between a willing buyer and a willing seller in an arm’s length transaction, after proper marketing and where the parties had acted knowledgeably, prudently and without compulsion”²⁸.

“In order that the price may not be pushed towards the liquidation value, the amendment also provides that the fair value and liquidation value shall be provided to the Committee of Creditors only after the receipt of the resolution plans and the same shall be kept confidential. No mention is made of providing the fair value and liquidation value to the operational creditors unless they have a representative on the Committee of Creditors as aforesaid which further handicaps the operational creditors. Even if the representative of the operational creditors is present, he/she cannot vote to accept a resolution plan which provides operational creditors with more than the liquidation value. The most that they can do is to attempt to convince the financial creditors to vote for such a resolution plan”²⁹.

“This can lead to absurd situations. For example, if an operational creditor approaches the adjudicating authority and initiates Corporate Insolvency Resolution Process against the corporate debtor by spending its own funds, even then the operational creditor will have no voting right to determine which resolution plan should be accepted. If the operational creditor had been owed a debt of Rs. 10 crores and financial creditors as a whole were only owed Rs. 5 crores, the decision-making power would still lie in the hands of the financial creditors and the operational creditor would be a spectator at best despite being owed the majority of the debt. The financial creditors will be free to accept a haircut of the debt owed to the operational creditor and force the operational creditor to accept the minimum repayment of the debt due i.e. liquidation value while the Financial Creditors enjoy full repayment of their loans. The

²⁷ Supra Note 23

²⁸ Ibid

²⁹ Ibid

Resolution Applicants would also be tempted to reduce the operational creditor's compensation to the liquidation value as long as they can obtain votes from the financial creditors to whom they promise full payment".³⁰

"The lack of safeguards for operational creditors in Code has been made apparent in the Corporate Insolvency Resolution Process of Binani Cements. From the decision of the National Company Law Tribunal, Kolkata, it is apparent that several operational creditors were not even being offered the liquidation value. Furthermore, while several financial creditors had not received any reduction in the debt owed to them, many operational creditors had been given severe reductions in the amounts due to them. Even the verification of the claims of the operational creditors had not been completed even though the resolution plans had already been submitted".³¹

"The National Company Law Tribunal had noted that it had been receiving several applications from operational creditors and that each carried a genuine grievance. The adjudicating authority also noted that due to the supremacy of financial creditors, the claims of operational creditors were being neglected or ignored. The adjudicating authority was of the view that it was high time that operational creditors also got a say in the process."³²

"The only practical difficulty in allowing the operational creditors access and voting rights in the insolvency process would be that achieving consensus of thousands of operational creditors would not be feasible. That can be resolved by having the operational creditors appoint representatives wherein every representative would represent operational creditors holding a certain percentage of the total operational debt and these representatives would have voting rights equivalent to the proportion of the total operational and financial debt that they represent."

"For example, operational creditors being owed 10% of the operational debt may band together to appoint a representative and in which case, ten representatives would represent the operational creditor but their voting rights would be equivalent to the percentage of the entire operational and financial debt that they represent which might be less or more than 10%. In case, the operational creditors are not able to agree on some common representatives within a

³⁰ Supra Note 23

³¹ Ibid

³² Ibid

fixed period, then the Insolvency and Bankruptcy Board of India (IBBI) might appoint representatives to safeguard interests of the operational creditors in such number as may be required keeping in mind the total number of operational creditors and such representatives should have proportionate vote share equivalent to the percentage of the total operational and financial debt owed to operational creditors. Such representatives would also be able to keep the operational creditors aware of the proceedings being conducted. However, in such a case, the voting share of financial creditors should also be calibrated *vide* the total operational and financial debt and not just financial debt.”

“Unless urgent steps are taken by the IBBI to allow operational creditors to participate and represent their interests in the Corporate Insolvency Resolution Process, there is every likelihood of the operational creditors receiving the liquidation value as opposed to the fair value causing grievous loss to them.”³³

CHAPTER 4: Through the lens of *Swiss Ribbons*

Whether Differential Treatment Is Given To The Operational Creditor In The Initiation Resolution Process Against Financial Creditor

“The point has been put forward in this case that there is unequal treatment with the operational creditor as to the initiation of the resolution of the dispute. The court first analyzed the definition provided for the financial and operational creditor in the Code and then continued with the procedure for the initiation of the insolvency procedure provided in the code for financial condition and operational creditor under Section 7 and 8, 9 respectively. The court said that according to Section 7, the financial creditor may trigger the Code either by itself or jointly with other financial creditors or such persons as may be notified by the Central Government when a —default occurs.”³⁴

The Explanation to Section 7(1) also makes it clear that the Code may be triggered by such persons in respect of a default made to any other financial creditor of the corporate debtor, making it clear that once triggered, the resolution process under the Code is a collective proceeding in rem which seeks, in the first instance, to rehabilitate the corporate debtor.

³³ Supra Note 23.

³⁴ *Swiss Ribbons Pvt Ltd. and Anr. vs. Union Of India and Ors*, https://www.livelaw.in/pdf_upload/pdf_upload-357795.pdf

Under Section 7(4), the Adjudicating Authority shall, within the prescribed period, ascertain the existence of a default on the basis of evidence furnished by the financial creditor and under Section 7(5), the Adjudicating Authority has to be satisfied that a default has occurred, when it may, by order, admit the application, or dismiss the application if such default has not occurred.³⁵ While under Sections 8 and 9, an operational creditor may, on the occurrence of a default, deliver a demand notice which must then be replied to within the specified period. The court said it is imperative to understand that, if an application is filed before the Adjudicating Authority for initiating the corporate insolvency resolution process, the corporate debtor can prove that the debt is disputed and if it accepted before the court of law that debt is disputed the application will be not be entertained any further”.³⁶

On the basis of this differential treatment, it was argued before the court of law that there is no intelligible differentia in place so as to bifurcate the two which has rationale relation with the objective of the Code.

The court said, “The distinction between Financial Creditor and Operational Creditor is clear that most financial creditors, particularly banks and financial institutions, are secured creditors whereas most operational creditors are unsecured, payments for goods and services as well as payments to workers not being secured by mortgaged documents and the like. The distinction between secured and unsecured creditors is a distinction that has obtained since the earliest of the Companies Acts both in the United Kingdom and in this country. Apart from the above, the nature of loan agreements with financial creditors is different from contracts with operational creditors for supplying goods and services. Financial creditors generally lend finance on a term loan or for working capital that enables the corporate debtor to either set up and/or operate its business. On the other hand, contracts with operational creditors are relatable to the supply of goods and services in the operation of the business. Financial contracts generally involve large sums of money. By way of contrast, operational contracts have dues whose quantum is generally less. In the running of a business, operational creditors can be many as opposed to financial creditors, who lend finance for the setup or working of the business. Also, financial creditors have specified repayment schedules, and defaults entitle financial creditors to recall a loan in totality. Contracts with operational creditors do not have any such stipulations. Also, the forum in which dispute resolution takes place is completely different. Contracts with

³⁵ Ibid

³⁶ Supra Note 34

operational creditors can and do have arbitration clauses where dispute resolution is done privately.

Operational debts also tend to be recurring in nature and the possibility of genuine disputes in case of operational debts is much higher when compared to financial debts. A simple example will suffice. Goods that are supplied may be substandard. Services that are provided may be substandard. Goods may not have been supplied at all. All these qua operational debts are matters to be proved in arbitration or in the courts of law. On the other hand, financial debts made to banks and financial institutions are well-documented and defaults made are easily verifiable. Most importantly, financial creditors are, from the very beginning, involved with assessing the viability of the corporate debtor. They can, and therefore do, engage in the restructuring of the loan as well as the reorganization of the corporate debtor's business when there is financial stress, which are things operational creditors do not and cannot do. Thus, preserving the corporate debtor as a going concern, while ensuring maximum recovery for all creditors being the objective of the Code, financial creditors are clearly different from operational creditors and therefore, there is obviously an intelligible differentia between the two which has a direct relation to the objects sought to be achieved by the Code".³⁷

1) Resolution Professional Has No Adjudicatory Powers.

In numerous cases, it has been observed that Resolution Professionals have either reduced, rejected, or refused to admit the claims of operational creditors by exercising adjudicatory powers. This has created significant challenges for operational creditors, particularly when they approach the Resolution Professional only to find that the resolution plan has already been approved under Section 31 of the Insolvency and Bankruptcy Code (IBC). Operational creditors have frequently argued that once a resolution plan is approved, they are entitled to receive only the amount corresponding to their admitted claims—or, in some cases, no payment at all. Addressing this issue, the Hon'ble Supreme Court clarified that, unlike a liquidator, a Resolution Professional is not vested with quasi-judicial authority under Sections 36 to 40 of the Code. Furthermore, the Court emphasized that a Resolution Professional cannot act independently, as evidenced by the constraints outlined in Section 28 of the IBC.

³⁷ Supra Note 34.

Thus, the resolution professional is merely the facilitator for the resolution of insolvency procedure conferred with the administrative powers.³⁸

Ensuring Fair Treatment of Operational Creditors in the Formulation of the Resolution Plan: Whether Sections 21 (Committee of Creditors) and 24 (Meetings of the Committee of Creditors) Violate Article 14 of the Indian Constitution

This issue has been contested in court on the grounds that the Committee of Creditors (CoC) is composed exclusively of financial creditors who hold voting rights, whereas operational creditors are excluded from both membership and decision-making in the resolution process. Their access to information from the Resolution Professional is restricted and granted only if their claims constitute at least 10% of the total debt.

While examining this challenge, the Hon'ble Supreme Court relied on the reasoning provided by the Bankruptcy Law Reforms Committee (BLRC). The Court based its justification for the differential treatment on the recommendations and logic put forth by the BLRC, which emphasized the distinct roles and interests of financial and operational creditors in the insolvency resolution framework.

“The members of the creditor's committee have to be creditors both with the capability to assess viability, as well as to be willing to modify terms of existing liabilities in negotiations. Typically, operational creditors are neither able to decide on matters regarding the insolvency of the entity nor willing to take the risk of postponing payments for better future prospects for the entity. The Committee concluded that, for the process to be rapid and efficient, the Code will provide that the creditor's committee should be restricted to only the financial creditors.”³⁹

Furthermore, the Court emphasized that while evaluating the viability and feasibility of resolution plans approved by the Committee of Creditors, the National Company Law Appellate Tribunal (NCLAT) must ensure that operational creditors receive treatment comparable to that of financial creditors. If such parity is absent, the resolution plan should either be rejected or revised to protect the rights of operational creditors.

³⁸ Ibid

³⁹ Swiss Ribbons Pvt Ltd. and Anr. vs. Union Of India and others,
https://www.livelaw.in/pdf_upload/pdf_upload-357795.pdf

The Court also clarified that a resolution plan cannot meet the requirements of Article 30(2)(b) in conjunction with Section 31 of the Insolvency and Bankruptcy Code unless operational creditors are paid at least the liquidation value. Based on this reasoning, the Court concluded that there is no discrimination between financial and operational creditors—neither in terms of the principle of equal treatment nor in the context of manifest arbitrariness.⁴⁰

2) Discrimination In The Waterfall Mechanism.

The argument was put forward with reference to section 53, that it places the operational creditor much below all other creditors, in particular, another unsecured creditor particularly financial creditor. Therefore, section 53 is manifestly discriminatory and arbitrary and violative of Article 14 of the Indian Constitution. The court for the purpose has analyzed the Section, mentioned hereunder

Section 53(1) Distribution of assets.

“Notwithstanding anything to the contrary contained in any law enacted by the Parliament or any State Legislature for the time being in force, the proceeds from the sale of the liquidation assets shall be distributed in the following order of priority and within such period and in such manner as may be specified, namely—

- a) the insolvency resolution process costs and the liquidation costs paid in full;
- b) the following debts which shall rank equally between and among the following—
 - i. workmen's dues for the period of twenty four months preceding the liquidation commencement date; and
 - ii. debts owed to a secured creditor in the event such secured creditor has relinquished security in the manner set out in Section 52;
- c) wages and any unpaid dues owed to employees other than workmen for the period of twelve months preceding the liquidation commencement date;

⁴⁰ Ibid

- d) financial debts owed to unsecured creditors;
- e) the following dues shall rank equally between and among the following:—
 - i. any amount due to the Central Government and the State Government including the amount to be received on account of the Consolidated Fund of India and the Consolidated Fund of a State, if any, in respect of the whole or any part of the period of two years preceding the liquidation commencement date;
 - ii. debts owed to a secured creditor for any amount unpaid following the enforcement of security interest;
- f) any remaining debts and dues
- g) preference shareholders, if any; and
- h) equity shareholders or partners, as the case may be”.⁴¹

After analyzing the provision the court relied in the BLRC report, which stated “The Committee has recommended keeping the right of the Central and State Government in the distribution waterfall in liquidation at a priority below the unsecured financial creditors in addition to all kinds of secured creditors for promoting the availability of credit and developing a market for unsecured financing (including the development of bond markets). In the long run, this would increase the availability of finance, reduce the cost of capital, promote entrepreneurship and lead to faster economic growth. The government also will be the beneficiary of this process as economic growth will increase revenues. Further, efficiency enhancement and consequent greater value capture through the proposed insolvency regime will bring in additional gains to both the economy and the exchequer. For the remaining creditors who participate in the collective action of Liquidation, the Committee debated on the waterfall of liabilities that should hold in Liquidation in the new Code. Across different jurisdictions, the observation is that secured creditors have first priority on the realizations and that these are typically paid out a net of the costs of insolvency resolution and Liquidation.”⁴²

⁴¹ Insolvency and Bankruptcy Code, 2016 , <https://ibclaw.in/section-53-distribution-of-assets/>

⁴² Swiss Ribbons Pvt Ltd. and Anr. vs. Union Of India and others, https://www.livelaw.in/pdf_upload/pdf_upload-357795.pdf

The committee recommends the waterfall mechanism in consonance with the global practice as follows with the intent to achieve the objective mentioned by the Code.

“The priority list is as follows.

1. Costs of IRP and liquidation.
2. Secured creditors and Workmen dues capped up to three months from the start of IRP.
3. Employees capped up to three months.
4. Dues to unsecured financial creditors, debts payable to workmen in respect of the period beginning twelve months before the liquidation commencement date and ending three months before the liquidation commencement date.
5. Any amount due to the State Government and the Central Government in respect of the whole or any part of the period of two years before the liquidation commencement date; any debts of the secured creditor for any amount unpaid following the enforcement of security interest.
6. Remaining debt.
7. Surplus to share-holders”.⁴³

It can be seen from the abovementioned conundrum that financial creditors are placed in priority over the operational creditors, particularly, the unsecured creditor because of the repayment of the credit to the financial debt to the financial creditor infuses capital in the economic activity. Thus, there is an intelligible differentia between the financial debt and operational and it has a rational relation with the objective of the Code, hence the waterfall mechanism prescribed in section 53 of the Code is not arbitrary.

SUGGESTION

The Insolvency and Bankruptcy Code (IBC), 2016, has evolved into a strong legislative framework, continually shaped by judicial interpretation and responsive policy changes. While

⁴³ Ibid

the Code has played a pivotal role in reforming India's insolvency system, the limited involvement and rights of operational creditors in the resolution process remain a pressing concern.

▪ **Enhancing the Role and Inclusion of Operational Creditors**

A key recommendation is to improve the participation and representation of operational creditors in the Corporate Insolvency Resolution Process (CIRP). One viable measure could be the provision of limited or proportional voting rights in the Committee of Creditors (CoC) for operational creditors whose claims exceed a certain threshold. This would ensure that key suppliers and service providers—often with significant financial stakes—are not excluded from crucial decision-making.⁴⁴

▪ **Improved transparency and stakeholder engagement are equally necessary.**

Resolution professionals could be obligated to conduct formal consultations with operational creditors during critical phases of the CIRP, even if they do not have voting authority. Additionally, establishing an official mechanism for submitting objections or suggestions on resolution plans would make the process more inclusive and participatory.

▪ **Proposed Legal and Policy Reforms.**⁴⁵

Several targeted legal amendments could address the disparity in creditor rights. These include:

- Modifying Section 24 of the IBC to grant operational creditors with sizable admitted claims the right to routinely attend CoC meetings, not just by invitation.⁴⁶
- Broadening the definition of "financial creditor" to encompass long-term service contracts or recurring supply agreements that effectively function as financial arrangements.

⁴⁴ Ms. Priya Kumari, Operational Creditors Under the IBC: Unequal Footing or Justified Differentiation?, International Journal for Multidisciplinary Research, 48663.pdf

⁴⁵ Ibid

⁴⁶ Supra Note 44

- Implementing measures to ensure that operational creditors receive a fair portion of the resolution proceeds, particularly when they have significantly supported the debtor's business prior to insolvency.
 - Reforms should also simplify the claims process for smaller operational creditors, such as MSMEs, many of whom struggle with the complex procedures of the IBC. Initiatives like digital claim filing, standardized formats, and access to legal support could greatly reduce this burden.⁴⁷
- **Advancing ADR Mechanisms for Minor Debt Recoveries**
- Given the difficulties small-scale suppliers face in recovering modest dues through formal insolvency channels, the use of Alternative Dispute Resolution (ADR) methods—such as mediation and arbitration—should be encouraged. The IBC can incorporate pre-admission ADR mechanisms for lower-value, uncontested operational debts, enabling faster and more cost-effective dispute resolution before triggering CIRP.⁴⁸

This would alleviate pressure on the National Company Law Tribunal (NCLT), facilitate quicker settlements, and help maintain business relationships. Concepts such as pre-packaged insolvency and expedited mediation could be adapted for this purpose.

CONCLUSION

The *Swiss Ribbons* judgment is poised to have a lasting impact on the role of operational creditors within the insolvency framework. It has brought clarity to the administrative duties of the Resolution Professional, particularly regarding the admission of claims made by operational creditors during insolvency proceedings. This ruling effectively moves away from the precedent set in the *ArcelorMittal* case, which had suggested that Resolution Professionals could form prima facie opinions on the validity of creditor claims.⁴⁹

⁴⁷ Ibid

⁴⁸ Supra Note 44

⁴⁹ India: Swiss Ribbon v. Union Of India-Foundation for Modern Bankruptcy law, L. Viswanathan, Bishwajit Dubey and Spandan Biswa, <http://mondaq.com/india/x/779498/Insolvency+Bankruptcy/Swiss+Ribbons+v+Union+Of+India+The+Foundation+For+Modern+Bankruptcy+Law>.

Additionally, the judgment reflects the Indian judiciary's restrained approach when interpreting economic legislation, emphasizing adherence to the legislative intent and objectives behind the Insolvency and Bankruptcy Code (IBC). Looking ahead, this decision is expected to have far-reaching consequences—it is likely to enhance investor and bidder confidence in acquiring distressed assets through the IBC process and contribute to improving India's overall business environment.⁵⁰

⁵⁰ Ibid