
A DOUBLE DILEMMA: HARMONIOUSLY CONSTRUING THE PROVISIONS OF RERA AND IBC 2016

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ABSTRACT

Home ownership is a subject that requires to be prioritized due to an array of factors that need to be taken into consideration before finalizing the deal. People having stable incomes and savings in today's time have a variety of options to choose from by virtue of the expansion in the real estate sector in our country. However, aside from the dilemma of selecting the right home another dilemma has arisen in recent times with regards to the rights and appropriate forum for resolving disputes of allottees in cases where the project is delayed and other similar circumstances that arise when the rights and expectations of the homebuyers are negatively affected due to default on part of the developer of the project.

This dilemma is focused on the two crucial pieces of legislation i.e. The RERA act 2016 and The IBC 2016 where the former elaborates on the rights of homebuyers in cases of project delays, misrepresentation by the developer about the property, issue regarding the condition and standard of the piece of real estate whereas the latter imposes penalties on developers by treating homebuyers as "financial creditors" who can start the insolvency process in case where the developer absconds after taking the money from the allottees before the completion of the project or keeps on delaying the same. This article dives deeply into how the court has attempted to harmoniously construe both provisions through its judgements and how these overlapping pieces of legislation have caused confusion while providing solutions as to how one shall not overpower the other and exist harmoniously.

Overlap between both legislations and judgements

Both pieces of legislation the IBC and RERA were enacted in the year 2016 where RERA or the Real estate regulation and development act 2016, took a more consumer centric approach where allottees can approach RERA authorities for restoration of rights including compensation in case of defaults under section 18 of the RERA act 2016 where subsequently the jurisdiction of the civil court is barred giving RERA authorities exclusive jurisdiction over such matters under section 79 of the act. On the contrary the IBC 2016 initially did not specifically include the debt accumulated from the allottees as financial debt and the same occurred post the 2018 amendment of the IBC under section 5(8)(f)¹ as a result of which other relevant provisions of the IBC became applicable to issues pertaining to the buyer and developer where the buyer (allottee) now has the right to initiate insolvency proceedings against developers who default or abscond before completion of the project.

By treating allottees as financial creditors an additional layer has been added in the waterfall mechanism in cases of insolvency resolution process under the IBC and the standing of allottees in this context was seen in the cases of ***Chitra Sharma vs Union of India (2017)*** and ***Pioneer Urban Land Infrastructure Limited & Anr. vs Union of India and Ors (2019)***² that are cases addressing the same issues before and after the 2018 amendment of the IBC where the NCLT (Allahabad) received a petition on behalf of IDBI Bank that initiated CIRP proceedings under the IBC against Jaypee Infratech Limited (JIL) on its default in payments in lieu of its commercial housing projects that were financed by the bank. However even home owners demanded to have an “equal status” as “financial creditors” who approached the Hon’ble SC and demanded the right to actively be involved in the CIRP process and were dissatisfied with the order of the NCLT that itself initiated the CIRP process against JIL and imposed a moratorium with regards to the same issue (i.e. that no pending or new suit having nexus to the same matter would continue) unfortunately these demands due to the lack of provisions in the IBC could not be addressed by the court and were a part of the case of ***Chitra Sharma vs Union of India (2017)*** where the NCLT further itself appointed an Interim Resolution Professional (IRP) which gave no locus or active involvement to allottees in the

¹ Pillai, Abhilash, & Agarwal, Tarun. “Home Buyers = Financial Creditors: Supreme Court Reigns.” *Lexology* (Cyril Amarchand Mangaldas), 14 August 2019

² “Resetting the Clock: Supreme Court Sends Jaypee Infratech Limited Back to NCLT for CIRP” L. Viswanathan, Srideepa Bhattacharyya, Aditya Marwah & CAM Disputes Team, August 27, 2018

CIRP process.

However, post the amendment and when these issues were addressed in the subsequent case of **Pioneer Infratech (2019)** The Supreme Court in lieu of the consideration of the homeowners the SC stayed the NCLT'S order but as an unintended consequence of this stay order the promoters of JIL were being transferred back the control of the company which would allow them to finish the projects and conduct new ventures without the repayment of outstanding dues due to which the SC responded by resuming the CIRP process by allocating the control of JIL's management to the IRP where JIL was ordered to pay a sum of Rs 2000 crore and not dispose of any asset by way of sale further the SC even appointed a senior counsel in the CoC or committee of creditors to represent the entire case of the allottees thus effectively understanding the giving effect to the demands of the allottees to be involved actively in the CIRP process along this "Home owners" as per the judgement were given separate treatment in contrast to operational and financial creditors where allottees could file claims against defaulting builders/ developers. As a part of the judgement the status quo as envisioned in the 2018 IBC amendment was upheld and the allottees were treated as financial creditors as was added in section 5(8)(f) of the code thus allowing allottees to institute CIRP under section 7 of the IBC and be a part of the committee of creditors (CoC) under section 21 of the code. This judgement effectively addressed the concerns of the allottees whose demands to be treated as creditors at par as IDBI bank was not earlier possible due to the absence of provisions in the IBC during the *Chitra Sharma vs Union of India case (2017)* as this case had occurred before the amendment of the code. The courts in Pioneer Infratech harmoniously construed section 2 (d) of RERA act that defines "Real Estate Allottees" and brought them under the ambit of financial creditors within the IBC's ambit and went on to uphold the constitutional validity of the IBC by stating that in cases of conflict between IBC and RERA the former will prevail.

The courts relied on the Insolvency Law committee reports dated 26th March, 2018 led by Injeti Srinivas³ where it was explicitly recommended by the committee for the treatment of home owners as financial creditors within the ambit of the insolvency code 2016 and observed that when collectively examined all home owners play a crucial role in the financing of such real estate projects and that since they are adequately represented in the CoC process they also can not be excluded from the ambit of "financial creditors" as is mentioned within the ambit of the

³ https://ibbi.gov.in/ILRReport2603_03042018.pdf

insolvency code.

In the case of *Vishal Chelani vs Debashish Nanda*⁴ there arose an overlap between RERA and IBC where the courts stated that allottees of real estate projects who obtain decrees under the RERA act will continue to be treated as a creditor under section 5(8)(f)⁵ of the IBC thus stating that the treatment of allottees will remain consistent throughout the matter and dismissed a portion of similarly positioned allottees who claimed differential treatment and wanted to receive monetary compensation as opposed to the possession of the flat thus producing a different claim than what was decided in the CIRP process. Here the courts stated that differential treatment was violative of article 14 of the constitution of India. Secondly, the courts placed emphasis on the non- obstante clause in the IBC i.e., Section 238 of the code where they reaffirmed Pioneer Infratech's holding by stating that the provisions of the IBC will override RERA act's provisions where both pieces of legislation cannot be treated as subordinate to each other which effectively suggests how the IBC will get primacy in cases concerning allottees where there exists a pre decided and fixed resolution plan. We can observe from this case that the court treated all allottees to be homogenous and granted the same relief to all allottees thus negating a segment of similarly placed allottees seeking a different compensation which overlooks the heterogenous nature of allottees who might have expected different outcomes which is a concern that requires to be addressed by harmoniously construing the relevant provisions of the IBC and RERA act, to give flexibility in terms of the compensation that can be availed by the distressed allottee.

Maintaining the balance between homebuyers and developers

The above cases have in deed set precedent allowing for adequate representation of allottees in the CoC and have given them a strong footing in terms of being actively involved in the CIRP process. This CIRP process that can be filed by homeowners under section 7 of the IBC 2016 against defaulting developers is however to be subjected to a two prong test which again is consistent with the concept of harmoniously interpreting RERA and IBC where firstly the developers are required to comply with RERA under section 4 of the act and are to supply relevant and necessary documents to the RERA authorities in respect of their projects to ensure accountability and for a home owner/ allottee to successfully establish a substantial claim

⁴ <https://ibclaw.in/vishal-chelani-ors-vs-debashis-nanda-supreme-court>.

⁵ <https://www.azbpartners.com/bank/sc-held-that-homebuyers-who-secure-decree-under-rera-cannot-be-treated-differently-from-other-financial-creditors-under-ibc>

against the developer in case of default by way of CIRP under section 7 of the IBC they are required to establish a prima facie case against the developer thus effectively putting the burden on them to prove whether or not a default in payment has even occurred or not, this leads to both the acts being balanced where both are adequately referred to without overpowering each other

Secondly, once default is initially proved by the allottee/owner then the burden of proof shifts over to the developer of the project to prove that he/ she is not liable to compensate the allottee and the same is to be done by referring to the relevant provisions of the RERA act that will essentially depend on a case to case basis and only when it is proved by using these relevant provisions of the RERA act that the allottee is not entitled to receive compensation or is a defaulter themselves then only can the entire CIRP process under section 7 of the IBC be made inapplicable to that particular case where the application for the resolution process will be dismissed by the court. Further, many times allottees attempt to fraudulently engage in such real estate investments to get their money back by coercive means where they themselves have no interest in a bona fide purchase of the property, in these cases section 65 of the IBC 2016 can be invoked by the developers thus preventing allottees from maliciously applying to the NCLT under section 7 thus adding a layer of protection for the developers of projects which maintains a healthy balance between both buyers and developers.

The 2020 Amendment of the IBC and protection of developers

While CIRP under section 7 of the IBC acts as an additional remedy for home owners along with the RERA act there is a minimum threshold that has been established before initiating CIRP under section 7 by way of a further amendment of the IBC in 2020, where section 7 of the code was amended and it was further provided that financial creditors specifically “allottees” of a real estate project before initiating the resolution process must ensure that at least ***“100 allottees or 10% of the allottees whichever is less”*** must initiate CIRP process against the developer i.e. (the corporate debtor) and these allottees must clearly be of the same real estate project.

This amendment has produced a sort of arrangement where allottees cannot individually seek for compensation from the courts as the same could result in various other allottees of the same project to file claims for compensation later on which is not favorable for the courts and is against the interests of the developer who would without this amendment be subjected to

unreasonable and numerous amounts of litigation for the same matter which also would have violated the civil procedural laws of *Res Judicata* and *Res Sub Judice* under section 11 and section 10 respectively of the Code of Civil Procedure 1908.

This minimum threshold to be established by the allottees via the amendment of the code in 2020 has been affirmed by the Hon'ble Supreme Court in the case of ***Manish Kumar vs Union of India 2020*** where the challenge on the minimum threshold for CIRP proceedings under section 7 of the code on the grounds of being violative of fundamental rights of right to practice any occupation, right to life and liberty were quashed by the Supreme court as no departure from the constitutional rights or principles was observed in the case.

Protection on buyers in cases where serious fraud or misconduct is alleged or proven

Nevertheless, even post Manish Kumar's case in an earlier case before the amendment of the IBC in 2020 imposing the threshold on allottees to initiate CIRP proceedings the infamous ***Bikram Chatterji vs Union of India (2019) (Amrapali case)***⁶ occurred where the Hon'ble Supreme court sympathized with the various petitions filed by homeowners seeking for the SC to exercise original writ jurisdiction when moratorium was imposed by the NCLT during CIRP against the corporate debtor (Amrapali Group) initiated by Bank of Baroda i.e. (the secured financial creditor) thus halting pending and the initiation of suits and proceedings against the corporate debtor. Here the allottees argued that section 53 of the code did not place them at par with secured creditors which here is the Bank of Baroda which resulted in discriminatory liquidation proceedings as the impugned section negates the fact that allottees play crucial role in financing such projects, and in consideration of these points the SC decided to allow the motion filed by allottees thus suggesting that allottees who are placed similarly can directly approach the SC via writ petitions thus avoiding adjudicating bodies such as RERA, NCLT and NCDRC in cases where the "Public Interest"⁷ is at stake, and in this case the SC was apprised of the dirty tactics used by the corporate debtor that engaged in including diversion of funds, manipulation of financial records, misrepresentation to the allottees for malicious intent of accumulating investments and even direct corporate frauds including embezzlement of funds which were exposed to the court post a financial audit that was conducted over the company's

⁶ Choudhary, Vaibhav, & Bharadwaj, Prakhar. "Decoding The Amrapali Judgment & Its Effect on The Real Estate Sector." *Atharva Legal, Snippet*, 6 Aug. 2020

⁷ Thomas, Abraham. "SC asks Centre to arrange funds for stalled Amrapali projects." *Hindustan Times*, New Delhi, updated on 13 Aug. 2020.

projects which infuriated the court and led them to directly invoke their jurisdiction and deliver complete justice under article 142 of the Indian Constitution where possession was granted over to the allottees along with the title rights over the property. Thus even though currently the 10% or 100 allottees threshold for initiating CIRP process against the corporate debtor under section 7 of the code is mandatory the Supreme court in regards to the “public interest at large” can pass orders and deliver complete justice in situations where fraudulent activities of the corporate debtor come to light thus effectively disallowing the misuse of the newly amended code in 2020 imposing the minimum threshold on buyers thus giving the allottees a variety of options for forums to seek remedies from.

Position of secured and unsecured creditors and purposively construing section 53 of the IBC 2016.

The NCLAT has in recent times has elaborated on the scope of projects that are covered within the ambit of the CIRP process in cases of default by a particular real estate company and have also commented on the position of unsecured creditors i.e. (allottees) in cases where both unsecured and secured creditors involved where secured creditors are the banks directly financing the real estate project. In the case of ***Flat buyers Association Winter Hills- 77, Gurgaon vs Umang Realtech Private Limited 2020***⁸ the issues brought before the court were firstly whether CIRP against a real estate company is restricted to the same impugned project or does it also include other projects within its ambit and secondly whether a financial institution / bank (Secured Creditor) will be given preference over allottees (unsecured creditors). Here the NCLAT clarified that the resolution process against a real estate company (corporate debtor) (in this case Umang Pvt. Ltd.) is restricted to the projects that pertain to the current case of the allottees applying for CIRP and does not cover other projects of the corporate debtor where there are different parties involved (i.e. different allottees, financial institutions and different landowners) thus clarifying that the CIRP process would not adversely impact other projects of the corporate debtor and is a process done only on a project basis where claims made by allottees and other relevant parties of other projects by the same corporate debtor can not be clubbed as one. The courts further stated that the aim here was not to maximize the scope of assets of the corporate debtor in one go which can prove to be fatal for

⁸ <https://www.vaishlaw.com/corporate-insolvency-resolution-process-against-a-real-estate-company-is-limited-to-the-project-concerned-and-will-not-affect-other-projects-nclat-new-delhi>

developers if allowed due to the obvious going concern threat to their company.

In regards to the second question pertaining to preference given to a specific category of creditors the appellate tribunal clearly stated that secured creditors can not be given preference over unsecured creditors as the final product is for the allottees for which the right has been created and even though these financial institutions are secured creditors handing them the possession over the securitized asset i.e.(the flat or apartment) is not in their favor as they do not have the expertise to deal with such assets (i.e. the flat itself) and would have to engage ARC's to productively reconstruct these non-liquid assets which is not what the banks would prefer and this would simultaneously defeat the claims of several joint allottees as the only way they could get compensation is by being allotted the flat or apartment which had been approved specifically for them.

The tribunal further elaborated on another course of action available for the allottees after allotment has been offered where they could approach the IRP and request them to find a third party who could purchase the flat and give the allottees their money back in case they do not want to take possession over the flat. From this one can clearly observe that the court did not follow the literal rule of interpretation of the IBC as section 53 of the code elaborates on the hierarchy of the waterfall where preference is according to the statute given to secured creditors over unsecured financial creditors but rather a purposive interpretation was taken considering the facts of the case which upholds reason for which the 2018 amendment of the IBC was passed.

This above case has shed light on the treatment of the assets of the real estate companies in situations where they become debtors to a variety of creditors and further protects the corporate debtors by not maximizing their assets in the CIRP process thus not adversely affecting unrelated ventures they are engaged in.

Conclusion

While the IBC has allowed for an alternative remedy available to homebuyers, we must also strengthen the existing RERA provisions that itself should be an exhaustive piece of legislation clarifying the forums allottees can approach and remedies available to them.

The creation of this overlap between IBC and RERA act without any clarity regarding the order

in which the consumers must avail these remedies increases the burden on the courts who then must harmoniously construe both legislations without any guidelines on the same thus necessitating further amendments in both acts in regards to the position of the allottees seeking to initiate action against defaulting developers.

Further, to lessen the burden of courts setting up of alternative forums must be done throughout all states to alleviate the burden of RERA authorities and courts recent developments in UP and Maharashtra have occurred where alternate forums prove to alleviate burden of courts in these disputes.⁹

The real estate sector being lucrative, provides for immense opportunities for both developers and buyers who must be made aware of the change in the regulatory landscape that navigates such transactions. Further amendments in the existing regime (i.e., the RERA act and IBC) will pave way for clarity required by the relevant parties attempting to indulge in such transactions and boost investments throughout the sector thus creating a robust real estate sector.

⁹ **Roy, Aastha, and Rohan Mitra.** “Navigating Crossroads of IBC and RERA: Are We There Yet with Addressing Homebuyers’ Woes?” *The Economic Times (ET Prime)*, 7 June 2023.