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**DEBTS OF UNSECURED FINANCIAL CREDITORS HAVE PRIORITY OVER OUTSTANDING ELECTRICITY DUES IN THE IBC LIQUIDATION PROCESS: PASCHIMANCHAL VIDYUT VITRAN NIGAM LTD v RAMAN ISPAT PVT LTD<sup>[1]</sup>**

04 September 2023



The Supreme Court has held that §238 of the Insolvency and Bankruptcy Act 2016 (IBC) overrides the provisions of the Electricity Act 2003 and has held that government debts and operational debts rank lower in priority than sums owed to unsecured financial creditors.

**Facts**

1. The electricity board supplied electricity to the corporate debtor, Raman Ispat, which was in liquidation proceedings. As per the agreement between the parties, any outstanding electricity dues would constitute a “charge” on Raman Ispat’s assets. Raman Ispat defaulted in paying for its electricity and its properties were attached.
2. In the liquidation proceedings, the NCLT, Allahabad directed the release of the attached properties in favour of the liquidator to enable their sale as per the provisions of the IBC.
3. The electricity board appealed to the NCLAT. It argued that the outstanding electricity dues were a security interest by relying on the definition of “secured creditor” and “transfer” under the IBC. The Electricity Board also argued that recovery of the electricity dues should be as per the Electricity Act, which prevailed over the IBC.
4. The NCLAT rejected the Electricity Board’s appeal, which was challenged before the Supreme Court.

**Supreme Court’s Decision**

The issue to be decided by the Supreme Court was whether a “security interest” created by operation of law can be treated at par with a first priority secured creditor under the IBC, and whether the provisions of the IBC prevail over the Electricity Act.

1. The Supreme Court explained the insolvency resolution process and the order of priority for asset distribution as per the waterfall mechanism.

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<sup>1</sup> Decision dated 17 July 2023 passed by the Supreme Court in Civil Appeal Nos. 7976 of 2019.

2. The Supreme Court held that a security interest created in favour of statutory corporations like the Electricity Board (which are not the Central or State Government) classify as a “financial debt” or “operational debt” under the IBC. Such dues do not fall under the ambit of dues owed to the Central Government or State Government under §53(1)(e)(i) of the IBC.
3. The Electricity Board had relied upon the judgment in *Rainbow Papers*<sup>[2]</sup> which had held that the statutory dues of the government are secured debts under the IBC. The Supreme Court noted that the finding in *Rainbow Papers* was in relation to the CIRP process, whereas the present case was a liquidation process, and the waterfall mechanism under §53 of the IBC was not considered in *Rainbow Papers*.
4. §52 of the IBC allows a secured creditor to opt out of liquidation proceedings if the secured creditor chooses to relinquish its security in favour of the liquidation estate. The secured creditors who relinquish their security are ranked higher in the waterfall mechanism under §53 of the IBC than the secured creditors which do not relinquish their security interest.
5. As per the waterfall mechanism under §53 of the IBC, “government dues” are lower in priority. The intention of Parliament was to treat debt owed to the government as distinct from debt owed to a secured or unsecured creditor.
6. The provisions of the IBC hold primacy over the Electricity Act, which allows for a structured recovery of debts.

## Conclusion

The judgment of the Supreme Court has confirmed the overriding effect of the IBC over other statistics as a basis for developing a sound insolvency and liquidation process.

*The content of this article is intended to provide a general guide to the subject matter. Specialist advice should be sought about your specific circumstances.*

**For further information on this topic please contact Tuli & Co**

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<sup>2</sup> *State Tax Officer versus Rainbow Papers Ltd* (2022) 13 SCR 808.