

Are home buyers financial creditors under the IBC?

By: Mustafa Kachwala, Disputes Partner, and Ketki Pansare, Associate, Majmudar & Partners

Introduction

Recently, in the case of *Vishal Chelani & Ors. v. Debashis Nanda* (Civil Appeal No. 3806 of 2023), India's Supreme Court (SC) ruled on the interface of the Insolvency and Bankruptcy Code, 2016 (IBC) with the Real Estate (Regulation and Development) Act, 2016 (RERA).

Factual background

The appellants, home buyers, invested in a real estate project developed by Bulland Buildtech Pvt. Ltd. (Developer). The Developer faced delays and did not complete the project in time. Aggrieved, the home buyers approached the Uttar Pradesh Real Estate Regulatory Authority and obtained a decree for a refund with interest. Simultaneously, proceedings were initiated against the Developer under the IBC, and a resolution plan was put forth. However, a crucial issue surfaced from the resolution plan - how to distinguish between home buyers who sought remedies under the RERA and those who did not? This led to disparate terms, and home buyers not seeking RERA remedies enjoyed 50% better conditions than those that did.

Dissatisfied with the resolution plan, the appellants contested it before the National Company Law Tribunal (NCLT). The NCLT rejected the application. In appeal, the National Company Law Appellate Tribunal also upheld the resolution plan, deeming it unflawed and not warranting interference. Consequently, the appellants filed an appeal in the SC.

Issue

The question before the SC was whether there should be differential treatment under the IBC for two categories of home buyers. The crux of the matter lay in the treatment of home buyers who sought remedies under the RERA as compared to those who did not, and whether the latter could be classified as "financial creditors."

Legal framework

To address this question, the SC delved into the key provisions of the IBC.

1. Section 5(7) defines a "financial creditor" as any person to whom a financial debt is owed.
2. Section 5(8)(f) specifies that financial debt, including amounts paid by allottees under real estate projects, shall be deemed to have the commercial effect of "borrowing."
3. Section 238 of the IBC reinforces the primacy of IBC provisions over other laws.

The SC relied on the ruling in *Natwar Agrawal (HUF) v. Ms Sakash Developers & Builders Pvt. Ltd.*, which established that an allottee in real estate project, who subsequently became a decree holder under the RERA continued to be a financial creditor in the class of home buyers

and was governed by the threshold limit prescribed under Section 7(1) second proviso of the IBC.

SC's reasoning and judgement

Relying on Section 5(8)(f) of the IBC, the SC dismissed the artificial distinction made in the resolution plan. It asserted that seeking different remedies under the RERA did not alter the appellants' status as home buyers. The SC found it inequitable to treat a segment differently solely based on the ground that some had elected to reclaim their deposits along with interest as ordered under the RERA and others had not.

The SC emphasized the overriding effect of Section 238 of the IBC and underscored the need for parity in the treatment of home buyers under Article 14 of the Constitution, which prohibits discrimination.

Conclusion

This is an important judgment, where the SC has ensured that home buyers, regardless of their choice of remedy under the RERA, are treated uniformly under the IBC. The decision not only upholds the principles of equity and non-discrimination but also reaffirms the supremacy and overriding effect of the IBC. This ruling is poised to have far-reaching implications, setting a precedent for future cases involving the intersection of real estate regulations and insolvency laws in India.