

6th AUGUST, 2021

Substantial Consolidation – The Videocon Industries decision

INTRODUCTION

1. State Bank of India (SBI) filed 15 different applications under Section 7 of the Insolvency and Bankruptcy Code, 2016 (IBC) for initiation of Corporate Insolvency Resolution Process (CIRP) against Videocon Industries Limited (VIL) and other companies under the umbrella of Videocon Industries.

2. The businesses of VIL including Consumer Home Appliances, Telecom services and Oil & Gas business was funded through various Rupee Term Loan Agreements and Letter of Credit/Stand-by Letter of Credit Agreements by SBI.

3. In the said CIRP proceedings, an application was filed for consolidation of the group companies.

4. On 8th August, 2019, the National Company Law Tribunal, Mumbai Bench, (NCLT) allowed the consolidation of 13 out of the 15 companies for the ease of process of CIRP by the Resolution Professional.

5. On 22nd August, 2019, the Tribunal granted interim protection by preventing SBI from selling assets of companies engaged in the oil and gas business, although they were by and large a part of the VIL group of companies, pending an application being MA 2385 of 2019 in CP (IB) 02/M-B/2018 filed by Venugopal Dhoot, Former Chairman, VIL under Section 60(5) of the Insolvency and Bankruptcy Code, 2016. The primary prayers of the applicant were:

- a. That the assets, properties of the foreign oil and gas business be considered and treated as the assets of VIL for the purpose of the present CIRP.
- b. That moratorium under section 14 of the IBC be applicable to the assets of the foreign oil and gas business.

6. In dealing with the above issues, the NCLT Mumbai Bench by an order dated 12th February, 2020, passed a detailed decision laying down the provisions relating to substantial consolidation of group companies.

Framework in India

1. There is no statutory framework under the IBC or otherwise dealing with the law relating to the doctrine of substantial consolidation. As such, the courts in India have applied discretionary methods for dealing with the same.

2. The Insolvency Law Committee Report of 2018 made a recommendation for inclusion of the doctrine in the Indian legislatures. However, the suggestion was not implemented by the reason that it might be “too soon” in the current state of insolvency regime owing to the complex corporate structures in India.

US Laws

1. The doctrine of substantial consolidation is well developed in United States under the US Bankruptcy Code

2. The NCLT relied on the decision of UK/US Courts in reaching to the decision of consolidation.

3. In Continental Vending Machine Corp. vs. Irving L. Wharton and Auto-Train Corporation Inc. Florida Corporation, the US Court of Appeal stated that since substantial consolidation vitally affects substantive rights, the courts must apply the formula of balancing interests such that the consolidation yields beneficial results offsetting the probable harms on resisting parties.

4. In Food Fair Inc. Debtor, the US Bankruptcy Court ruled several elements to be evaluated before a motion for consolidation may be permitted.

5. The NCLT relied exhaustively on the decision in Food Fair Inc. to list the considerations for consolidation in the present matter.

Substantial Consolidation

1. The NCLT relied on the financial documents and agreements leading to the cause of action and the chronological list of events in deriving the conclusion as to whether the assets of foreign oil & gas business could be utilized in the CIRP of VIL.

2. Following observations were made:

a. Videocon group was a conglomerate with diversified businesses and around 40% of the total claims made against the group companies were from the oil and gas business clarifying that it formed a substantial part of the claims.

b. The respondents including VIL along with the oil and gas business entities were being treated as a single economic entity in the manner of their operations leading to the clear indication that the businesses were interwoven through a single thread.



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c. Initially assets were acquired in the name of VIL and subsequent creation of the oil & gas business structure without any real or legal transfer of the ownership and rights would not mean that VIL is not the owner of such assets.

d. Relying on Section 18 of IBC, it was noted that the assets of foreign subsidiary may not be treated as assets of the corporate debtor only when such source is undoubtedly proved. In this case, the acquisition documents still include the name of VIL as the owner and no subsequent transfer has been proved.

3. The NCLT placed reliance on *State of UP vs. Renusagar Power Co. (1988)* 4 SCC 59 to shed light on the applicability of the principle of lifting of corporate veil. The Supreme Court in this case held that lifting of corporate veil must be dependent on realities of the situation in the expanding horizon of modern jurisprudence. It also held that when three companies are so interconnected that one can control the movement of the other, such companies must be treated as group companies.

4. The term “consolidation” and its elements were explained through the decision of 8th August, 2019. The NCLT held that each of the following parameters were to be fulfilled in order to allow the prayers of the applicant:

- Common Control: Control of all decisions were with VIL and oil & gas business were acting as extended arm of VIL.
- Common Directors: The Dhoot family were common directors of all the companies consolidated together.
- Common assets: The lenders in the RTL and LOC/SBLC agreements always treated the companies as a single economic entity and all assets were being treated as the assets of Videocon group.
- Common liabilities: The clauses of agreements demonstrated availability of common securities.
- Interdependence: The oil & gas business entities were dependent on VIL for funding as well as acquisition of assets.
- Interlacing of finance: The financial agreements between lenders and VIL were interlaced.
- Pooling of resources: Oil & gas business was financed through the resources of VIL.
- Co-existence for survival: Oil & gas business had no separate financial capabilities.

- Intricate link of subsidiaries: Loan documents and security arrangements establish the intricate link clearly.

- Intertwined accounts and Inter-looping of debts

- Singleness of economics of units

- Common financial creditors: The lenders are the members of ‘consortium of banks’ and SBI had filed the application on behalf of the Joint Lenders’ Forum substantiating the fact that there are common financial creditors between the companies.

5. Relying on the above observations, it was held that all the 13 companies consolidated vide order dated 8th August, 2019 were group companies and hence the assets of single entity could not be transgressed separately from the assets of VIL.

6. The rationale behind the decision was that the elements of consolidation were met and hence the debtor could not be forced into liquidation despite having sufficient means and assets that could lead to resolution of the debts.

Conclusion

The NCLT in its decision dated 8th August, 2019 and 12th February, 2020 has laid down relevant considerations and elements for the implication of the doctrine of substantial consolidation.

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Moreover, substantial consolidation of assets. Including foreign assets is a welcome step for the stakeholders as it shall assist in adequate and proper completion of CIRP process, apart from the fact that inclusion shall also be an incentive for the prospective Resolution Applicant to apply for the revival of the corporate debtor.

This may also be a significant decision in achieving the object of “ease of doing business” and “increase in foreign investments”.