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SET-OFF AFTER EXTINGUISHMENT: RECALIBRATING THE CLEAN SLATE DOCTRINE UNDER THE IBC

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A CASE COMMENT ON *UJAAS ENERGY LTD. V. WEST BENGAL POWER DEVELOPMENT CORPORATION LTD*[3]

ABSTRACT

The Insolvency and Bankruptcy Code 2016 brought about a drastic change in the world of Indian corporate resolution by implementing the "Clean Slate Doctrine", under which all claims not part of an accepted resolution plan will be extinguished. Absolute implementation of this doctrine is questionable, as there is a case in which one party had a valid defense that was not settled on the merits. This case comment analyzes the Supreme Court's judgment in Ujaas Energy Ltd. vs. West Bengal Power Development Corporation Ltd. In this case, an interesting conflict emerged between the principle of the finality of the resolution process and the doctrine of natural justice. Using a doctrinal and analytical methodology, the study examines the Court's approach to the enforceability of claims versus their continuing residual utility in law by considering judicial precedents, statutory interpretation, and the wording of the resolution plan. The findings show how the Court avoided the literal interpretation of extinguishment in allowing the utilization of a claim that would have otherwise been considered extinguished as a counterclaim, but not its enforcement on its own merits. Even as the exception

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[3] *Ujaas Energy Ltd. V. West Bengal Power Development Corporation Ltd* 2026 LiveLaw (SC) 272 (India).

maintains commercial certainty regarding the "clean Slate approach", there are notable criticisms, as highlighted above, including the possibility that the exception will make it difficult to draw the line between claims and defenses. The comment ends on the note that the decision ensures bankruptcy law remains an effective process, while also highlighting the importance of careful framing when drafting a resolution plan.

Keywords: *IBC, clean slate doctrine, set-off, resolution plan, extinguishment of claims*

I. INTRODUCTION

India's insolvency system has undergone a major transformation due to the provisions of the Insolvency and Bankruptcy Code of 2016 (IBC). Whereas previous systems focused on resolving claims against a corporate debtor through prolonged litigation and negotiations, leading to lengthy court proceedings, the IBC emphasizes quick resolutions and provides businesses with some certainty in the future. One of the major elements of this regulatory framework is the "Clean Slate" doctrine, which provides that, once a resolution plan is approved, a corporate debtor will not have to pay any debts not included in the plan. This Supreme Court has appreciated this principle as an important part of the insolvency regime and as a way to incentivize settlements. At the same time, its strict application has raised concerns about fairness, as claims against corporate debtors have been dismissed for procedural reasons.

The Supreme Court's decision in ***Ujaas Energy Ltd. v. West Bengal Power Development Corporation Ltd.*** deserves special mention in the context of the interplay between the two fields of law – insolvency and arbitration. An important and difficult question was put before the Supreme Court: whether a proved claim can be set off during arbitration after the implementation of the approved resolution plan. The importance of this ruling lies in the fact that it did not deviate from the principle of fresh start, but provided the clarification with the help of an exception..

II. FACTUAL BACKGROUND OF THE CASE

The conflict originated from an agreement between the parties concerning the installation of solar photovoltaic plants. The respondent, a public-sector company, advertised the e-tender in February 2017. The appellant, a small entity in the field of solar energy, secured the contract, which was awarded by way of a Letter of Award dated 12 May 2017. As is often the case in such business ventures, there was confusion among the parties regarding their respective responsibilities. However, before the issues could be sorted through normal legal procedures, the appellant was entered into the Corporate Insolvency Resolution Process on September 17, 2020 as per IBC provisions.

The procedural changes necessitated by the CIRP process are claimed to form the basis of the objections made by both the appellants and the respondents. The resolution professional had referred the matter to arbitration at the appellants' request. It was due to this referral that the respondent filed a counterclaim against the appellants' claim. The main issue with the counterclaim filed by the respondent was that the respondent did not make a claim through the resolution professional during this CIRP process. Even though this may seem like a small issue, the absence of the claim became relevant when the adjudicating authority approved the resolution plan on November 17, 2023, as it would be seen to have effectively terminated the CIRP process.

After the resolution plan was approved, the appellant asked that the respondent's counterclaim be dismissed because all claims not part of the resolution plan were no longer valid. The arbitral tribunal agreed with this argument and turned down the counterclaim in an interim award. A Single Judge of the High Court first agreed with this point of view. The Division Bench, on the other hand, took a different approach. They said the tribunal had conducted a detailed adjudication that was more like a final judgment and directed that the arbitral proceedings continue. It was in this situation that the case went to the Supreme Court.

III. CENTRAL LEGAL ISSUE

A. Whether The Respondent Ought To Be Allowed To Raise The Plea Of Set-Off Before The Tribunal, Having Regard To The Extinguishment Of The Respondent's Counterclaim?

The question below raises three questions:

1. Does The Approval Of A Plan Under Section 31(1) Of The Insolvency And Bankruptcy Code Completely Bar Any Claims Not Included In The Plan?

2. Is a defence Equivalent To An Independent Claim, Or Does It Have Different Effects And Limitations?

3. Does The Clean Slate Doctrine Apply Absolutely To Every Situation, Or Are There Situations Where Exceptions Exist?

IV. <u>Extinguishment vs. Enforceability: the court's interpretative shift</u>

Even though this language seems drastic, the Court took a cautious, delicate approach to interpretation. The clause merely prohibits claims for "payments or settlements" but does not clearly state that these can not be used in defense. In this context, the Court said:

This position has been authoritatively settled in ***Ghanashyam Mishra v. Edelweiss Asset Reconstruction Co. Ltd***[4], where the Court held:

"All such claims, which are not a part of the resolution plan, shall stand extinguished, and no person will be entitled to initiate or continue any proceedings in respect to a claim, which is not part of the resolution plan."

Applying this principle, the Court had no trouble holding that the respondent's counterclaim could not be pursued as a separate claim because it was not filed during the CIRP. It said without a doubt. But what makes this decision different from earlier ones is that the Court didn't see extinguishment as a complete barrier for all purposes. Instead, it looked into whether a claim that had been dropped could still be used in a limited way, such as for a defense by set-off.

A particularly noteworthy Supreme Court ruling on the issue at hand is ***Ujaas Energy Ltd. v. West Bengal Power Development Corporation Ltd.,***[5] which addresses the relationship between insolvency law and arbitration law. Indeed, the Supreme Court was dealing with a challenging question: whether a proved claim can be set off during arbitration proceedings after the execution of a resolution plan. What makes the ruling remarkable is not that it diverges from the idea of a new beginning, but rather how the issue was explained through an exception to the rule.

The Court's resolution of this tension turned on a close reading of the resolution plan itself, particularly ***Clause 12.4.1***, which provided:

"no other payments or settlements… will have to be made… all such claims… including counter claims… shall stand irrevocably and unconditionally abated, discharged, settled and extinguished in perpetuity…"

[4] *Ghanashyam Mishra v. Edelweiss Asset Reconstruction Co. Ltd* (2021) 9 SCC 657

[5] *Supra note* 1

Even though this language seems drastic, the Court took a cautious, delicate approach to interpretation. The clause merely prohibits claims for "payments or settlements" but does not clearly state that these cannot be used in defense. In this regard, the Court held:

"It does not appear to bar a plea of set-off being raised as a 'defense'... although claims for any 'payment' or 'settlement'... are specifically not recoverable."

Further clarifying its position, the Court stated:

"The abovementioned clause... does not expressly, or even impliedly, exclude the plea of set-off as a defense."

This interpretive action is important. The Court didn't view extinguishment as a means to completely extinguish the claim; instead, it viewed it as a means to limit its enforceability. In other words, the claim can't be used to get money back, but it might still be used as a defense. The Court's readiness to take this position was also based on fair considerations. It noted that the respondent had raised its counterclaim before the arbitral tribunal before the approval of the resolution plan, and that the Resolution Professional was aware of the claim. But it wasn't included in the plan.

The IBC jurisprudence has shifted towards equity, marking a new era for courts that have historically emphasized technical compliance; however, the inclusion of equitable factors will support balanced outcomes and demonstrate that a lack of technical reliability will not always result in an unjust outcome. The Court will also provide a remedy that is equitably founded by determining that a defendant can use an inherently unlitigated counterclaim as a defense (through set-off) while remaining barred from an independent counterclaim as the only basis for seeking a remedy from the plaintiff.[6]

V. CRITICAL APPRAISAL OF THE DECISION

In its ruling, the Supreme Court's decision in Ujaas Energy Ltd. v. West Bengal Power Development Corporation Ltd. represents a landmark development in the evolution of Insolvency law — as interpreted in the context of the Clean Slate doctrine under the Code to Insolvent Individuals (Insolvency and Bankruptcy Code) 2016 (Code). The Court's reaffirmation of its ruling in Ghanashyam Mishra & Sons vs. Edelweiss Asset Reconstruction Co., Ltd., establishes that all claims not included within an approved resolution plan will be

[6] Udey Singh, The Bankruptcy of Certainty: The Clean Slate Doctrine, 9 Int'l J.L. Mgmt. & Human. 321 (2026). https://ijlmh.com/paper/the-bankruptcy-of-certainty-the-clean-slate-doctrine/

extinguished upon approval of the Plan, is well established in precedent, and so is fundamental to how the Code will function. In doing so, the Court has reiterated the rationale upon which it rests the decision — "*no one can file or continue with a claim that was not part of the resolution plan after approval"* — and maintained this important principle to provide the level of certainty and predictability required to attract prospective resolution applicants and achieve the goal of corporate recovery through the resolution process. Thus, by limiting any reduction in the enforceability of the order as to net claims, the Court was able to maintain the integrity of the insolvency process's structure.

4.1 The defensive set-off exception

This is particularly relevant given the ruling's importance, as it involves a subtle deviation from the doctrine itself by recognizing a limitation on its application to set-offs made purely in defense, since, both conceptually and practically, such an approach makes sense and is necessary. Moreover, the court recognizes that by accepting a destroyed claim to set off creates harmony in the application of insolvency laws and the principles of fairness; also, that if one denies the possibility of making such a defense, then the other party will have to settle everything that he owes him completely, although according to the principle of reciprocity they both should do so, thus causing an unjustified benefit to one side. Thus, by considering all the above-mentioned points, the function of the set-off is to extinguish liability.[7]

4.2 textual interpretation: clause 12.41 and expression unius

Moreover, the Court's interpretation also provides clarity to the judgment. No prohibition against set-off is being imposed by the Court, as indicated by its analysis of the text of the Resolution Plan, namely Claim 12.4.1, which prohibits the parties from making "payments" or "settlements" in relation to claims not specified in the Resolution Plan. The Court applies a rigorous textual method of interpretation and concludes that the clause imposes no limitations on the prohibition of payments or settlements. Consequently, the Court does not impose any restrictions on the Resolution Plan that are not mentioned in the Plan itself. In conclusion, this ruling indicates the increasing importance of drafting proper Resolution Plans by encouraging stakeholders to consider identifying Observable claims.

4.3 concerns, misuse, and precedential distinction (distinguishing Bharti Airtel vs. Aircel)

[7] Shubham Saini & Suyash Goverdhan, Set-Off Conundrum Under Insolvency and Bankruptcy Code, 2016, LiveLaw (Aug. 27, 2024). https://www.livelaw.in/articles/set-off-conundrum-under-insolvency-and-bankruptcy-code-2016-267740

However, the ruling raises serious questions that must be answered. The main issue at stake seems to be whether the concept of "claim" would be used to commit a fault. Indeed, someone might be interested in using a barred claim's defensive posture to avoid consequences arising from failing to file a CIRP claim. Hence, there would be a likelihood of more cases being brought to court, which would involve determining what kind of defense would be considered appropriate to raise before the court. Nonetheless, although this narrow exception is fair, it risks creating problems by making it impossible to achieve the predictability required when using the clean slate doctrine.

Moreover, the Court's rationale in its current judgment departs from the earlier decision of the Supreme Court in ***Bharti Airtel Ltd. v. Aircel Ltd.,***[8] which considered the right to set off arising during the ongoing CIRP proceedings. By distinguishing this case on the ground that it arose after the court approved the resolution plan, the Court highlights the contextual nature of insolvency jurisprudence, as it relates to individual facts. That the distinction made is persuasive, as the nature of the legal effect of the claims is different pre- and post-conclusion of the CIRP. However, this distinction adds further confusion to the permissibility of set-off, which depends on the stage of the insolvency process and the specific terms of the resolution plan.

VI. STRIKING THE BALANCE: FINALITY PRESERVED, JUSTICE NOT SACRIFICED

In ***Ujaas Energy Ltd vs West Bengal Power Development Corporation Ltd***, the Supreme Court's verdict has brought about an important change and new development in the insolvency laws under the Insolvency and Bankruptcy Code, 2016. As the court has upheld the clean slate doctrine, the ruling constitutes a narrow and relevant exception from the established regulation of the set-off process. Nevertheless, the various claim categories will maintain the essence of Section 31(1) without being overly rigid or excessively harsh in particular cases. Moreover, the ruling conveys the message that claims that have been extinguished will still retain their significance and relevance if employed as an instrument to defend the claimant against another party’s claim.

However, the ruling raises the question of how to correctly differentiate between claims and defenses, which may complicate its application in practice. Besides, there is a risk of misapplication of the possibility of recharacterization, which may serve as an additional lever, putting judges and tribunals under pressure when applying the discussed principle.

[8] *Bharti Airtel Ltd. v. Aircel Ltd.* (2024) 4 SCC 668

Still, the Court of Appeal ruling regarding the nature of the right of set-off minimizes the aforementioned risks.