

## ***Polluters Escape? Plight of Environmental Claims in India’s Insolvency Framework***

*CS (Dr) Pallavi Baghel, Bandana Mishra & Lekhana MS\**

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### **ABSTRACT**

*The Insolvency and Bankruptcy Code, 2016 (**The Code** or **IBC**) is a guiding statute for reorganization and insolvency resolution in India, which necessitates the streamlining of credit availability, balancing the interests of stakeholders, prioritizing government dues, and maximizing asset value. However, the primary objective of the Code is to secure an equitable division of property for the creditors of insolvent debtors and safeguard the creditors from any detrimental conduct by the insolvent debtor by ensuring remediation through resolution or liquidation processes. This paper examines the treatment of environmental claims under India’s IBC, highlighting systemic loopholes that allow polluters to evade liability in the context of safeguarding such creditors. Environmental claims, categorized as unsecured or contingent debts, are relegated to the lowest*

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\* CS (Dr) Pallavi Baghel is an Assistant Professor at Symbiosis Law School, Pune. Bandana Mishra and Lekhana MS are fourth-year BA, LLB (Hons) and BBA, LLB (Hons) students respectively at Symbiosis Law School, Pune. The authors may be contacted at 22010125415@symlaw.ac.in.

*priority under the IBC's waterfall mechanism, enabling insolvent corporations to circumvent cleanup costs and penalties through strategic insolvency filings. Judicial precedents, such as the Essar Steel case, exacerbate this issue by devaluing environmental liabilities during resolution processes. The analysis contrasts India's framework with international approaches, such as the United Kingdom's (UK) prioritization of remediation costs as liquidation expenses and the United States of America's (US) non-dischargeability of environmental obligations, to propose reforms. Methods of computing environmental compensation and interim solutions have been proposed, which include stricter Environmental, Social and Governance (ESG) reporting requirements, granting environmental claims 'secured creditor' status with a Pollution Index over 50, and exempting public-interest environmental actions from moratoriums. The paper underscores the need to balance creditor rights with ecological accountability, and further advances research to advocate for legislative clarity and alignment with global best practices to prevent exploitation of insolvency frameworks.*

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## I. INTRODUCTION

An insolvent debtor's assets are distributed amongst the creditors during liquidation in accordance with the priority order outlined under Section 53 of the Code, known as the waterfall mechanism. The Code provides a wide array of grounds for the process, including 'judgments, contractual, legal, equitable, secured and unsecured debts.' One such type of ground involves environmental claims, such as Government fines and cleanup costs.

When an insolvent or 'corporate debtor' files for bankruptcy with an existing environmental liability, the latter by default slips under the category of unsecured debts as per the waterfall mechanism, creating a dichotomy between insolvency and environmental law. A two-fold distinction can further be made under the unsecured category: **a)** In case a decree has already been passed by the court, such claimants become decree-holders;<sup>1</sup> **b)** In case the debtor is already declared insolvent, a moratorium is imposed, prohibiting any further judicial intervention. It is then categorized as a contingent claim, which cannot be freshly adjudicated after the initiation of the Corporate Insolvency Resolution Process (**CIRP**).<sup>2</sup>

The latter paves an easy path for the companies to exploit the existing framework by voluntarily committing environmental defaults, then applying for insolvency, and creating a moratorium. Moreover, judicial interpretations by the Supreme Court, such as that in the case of *Committee of Creditors of Essar Steel India Limited v Satish Kumar*

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<sup>1</sup> *Subhankar Bhowmik v Union of India*, WP(C)(PIL) No 18/2022.

<sup>2</sup> Insolvency and Bankruptcy Code 2016, s 14 (**IBC**).

*Gupta & Ors*,<sup>3</sup> validated the resolution process by holding that “the resolution professional was correct in only admitting the environmental claim at a notional value of INR one (1) due to the pendency of disputes”. This develops a pitfall for environmental claims, by ranking them at the bottom of the spectrum, and takes an exploitative form, especially owing to the adverse effects on the ecosystem.

Therefore, this paper critically examines the treatment of environmental claims under IBC, 2016, highlighting loopholes that enable polluters to evade liability. It explores how environmental claims are deprioritized in insolvency proceedings and contrasts this with international frameworks from the UK, the US, and the United Nations Commission on International Trade Law (**UNCITRAL**). The study discusses judicial precedents, the principle of a fresh start, and how environmental obligations are treated as unsecured claims. It proposes reforms such as granting secured status to environmental claims and integrating ESG reporting.

It also attempts to propose possible interim solutions, ensuring a balanced approach between creditor rights and environmental protection by evaluating the feasibility of granting secured creditor status to environmental claims and its implications on the CIRP. The authors in this paper primarily use a doctrinal methodology of research using relevant data from primary sources like legislation, judgments, and secondary sources such as survey statistics, existing legal doctrines, published reports, etc.

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<sup>3</sup> [2020] 8 SCC 531.

## II. LITERATURE REVIEW

Within the existing literature, Mr Devendra Mehta, in his paper *Should Environment Claims Be Granted the Status of Secured Creditors in the Insolvency and Bankruptcy Code, 2016?*,<sup>4</sup> examines how insolvency law interacts with environmental obligations. He argues that environmental claims should be given secured creditor status to prevent polluters from escaping liability. However, he fails to address a key challenge, which is how to ascertain the valuation of environmental claims.

Similarly, in the paper *Environmental Claims under Indian Insolvency Law: Concepts and Challenges*,<sup>5</sup> P Ram Mohan explores how the Code handles environmental liabilities. He argues that the current system prioritizes economic recovery over environmental responsibility and suggests bridging this gap by either securing environmental claims as debt or using insurance mechanisms. However, his study does not propose any interim solutions that could be implemented while legislative reforms are still in progress.

On the international front, the *UNCITRAL Legislative Guide on Secured Transactions*<sup>6</sup> offers a structured approach to modernizing secured credit laws by providing clear guidelines on creating and enforcing security interests. Likewise, the *UNCITRAL Legislative Guide on*

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<sup>4</sup> Devendra Mehta, 'Should Environment Claims Be Granted the Status of Secured Creditors in the Insolvency and Bankruptcy Code, 2016?' (2023) IV GNLU Student Law Review, <<https://ssrn.com/abstract=4701415>>.

<sup>5</sup> MP Ram Mohan and Sriram Prasad, 'Environmental Claims under Indian Insolvency Law: Concepts and Challenges' (2024) 59(1) Texas International Law Journal

<sup>6</sup> United Nations, *UNCITRAL Legislative Guide on Secured Transactions*, United Nations Commission on International Trade Law 20 (2010) <[https://uncitral.un.org/en/texts/securityinterests/legislativeguides/secured\\_transactions](https://uncitral.un.org/en/texts/securityinterests/legislativeguides/secured_transactions)> accessed 16 February 2025 (ULGST).

*Insolvency Law*<sup>7</sup> provides a comprehensive blueprint for effective insolvency laws, aiming to balance financial restructuring with the interests of all stakeholders. However, their detailed framework, with little autonomous flexibility, might be impractical for resource-constrained jurisdictions owing to varying developmental rates and policy approaches.

Furthermore, Judson Boomhower, in his paper *Drilling Like There's No Tomorrow: Bankruptcy, Insurance, and Environmental Risk*,<sup>8</sup> delves into the effect of bankruptcy on the environmental outcomes, specifically in the oil and gas extraction sector prevalent in the United States. The 'judgment-proof problem' is identified, where firms with limited assets take excessive risks because they know they can discharge liabilities through bankruptcy. Furthermore, the paper reviews existing policy interventions, such as the mandatory purchase of surety bonds or insurance, that compel firms to internalize expected environmental costs. On the aspect of International Insolvency, David Neiman,<sup>9</sup> correlates the doctrine of fresh start with the polluter pays principle to bear the cost of remediation and then critically examines how globalization and the resultant increase in cross-border insolvencies have driven the development of international frameworks, such as the

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<sup>7</sup> United Nations, UNCITRAL Legislative Guide on Insolvency Law, United Nations Commission on International Trade Law 86 (2010) <[https://uncitral.un.org/sites/uncitral.un.org/files/media-documents/uncitral/en/09-82670\\_ebook-guide\\_09-04\\_10english.pdf](https://uncitral.un.org/sites/uncitral.un.org/files/media-documents/uncitral/en/09-82670_ebook-guide_09-04_10english.pdf)> accessed 16 February 2025 (ULGIL).

<sup>8</sup> Judson Boomhower, 'Drilling Like There's No Tomorrow: Bankruptcy, Insurance, and Environmental Risk' (2019) 109 (2) American Economic Review.

<sup>9</sup> David Neiman, 'International Insolvency and Environmental Obligations: A Prelude to Resolving the Conflicting Policies of a Clean Slate versus a Clean Site in Transnational Bankruptcies' (2003) 8(3) Fordham Journal of Corporate & Financial Law.

*UNCITRAL Model Law*, designed primarily to coordinate creditor claims and streamline bankruptcy proceedings, but often neglect the integration of non-bankruptcy obligations, notably environmental claims. It rightly illustrates how courts have struggled to reconcile the discharge of environmental liabilities with the overarching goal of debtor rehabilitation, thus exposing a regulatory lacuna in handling transnational insolvency cases, underscoring the necessity of a hybrid legal framework.

The literature review effectively highlights key gaps in existing research on environmental claims within insolvency frameworks. However, to make this section more relevant to the paper's discussion, it would be beneficial to further emphasize how the identified gaps directly impact India's insolvency landscape. While previous studies argue for granting secured creditor status to environmental claims, they do not fully address the procedural and economic challenges of implementing such reforms within the Indian context. For instance, the lack of a standardized valuation framework for environmental claims could lead to inconsistent judicial interpretations, undermining the feasibility of prioritizing such claims in insolvency proceedings. Additionally, while international frameworks like UNCITRAL offer structured insolvency guidelines, their applicability to India requires adaptation to align with domestic legal and financial systems. By integrating this perspective, the literature review supports the paper's argument that legislative and judicial interventions must be tailored to India's unique regulatory environment rather than relying solely on international precedents. In this paper, the authors have tried to address some of these inconsistencies. However, the scope of further research always exists, such as analyzing the reverse impact of

the environment on businesses and procedural and economic challenges of granting the status of secured creditor to environmental claims.

### III. ENVIRONMENTAL CLAIM AND PRINCIPLE OF FRESH START

Claims can be understood as the rights or grounds of the creditors to assert their amounts through the resolution process, commonly known as the “right to payment”. It is defined under Section 3(6) of the Code, and has a very broad scope encompassing “judgments; fixed, undisputed, secured, unsecured, legal, equitable debts”, etc. It can also be referred to as the ‘right to remedy’ in the event of a breach of a lawful contract, leading to a violation of monetary payments, determinative or otherwise. Any creditor (operational or financial, along with the concerned proof), workmen, employees, home buyers, or any other party, is allowed to submit their claims under the Code. However, a Financial Creditor cannot contest another Financial Creditor’s order of admission to CIRP solely for the reason or on the presumption that it has a stronger claim than the other Financial Creditor. Such reasoning of ‘first claim’ or ‘superior claim’ was dismissed by the National Company Law Appellate Tribunal (NCLAT) in the case of *L&T Infrastructure*.<sup>10</sup>

Judicially, claims can be defined as a demand for something due or to seek/ask for the ground of right.<sup>11</sup> However, these demands/amounts are to be verified and subject to revision based on various documentation through the creditor or corporate debtors. This definition has been

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<sup>10</sup> *L&T Infrastructure Finance Company Ltd v Gwalior Bypass Project Ltd.*, Company Appeal (AT) (Insolvency) No. 676 of 2019

<sup>11</sup> *Hameedia Hardware Stores v B Mohan Lal Sowcar* [1988] 2 SCC 513 (India).

broadened by the courts<sup>12</sup> by lifting the mandate on the debts to be matured. Even the debts scheduled to be paid in the future could be taken into consideration as claims and do not get extinguished automatically.<sup>13</sup> This can be inferred from the broad definition of claims given under the Code.<sup>14</sup> The wording “...whether or not reduced to...” provides the scope of such possible interpretations. Furthermore, if a claim charged is penal or punitive in nature, for example, a fine for environmental destruction, then the interest levied on the same also forms a part of the claim, the condition being that no interests shall be charged thereafter.<sup>15</sup>

Herein, it becomes imperative to note that no statute specifically defines environmental claims. Judicial bodies have dealt with environmental claims in multiple cases.<sup>16</sup> It came to be streamlined as claims emerging from environmental harm,<sup>17</sup> covering pollution, biodiversity loss, contamination, etc. It may also entail clean-up costs, including but not limited to government fines. In terms of legislative definition, the environmental claims are probably covered by the first category of “right to payment,” i.e., the judgments. This can further be classified into two

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<sup>12</sup> *Andhra Bank v FM Hammerle Textile Ltd.*, Company Appeal (AT) (Insolvency) No. 61 of 2018

<sup>13</sup> *Export Import Bank of India and Ors v Resolution Professional JEKPL Private limited and Ors* Company Appeal (AT) (Insolvency) No 304 of 2017; *Andhra Bank v M/s FM Hammerle Textiles Ltd.* Company Appeal (AT) (Insolvency) No 61 of 2018.

<sup>14</sup> IBC, s 3(6).

<sup>15</sup> *Central Bank of India v Ravindra and Ors* [2001] AIR 2001 SC 3095.

<sup>16</sup> *Union Carbide Corporation v Union of India* [1988] AIR 1988 SC 1531 (India); *M C Mehta v Union of India* [1986] 2 SCC 176 (India) (Oleum Gas Leak case); *M C Mehta v Union of India* [1988] AIR 1988 SC 1037 (India) (Tanneries case); *K K Muhammed Iqbal v Kerala State Pollution Control Board* Original Application No 143 of 2020 (SZ); *Sidhgarbyang Kalyan Sewa Samiti v State of Uttarakhand* Original Application No 123/2018; *Saloni Ailawadi v Union of India* [2019] Original Application No 509/2015 (Volkswagen emissions case).

<sup>17</sup> *A P Pollution Control Board v M V Nayudu* [1999] 2 SCC 718 (India).

categories: contingent claims and other types of creditors or decree holders.<sup>18</sup> The contingent claims are the ones that cannot be precisely determined and depend on factors such as the outcomes of a trial, whereas for the decree holders, the court directs the company to compensate the claimant a certain amount. Furthermore, if an exact amount cannot be devised by the creditor owing to a contingency, the Interim Resolution Professional or Resolution Professional shall compute the best estimate of such an amount, based on the available information.<sup>19</sup> But because of the moratorium imposed, even the decree holders are bound to enter into the resolution process. In broader terms, the above two creditors, along with operational creditors<sup>20</sup> fall under the ambit of “any remaining debtors”, meaning their claims generally remain unrealized.

An example of exploitation of the aforesaid scheme is coal mining companies in the United Kingdom. They register themselves as subsidiaries, paying out ascertained profits to the parent company, and declaring liquidation, to escape environmental damage liabilities.<sup>21</sup> It becomes prudent to question if such a “fresh start” of the company post-liquidation would still make environmental claims admissible.

M P Ram Mohan Prasad, in his paper *Environmental Claims under Indian Insolvency Law: Concepts and Challenges*,<sup>22</sup> examined

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<sup>18</sup> *Subhankar Bhowmik v. Union of India* (2022) 233 Comp Cas 163.

<sup>19</sup> Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations 2016, reg 14.

<sup>20</sup> IBC, s 5(21).

<sup>21</sup> *BTI 2014 LLC v. Sequana S.A.* [2022] UKSC 25 (UK); Joshua Macey and Jackson Salovaara, ‘Bankruptcy as Bailout: Coal Company Insolvency and the Erosion of Federal Law’ (2019) 71 *Stanford Law Review*.

<sup>22</sup> n 5.

insurance policies and proved that the language of the policy provided an avenue of exemptions via the principle of fresh start, and saved the companies from having to defend themselves from earlier environmental claims. Such practices are further supported by Section 6 of the Code, which creates a beneficial status for the principle of a fresh start<sup>23</sup> and whether such environmental claims can be initiated by a subsequent suit. The principle of “fresh start” in insolvency law allows a successfully rescued company to begin anew financially, free from previous liabilities, except as specified in the resolution plan. This is similar to the doctrine of Clean Slate, which has been diluted by the introduction of contingent claims into the picture.<sup>24</sup> It can be understood as absolving all pending claims and liabilities, once the National Company Law Tribunal (NCLT) has approved a resolution plan. This works in conjunction with Section 31(1) and Section 14 of the Code, which disallows revival of any claims against the corporate debtor.<sup>25</sup> Consequently, insurers may seek to avoid liability, as their obligations are directly tied to the company’s former liabilities. While this scenario remains largely untested, a straightforward amendment permitting claimants to sue insurance companies directly might address such issues.

#### IV. INDIAN FRAMEWORK

Let us imagine a situation where pollution results in a high death toll and significant property damage in India. A freeze or moratorium on lawsuits against the polluting company is enforced if it defaults and is

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<sup>23</sup> Public Liability Insurance Act 1991, s 6.

<sup>24</sup> *Ultra Tech Cement Ltd v Minita D Raja* IA 1304/NCLT/MB-IV/2020.

<sup>25</sup> *Ghanashyam Mishra & Sons Ltd v Edelweiss Asset Reconstruction Co Ltd* [2021] 9 SCC 657 (India).

acknowledged as insolvent under the Code. If any parties have any ongoing litigation, they must register it with a resolution professional, and such claims shall be considered contingent.

As per the hierarchy of the waterfall mechanism, the financial or secured creditors get priority over unsecured creditors/decreed holders/contingent claimants, pushing them to the very bottom of the priority ranking and hence leaving them with paltry returns (if any). Furthermore, if the CIRP is successfully accomplished, then no previous liabilities are carried forward, and the company gets a fresh chance to establish its base by the principle of a fresh start. It was reiterated in the case of *Ghanashyam Mishra and Sons (P) Ltd v Edelweiss Asset Reconstruction Co Ltd*,<sup>26</sup> with the only exception being contingent claims, which might be litigated later to determine their exact value.<sup>27</sup> However, this is seldom utilized. Therefore, this asserts the fact that environmental claimants are unlikely to receive any amounts.

#### A. Statutory Basis

In the broader spectrum, the Public Liability Insurance Act 1991 (**PLI Act**) provides for compensation to victims of accidents, damage to public or private property.<sup>28</sup> Such compensation is sought for accidents caused by industries or organizations handling hazardous substances<sup>29</sup> and can be claimed on a no-fault liability basis.<sup>30</sup> ‘Accidents’ defined under

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<sup>26</sup> *Ghanashyam Mishra & Sons (P) Ltd v Edelweiss Asset Reconstruction Co Ltd* [2021] 9 SCC 657 (India).

<sup>27</sup> *Punjab National Bank v Bhushan Power & Steel Limited* (2022) 233 Comp Cas 572; *Shaji Purushothaman v S Rajendran Company Appeal (AT) (Insolvency)* No 551 of 2020.

<sup>28</sup> The Public Liability Insurance Act 1991, s 3(e).

<sup>29</sup> The Public Liability Insurance Act 1991, Preamble.

<sup>30</sup> The Public Liability Insurance Act 1991, s 3.

Section 2(a) of the PLI Act are said to include accidental derelictions in the handling of a hazardous substance that affects individuals by “...continuous, intermittent, or repeated exposure that causes death, injury to a person, or damage to property”.

Hazardous substances, on the other hand, are said to include only those substances enumerated in the Environment (Protection) Act, 1986, and that exceed the prescribed standards as notified by the Central Government.<sup>31</sup> This thereby excludes many instances of environmental damages which may be caused by voluntary acts of the defaulting companies or by any of the non-listed hazardous/non-hazardous substances, hence escaping liability from the framework of the PLI Act. However, the PLI Act provides powers to the Collector to grant a temporary injunction to prevent the removal or disposal of property to evade payment under the Act.<sup>32</sup>

While the PLI Act empowers authorities to restrain assets from being disposed of or removed through injunctive measures to prevent the evasion of liability, the safeguards so carefully established stand neutralized once the IBC moratorium attaches upon the commencement of CIRP proceedings. The pecuniary liabilities arising under the PLI Act thereby subsume into the IBC claims process and when subjected to the waterfall mechanism, stands diluted to the point of a de facto evasion. The resulting gap thereby lies in the misalignment of the intersection of the statutes: despite public interest imperative of environmental protection, environmental remediation claims remain structurally

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<sup>31</sup> The Public Liability Insurance Act 1991, s 2(d).

<sup>32</sup> The Public Liability Insurance Act 1991, s 7(8).

vulnerable under the IBC waterfall that seeks to maximize value and equitable allocation of the same.

*B. Role of the Indian Judiciary*

The objective of the Code has already been established by the legislature in the preamble to the Code. Even the judiciary has reiterated that the “...primary focus of the legislation is to ensure revival and continuation of the corporate debtor by protecting the corporate debtor from its own management and a corporate death by liquidation. The Code is thus beneficial legislation which puts the corporate debtor back on its feet”.<sup>33</sup> Herein, it is important to note the primacy of twin tests for the said resolution process, ie, the existence of debt and default. This is not contingent on the presence of any other factors.

However, the judiciary, on various occasions, has tried to curb the malpractice of using insolvency as a shield to circumvent environmental penalties. At times, they have even denied insolvency on the grounds of escaping environmental claims. It was upheld in the case of *Canara Bank v GTL Infrastructure Limited*<sup>34</sup> that, regardless of the existence of debt and default, the court has discretion to deny the insolvency resolution on account of evading environmental claims. Such steps were also taken by the NCLT in certain cases, like the *Hytone Merchants (P) Ltd v Shatabdi Investment Consultants (P) Ltd*.<sup>35</sup> The practicality of this approach is still uncertain, considering the imposition of the moratorium on judicial procedures. The criticism of the judgment of *Vidarbha Industries Power*

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<sup>33</sup> *Swiss Robbins Private Limited v Union of India* [2019] 3 SCR 535 (India).

<sup>34</sup> *Canara Bank v GTL Infrastructure Limited* CP (IB)-3604(MB)/2018.

<sup>35</sup> *Hytone Merchants (P) Limited v Satabadi Investment Consultants (P) Limited* Company Appeal (AT) (Insolvency) No 258 of 2021.

*Limited v Axis Bank Limited*<sup>36</sup> by the NCLAT shows the non-acceptance of this approach. However, the SC clarified the legislative intent by explaining the wording of Section 7(5) of the Code. “It may, by order, admit such application...” upholds the discretion of courts irrespective of satisfaction of the twin tests. The court observed that “...the Adjudicating Authority (which is the NCLT) might examine the expediency of initiation of CIRP, taking into account all relevant facts and circumstances, including the overall financial health and viability of the Corporate Debtor. The Adjudicating Authority may, in its discretion, not admit the application of a Financial Creditor.”

An example of such discretion can be seen when homebuyers were granted the status of financial creditors in the mid-2018s, which was later challenged in the court of law as going against the hierarchy of the waterfall mechanism and hence, unconstitutional.<sup>37</sup> The Supreme Court, in this case, upheld the validity of the said inclusion by reasoning it to be in line with the Real Estate (Regulation and Development) Act, 2016 and owing to the pressing need of the society.<sup>38</sup> Furthermore, the step was considered to be important given the limited legal resources available to the homebuyers against the insolvent developers. If an analogy were to be drawn from this aspect, it can be inferred that there is a need for further amendment with regard to environmental claims, especially considering the limited rights available against such exploitation.

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<sup>36</sup> *Vidarbha Industries Power Limited v Axis Bank Limited* [2022] 8 SCC 352 (India).

<sup>37</sup> The Insolvency and Bankruptcy (Amendment) Ordinance 2018.

<sup>38</sup> *Pioneer Urban Land and Infrastructure Limited & Anr v Union of India & Ors* [2019] 10 SCR 381 (India).

### C. *The Problem with the Current Framework*

By the aforesaid explanation, it is quite clear that the objective of the Code, that is, allowing the successful resurrection of the companies, and that of the environmental laws, which is to protect the environment, do not align. One of the primary reasons for this disproportionality is that the damage caused by pollution is priced at zero currently, assigning no monetary value to the emissions. This runs on the assumption that they will be priced at zero in the future, too. But if this were to change in the future, then it would have a detrimental effect on the company's resolution process. For example, the practice of purchasing carbon footprints assigns a pecuniary value to greenhouse gas emissions, hence evaluating the environment monetarily.<sup>39</sup>

This, at times, results in contingent claims being entirely waived off, especially in cases where the financial creditors have a debt higher than the liquidation value. For example, Rs 112 is the debt of a financial creditor, and Rs 100 is the liquidation value.<sup>40</sup> Therefore, the procedure laid down is not prospective in nature and needs amendments to adapt to changing circumstances.

## V. INTERNATIONAL PERSPECTIVE

The United States, being the second largest manufacturing superpower in the world, and along with the UK, which is in the top ten of the Ease

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<sup>39</sup> Gareth Vipers, 'Shell Directors are sued over Action on Climate', (*The Wall Street Journal*, 9 February 2023) <<https://www.wsj.com/articles/shell-directors-are-sued-over-action-on-climate-11675938744>> accessed 16 February 2025.

<sup>40</sup> *Karad Urban Co-operative Bank Limited v Khandoba Prasanna Sakhar Karkhana Ltd* (2020) 12 Comp Cas-OL 576; *Percula Shipping & Trading INC v Dadi Impex Pvt Limited* (2019) 151 CLA 172.

of Doing Business Index,<sup>41</sup> are among the countries that have committed to net-zero carbon emissions by 2050 in Conference of Parties 26.<sup>42</sup> Commitments to net-zero carbon emissions, along with growing industrial development, are being driven by regulatory measures that prioritize environmental obligations. In addition, the US faces the evasion of environmental liabilities by coal companies, where they strategically sell such damaged properties to underfunded subsidiaries to claim bankruptcy.<sup>43</sup> The intersection between bankruptcy law and environmental protection in these jurisdictions thereby highlights the prioritisation that is requisite for environmental obligations, despite such companies lacking funding to satisfy debts. It thereby provides an interplay between the polluter pays principle and the waterfall mechanism and priority of claims for effective liquidation processes, balancing financial viability.

#### A. Remediation costs in the United Kingdom

In the *Doonin Plant Limited* case,<sup>44</sup> a recycling firm had deposited hazardous wastes while its waste license had been revoked and subsequently went into liquidation. The company, having not complied with the obligation of asset remediation earlier, fell insufficient in funding on the notice of the same. The Scottish Court in this case gave preference for remediation costs, terming them as liquidation costs which are to be paid in priority before other debts, creating a landmark

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<sup>41</sup> World Bank, 'Ease of Doing Business Rankings' <<https://archive.doingbusiness.org/en/rankings>> accessed 7 November 2025.

<sup>42</sup> Adam Fam and Sami Fam, 'Review of the US 2050 Long Term Strategy to Reach Net Zero Carbon Emissions' (2024) 12 Energy Rep 845.

<sup>43</sup> Joshua Macey and Jackson Salovaara, 'Bankruptcy as bailout: coal company insolvency and the erosion of federal law' (2019) 71 Stanford Law Review 879.

<sup>44</sup> *Re Doonin Plant Limited* [2018] ScotCS CSOH 89 (UK).

ruling potentially impacting decisions across the UK. It upheld that if such measures were not considered, it would allow insolvent debtors to escape environmental liability and damages caused by their conduct.

In the *Administrator of Dawson International PLC*<sup>45</sup> case in Scotland, Dawson International faced significant financial distress, with assets of approximately £3.3 million and pension liabilities of £10.4 million. A key issue arose concerning a contaminated site, previously operated by its subsidiary, which was causing ongoing groundwater pollution by tetrachloroethylene. The administrator sought judicial direction on the classification of potential remediation costs to consider whether expenses in potential remediation costs of environmental damage were merely an administrative expense or a liability of the organisation, constituting a priority over other creditor claims. In India, a parallel application of the same can be strengthened by clarifying the role of environmental regulators in insolvency proceedings and granting them the right to participate in meetings of the Committee of Creditors (CoC) for relevant environmental issues based on the extent of environmental damage caused.

### *B. United States*

The United States has a Bankruptcy Code, which has helped courts to address and remedy the injustices caused to the environment. It creates a statutory duty on the corporate debtor during its bankruptcy proceedings to operate in compliance with the local laws of the respective state, which is inclusive of the environmental regulations. In the case of

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<sup>45</sup> *Nimmo CA Administrator of Dawson International PLC* [2018] CSOH 52 (UK).

*Mid-Atlantic National Bank v New Jersey Department of Environmental Protection*,<sup>46</sup> the courts have judicially supported this standpoint by stating that assets containing toxic wastes “posing an immediate and identifiable threat to public health or environmental safety” cannot be abandoned by a trustee.

Furthermore, under Section 362 of the US Bankruptcy Code, an automatic stay is provided to the corporate debtor on pending legal actions and claims arising previous to instituting insolvency proceedings, which operates similarly to the moratorium. It, however, allows for a ‘Policing and Regulatory Claim’, where such a stay can be lifted to claim costs of Environmental Damages. Any party claiming such damage, however, must prove that the interest in claiming such damages lies with prioritising general safety as public policy and not in the pecuniary interest of the property being damaged.

Additionally, in *United States v Apex Oil Company Ltd*,<sup>47</sup> the court answered whether a fresh suit can be instituted against a reorganized debtor post the resolution process against its environmental liabilities. It was held that such a claim is not dischargeable by the institution of bankruptcy, and thereby, under the Resource Conservation and Recovery Act (**RCRA**), the defendant was to be asked to ensure the clean-up of the contaminated site, instead of being sued for money. Although claims before the initiation of bankruptcy can be unfettered, the Supreme Court clarified that clean-ups at a third-party hazardous waste disposal site are a debt or liability that can be sought under the

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<sup>46</sup> *Midlantic National Bank v New Jersey Department of Environmental Protection* [1986] 474 US 494 (US).

<sup>47</sup> *Apex Oil Company, Inc v United States* [2002] 208 F Supp 2d 642 (E D La 2002) (US).

Bankruptcy Code. However, it is to noting that a company may not have the requisite resources to effectively clean up such contamination, especially post-bankruptcy.

On the other hand, in the *Wellman Dynamics Corporation* dispute,<sup>48</sup> the buyer and the environmental agency negotiated a settlement by admitting that the former had to fulfil various requirements under the RCRA, inclusive of financial support and corrective actions, offering a unique outcome to address such a liability.

These unique approaches can be applied to the perspective of India's IBC by prioritizing environmental clean-up costs. Incorporating a distinction between public policy and pecuniary interests would allow continued regulation and ensure that other liquidation liabilities are also prioritised.

Although judicial developments in the US have only dealt with environmental damage on the property of a third party, scrutiny can be made into such insolvent debtors who, on their own properties, have generated environmentally hazardous waste, as in the UK. In such instances, an examination can be made on the levels of damage, its effect on the environment and the people surrounding such property, and the priority that needs to be given to such damage. Based on such categorisation of levels of damage, environmental damages can be treated either as a priority as part of liquidation costs or given a lower priority as a contingent claim.

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<sup>48</sup> *Miller v Wellman Dynamics Corp* [1988] 419 NW2d 380 (US).

*C. International Insolvency Literature on Secured Status to Environmental Claims*

The topic of the environment is of global concern. International organizations such as the UN become imperative in consideration for any global standardization. In view of this, the authors in this section try to analyze the *UNCITRAL Legislative Guide on Secured Transactions*<sup>49</sup> (ULGST) and the *UNCITRAL Legislative Guide on Insolvency Law*<sup>50</sup> (ULGIL) to understand their approach to the concerned research problem.

The main goal of ULGST is to encourage credit at a reasonable price and create expedited processes for acquiring security rights. All parties must be able to determine the extent of a grantor's and third parties' interests in the encumbered assets for a secured transactions regime to be effective. A prospective creditor must be able to ascertain, at the time of credit issuance, the priority of its security right over encumbered assets over the rights of other creditors, including an insolvency representative. Environmental claims are fundamentally contingent since the clean-up costs may not have been incurred, the level of harm might not be determinative, or the cure may not be immediately apparent. As a result, one could argue that it is challenging to evaluate environmental claims with certainty. Claims may surface when pollution is found, cleaned up, or the environment is polluted, adding to the uncertainty surrounding the time. Nonetheless, the majority of countries, including India, are

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<sup>49</sup> ULGST (n 6).

<sup>50</sup> United Nations Commission on International Trade Law, *UNCITRAL Legislative Guide on Insolvency Law* (2004) <[https://uncitral.un.org/en/texts/insolvency/legislativeguides/insolvency\\_law](https://uncitral.un.org/en/texts/insolvency/legislativeguides/insolvency_law)> accessed 16 February 2025.

currently working to impose reporting ESG requirements. Therefore, requesting required ESG data at loan disbursement and including it in periodic reports by the borrower, together with other financial data, will remove confusion and make it easier for lenders to account for risk in their decisions.

Therefore, it is not against the law to grant security rights to environmental claims in and of themselves, provided that sufficient clarity is given beforehand. In addition, according to ULGST, a contemporary secured transactions regime ought to include a comprehensive set of precise rules that, (a) have a broad scope; (b) are founded on general principles that are widely understood and expressed; (c) cover a variety of secured obligations, both present and future; (d) apply to all encumbered assets, including future assets and proceeds; and (e) provide procedures for resolving priority conflicts among a wide range of competing claimants.<sup>51</sup>

Herein, environmental protection can be seen as a generally accepted principle, as a part of the current or future secured obligation of the company. If set guidelines are formulated in compliance with other requirements of ULGST, then environmental claims may, under the category of “general social goals”, be given the secured status, and hence, urging the review of the current legislative mechanism.

Furthermore, the insolvency laws provide for a moratorium on the application of the filing of bankruptcy. However, the ULGIL notes that despite stay laws, action can still be taken to safeguard urgent and essential public interests and stop activities that endanger the

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<sup>51</sup> *Apex Oil Company* (n 47).

environment. This is to be read with the proviso that transparency and predictability can be maintained if an insolvency law specifically designates the operations that fall beyond the cover of the stay. Furthermore, ULGIL permits the estate to give up its interest as long as doing so does not conflict with the public interest, as would be the case in situations where the asset poses a risk to the environment or the public's health and safety.<sup>52</sup> Herein, it is crucial to comprehend that regardless of the stay, environmental obligations as forming a part of the public interest regime, can be allowed to be adjudicated in the latter stage of the moratorium process. Similarly, ULGIL also necessitates giving effect to obligations under international treaties, primarily environmental protection, as one of the important considerations in evaluating whether there are compelling grounds to confer privileged status to any sort of debt.

Consequently, the ULGIL also points out that certain bankruptcy regulations do not give secured creditors precedence. Payment to secured creditors could be prioritized, for instance, over administration expenses and other claims that are protected by insolvency legislation. As a result, ULGIL, as it currently exists, brings up the subject of environmental claims frequently. Therefore, on the international front, there are provisions inviting amendments on environmental aspects, which can be relied on as an inspiration.

India can integrate principles from the ULGST and ULGIL into the Code with specific modifications to prioritize environmental concerns. First, the introduction of a super-priority lien for specific and urgent

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<sup>52</sup> ULGIL (n 7).

environmental remediation costs could be considered. This necessitates the introduction of a new sub-clause in Section 53, granting these narrowly defined claims priority even over secured creditors. For the same, strict criteria such as confirmation by an independent environmental authority, an immediate threat, and quantified costs, etc, could be devised to prevent misuse and maintain predictability for secured creditors. This shall act as a ‘carve out’ in the moratorium process by permitting the environmental regulatory bodies to initiate or continue actions related to public health, safety, or the prevention of further environmental damage during the CIRP. Finally, the CIRP Regulations could be amended to mandate the inclusion of certain elements in resolution plans. These elements would comprise a detailed assessment of the corporate debtor’s environmental liabilities (including a site-specific audit), a concrete remediation plan for existing damage and compliance, and an estimation of costs along with a funding proposal from the Resolution Applicant.

## **VI. SCOPE OF TRANSITION IN THE CODE**

Financial institutions and companies have become increasingly concerned about the environment and their green duties towards the ecosystem because of the changing times. The principle that governs such behavior is the Equator’s Principle, as a framework for risk management, inclusive of identifying, evaluating, and controlling social and environmental risks. Its primary objective is to provide a minimal standard for due diligence and monitoring to enable decision-making. It tries to strike a balance between the external and internal environment and the company’s objectives. This can somehow be seen internalised latently in the Code.

Specifically, talking from the perspective of the Code, the Insolvency and Bankruptcy Board of India recognizes the costs of sustaining a continuing concern as costs associated with the insolvency resolution process. This, when read with Section 17(2)(e) of the Code, requires insolvency practitioners to abide by all applicable laws. The combined interpretation of the aforementioned calls for abiding by the environmental regulations while maintaining a business, including but not limited to cleaning up previous pollution, hence hinting towards environmental expenditures to also be included as a going concern. If such claims are further subjected to Section 5(13)(e), the environmental claims shall take precedence over the ‘traditional’ secured claims, given that the legislature specifies the costs related to environmental claims from previous years to be treated equally with “traditional” secured creditors. This approach might acquire feasibility if a way can be devised to determine the level of harm/pollution caused. Therefore, such a transition is not strictly debarred and can be interpreted to be allowed if the legislature intends so.

To substantiate, in *Orphan Well Association v Grant Thornton Ltd*<sup>53</sup> (**Redwater**), the Supreme Court of Canada said,

*“Bankruptcy is not a license to ignore rules, and insolvency professionals are bound by and must comply with valid provincial laws during bankruptcy. They must, for example, comply with non-monetary obligations that are binding on the bankrupt estate, that cannot be*

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<sup>53</sup> *Orphan Well Association v Grant Thornton Ltd* [2019] SCC 5 [160].

*reduced to provable claims, and the effects of which do not conflict with the Bankruptcy and Insolvency Act.”*

The Code is not a superior law; it has to be read in consonance with every other law, such as the Environmental Protection Act, the Pollution Act, etc. There are multiple advantages to making green insolvency a part and parcel of the resolution process under the Code. It facilitates an examination and mitigation of environmental risks associated with financially distressed businesses, thus averting further environmental harm. Apart from encouraging the application of eco-friendly procedures and technologies, leading to a more socially and ecologically conscious business environment, it also promotes openness and stakeholder participation by including environmental specialists and stakeholders in decision-making procedures. All of these can be observed once green insolvency practices are generalised.

## VII. COMPUTATION OF ENVIRONMENTAL COMPENSATION (EC)

Generally, the National Green Tribunal (NGT), while hearing the cases, vests the Central Pollution Control Board (CPCB) or State Pollution Control Board (SPCB) with the task of reviewing the site and computing damages. In 2018, the CPCB was therefore asked to devise a compensation scheme in furtherance of *Paryavaran Suraksha Samiti v UOI*.<sup>54</sup> The committee<sup>55</sup> set up by the CPCB under the chairmanship of

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<sup>54</sup> Writ Petition (Civil) No 375 of 2012 (India).

<sup>55</sup> Central Pollution Control Board, *Report of the CPCB In-house Committee on Methodology for Assessing Environmental Compensation and Action Plan to Utilize the Fund* [2019] <<https://cpcb.nic.in/uploads/report-15.07.2019.pdf>> accessed 25 June 2025. (**CPCB In-house Committee Report**)

Shri A Sudhakar, formulated a policy named “Methodology for Assessing Penalty & Environmental Compensation and Action Plan to Utilize the Fund” and suggested the following formula for EC computation:

$$EC=PI \times N \times R \times S \times LF^{56}$$

Where, EC is Environmental Compensation in (₹).

PI = Pollution Index is a number from 0 to 100. An increasing value of PI denotes an increasing degree of pollution hazard from the industrial sector. It was first used to categorize the industrial sectors into Red, Orange, Green, and White based on the level of pollution in the area. The Pollution Index in the range of 60 to 100 is identified as Red Industry, while 41 to 59 is Orange Industry, and lastly 21 to 40 as Green Industry; anything below 21 is termed as white. To standardize the compensation calculation process, the average pollution index suggested for each category was set at 80, 50, and 30, respectively.

N = Number of days since the violation took place. It shall be counted from the date of non-compliance observed to the date of implementation of the closure order or date of compliance verified. In the absence of an exact date of violation, environmental compensation should be imposed for the last 5 years.<sup>57</sup>

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<sup>56</sup> National Green Tribunal, *Joint Committee Report on Assessment of Environmental Compensation* [2020]  
<[https://www.greentribunal.gov.in/sites/default/files/news\\_updates/Final%20Report%20on%20EC%20calculation%20O.A.%20No.%2061-2020%20%20Maj.%20Gen.%20Harpreet%20Singh%20Bedi%20\(Retd.\)%20&%20ors.%20VS.%20Vijay%20Singh,%20Dwarkadheesh%20Haveli%20Builder%20&%20ors..pdf](https://www.greentribunal.gov.in/sites/default/files/news_updates/Final%20Report%20on%20EC%20calculation%20O.A.%20No.%2061-2020%20%20Maj.%20Gen.%20Harpreet%20Singh%20Bedi%20(Retd.)%20&%20ors.%20VS.%20Vijay%20Singh,%20Dwarkadheesh%20Haveli%20Builder%20&%20ors..pdf)> accessed 25 June 2025.

<sup>57</sup> Haryana State Pollution Board, *Methodology for Assessment of Environmental Compensation* [2021]

R = Factor in Rupees (₹) for deriving the EC, which may be a minimum of 100 and a maximum of 500 mentioned in the report of CPCB. The CPCB has suggested R as 250 for the calculation of the Environmental Compensation in cases of violation. This is the only category wherein discretion of the board/judiciary can be exercised, viewing the degree or extent of pollution.

S = Factor for scale of operation, which could be based on small/medium/ large industry categorization, which may be 0.5 for micro or small, 1.0 for medium, and 1.5 for large units.

LF = Location factor. It can further be explained as a designated number assigned to areas with a certain population. For example, 1 for the locations with less than 1 million population, 1.25 for the locations with a population between 1 to 5 million, 1.5 for locations with a population of 5 to 10 million, and 2 for 10 million and above.

A sample calculation can be seen in the table below:

Industrial Category	Red	Orange	Green
Pollution Index (PI)	60-100	41-59	21-40
Average PI	80	50	30
R-Factor	250		
S-Factor	0.5-1.5		
L-Factor	1.00-2.00		
Environmental Compensation (₹/day)	10,000-60,000	6,250-37,500	5,000-22,500

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<[https://hspcb.org.in/uploads/pages/order\\_dated\\_22\\_12\\_2021\\_66ab56004c25c.pdf](https://hspcb.org.in/uploads/pages/order_dated_22_12_2021_66ab56004c25c.pdf)> accessed 25 June 2025.

<sup>58</sup> CPCB In-house Committee Report (n 55).

Beyond the standard EC calculation, the CPCB has developed violation-specific formulas to address particular infringements. These include methodologies for illegal groundwater extraction, untreated sewage discharge, breaches of the Bio-Medical Waste Rules, 2016, violations under the Solid Waste Rules, and the Graded Response Action Plan for Air Pollution in the Delhi region. While the formula for illegal groundwater extraction was formulated by a CPCB-convened committee, comprising experts from various regulatory bodies, including the Central Ground Water Authority (**CGWA**), the authority to impose the corresponding penalty remains vested with the CGWA.

Specifically, for plastic waste, the compensation to be computed is enshrined in the 'Guidelines for Assessment of Environmental Compensation to be levied for Violation of Plastic Waste Management Rules, 2016' by the CPCB. It primarily uses components such as Collection & Transportation costs, cost of setting up of Material Recovery Facility, RDF facility, Operation and Management costs to determine the liability of each violator. A combination of the aforesaid can be used by the SPCB if the industry has polluted more than one source from amongst the enlisted categories provided by the CPCB. This was seen in the case of *Maj Gen Harpreet Singh v Shri Vijay Singh* before the Principal Bench of NGT.<sup>59</sup>

The Haryana SPCB<sup>60</sup> is a glaring example of this delegated responsibility. It has devised various formulae based on whether the pollution is caused by biomedical waste treatment, improper solid waste management,

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<sup>59</sup> Original Application No 61/2020 (CZ) (India).

<sup>60</sup> Haryana State Pollution Control Board, Order (22 December 2021) <[https://hspcb.org.in/uploads/pages/order\\_dated\\_22\\_12\\_2021\\_66ab56004c25c.pdf](https://hspcb.org.in/uploads/pages/order_dated_22_12_2021_66ab56004c25c.pdf)> accessed 25 June 2025.

disposal of untreated sewage, etc, in addition to the general formula. Such proactive measures taken by the SPCBs will further help in quantifying the environmental pollution and hence negating the scope of uncertainty.<sup>61</sup>

Herein, the authors propose that the locations with a pollution index of fifty (50) (Orange) or above shall be given the status of secured creditors, while the ones with an index of fifty (50) or less (Green and below) can be continued at the status of unsecured creditors, owing with regards to the urgency of recovery and the degree of pollution caused. The reasoning behind this realistic approach is the debate of Pecuniary Interests versus Public Cost. In both scenarios, the pecuniary interest of the company serves as the common ground while determining the compensation. However, in the first category, the Public Cost involved is much higher owing to the intensity of pollution or the volatility of the area. Therefore, the EC calculated for the areas with PI above fifty (50) shall be given a place at the top of the priority list, whereas the ones with PI below fifty (50) can be treated as contingent claims subject to the realisation of other debts.

### VIII. WAY FORWARD

No proposition is absolute and error-free. There are myriad challenges involved in the aforesaid proposition as well. Certain fractions express their concerns that the introduction of environmental claimants as secured-equivalent creditors could dilute the sense of security upheld by the ‘traditional secured creditors’, causing them to raise interest rates. Prioritizing environmental obligations in the context of bankruptcy is

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<sup>61</sup> *Techi Tagi Tara v Rajendra Singh Bhandari and Ors* [2018] 11 SSC 734.

also a poor solution, as it might cause other debts to want a higher priority, which would lead to an influx of claims. Hence, the challenges cannot be single-handedly overseen by the advantages. To implement an effective and futuristic method, solutions to these challenges ought to be devised. The grant of secured status to environmental claimants is not a process to be accomplished overnight. Meanwhile, there is a pressing need to come up with interim solutions to help handle the situation in a better manner. Secured creditors may allow debtors to upgrade to meet modern environmental standards for a period of three to five years.

The lenders can take two actions in the interim transition period: *first*, they can impose more stringent criteria for periodic ESG reporting; and *second*, they can add a new covenant to the terms of the current loans. The realization of any environmental claim may be regarded as a default event under this supplementary covenant. This could make it possible for lenders to act suitably and promptly. As an alternative, if the deficiencies are fixed in a span of three to five years, a grandfathering clause may be added.<sup>62</sup> A grandfathering clause in this context would exempt the debtor from new, stricter environmental standards, allowing them to operate under older regulations, given that existing deficiencies are fixed within three to five years. This provides a practical transition, acknowledging remediation efforts while encouraging proactive compliance and offering regulatory stability. In addition, the projects can be evaluated by the secured creditors using “The Equator Principle”, as discussed earlier, as a benchmark used by the financial industry since 2010 to evaluate and control any environmental hazards. Therefore, to avoid such charges, it is best for all parties involved in the insolvency ecosystem, including

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<sup>62</sup> Mohan and Prasad (n 5).

‘traditional’ secured lenders, to adopt a path that gives environmental claims the same standing as secured claims. Additionally, the moratorium imposed can exclude non-pecuniary and public interest-based actions toward the safety of health and protection of the environment.

ULGIL uses labour contracts as an example and lists the reasons why they are prioritized, including societal considerations, labor protection, and preventing a debtor from ending an unfavorable contract. Sections 53(1)(c) and 53(1)(b)(i) of the Code, protecting the labour and employees, are written with comparable goals in mind. The environment is a societal issue that is equally important today. It is only feasible that a high-class committee is formulated to look into the matter and reformulate the legislation as per the urgency if such exploitations are to be curbed. The Honorable Supreme Court of India, while succinctly articulating this predicament, noted that,

*“The Court is, at its heart, an institution that responds to concrete cases brought before it. It is not within its province to engraft into laws its views as to what constitutes good policy. This is a matter falling within the legislature’s remit. Equally, when presented with a novel question on which the legislature has not yet made up its mind, we do not think this Court can sit with folded hands and simply pass the buck onto the Legislature.”*<sup>63</sup>

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<sup>63</sup> *Gujarat Urja Vikas Nigam Limited v Amit Gupta* [2021] 7 SCC 209.

Therefore, the judiciary is also under an obligation to take stringent measures, if needed, rather than relying only on the legislature to come to a decision. Meanwhile, the proposed interim solutions may be implemented for better and more proficient handling of environmental resources.