Corporate Debtors revival under the insolvency and bankruptcy code

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INTRODUCTION

The Insolvency and Bankruptcy Code, 2016, since its inception has been a subject matter of discussion and debate among the members of the legal fraternity. The mechanism adopted for recovery of loan under the IBC Regime was criticized by some people (mostly Corporates) as a ‘draconian legislation’ and others (mostly the financial creditors) felt that this legislation would work towards a plausible remedy for the recovery of loans from the Corporates.

The quintessence of the Insolvency and Bankruptcy Code is the fast track mechanism adopted in disposing of the cases relating to insolvency and liquidation, etc.

The latest data from the Insolvency and Bankruptcy Board of India (IBBI) showed that 378 companies with total creditor claims of Rs.2,57,642 Crores have so far been sent into liquidation under the Insolvency and Bankruptcy Code till March 31, 2019. Of these, 64 companies had received Resolution Plan higher than the liquidation value of the assets, but lenders rejected them—not being comfortable with the deferred payments offered by the Resolution Applicant.¹

The Insolvency and Bankruptcy Code, 2016 (Code) provides for a robust mechanism for revival of a viable Corporate Debtors (CDs). However there is no precise mathematical formula, to identify a CD as non-viable. The creditors may wrongly classify a viable CD as non-viable and vice versa because of market imperfections and accordingly, it may rescue a non-viable CD and close a viable one. Rescuing a non-viable CD may not be of great concern as it can be closed later. But closing a viable CD is a grave concern as it impacts the daily bread of its stakeholders and it cannot be rescued later.

The I&B Code, therefore, has adopted a very cautious approach. At first, the I&B code makes an endeavour to rescue the CD and if it arrives at a conclusion that it is not viable to rescue, then proceeds for liquidation. It also envisages course correction, if it wrongly proceeds to liquidate a viable CD. The law does not envisage the State to intervene in wrong identification but provides a flexibility to market to make course corrections if it so wishes.

OBJECT OF THE CODE – EXEGESIS BY NCLAT AND HON’BLE SUPREME COURT

The Code is a law for insolvency resolution, as evident from the long title to the Code, Which reads as under: “An Act to consolidate and amend the laws relating to reorganization and insolvency resolution of corporate persons, partnership firms and individuals in a time bound manner for maximization of value of assets of such persons, to promote entrepreneurship, availability of credit and balance the interests of all the stakeholders including alteration in the order of priority of payment of Government dues and to establish an Insolvency and Bankruptcy Board of India, …..”

The Hon’ble NCLAT, in the matter of Binani Industries Limited Vs. Bank of Baroda &Anr.,2 clarified the objectives of the Code as under: “The first order objective is “resolution”. The second order objective is “maximization of value of assets of the ‘Corporate Debtor’” and the third order objective is “promoting entrepreneurship, availability of credit and balancing the interests”. This order of objective is sacrosanct.”

Section 12A, inserted by an Ordinance, allows withdrawal of application after it has been admitted. It reads as under: “12A. Withdrawal of application admitted under section 7, 9 or 10.
– The Adjudicating Authority may allow the withdrawal of application admitted under section 7 or section 9 or section 10, on an application made by the applicant with the approval of ninety per cent voting share of the committee of creditors, in such manner as may be specified.”

The Hon’ble Supreme Court, in the matter of Brilliant Alloys Private Limited Vs. Mr. S. Rajagopal&Ors.3 clarified that withdrawal may be allowed even after invitation of expression of interest: “According to us, this Regulation (30A allowing withdrawal up to invitation of expression of interest) has to be read along with the main provision Section 12A which contains no such stipulation. Accordingly, this stipulation can only be construed as directory depending on the facts of each case.”

The Hon’ble Supreme Court, in the matter of Swiss Ribbons Pvt. Ltd. &Anr. Vs. Union of India &Ors., clarified as under: “We make it clear that at any stage where the committee of creditors is not yet constituted, a party can approach the NCLT directly, which Tribunal may, in exercise of its inherent powers under Rule 11 of the NCLT Rules, 2016, allow or disallow an application for withdrawal or settlement. This will be decided after hearing all the concerned parties and considering all relevant factors on the facts of each case.”

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2 In Company Appeal (AT)(Insolvency) No.82 of 2018
3 Special Leave to Appeal (C) No(s)-31557/2018
The Companies Act, 2013 (Act) envisages compromise or arrangements. Section 230 thereof, as amended by the Code, enables compromise or arrangement on the application by a liquidator appointed under the Code, as under: “230. Power to compromise or make arrangements with creditors and members. — (1) Where a compromise or arrangement is proposed— (a) between a company and its creditors or any class of them; or (b) between a company and its members or any class of them, the Tribunal may, on the application of the company or of any creditor or member of the company, or in the case of a company which is being wound up, of the liquidator, appointed under this Act or under the Insolvency and Bankruptcy Code, 2016, as the case may be, order a meeting of the creditors or class of creditors, or of the members or class of members, as the case may be, to be called, held and conducted in such manner as the Tribunal directs….”

Regulation 32 of the IBBI (Liquidation Process) Regulations, 2016 (Regulations) envisage “sale as a going concern”. It reads as under:

“32. Sale of Assets, etc. The liquidator may sell—
(a) an asset on a standalone basis;
(b) the assets in a slump sale;
(c) a set of assets collectively;
(d) the assets in parcels;
(e) the corporate debtor as a going concern; or
(f) the business(s) of the corporate debtor as a going concern:
Provided that where an asset is subject to security interest, it shall not be sold under any of the clauses (a) to (f) unless the security interest therein has been relinquished to the liquidation estate.”

While relying on Regulation 32 (e) of the Regulations, the Hon’ble Supreme Court in the matter of ArcelorMittal India Private Limited Vs. Satish Kumar Gupta &Ors.4 Observed:

“The only reasonable construction of the Code is the balance to be maintained between timely completion of the corporate insolvency resolution process, and the corporate debtor otherwise being put into liquidation. We must not forget that the corporate debtor consists of several employees and workmen whose daily bread is dependent on the outcome of the corporate insolvency resolution process. If there is a resolution applicant who can continue to run the corporate debtor as a going concern, every effort must be made to try and see that this is made possible.” While relying on Regulation 32 (e) of the Regulations, the Hon’ble Supreme Court in the matter of Swiss Ribbons Pvt. Ltd. &Anr. Vs. Union of India &Ors., 5 observed: “What is interesting to note

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4 (2019) 2 SCC 1
5 WP (Civil) Nos. 99, 100, 115, 459, 598, 775, 822, 849, and 1221 of 2018, SLP (Civil) No. 28623 of 2018 and WP (Civil) 37 of 2019]
is that the Preamble does not, in any manner, refer to liquidation, which is only availed of as a last resort if there is either no resolution plan or the resolution plans submitted are not up to the mark. Even in liquidation, the liquidator can sell the business of the corporate debtor as a going concern. … It can thus be seen 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 from a corporate death by liquidation.”

The Hon’ble NCLAT, in the matter of S. C. SekaranVs. Amit Gupta &Ors.,6 directed as under:“ .. we direct the ‘Liquidator’ to proceed in accordance with law. He will verify claims of all the creditors; take into custody and control of all the assets, property, effects and actionable claims of the ‘corporate debtor’, carry on the business of the ‘corporate debtor’ for its beneficial liquidation etc. as prescribed under Section 35 of the I&B Code…. Before taking steps to sell the assets of the ‘corporate debtor(s)’ (companies herein), the Liquidator will take steps in terms of Section 230 of the Companies Act, 2013. The Adjudicating Authority, if so required, will pass appropriate order. Only on failure of revival, the Adjudicating Authority and the Liquidator will first proceed with the sale of company’s assets wholly and thereafter, if not possible to sell the company in part and in accordance with law.

. The ‘Liquidator’ if initiates, will complete the process under Section 230 of the Companies Act within 90 days…”

One of the key objectives of the Code was to achieve time-bound resolution of distress since delays severely affect deal value, particularly as scare capital does not wait to be deployed. However, since the implementation of the Code, delays in obtaining approvals from the Committee of Creditors (CoC) and delays due to litigation have been a cause for Concern.

As per the source from the IBBI, of the total 1,298 admitted cases, only 52 (4%) have been disposed of with approved resolution plans, 259 (20%) are in liquidation and 987 (76%), ongoing. Of those 52 cases which have been disposed of with the approved Resolution Plan, over 35 cases took more than 270 days to obtain approval. All Steps have been taken to provide a model timeline for the processes under the Corporate Insolvency Resolution Process (CIRP), and the Supreme Court has emphasized the mandatory nature of the 180+90 days timeline under the Code. Notwithstanding this, the timelines pertaining to admission of an application have been held to be directory and not mandatory, and time taken by the adjudicating authority (AA) to pass orders has been excluded from the scope of the 180+90 days timeline. This is particularly concerning, since severe delays are experienced once a resolution plan is filed with the Adjudicating Authority for its approval.7

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6 Company Appeal (AT) (Insolvency) No. 495 & 496 of 2018
INITIATION OF THE IBC PROCEEDINGS

If a Corporate Debtor makes a default in repayment of dues to the creditors, the Financial creditor or an Operational Creditor, as the case may be, has the power to start the Corporate Insolvency Resolution Process (CIRP). In order to initiate the CIRP, an application has to be made to National Company Law Tribunal (NCLT) under Section 7 and 9 of IBC, 2016 in case of Financial Creditors and Operational Creditors respectively. Before initiation of the Corporate Insolvency Resolution Process, in case of Operational Creditors, a 10 days demand notice under Section 8(2) of IBC, 2016 has to be given to the Corporate Debtor before he approaches the NCLT under Section 9 of IBC, 2016. However, a Financial Creditor can directly approach the NCLT if the Corporate Debtor does not repay the outstanding dues or fails to show any existing difference. The new Code states that the Insolvency Process of a Corporate Debtor must be concluded within a period of 180 days from the date of initiation of the Corporate Insolvency Resolution Process. Further, the claims of the Creditors shall be frozen for a period of six months on admission of application by NCLT. Further, upon initiation of the Corporate Insolvency Resolution Process, as per Section 14 of the IBC, the NCLT shall declare moratorium for prohibiting, institution or continuation of pending suits or proceedings against the Corporate Debtor. Unless a Resolution Plan is made or Liquidation process is initiated, no legal claim shall be sought against the corporate debtor in any other forum or Court. When the Application for Insolvency is accepted under Section 7 or 9 of IBC, 2016, as the case may be, the NCLT, within fourteen days appoints an Interim Resolution Professional (IRP). The appointed IRP then takes up the responsibility of the Corporate Debtor’s properties and functions accordingly. He further collects all the information that is Relevant with regard to the financial condition of the corporate debtor from Information utilities. As per Section 16 of the IBC Code, the IRP is initially appointed only for a term of thirty days within which he does all the necessary scrutinization.

The next step in this process is to make a public announcement about the commencement of Corporate Insolvency Resolution Process so that claims from any other creditors can also come forward, if any. As per Sec. 18 of the I&B code, the Committee of Creditor’s (CoC) is constituted by the IRP post receiving any claims by public announcement. In the event any financial creditor is a related party of the defaulting debtor, such a creditor will not have the right to represent, participate or vote in the Committee of Creditors so constituted by the IRP. In order to be a part of the Committee of Creditors, the average dues of the Operational Creditors must be at least ten percent of the total debt. The Committee of Creditors shall during the first seven days of its incorporation decide through 75% votes, whether the IRP should be used as a Resolution Professional (RP) or should be replaced with someone else.
As per Section 22 of the I&B Code, 2016, after the Committee of Creditors finalizes the Resolution Professional he is appointed by the NCLT. The Resolution Professional so appointed can be replaced anytime by the Committee of Creditors with a majority of 75% votes. In the interim, i.e. till the appointment of any new Resolution Professional, the Committee of Creditors can take decisions with regard to insolvency resolution by 75% majority voting.

In the event majority of the financial creditors are of the view that the case is very complex and requires more time, the NCLT may grant a one-time extension of up to a maximum of 90 days over and above the tenure of 180 days, upon moving a requisite application by the Resolution Professional before the NCLT. It shall be the sole responsibility of the Resolution Professional to manage and conduct the corporate insolvency resolution procedure during such a term. To enable the Resolution Applicant for preparing a Resolution Plan, the Resolution Professional shall compile a statistical note. A Resolution Applicant can be defined as an individual who has the duty and responsibility to submit a Resolution Plan to the Resolution Professional. The Committee of Creditors further receives the plan from the Resolution Professional for its approval.8

Upon the Resolution Plan being approved, the next step by the Committee of Creditors is to come up with options on restructuring, which can be either by adhering to the modified repayment plan as per the Resolution Plan or to simply liquidate the properties of the company in order to recover dues. If the Committee of Creditors fails to take any binding decision with regard to the repayment by the debtor, the debtor’s assets are liquidated in order to pay back the creditors. If the Committee of Creditors approves the Resolution Plan, the same shall be sent to NCLT for its approval and implementation.

As rightly pointed out by the Hindu8, the experiment conducted in enacting the Code is proving to be largely successful. The defaulter’s paradise is lost. The I&B Code, despite all the challenges that it has faced, has been successful in sending a message to recalcitrant defaulters that there can be no more business as usual when they default.

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