

CORPORATE INSOLVENCY AND ITS RESOLUTION UNDER INSOLVENCY AND BANKRUPTCY CODE, 2016

The Insolvency and Bankruptcy Code, 2016 is truly a landmark piece of legislation which has completely re-designed the India's existing Insolvency and bankruptcy laws and consolidated them under Single Window System. In the past 70 years it is not very often that any New Body of Law has been constituted, implemented and started working in full force as we have witnessed in Insolvency and Bankruptcy Code, 2016. We have just stepped into this unique legislature of Corporate Insolvency Resolution w.e.f. 15th December, 2016 and within a period of just 6 months entire legal framework for Corporate Insolvency Resolution has been put in place. The Code has revamped the process of Corporate Insolvency Resolution. The Code brings a paradigm shift in process by a slew of legislative amendments, establishment of regulations and model bye-laws that govern insolvency resolution professionals, and the mechanism for transitioning from existing laws such as the Presidency Towns Insolvency Act, 1909, the provincial Insolvency Act, 1920, the Sick Industrial Companies (Special Provisions) Act, 1985 to name few which have been repealed by the Code.

An effective and efficient insolvency regime is the foundation of a strong economy. Before the enactment of the Insolvency and Bankruptcy Code, 2016, there was no single legal framework in India that dealt with Insolvency and Bankruptcy. The provisions related to insolvency and bankruptcy were scattered over many legislations viz.

(1) For Companies

- a. Sick Industrial Companies (Special Provisions) Act, 1985
- b. The Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002
- c. The Companies Act, 2013.

(2) For Individuals

- a. The Presidency Towns Insolvency Act, 1909
- b. The Provincial Insolvency Act, 1920

Liquidation of Companies were dealt by the High Court while the Bankruptcy and Insolvency proceedings were handled by the District Courts or the High Court as the case may be.

The objective of the Insolvency and Bankruptcy Code, 2016 is *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 of 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 and for matters connected therewith or incidental thereto.*

Applicability of Insolvency and Bankruptcy Code, 2016

As you are aware, the Insolvency and Bankruptcy Code, 2016 (the Code) provides for a specialized forum to oversee insolvency and liquidation proceedings for individuals, firms and Corporates. Insolvency Proceedings under the Code can be initiated against a Company (Corporate Debtor) by a Financial Creditor (Sec 7), an Operational Creditor (Sec 8 & 9) or by the Corporate Debtor itself (Sec 10).

Insolvency and Bankruptcy Code, 2016 is applicable to:

1. All companies incorporated under Companies Act, 2013 or any other previous company law;
2. Any other company governed by any special Act for the time being in force, except in so far as the said provisions are inconsistent with the provisions of such special Act;
3. Any Limited Liability Partnership incorporated under the Limited Liability Partnership Act, 2008;
4. Such body incorporated under any law for the time being in force, as may be specified by the Central Government by notification in addition to partnership firms and individuals;
5. Partnership firms and Individuals.

As per Section 5(1) of the Insolvency and Bankruptcy Code, 2016, the National Company Law Tribunal (NCLT) constituted under Section 408 of the Companies Act, 2013 will be the Adjudicating Authority for corporate persons and as per section 79(1) of the Code, the Debt Recovery Tribunal (DRT) constituted under section 3(1-A) of the Recovery of Debts and Bankruptcy Act, 1993 will be the Adjudicating Authority for individuals and partnership firms.

Claim: Under Section 3(6) of the Insolvency and Bankruptcy Code, 2016 Claim has been given a very wide definition and it means following:

- a. A right to payment whether or not such right is reduced to judgement, fixed, disputed, undisputed, legal equitable, secured or unsecured; and
- b. A right to remedy for breach of contract under any law for the time being in force if such breach gives rise to a right to payment, whether or not such right is reduced to judgement, fixed, matured, unmatured, disputed, undisputed, secured or unsecured.

Section 8(2)(a) of IBC suggests that a dispute between the operational creditor and the corporate debtor will be in existence only if a suit or an arbitration proceeding on the dispute is pending before receipt of Demand Notice. **The Supreme Court held that such an interpretation would lead to a great hardship and therefore, a dispute in the payments, existing before the receipt of demand notice, even if the same is not a part of any suit or arbitration proceeding, would disqualify the debt from being adjudicated under CIRP.**

Debt has been categorized into two parts i.e. financial debt and Operational debt.

Financial Debt relates with 'financial products' which means a debt along with interest, if any, which is disbursed against the consideration for the time value of money and includes-

- a. Money borrowed against the payment of interest;
- b. Any amount raised by acceptance under any acceptance credit facility or its dematerialized equivalent;
- c. Any amount raised pursuant to any note purchase facility or the issue of bonds, notes, debentures, loan stock or any similar instrument;
- d. The amount of any liability in respect of any lease or hire purchase contract which is deemed as a finance or capital lease under the Indian Accounting Standards or such other accounting standards as may be prescribed;
- e. Receivables sold or discounted other than any receivables sold on non-recourse basis;
- f. Any amount raised under any other transaction, including any forward sale or purchase agreement, having the commercial effect of a borrowing;
- g. Any derivative transaction entered into in connection with protection against or benefit from fluctuation in any rate or price and for calculating the value of any derivative transaction, only the market value of such transaction shall be taken into account;
- h. Any counter indemnity obligation in respect of a guarantee, indemnity, bond, documentary letter of credit or any other instrument issued by a bank or financial institution;
- i. The amount of any liability in respect of any of the guarantee or indemnity for any of the items referred to in sub clauses (a) to (h) of this clause.

Operational Debt: means a claim in respect of the provision of goods or services including employment or a debt in respect of the repayment of dues arising under any law for the time being in force and payable to the Central Government, any State Government or any local authority.

Overall Scheme of the Insolvency and Bankruptcy Code, 2016: An Insolvency and Bankruptcy Board of India (established under 188(1) of the Insolvency and Bankruptcy Code, 2016 on 01/10/2016 vide Notification no. 3110(E) dated 01/10/2016) will oversee the work of insolvency and bankruptcy of corporate person, firms and individuals. Actual work relating to the insolvency and bankruptcy will be handled mostly by the insolvency professionals under the supervision of the Adjudication Authority (NCLT). Insolvency Professionals are the members of the Insolvency Professional Agencies which are registered with the Insolvency and Bankruptcy Board of India (IBBI). The basic crux of entire process is that when any enterprise (corporate, firm or individual) defaults, the control shifts to the Insolvency Professional who shall form a Committee of Creditors. The Committee shall within the specified time limit has to evaluate proposal for resuscitating the enterprise or move towards liquidation if any proposal does not work out.

Herein below we will discuss about the Corporate Insolvency Resolution Process.

Corporate Insolvency Resolution Process Summary: At first instance an application to initiate the Corporate Insolvency Resolution Process is made by the Creditor to the bench of the Adjudicating Authority along with the consent of the Insolvency Resolution Professional to act as the Interim Resolution Professional. Adjudication Authority decides the applicability of the Application within a period of 14 days from the date of application and appoints the Interim Resolution Professional for a period of 30 days. Who shall form a committee of creditors to evolve a resolution plan to rehabilitate the ailing corporate within a period of 180 days further extended by maximum 90 days. Committee of Creditors appoints a new or re-appoints the Interim Resolution Professional as the Resolution Professional. If the efforts fail the Corporate will be liquidated by the Adjudication Authority in a time bound manner.

Initiation of Corporate Insolvency Resolution Process (CIRP):

The trigger to initiate the Corporate Insolvency Resolution process against a Corporate Debtor is the occurrence of default.

1. By Financial Creditor:

Under Section 7 of the Code, a financial creditor either himself or jointly with other financial creditors may initiate the Corporate Insolvency Resolution process (CIRP) by filing an Application to Initiate Corporate Insolvency Resolution Process (without having issued any notice for default of repayment to the corporate debtor because Financial Debt is Time Value for Money) to the Adjudication Authority i.e. NCLT at the bench within whose jurisdiction the registered office of the Corporate Debtor is situated along with a filing fee as specified As per the schedule to the insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016 fee of Rs. 25,000/- is required to be paid by the financial creditor).

The financial creditor shall along with the application furnish to the Adjudication Authority:

- i. Record of the default recorded with the information utility or such other record or evidence of default as may be specified;
- ii. The name of the resolution professional proposed to act as an interim resolution professional (with his consent in specified form).

The Adjudication Authority shall within a period of 14 days of the receipt of the application ascertain the existence of the default from the records or on the basis of the evidence furnished by the Creditor and:

- i. If it is satisfied that the default has occurred and application is complete and there is no disciplinary proceedings are pending against the proposed resolution professional, it may, by order, admit such application; or
- ii. If it is satisfied that the default has not occurred or the application is incomplete or any disciplinary proceedings are pending against the proposed resolution professional, it may, by order, reject such application or give a notice to the applicant to rectify the

defects in his application within 7 days of receipt of such notice from the Adjudication Authority.

2. By Operational Creditor:

Under Section 9 of the Code, an operational creditor has to issue a demand notice to the Operational Debtor with the copy of invoice demanding payment of the amount involved in the default in the specified form. The Corporate debtor shall within a period of 10 days of the receipt of the demand notice bring to the notice of the operational creditor:

- i. Existence of a dispute, if any, and record of the pendency of the suit or arbitration proceedings filed before the receipt of such notice or invoice in relation to such dispute;
- ii. the payment of unpaid operational debt to the corporate creditor by sending the adequate proof.

After expiry of the period of ten days from the date of delivery of the notice, if the operational creditor does not received payment or proof of payment from the corporate debtor or any notice of the existence of dispute, the Operational Creditor may file an application to the Adjudication Authority i.e. NCLT at the bench within whose jurisdiction the registered office of the Corporate Debtor is situated along with a filing fee as specified. As per the schedule to the insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016 fee of Rs. 2,000/- is required to be paid by the operational creditor)

The operational creditor shall along with the application furnish to the Adjudication Authority:

- i. copy of the demand notice or invoice delivered to the operational creditor;
- ii. an affidavit to the effect that there is no notice given by the corporate debtor relating to a dispute of the unpaid operational debt;
- iii. a copy of the certificate from the financial institution maintaining accounts of the operational creditor confirming that there is no payment of an unpaid operational debt by the corporate debtor;
- iv. Record of the default recorded with the information utility or such other record or evidence of default as may be specified;
- v. The operational creditor may also propose the name of the resolution professional to act as an interim resolution professional (with his consent in specified form);

The Adjudication Authority shall within a period of 14 days of the receipt of the application ascertain the existence of the default from the records or on the basis of the evidence furnished by the Creditor and:

- i. If it is satisfied that the default has occurred and application is complete, there is no repayment of the unpaid debt, demand notice was delivered to the debtor, there is no dispute in existence and there is no disciplinary proceedings are pending against the proposed resolution professional, it may, by order, admit such application; or
- ii. If it is satisfied that the default has not occurred or the application is incomplete or there has been payment of unpaid debt or the creditor has not delivered the demand notice or

invoice to the debtor for payment or notice of dispute has been received by the operational creditor or there is record of dispute in the information utility or any disciplinary proceedings are pending against the proposed resolution professional, it may, by order, reject such application or give a notice to the applicant to rectify the defects in his application within 7 days of receipt of such notice from the Adjudication Authority.

3. By Corporate Applicant

Wherein a Corporate Debtor has committed a default, a Corporate Applicant **thereof** may file an application for initiating Corporate Insolvency Resolution Process (CIRP) to the Adjudication Authority i.e. NCLT at the bench within whose jurisdiction the registered office of the Corporate Debtor is situated along with a filing fee as specified. As per the schedule to the insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016 fee of Rs. 25,000/- is required to be paid by the Corporate Applicant).

The Corporate Applicant of the Corporate Debtor shall along with the application furnish to the Adjudication Authority:

- iii. Its books of accounts and such other documents relating to such period;
- iv. The name of the resolution professional proposed to act as an interim resolution professional (with his consent in specified form).

The Adjudication Authority shall within a period of 14 days of the receipt of the application ascertain the existence of the default from the records or on the basis of the evidence furnished by the Corporate Applicant and:

- iii. If it is satisfied that the default has occurred and application is complete and there is no disciplinary proceedings are pending against the proposed resolution professional, it may, by order, admit such application; or
- iv. If it is satisfied that the default has not occurred or the application is incomplete or any disciplinary proceedings are pending against the proposed resolution professional, it may, by order, reject such application or give a notice to the applicant to rectify the defects in his application within 7 days of receipt of such notice from the Adjudication Authority.

Under above 1, 2 and 3, the Corporate Insolvency Resolution Process (CIRP) shall commence from the date of admission of the application.

Directory / Mandatory Time Period:

One of the basic objectives of the IBC, the resolution of corporate insolvency in time bound manner is the utmost important.

However in relation to 14 days time period within which the adjudication authority has to admit / reject the application caused quite a lot of chaos. The controversy was resolved in the case of

JK Jute Mills Compound Limited V M/s Surendra Trading Company wherein the NCLAT has held that the time period of 14 days from receipt of the application from the financial creditor within which the NCLT has to admit or reject the application is directory/procedural in nature and not mandatory. The NCLAT also clarified that the receipt of application means the date on which the application is listed before the NCLT for admission / order, and not the date of filing of the application.

Persons not entitled to make application

Under Section 11 of the Insolvency and Bankruptcy Code, 2016 following persons shall not be entitled to make an application to initiate CIRP:

- a) A corporate debtor undergoing a corporate insolvency resolution process;
- b) A corporate debtor having completed corporate insolvency resolution process twelve months preceding the date of making the application;
- c) A corporate debtor or a financial creditor who has violated any of the terms of resolution plan which was approved twelve months before the date of making of an application under this Chapter;
- d) A corporate debtor in respect of whom a liquidation order has been made.

Explanation: For the purpose of this section, a corporate debtor includes a corporate applicant in respect of such corporate debtor.

After admission of the application the Adjudication Authority shall by order:

1. Declare a moratorium :
 - a. for the purposes of institution of suits or continuation of pending suits or proceedings against the corporate debtor including execution of any judgement, decree or order in any court of law, tribunal, arbitration panel or other authority;
 - b. transferring, encumbering, alienating or disposing of by the corporate debtor any of its assets or any legal right or beneficial interest therein;
 - c. any action to foreclose, recover or enforce any security interest created by the corporate debtor in respect of its property;
 - d. the recovery of any property by an owner or less or lessor where such property is occupied by or in the possession of the corporate debtor.
2. Cause a public announcement of the initiation of CIRP and call for the submission of claims with details of the Insolvency Professional and time limit to file claim;

3. Appoint an Interim Resolution Professional for a period of 30 days to:
 - a. Collect all information relating to the assets, finances and operations of the corporate debtor including business operations, finances and operational payment for the previous two years, list of assets and liabilities and such other information as may be specified;
 - b. Receive and collage all the claims submitted by the creditors to him;
 - c. Constitute a committee of creditors;
 - d. Monitor the assets of the corporate debtor and manage its operations until a resolution professional is appointed by the committee of Creditors;
 - e. File information collected with the information utility, if necessary;
 - f. Take control and custody of any assets over which the corporate debtor has ownership rights as recorded in the balance sheet or information utility or any other registry;
 - g. Perform such other duties as may be specified by the Board.

Management of the affairs of Corporate Debtor by Interim Resolution Professional: From the date of appointment of the interim resolution professional:

- i. The management of the affairs of the Corporate Debtor shall vest in the interim resolution professional;
- ii. The powers of the Board of Directors or the partners of the corporate debtor, as the case may be, shall stand suspended and be exercised by the Interim Resolution Professional;
- iii. The officers and managers of the Corporate Debtor shall report to the interim resolution professional and provide access to such documents and records of the corporate debtor as may be required by the interim resolution professional;
- iv. The financial institution maintaining account of the corporate debtor shall act on the instruction of the interim resolution professional in relation to such accounts and furnish all information relation to the corporate debtor available with them to the interim resolution professional.

The Interim Resolution Professional shall manage the affairs of the Corporate Debtor on a going concern basis.

Committee of Creditors(CoC): The Interim Resolution Professional shall after collation of all claims received by him against the Corporate debtor and after determination of the financial position of the corporate debtor, constitute a Committee of Creditors. The CoC shall comprise of all financial creditor of the corporate debtor.

Appointment of Resolution Professional: At the First meeting of the CoC which shall be held within 7 days of its constitution, may, by a majority of votes not less than seventy five percent of the voting share of the financial creditors either appoint the interim resolution professional as a Resolution Professional or replace the interim resolution professional with a new Resolution Professional (with the approval of the Adjudication Authority).

The Resolution Professional shall conduct the corporate insolvency resolution process and manage the operations of the Corporate Debtor during CIRP. The Resolution Professional shall exercise powers and perform duties as are vested or conferred on the Interim Resolution Professional.

Information Memorandum and Resolution Plan:

The Resolution Professional shall prepare an information memorandum for formulating a Resolution Plan. The Resolution Professional shall collect the information relating to the assets and affairs of the Corporate Debtor and prepare the Information Memorandum on the basis of which the Resolution Professional would invite and collect the Resolution Plans to keep the Corporate Debtor going.

The Copy of Information Memorandum to be given to every member of the CoC and every member shall have a right to submit a resolution plan.

The Resolution Professional shall examine each resolution plan received by him and present before the CoC such plans which have complied the provisions of Section 30(2). The CoC may approve the resolution plan by a vote of not less than seventy percent of voting share of the financial creditors.

The Resolution Professional shall submit the resolution plan as approved by the CoC to the Adjudication Authority for approval. The Adjudication Authority shall, if it is satisfied with the Resolution Plan, approve the resolution plan which shall be binding on the Corporate Debtor, its employees, members, creditors, guarantors and other stakeholders involved in the resolution plan and the moratorium order passed by the Adjudication Authority shall cease to have effect.

Otherwise the Adjudication Authority, if it is not satisfied with the Resolution Plan, shall reject the resolution plan and pass appropriate orders for the liquidation of the Corporate Debtor and the Corporate Debtor move towards liquidation.

Thanks and Regards
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