CA – Final

Paper 4: Corporate and Allied Laws

Overview of Insolvency & Bankruptcy Code, 2016

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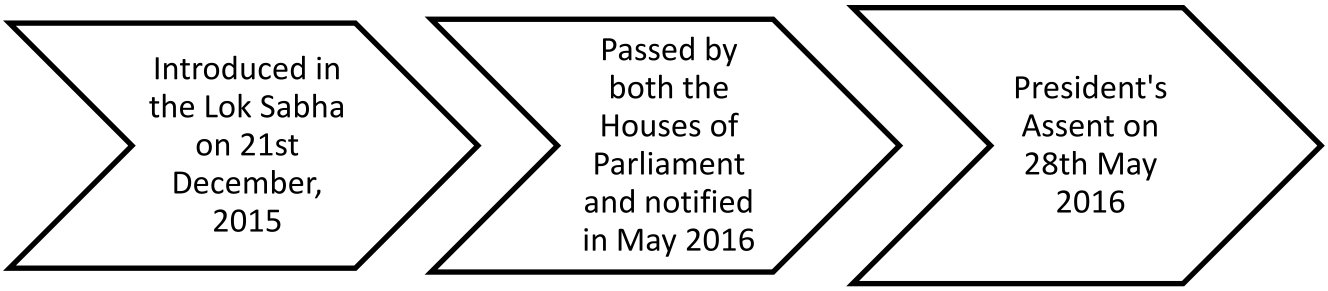
Overview of Insolvency and Bankruptcy Code 2016 (10 Marks)

(I) Introduction:

- One of the major economic reform Code initiated by the Government in the year 2015
- Multiple overlapping laws and adjudicating forums dealing with financial failure and insolvency of companies and individuals in India.
- Provisions relating to insolvency and bankruptcy for companies could be found in the Sick Industrial Companies (Special Provisions) Act, 1985, the Recovery of Debt Due to Banks and Financial Institutions Act, 1993, the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 and the Companies Act, 2013.
- To facilitate easy and time bound closure of business in India and to overcome these challenges, a strong bankruptcy law was required.



Understanding the terms - Insolvency & Bankruptcy

- Both refer to a situation when an individual or company are not able to pay the debt in present or near future and the value of assets held by them are less than liability.

Insolvency:

- The term insolvency is used for both individuals and organizations. For individuals, it is known as bankruptcy and for corporate it is called corporate insolvency.
- Insolvency in this Code is regarded as a "state" where assets are insufficient to meet the liabilities. If untreated, insolvency will lead to bankruptcy for non-corporates and liquidation of corporates.

Bankruptcy:

- While insolvency is a situation which arises due to inability to pay off the debts due to insufficient assets, bankruptcy is a situation wherein application is made to an authority declaring insolvency and seeking to be declared as bankrupt, which will continue until discharge.

Conclusion:

- From the above, it is evident that insolvency is a state and bankruptcy is a conclusion. A bankrupt would be a conclusive insolvent whereas all insolvencies will not lead to bankruptcies. Typically insolvency situations have two options – resolution and recovery or liquidation

Relationship between Bankruptcy, Insolvency & Liquidation:

Bankruptcy	Insolvent	Liquidation
It is a <u>legal proceeding</u> involving a person or business that is unable to repay outstanding debts. The bankruptcy process begins with a petition filed by the debtor, or by the creditors. All of the debtor's assets are measured and evaluated, and then these assets may be used to repay a portion of outstanding debt.	If any person or entity is unable to pay off the debts, it owes to its creditors, on time or as and when they became due and payable, then such person or entity is regarded as "insolvent".	Liquidation is the winding up of a corporation or incorporated entity. There are many entities that can initiate proceedings that will lead to Liquidation, those being:- ♦ The Regulatory Bodies; ♦ The Directors of a Company; ♦ The Shareholders of a Company; and ♦ An Unpaid Creditor of a Company
In nut shell, insolvency is common to both bankruptcy and liquidation. Not being able to pay debts as and when they became due and payable is the leading cause for Liquidation and is the only way that can cause a natural person to become a bankrupt.		

Purpose behind enactment of Insolvency and Bankruptcy Code, 2016:

As per the Preamble to the Code, the purpose of this Act is as under:-

(a) To <u>consolidate and amend the laws</u> relating to re-organisation and insolvency resolution of corporate persons, partnership firms and individuals.

(b) To <u>fix time periods for execution</u> of the law in a time bound manner.

(c) To <u>maximize the value of assets</u> of interested persons.

(d) To <u>promote entrepreneurship</u>

(e) To <u>increase availability of credit</u>.

(f) To <u>balance the interests of all the stakeholders</u> including alteration in the order of priority of payment of Government dues.

(g) To <u>establish an Insolvency and Bankruptcy Board of India</u> as a regulatory body for insolvency and bankruptcy law.

<u>Conclusion:</u>

The Insolvency and Bankruptcy Code, 2016 is intended to strike the right balance of interests of all stakeholders of the business enterprise so that the corporates and other business entities enjoy availability of credit and at the same time the creditor do not have to bear the losses on account of default.

Distinguishing features of Code:

(i) Comprehensive Law which envisages and regulates the process of insolvency and bankruptcy of all persons including corporates, partnerships, LLPs and individuals.

(ii) Withering away of Multiplicity of Laws: The Code has withered away the multiple laws covering the recovery of debts and insolvency and liquidation process and presents singular platform for all the reliefs relating to recovery of debts and insolvency.

(iii) Low Time Resolution: The process is mandated to be completed within 180 days, extendable by maximum of 90 days. Further, for a speedier process there is provision for fast-track resolution of corporate insolvency within 90 days. If insolvency cannot be resolved, the assets of the borrowers may be sold to repay creditors.

(iv) One Window Clearance: Whereby the applicant gets the appropriate relief by the same authority unlike the earlier position of law.

(v) Clarity in Process: There is a clear and unambiguous process to be followed by all stakeholders. There is also shift of control from shareholders and promoters to creditors.

(vi) One Chain of Authority: It does not even allow the Civil Courts to interfere with the application pending before the adjudicating authority, thereby reducing the multiplicity of litigations.

The National Company Law Tribunal (NCLT) will adjudicate insolvency resolution for companies. The Debt Recovery Tribunal (DRT) will adjudicate insolvency resolution for individuals.

(vii) Protects the Interests of Workmen and Employees: It excludes dues payable to workmen under provident fund, pension fund and gratuity fund from the debtor's assets during liquidation.

(viii) New Regulatory Authority: 'Insolvency and Bankruptcy Board of India' to regulate professionals, agencies and information utilities engaged in resolution of insolvencies of companies, partnership firms and individuals. The Board has already been established and has started functioning.

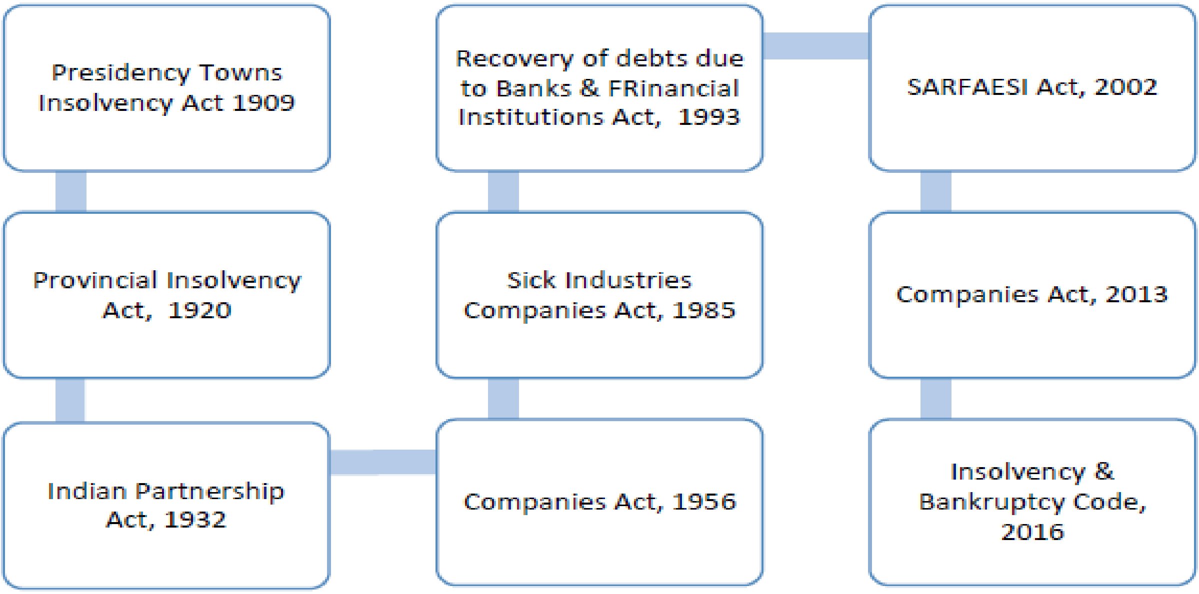
(ix) Establishment of Information Utilities (IUs): IU's are intended to function as a databank to collect, collate and disseminate (circulate) financial information and to facilitate insolvency resolution.

It is envisioned that in the long run, IUs will have data on debts and credits of all the business houses and it will be able to create an automatic trigger in case of default by any debtor and the authority may initiate the insolvency process as required. Such a system will reduce the risk of credit in the economy.

Need for a New Law:

According to the Ease of Doing Business Report of the World Bank, it takes an average of four to five years in insolvency resolution process in India. The main reason behind such delay in the legal process is the existence of overlapping legislations and adjudicating authorities dealing with insolvency of companies and individuals in India.

The Government of India then formulated a plan to refurbish the prevailing bankruptcy laws and replace them with one that will facilitate hassle-free and time-bound revival and closure of businesses.



Loopholes in the Earlier Laws:

The laws which were in existence were not aligned with the market realties and had several inadequacies.

There was no single window resolution available and the resolution and jurisdiction was with the multiple agencies with overlapping powers that was leading to delays and complexities in the process.

The Companies Act deals with the corporate insolvency law.

The Individual Insolvency laws were being dealt by a century old two Acts, i.e., The Provincial Towns Insolvency Act and the Presidency Towns Insolvency Act.

The framework of law which was in existence earlier had failed to resolve insolvency situations.

♦ Financial failure – a persistent mismatch between payments by the enterprise and receivables into the enterprise, even though the business model is generating revenues.

♦ Business failure – which is a breakdown in the business model of the enterprise, and is unable to generate sufficient revenues to meet payments.

♦ Malfeasance and mismanagement by promoters

♦ Multiple laws governing Debt resolution and multiple forums

♦ Parallel proceedings by different parties on the same debtor in different forums and Conflicts between laws and over jurisdictions.

♦ Multiple laws governing Debt resolution and multiple forums

♦ Asymmetry of information

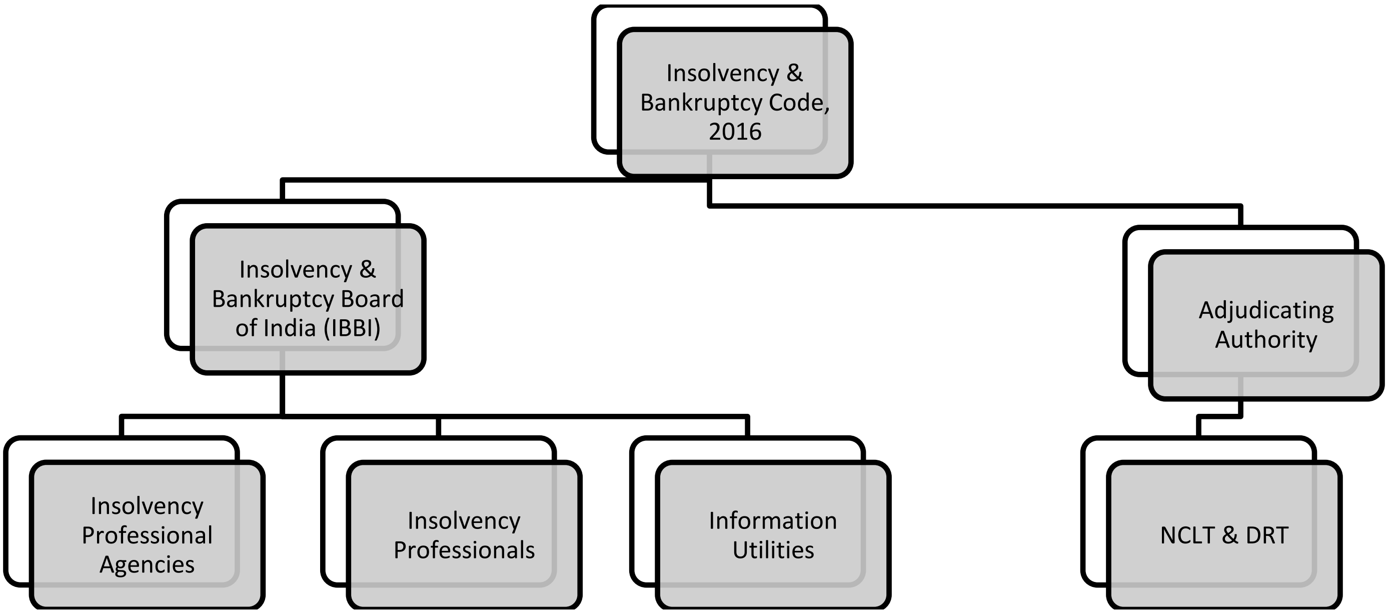
Structure of the Code:

The Code has been divided in to five parts comprising of 255 sections and 11 Schedules. Out of these some sections have been notified by the Ministry of Corporate Affairs.

Structure of the Code				
Part I – Preliminary (Section 1 – 3)	Part II – Insolvency Resolution & Liquidation for Corporate Persons. (Section 4 – 77)	Part III - Insolvency Resolution & Bankruptcy for Individuals and Partnership Firms (Section 78 – 187)	Part IV – Regulation of Insolvency Professionals, Agencies & Information Utilities (Section 188 – 223)	Part V – Miscellaneous (Section 224 – 255)

<u>Regulatory Mechanism:</u>

The Insolvency and Bankruptcy Code, 2016 provides a new regulatory mechanism with an institutional set-up comprising of five pillars:-



1. Insolvency Professionals- Intermediaries who would play a key role in the efficient working of the bankruptcy process.

In the resolution process, the insolvency professional verifies the claims of the creditors, constitutes a creditors committee, runs the debtor's business during the moratorium (cessation) period and helps the creditors in reaching a consensus for a revival plan. In liquidation, the insolvency professional acts as a liquidator and bankruptcy trustee.

2. Insolvency Professional Agencies- To enroll and regulate insolvency professionals as its members in accordance with Code.

3. Information Utilities - A notable feature of the Code is the creation of information utilities to collect, collate, authenticate and disseminate financial information of debtors in centralized electronic database.

4. Insolvency and Bankruptcy Board of India (Board)- The Code provides for establishment of a Regulator who will oversee these entities and to perform legislative, executive and quasi-judicial functions with respect to the Insolvency Professionals, Insolvency Professional Agencies and Information Utilities. The Insolvency and Bankruptcy Board of India was established on October 1, 2016. The head office of the Board is located at New Delhi.

5. Adjudicating Authority- The AA for corporate insolvency and liquidation is the NCLT. Appeals arising out of NCLT orders lie to the National Company Law Appellate Tribunal and, thereafter, to the Supreme Court of India.

The Code has created one chain of authority for adjudication under the Code. Civil Courts have been prohibited to interfere in the matters related with application pending before the adjudicating authority. No injunction shall be granted by any Court, Tribunal or Authority in respect of any action taken by the NCLT.

Extent and Commencement of the Code:

As per section 1 of the Insolvency and Bankruptcy Code, it extends to the whole of India except Part III (Insolvency Resolution and Bankruptcy for Individuals and Partnership Firm) which excludes the state of Jammu and Kashmir.

Applicability of the Code

The Code shall apply for insolvency, liquidation, voluntary liquidation or bankruptcy of the following entities:-

(a) Any company incorporated under the Companies Act, 2013 or under any previous law.

(b) Any other company governed by any special act for the time being in force, except in so far as the said provision is inconsistent with the provisions of such Special Act.

(c) Any Limited Liability Partnership under the LLP Act 2008.

(d) Any other body incorporated under any law for the time being in force, as the Central Government may by notification specify in this behalf.

(e) Partnership firms and individuals.

(II) Corporate Insolvency Resolution Process [Sections 4, 6- 32]

Provisions related to Insolvency Resolution and Liquidation process for Corporate Persons are covered in Part II of the Code.

Corporate Insolvency Resolution is a process during which financial creditors assess whether the debtor's business is viable to continue and the options for its rescue and revival. If the insolvency resolution process fails or financial creditors decide that the business of debtor cannot be carried on profitably and it should be wound up, the debtor will undergo liquidation process and the assets of the debtor are realized and distributed by the liquidator.

(1) Applicability of this Part II on the commitment of default: The process of insolvency starts only when there is a default of 1 lakh rupees or more. However, the Central Government may, by notification, specify the minimum amount of default of higher value which shall not be more than 1 Crore rupees. [Section 4]

(2) Persons who may initiate corporate insolvency resolution process:

Where any corporate debtor commits a default, following persons:

(a) a financial creditor, **(b) an operational creditor, or** **(c) the corporate debtor itself** -may initiate corporate insolvency resolution process in respect of such corporate debtor. [Section 6]

(a) <u>If Application is made by Financial Creditor:</u>

(i) **Filing of application before adjudicating authority**

(ii) **Furnishing of information:**

(a) **record of the default** recorded with the information utility or such other record or evidence of default as may be specified;

(b) **the name of the resolution professional** proposed to act as an interim resolution professional; and

(c) **any other information** as may be specified by the Board.

(iii) **Time period for determination of default**: AA shall within 14 days of the receipt of the application, ascertain the existence of a default from the records.

(iv) **Order:** Where the Adjudicating Authority is satisfied that—

(a) a **default has occurred,** it may, by order, admit such application; or

(b) **default has not occurred** it may, by order, reject such application:

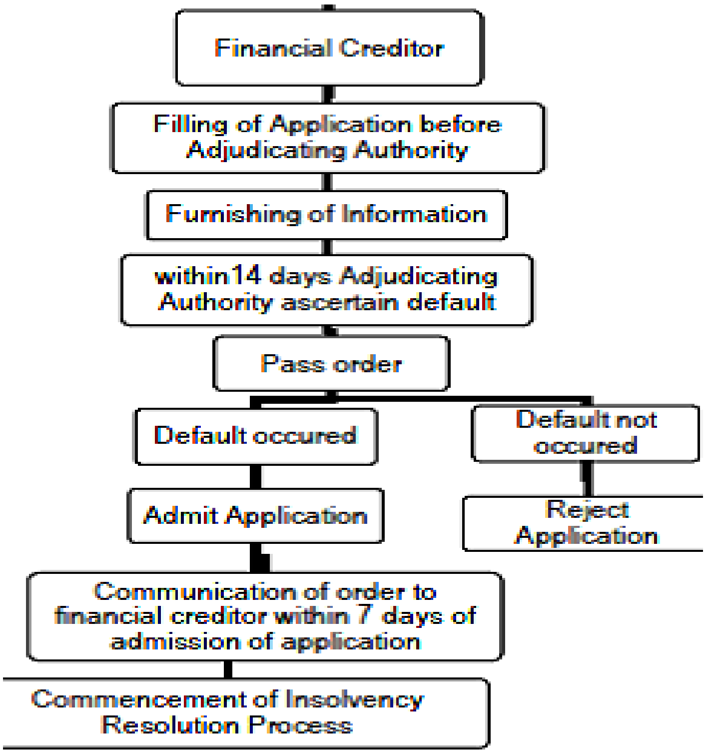
Provided that the Adjudicating Authority shall, before rejecting the application, give a notice to the applicant to rectify the defect in his application within 7 days of receipt of such notice from the AA.

(v) **Commencement of corporate insolvency resolution process** from the date of admission of the application.

(vi) **Communication of Order:** The Adjudicating Authority shall communicate—

(1) the order to the financial creditor and the corporate debtor;

(2) the order to the financial creditor, within seven days of admission or rejection of such application, as the case may be. [Section 7]



<u>(b) Insolvency resolution by operational creditor</u> (Between Creditor & Debtor)

(i) **Serving of demand Notice:** On the occurrence of default, an operational creditor shall first send a <u>demand notice</u> and a <u>copy of invoice</u> to the corporate debtor.

(ii) **On receipt of demand notice by corporate debtor:** The corporate debtor shall, within a period of 10 days of the receipt of the demand notice or copy of the invoice bring to the notice of the operational creditor about-

(1) **existence of dispute OR** (2) **repayment of unpaid operational debt**

<u>Application for initiation of corporate insolvency resolution process by operational creditor:</u>

(i) Filing of application by operational creditor: After the expiry of the period of 10 days from the date of delivery of the notice or invoice demanding payment, if the operational creditor does not receive payment from the corporate debtor or notice of the dispute, the operational creditor may file an application before the AA for initiating corporate insolvency resolution process.

(ii) Providing of documents/ information: The operational creditor shall, along with the application furnish the following documents—

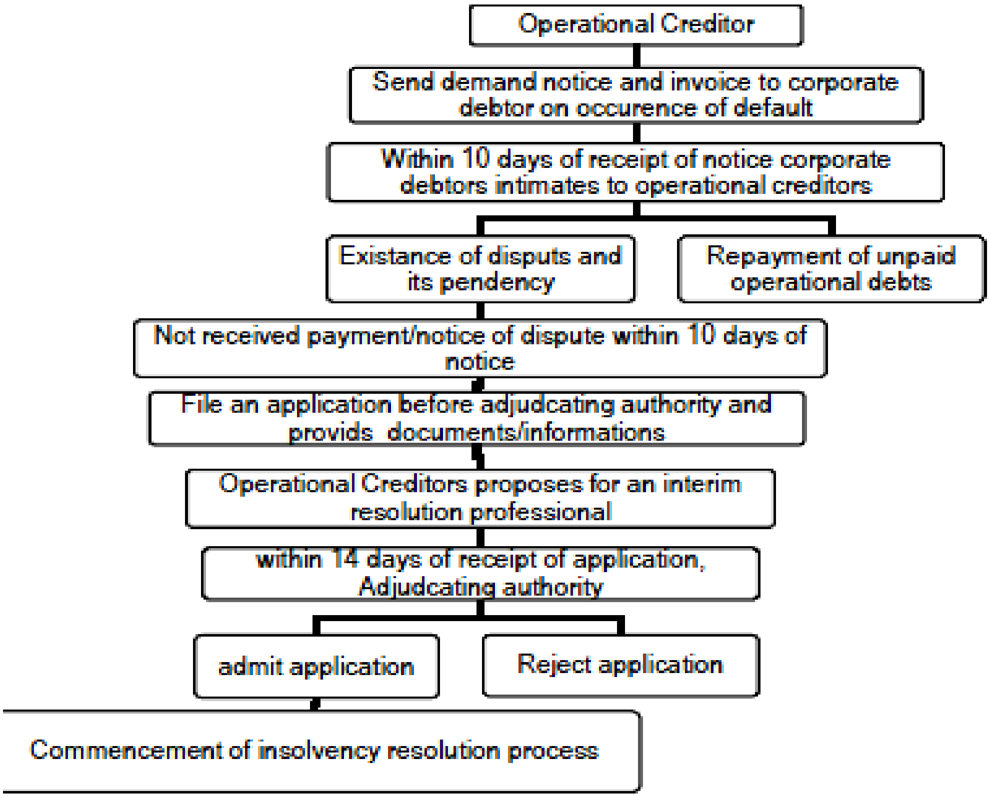
(a) a copy of the **invoice** or **demand notice**

(b) **an affidavit** to the effect that there is no notice given by the corporate debtor relating to a dispute of the unpaid operational debt;

(c) **a copy of the certificate** from the financial institutions maintaining accounts of the operational creditor confirming that there is no payment of an unpaid operational debt by the corporate debtor; and

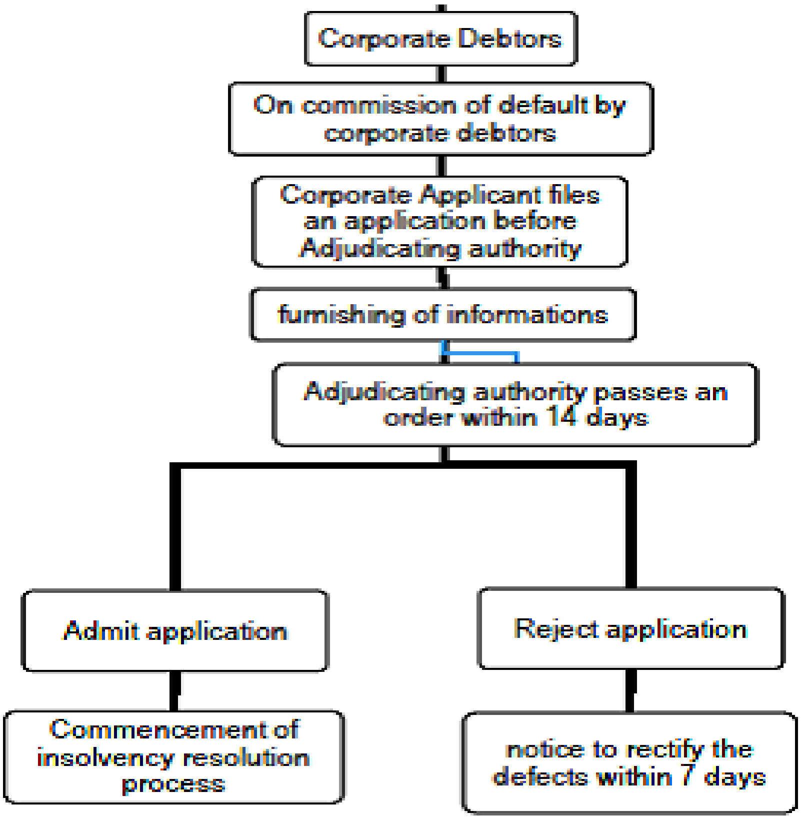
(d) **such other information** as may be specified.

(iii) An operational creditor propose for an interim resolution professional during the resolution process: An operational creditor initiating a corporate insolvency resolution process, may propose a resolution professional to act as an interim resolution professional.
(iv) Order of an adjudicating authority: The Adjudicating Authority shall, within 14 days of the receipt of the application, by an order—
(1) admit the application and communicate such decision to the operational creditor and the corporate debtor
(2) reject the application
Provided that Adjudicating Authority, shall before rejecting an application which is incomplete, gives a notice to the applicant to rectify the defect in his application within 7 days of the date of receipt of such notice from the adjudicating Authority.
(v) Commencement of insolvency resolution process: The corporate insolvency resolution process shall commence from the date of admission of the application. **[Section 9]**



<u>**(c) Initiation of corporate insolvency resolution process by corporate applicant.**</u>
(i) Commission of default: Where a corporate debtor has committed a default, the corporate applicant thereof may file an application for initiating corporate insolvency resolution process with the Adjudicating Authority.
(ii) Furnishing of information: The corporate applicant shall, along with the application furnish the information relating to—
(a) its **books of account and such other documents** relating to such period as may be specified; and
(b) the **resolution professional** proposed to be appointed as an interim resolution professional.

(iii) Admission/rejection of application: The Adjudicating Authority shall, within a period of 14 days of the receipt of the application, by an order—
(a) admits the application, if it is complete; or
(b) rejects the application, if it is incomplete:
Provided that Adjudicating Authority shall, before rejecting an application, gives a notice to the applicant to rectify the defects in his application within 7 days from the date of receipt of such notice from the Adjudicating Authority.
(iv) Commencement of insolvency resolution process: The corporate insolvency resolution process shall commence from the date of admission of the application under sub-section (4) of this section. [Section 10]



(3) Persons not entitled to make application: The following persons shall not be entitled to make an application to initiate corporate insolvency resolution process -
(a) a corporate debtor undergoing a corporate insolvency resolution process; or
(b) a corporate debtor having completed corporate insolvency resolution process 12 months preceding the date of making of the application; or
(c) a corporate debtor or a financial creditor who has violated any of the terms of resolution plan which was approved 12 months before the date of making of an application under this Chapter; or
(d) a corporate debtor in respect of whom a liquidation order has been made.

(4) Time-limit for completion of insolvency resolution process:
(a) **Period for completion of insolvency process:** The corporate insolvency resolution process shall be completed within a period of **180 days** from the date of admission of the application to initiate such process.

(b) **Filing of application for extension of period:** The resolution professional shall file an application to the AA to extend the period of the corporate insolvency resolution process beyond 180 days, if instructed to do so by a resolution passed at a meeting of the committee of creditors by a vote of 75% of the voting shares.
(c) **Period of extension:** On receipt of an application , if the AA is satisfied that the subject matter of the case is such that corporate insolvency resolution process cannot be completed within 180 days, it may by order extend the duration of such process beyond 180 days by such further period as it thinks fit, **but not exceeding 90 days**: Provided that any extension of the period of corporate insolvency resolution process under this section shall not be granted more than once**. [section 12]**

(5) Declaration of moratorium and public announcement: The AA, after admission of the application, shall, by an order—
(a) declare a moratorium;
(b) cause a public announcement of the initiation of corporate insolvency resolution process and call for the submission of claims , and
(c) appoint an interim resolution professional in the manner as laid down in section 16.
The public announcement as referred above, shall be made immediately after the appointment of the interim resolution professional. **[Section 13]**

Moratorium:
After the commencement of corporate insolvency resolution, a calm period for 180 days is declared, during which all suits and legal proceedings etc. against the Corporate Debtor are kept in abeyance to give time to the entity to resolve its status. It is called the Moratorium Period.
(i) Declaration of moratorium period: According to the section 14 of the Code, on the insolvency commencement date, the AA shall by order, declare moratorium prohibiting all of the following acts—
(a) **the institution of suits or continuation of pending suits or proceedings** against the corporate debtor;
(b) **transferring, encumbering, alienating or disposing** any of its assets;
(c) **any action to foreclose, recover or enforce any security interest** created by the corporate debtor in respect of its property including any action under the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002;
(d) **the recovery of any property** by an owner where such property is occupied by or in the possession of the corporate debtor.

(ii) The supply of essential goods or services to the corporate debtor as may be specified shall not be terminated or suspended or interrupted during moratorium period.

(iii) Prohibited Acts: Acts prohibited during Moratorium period, shall not apply to such transactions as may be notified by the Central Government in consultation with any financial sector regulator.

(iv) Effect of the order of moratorium: The order of moratorium shall have effect from the date of such order till the completion of the corporate insolvency resolution process:

(v) When Moratorium period shall cease to have effect: Provided that where at any time during the corporate insolvency resolution process period, if the AA approves the resolution plan or passes an order for liquidation of corporate debtor, the moratorium shall cease to have effect from the date of such approval or liquidation order, as the case may be.
[Section 14]

(6) Appointment, tenure and Power of interim resolution professional: The Adjudicating Authority shall appoint an interim resolution professional within 14 days from the insolvency commencement date. As per section 16 of the Code, following is the process for the appointment of interim resolution professional-

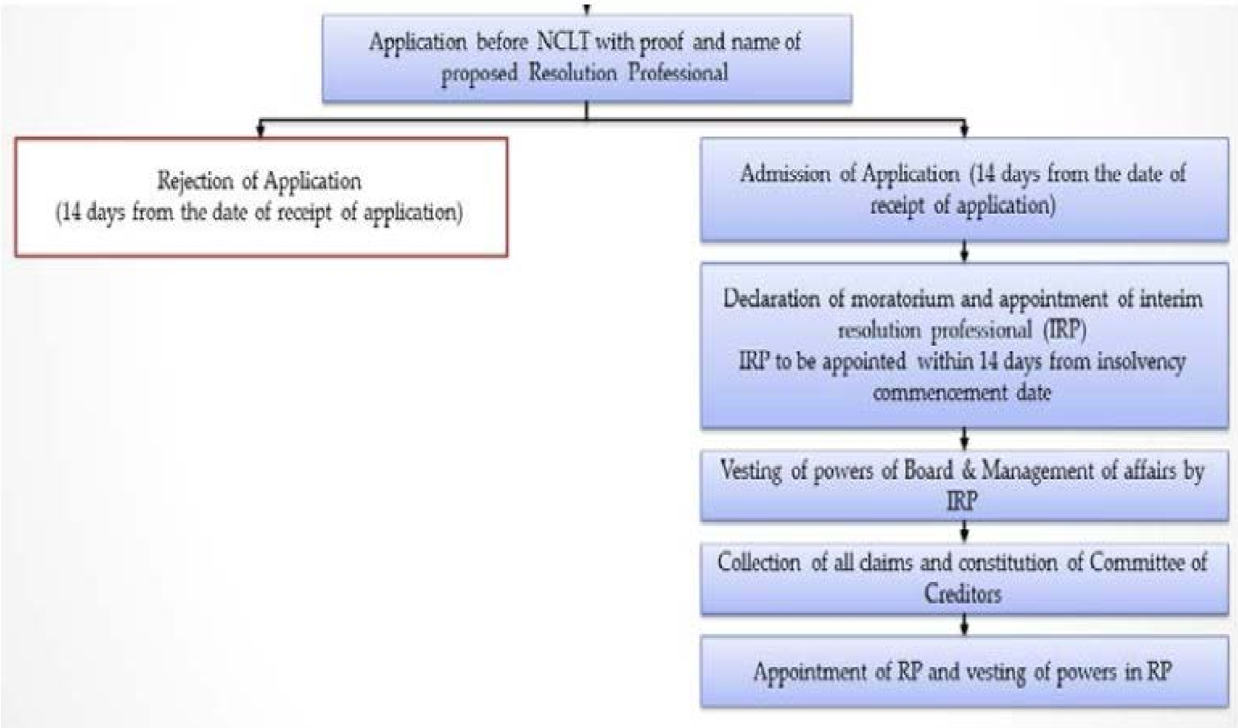
Process of appointment of Interim resolution professional
(i) Where the application for corporate insolvency resolution process is made by a <u>financial creditor or the corporate debtor</u>, as the case may be, the resolution professional, as proposed in the application shall be appointed as the interim resolution professional, if no disciplinary proceedings are pending against him.
(ii) Where the application for corporate insolvency resolution process is made by an <u>operational creditor</u> and—
(a) **no proposal for an interim resolution professional is made**, the Adjudicating Authority shall make a reference to the Board for the recommendation of an insolvency professional who may act as an interim resolution professional;
(b) **a proposal for an interim resolution professional is made**, the resolution professional as proposed, shall be appointed as the interim resolution professional, if no disciplinary proceedings are pending against him.
The Board shall, within 10 days of the receipt of a reference from the Adjudicating Authority, recommend the name of an insolvency professional to the Adjudicating Authority against whom no disciplinary proceedings are pending.

<u>**Term of appointment**</u>
The term of the interim resolution professional shall not exceed thirty days from date of his appointment.
The **key roles of an Interim Resolution Professional** are:-
(a) Issuance of public notice of the Corporate Insolvency
(b) Resolution process
(c) Collation of claims received
(d) Constitution of the Committee of Creditors
(e) Conduct of the first meeting of the Committee of Creditors

<u>**Powers of Interim Resolution Professional:**</u>
As Per Section 17 of the Code, the interim resolution professional shall have following powers:-
(a) Management of Affairs of the corporate debtor from the date of his appointment.
(b) Exercise of Power of BoD/ partners as their powers shall stand suspended and be exercised by the interim resolution professional.
(c) Reporting of officers/managers: 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.

(d) Instructions to financial institutions: The financial institutions maintaining accounts of the corporate debtor shall act on the instructions of the interim resolution professional in relation to such accounts and furnish all information relating to the corporate debtor available with them to the interim resolution professional.

The chart below explains the flow of interim resolution professional



(7) Public Announcement: Interim Resolution Professional shall make the Public Announcement immediately (maximum within 3 days from the date of appt)

As per Section 15 of the Code, public announcement shall include the following:-

(a) Name & Address of Corporate Debtor under the Corporate Insolvency Resolution Process.

(b) Name of the authority with which the corporate debtor is incorporated or registered.

(c) Details of interim resolution Professional who shall be vested with the management of the Corporate Debtor and be responsible for receiving claims.

(d) Penalties for false or misleading Claims.

(e) The last date for the submission of the claims.

(f) The date on which the Corporate Insolvency Resolution Process ends.

The expenses of public announcement shall be borne by the applicant, which may be reimbursed by the Committee of Creditors, to the extent, it ratifies them.

(8) Committee of creditors: As per the Section 21 of the Code, the interim resolution professional shall after collection of all claims received against the corporate debtor and determination of the financial position of the corporate debtor, constitute a committee of creditors.

Constitution of Committee of creditors:

(i) The committee of creditors shall comprise of all financial creditors of the corporate debtor.

Provided that a related party to whom a corporate debtor owes a financial debt shall not have any right of representation, participation or voting in a meeting of the committee of creditors.

(ii) Where the corporate debtor owes financial debts to **two or more financial creditors** as part of an agreement, each such financial creditor shall be part of the committee of creditors and their voting share shall be determined on the basis of the financial debts owed to them.

(iii) Where any person is a **financial creditor as well as an operational creditor**,—

(a) such person shall be a financial creditor to the extent of the financial debt owed by the corporate debtor, and shall be included in the committee of creditors, with voting share proportionate to the extent of financial debts owed to such creditor;

(b) such person shall be considered to be an operational creditor to the extent of the operational debt owed by the corporate debtor to such creditor.

(iv) Each financial creditor may—

(a) authorise the trustee or agent to act on his behalf in the committee of creditors to the extent of his voting share;

(b) represent himself in the committee of creditors to the extent of his voting share;

(c) appoint an insolvency professional (other than the resolution professional) at his own cost to represent himself in the committee of creditors to the extent of his voting share; or

(d) exercise his right to vote to the extent of his voting share with one or more financial creditors jointly or severally.

(v) All decisions of the committee of creditors shall be taken by a vote of not less than 75% of voting share of the financial creditors.

(vi) The committee of creditors shall have the right to require the resolution professional to furnish any financial information in relation to the corporate debtor at any time during the corporate insolvency resolution process.

(vii) The resolution professional shall make available any financial information so required by the committee of creditors within a period of 7 days of such requisition.

(ix) The first meeting of the committee of creditors shall be held within 7 days of the constitution of the committee of creditors. (Section 22)

Meeting of committee of creditors (Section 24):

(i) Conduct of meeting: The members of the committee of creditors may meet in person or by such electronic means as may be specified. All meetings of the committee of creditors shall be conducted by the resolution professional.

The resolution professional shall give notice of each meeting of the committee of creditors to—

(a) members of Committee of creditors;

(b) members of the suspended Board of Directors or the partners of the corporate persons, as the case may be;

(c) operational creditors or their representatives if the amount of their aggregate dues is not less than 10% of the debt.

The directors, partners and one representative of operational creditors, may attend the meetings of committee of creditors, but shall not have any right to vote in such meetings.

Provided that the absence of any such director, partner or representative of operational creditors, as the case may be, shall not invalidate proceedings of such meeting.

(ii) Appointment of insolvency professional to represent creditor in a meeting of the committee of creditors: Any creditor who is a member of the committee of creditors may appoint an insolvency professional other than the resolution professional to represent such creditor in a meeting of the committee of creditors: Provided that the fees payable to such insolvency professional representing any individual creditor will be borne by such creditor.

(iii) Right to vote to creditor: Each creditor shall vote in accordance with the voting share assigned to him based on the financial debts owed to such creditor.

(9) Appointment and functions of resolution professional: According to Section 22 of the Code, the committee of creditors, may, in the first meeting, by a majority vote of not less than 75% of the voting share of the financial creditors, either resolve to appoint the interim resolution professional as a resolution professional or to replace the interim resolution professional by another resolution professional.

Functions of Resolution professional (Section 23):

(i) The resolution professional shall conduct the entire corporate insolvency resolution process and manage the operations of the corporate debtor during the corporate insolvency resolution process period.

(ii) The resolution professional shall exercise powers and perform duties as are vested or conferred on the interim resolution professional.

(iii) In case of any appointment of a resolution professional, the interim resolution professional shall provide all the information, documents and records pertaining to the corporate debtor in his possession and knowledge to the resolution professional.

The Resolution Professional's primary function is to take over the management of the corporate borrower and operate its business as a going concern under the broad directions of committee of creditors.

The thrust of the Code is to allow a shift of control from the defaulting debtor's management to its creditors, where the creditors drive the business of the debtor with the Resolution Professional acting as their agent.

(10) Replacement of resolution professional by committee of creditors: Section 27 provides manner of replacement of resolution professional with another resolution professional by committee of creditors. Process of replacement of resolution professional is as follows:

(i) Committee of creditors is of the opinion that a resolution professional as appointed, is required to be replaced, it may replace him with another resolution professional.

(ii) By majority: The committee of creditors may, at a meeting, by a vote of 75 % of voting shares, propose to replace the resolution professional appointed with another resolution professional.

(iii) Forwarding of name to Adjudicating Authority: The committee of creditors shall forward the name of the insolvency professional proposed by them to the Adjudicating Authority.

(iv) Further forwarding name to Board: The Adjudicating Authority shall forward the name of the proposed resolution professional to the Board for its confirmation and a resolution professional shall be appointed in the same manner as laid down in section 16.

(v) Continuation of office: Where any disciplinary proceedings are pending against the proposed resolution professional, the resolution professional appointed shall continue till the appointment of another resolution professional under this section.

(11) Approval of committee of creditors for certain actions of resolution professional, during the corporate insolvency resolution process: The resolution professional, during the corporate insolvency resolution process, shall not take any of the following actions without the prior approval of the committee of creditors—

(a) **raise any interim finance** in excess of the amount as may be decided by the committee of creditors in their meeting;

(b) **create any security interest** over the assets of the corporate debtor;

(c) **change the capital structure** of the corporate debtor, including by way of issuance of additional securities, creating a new class of securities or buying back or redemption of issued securities in case the corporate debtor is a company;

(d) record any change in the ownership interest of the corporate debtor;

(e) **give instructions to financial institutions** maintaining accounts of the corporate debtor for a debit transaction from any such accounts in excess of the amount as may be decided by the committee of creditors in their meeting;

(f) **undertake any related party transaction;**

(g) **amend any constitutional documents** of the corporate debtor;

(h) **delegate its authority** to any other person;

(i) dispose of or permit the disposal of shares of any shareholder of the corporate debtor or their nominees to third parties;

(j) **make any change in the management** of the corporate debtor or its subsidiary;

(k) transfer rights or financial debts or operational debts under material contracts otherwise than in the ordinary course of business;

(l) **make changes in the appointment or terms of contract of such personnel** as specified by the committee of creditors; or

(m) **make changes in the appointment or terms of contract of statutory auditors or internal auditors** of the corporate debtor.

<u>Approval of the committee of creditors</u>

The resolution professional shall convene a meeting of the committee of creditors and seek the vote of the creditors prior to taking any of the actions.

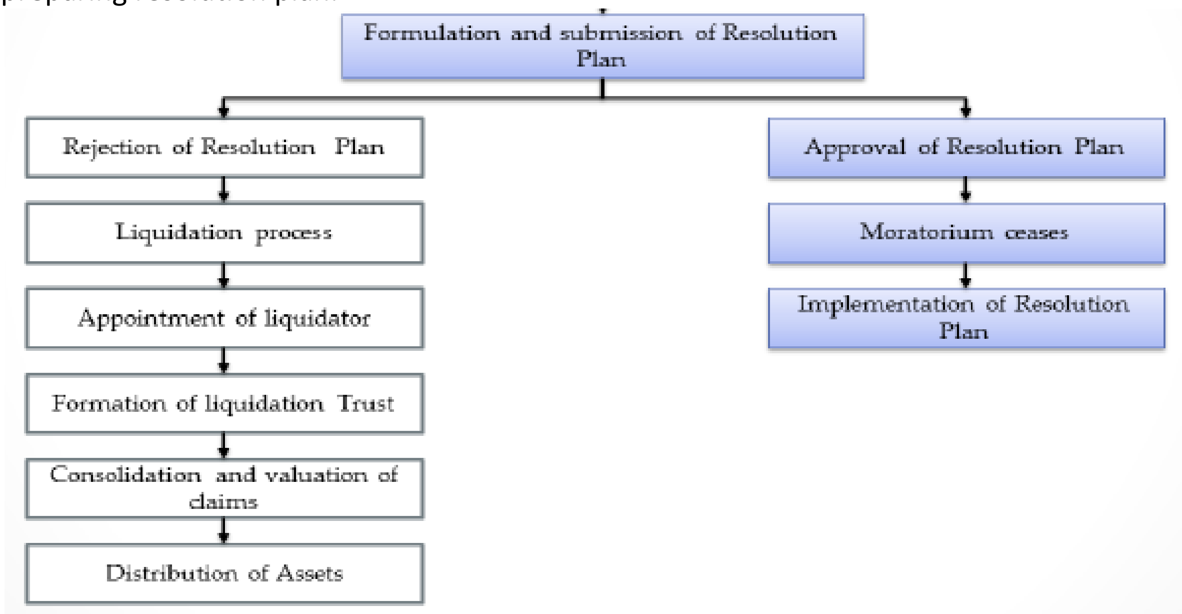
No action shall be approved by the committee of creditors unless approved by a vote of 75% of the voting shares. Where any action is taken by the resolution professional without seeking the approval of the committee of creditors in the manner as required in this section, such action shall be void.

<u>Report the actions of the resolution professional to the Board:</u> The committee of creditors may report the actions of the resolution professional to the Board for taking necessary actions against him under this Code.[Section 28]

(12) Preparation of information memorandum: According to section 29 of the code, the resolution professional shall prepare an information memorandum containing such relevant information as may be specified by the Board for formulating a resolution plan.

The resolution professional shall provide to the resolution applicant access to all relevant information in physical and electronic form.
"Relevant information" means the information required by the resolution applicant to make the resolution plan for the corporate debtor, which shall include the financial position of the corporate debtor, all information related to disputes by or against the corporate debtor and any other matter pertaining to the corporate debtor as may be specified.

(13) Resolution plan: Section 30 to 31 of the Code deals with resolution plan. Resolution professional shall prepare an Information Memorandum which shall contain information for preparing resolution plan.



Submission of resolution plan: A resolution applicant may submit a resolution plan to the resolution professional prepared on the basis of the information memorandum.

Examination of Resolution Plan: The resolution professional shall examine each resolution plan received by him to confirm that each resolution plan—
(a) **provides for the payment of insolvency resolution process costs** in a manner specified by the Board in priority to the repayment of other debts of the corporate debtor;
(b) **provides for the repayment of the debts of operational creditors** in such manner as may be specified by the Board which shall not be less than the amount to be paid to the operational creditors in the event of a liquidation of the corporate debtor under section 53;
(c) **provides for the management of the affairs of the Corporate debtor** after approval of the resolution plan;
(d) the **implementation and supervision** of the resolution plan;
(e) **does not contravene any of the provisions of the law** for the time being in force;
(f) **conforms to such other requirements** as may be specified by the Board.

Approval from Committee of creditors: The resolution professional shall present to the committee of creditors for its approval such resolution plans which confirm the conditions as mentioned above. The committee of creditors may approve a resolution plan by a vote of not less than 75 % of voting share of the financial creditors.

Right of resolution applicant to attend the meeting of the committee of creditors: The resolution applicant may attend the meeting of the committee of creditors in which the resolution plan of the applicant is considered:
Provided that the resolution applicant shall not have a right to vote at the meeting of the committee of creditors unless such resolution applicant is also a financial creditor.

Submission of approved resolution plan to adjudicating authority: The resolution professional shall submit the resolution plan as approved by the committee of creditors to the Adjudicating Authority.

Approval of resolution plan adjudicating authority: If the Adjudicating Authority is satisfied that the resolution plan as approved by the committee of creditors meets the requirements , it shall by order approve the resolution plan which shall be binding on the corporate debtor and its employees, members, creditors, guarantors and other stakeholders involved in the resolution plan.
Where the Adjudicating Authority is satisfied that the resolution plan does not confirm to the requirements, it may, by an order, reject the resolution plan.

After the order of approval of resolution plan—
(a) the moratorium order passed by the Adjudicating Authority shall cease to have effect; and
(b) the resolution professional shall forward all records relating to the conduct of the corporate insolvency resolution process and the resolution plan to the Board to be recorded on its database.

(III) Liquidation Process

The Code concerns itself only with those corporate debtors which have defaulted in payment of debts.

The corporate debtor, at the first stage, is put into resolution mode. The process is called the corporate insolvency resolution process.

<u>However, if attempts to resolve the insolvency of the corporate debtor fail, then only the liquidation provisions of the Code are triggered.</u>

Where no plan is presented or where the plan presented is not approved by the Adjudicating Authority it shall pass an order requiring the Corporate Debtor to be liquidated in the manner as laid down in Chapter III of the Act.

Section 33 to 54 of the Code provides the law related to the liquidation process.

(1) Initiation of liquidation: Section 33 of the Code deals with the initiation of liquidation process.

Under the Code, a corporate debtor may be put into liquidation in the following scenarios:

(i) A <u>75% majority of the creditor's committee</u> resolves to liquidate the corporate debtor at any time during the insolvency resolution process;

(ii) The <u>creditor's committee does not approve a resolution</u> plan within 180 days (or within the extended 90 days);

(iii) The <u>NCLT rejects the resolution plan</u> submitted to it on technical grounds; or

(iv) The <u>debtor contravenes the agreed resolution plan</u> and an affected person makes an application to the NCLT to liquidate the corporate debtor.

Once the NCLT passes an order of liquidation, a moratorium is imposed on the pending legal proceedings against the corporate debtor, and the assets of the debtor (including the proceeds of liquidation) vest in the liquidation estate.

(2) Appointment of liquidator: Section 34 of the Code provides for appointment of liquidator.

- **By Default: Resolution professional to act as liquidator** unless replaced by the Adjudicating Authority.
- **Powers of Board of Director (BOD)/ Key Managerial Personnel (KMP) shall now vest with liquidator**
- **Personnel to extend cooperation to liquidator** as may be required by him in managing the affairs of the corporate debtor in relation to voluntary liquidation process.
- **Order to replace the resolution professional**: The Adjudicating Authority shall by order replace the resolution professional, if—

  (a) the resolution plan submitted by the resolution professional **was rejected for failure to meet the requirements**; or

  (b) the **Board recommends the replacement of a resolution professional** to the Adjudicating Authority for reasons to be recorded in writing.

  The Adjudicating Authority may direct the Board to propose the name of another insolvency professional to be appointed as a liquidator. The Board shall propose the name of another insolvency professional within 10 days of the direction issued by the Adjudicating Authority.

- **Adjudicating Authority shall appoint insolvency professional as the liquidator on** receipt of the proposal of the Board.

- **An Insolvency Professional shall charge fees for conduct of liquidation proceedings** and in such proportion to the value of the liquidation estate assets, as may be specified by the Board & such fees shall be paid from the proceeds of the liquidation estate.

(3) Powers and duties of liquidator: Section 35 of the Code specifies the following power and duties of liquidator-
(a) to **verify claims** of all the creditors;
(b) to **take into his custody or control** all the assets, property, effects and actionable claims of the corporate debtor;
(c) to **evaluate the assets and property** of the corporate debtor in the manner as may be specified by the Board and prepare a report;
(d) to take such **measures to protect and preserve the assets and properties** of the corporate debtor as he considers necessary;
(e) **to carry on the business** of the corporate debtor for its beneficial liquidation as he considers necessary;
(f) to **sell the immovable and movable property and actionable claims** of the corporate debtor in liquidation by public auction or private contract;
(g) to **draw, accept, make and endorse any negotiable instruments** including bill of exchange, hundi or promissory note in the name and on behalf of the corporate debtor;
(h) **to take out, in his official name, letter of administration to any deceased contributory** and to do in his official name any other act necessary for obtaining payment of any money due and payable from a contributory or his estate;
(i) to **obtain any professional assistance** from any person or appoint any professional, in discharge of his duties, obligations and responsibilities;
(j) to **invite and settle claims** of creditors and claimants and distribute proceeds in accordance with the provisions of this Code;
(k) to **institute or defend any suit, prosecution or other legal proceedings**, civil or criminal, in the name of on behalf of the corporate debtor;
(l) to **investigate the financial affairs** of the corporate debtor to determine undervalued or preferential transactions;
(m) **to take all such actions, steps, or to sign, execute and verify any paper, deed, receipt document, application, petition, affidavit, bond or instrument** and for such purpose to use the common seal, if any, as may be necessary for liquidation, distribution of assets and in discharge of his duties and obligations and functions as liquidator;
(n) to **apply to the Adjudicating Authority for such orders or directions** as may be necessary for the liquidation of the corporate debtor and to report the progress of the liquidation process in a manner as may be specified by the Board; and
(o) to **perform such other functions** as may be specified by the Board.
The liquidator shall have the power to consult any of the stakeholders entitled to a distribution of proceeds : Provided that any such consultation shall not be binding on the liquidator.

Powers of liquidator to access information:

The liquidator shall have the power to access any information systems for the purpose of admission and proof of claims and identification of the liquidation estate assets relating to the corporate debtor.

The creditors may require the liquidator to provide them any financial information relating to the corporate debtor.

The liquidator shall provide information to such creditors who have requested for such information within a period of 7 days from the date of such request or provide reasons for not providing such information [Section 37]

(4) Liquidation estate: According to section 36 of the code, for the purposes of liquidation, the liquidator shall form an estate of the assets, which will be called the liquidation estate in relation to the corporate debtor.

The liquidator shall hold the liquidation estate as a fiduciary for the benefit of all the creditors.

Comprising of liquidation estate: The liquidation estate shall comprise of all liquidation estate assets as follows:

Inclusions	Exclusions
Any assets over which the corporate debtor has ownership rights;	Assets owned by a third party which are in possession of corporate debtor;
Encumbered assets, Tangible & Intangible Assets	Personal assets of any shareholder or partner of corporate debtor as the case may be provided such assets are not held on account of avoidance transactions;
Assets issued as collateral over which creditors have relinquished rights;	Assets of any Indian or Foreign subsidiary of the corporate debtor
All proceeds of liquidation as and when they are realized	--

(5) Consolidation of claims: Section 38 of the Code deals with provisions related to the consolidation of claims. Accordingly-

(1) **Collection of claims by liquidator:** The liquidator shall receive or collect the claims of creditors within a period of 30 days from the date of the commencement of the liquidation process.

(2) **Submission of claims:** A financial creditor may submit a claim to the liquidator by providing a record of such claim with an information utility.

(3) **Supportive documents:** An operational creditor may submit a claim to the liquidator in such form and in such manner and along with such supporting documents required to prove the claim as may be specified by the Board.

(4) **Amount of claims to be submitted:** A creditor who is partly a financial creditor and partly an operational creditor shall submit claims to the liquidator to the extent of his financial debt and to the extent of his operational debt.

(5) **Alteration in claim**: A creditor may withdraw or vary his claim under this section within 14 days of its submission.

Verification of claims.
The liquidator shall verify the claims submitted within such time as specified by the Board. The liquidator may require any creditor or the corporate debtor or any other person to produce any other document or evidence which he thinks necessary for the purpose of verifying the whole or any part of the claim.[Section 39]

Admission or rejection of claims.
The liquidator may, after verification of claims, either admit or reject the claim, in whole or in part, as the case may be.
Provided that where the liquidator rejects a claim, he shall record in writing the reasons for such rejection.
The liquidator shall communicate his decision of admission or rejection of claims to the creditor and corporate debtor within 7 days of such admission or rejection of claims.
[Section 40]

Determination of valuation of claims: The liquidator shall determine the value of claims admitted in such manner as may be specified by the Board. [Section 41]

Appeal against the decision of liquidator: A creditor may appeal to the AA against the decision of the liquidator rejecting the claims within 14 days of the receipt of such decision.
[Section 42]

(6) Secured creditor in liquidation proceedings:
(i) A secured creditor in the liquidation proceedings may—
(a) **relinquish its security interest to the liquidation estate** and receive proceeds from the sale of assets by the liquidator , or
(b) **realise its security interest** in the manner specified in this section.

(ii) **To inform the liquidator about realisation of security interest:** Where the secured creditor realises security interest under clause (b) above, he shall inform the liquidator of such security interest and identify the asset subject to such security interest to be realised.

(iii) **Verification by liquidator of security interest:** Before any security interest is realised by the secured creditor under this section, the liquidator shall verify such security interest and permit the secured creditor to realise only the required security interest.

(iv) **Restriction in realising of secured asset:** If in the course of realising a secured asset, any secured creditor faces resistance from the corporate debtor or any person connected therewith in taking possession of, selling or otherwise disposing off the security, the secured creditor may make an application to the AA to allow the secured creditor to realise such security interest in accordance with law for the time being in force.

(v) **Passing of order by Adjudicating Authority** to permit a secured creditor to realise security interest in accordance with law for the time being in force.

(vi) **Yield of surplus:** In case of Surplus, the secured creditor shall—
(a) account to the liquidator for such surplus; and

(b) hand over to the liquidator any surplus funds received from the enforcement of such secured assets.

(vii) **Unpaid debts to be paid by liquidator:** Where the proceeds of the realisation of the secured assets are not adequate to repay debts owed to the secured creditor, the unpaid debts of such secured creditor shall be paid by the liquidator [Section 52]

(7) Distribution of assets: The Code significantly changes the priority waterfall for distribution of liquidation proceeds.

(i) Distribution of proceeds from the sale of the liquidation assets: The proceeds from the sale of the liquidation assets shall be distributed in the following order of priority —
(a) the insolvency resolution process costs and the liquidation costs paid in full;

(b) the following debts which shall rank equally between and among the following :—
(I) workmen's dues for the period of 24 months preceding the liquidation commencement date; and
(II) debts owed to a secured creditor in the event such secured creditor has relinquished security in the manner set out in section 52;

(c) wages and any unpaid dues owed to employees other than workmen for the period of 12 months preceding the liquidation commencement date;

(d) financial debts owed to unsecured creditors;

(e) the following dues shall rank equally between and among the following:—
(I) any amount due to the CG & SG, if any, in respect of the whole or any part of the period of two years preceding the liquidation commencement date;
(II) debts owed to a secured creditor for any amount unpaid following the enforcement of security interest;

(f) any remaining debts and dues;

(g) preference shareholders, if any; and

(h) equity shareholders or partners, as the case may be.

(ii) **Disregard of order of priority:** Any contractual arrangements between recipients with equal ranking, if disrupting the order of priority shall be disregarded by the liquidator.

(iii) **Fees to liquidator:** The fees payable to the liquidator shall be deducted proportionately from the proceeds payable to each class of recipients, and the proceeds to the relevant recipient shall be distributed after such deduction.

(8) Dissolution of corporate debtor

Application by liquidator dissolution: Where the assets of the corporate debtor have been completely liquidated, the liquidator shall make an application to the AA for the dissolution of such corporate debtor.

Date of dissolution: The AA shall on application filed by the liquidator orders that the corporate debtor shall be dissolved from the date of that order and the corporate debtor shall be dissolved accordingly.

Submission of order copy: A copy of an order shall within 7 days from the date of such order, be forwarded to the authority with which the corporate debtor is registered.