Confederation of Indian Industry

The IBC Code, 2016

Balancing Fairness and Equity

May 2024

SUMEDHA
adding values to value

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Foreword

The effectiveness of the Insolvency and Bankruptcy Code (IBC) lies in the overall efficiency, value maximisation and balancing fairness and equity for all stake holders. The IBC is still evolving and number of provisions focusing upon individual insolvency, group insolvency, cross-border insolvency, mediation, real estate insolvency is to take gigantic steps ahead. A series of steps taken by the National Company Law Tribunal (NCLT), along with govt and the Insolvency and Bankruptcy Board of India (IBBI) has resulted in a record number of cases being decided during the last financial year.

The IBC has helped improve the lending culture in India as promoters are now keen to repay the debt to banks and also clear the dues of vendors and other creditors, fearing loss of control over their business in case of continued default. With an insolvency process getting streamlined, the ratio of the number of cases ending with resolution and cases in which liquidation is ordered, has improved from 0.46 in FY23 to 0.61 during the FY24.

Recently RBI released a Master Direction, affecting from 24 April 2024, that for business of securitisation or asset reconstruction, an Asset Reconstruction Companies (ARCs) is required to have a minimum net owned fund of Rs. 300 crore and thereafter on an ongoing basis, which means mandating them to maintain a minimum net owned fund (NOF) of INR 300 crores in a phased manner by FY26. If all the ARC fails to comply with, then it shall be subject to supervisory action including prohibition on undertaking incremental business till it reaches the required minimum NOF applicable at that time.

The objective of the report is to update readers on the Judicial Interpretation of Fairness and Equity under the IBC. It also aims to identify opportunities for enhancing fairness and equity within the framework and to outline the future direction towards a more equitable insolvency regime.

Additionally, the report broadly covers innovative and hybrid mechanisms for resolving insolvency, including the pre-packaged insolvency process for MSMEs. Finally, it highlights selected judgments that hold immense importance in shaping the IBC processes.

Bijay Murmuria
Chairman, Banking & Financial Services Subcommittee,
CII Eastern Region

Introductory Message

The Insolvency and Bankruptcy Code (IBC, the Code) has been a game changer in the realm of economic legislations as by putting in place a comprehensive *'one-stop-shop'* for insolvency resolution. The Insolvency and Bankruptcy Code was introduced in 2016 to resolve claims involving insolvent companies so as to tackle the bad loan problems that were affecting the banking system at large.

This legislation provides a structured and time-bound mechanism for distressed businesses to navigate insolvency. By replacing the previous legal framework with a more predictable, market-driven, and incentive-aligned system, the IBC has significantly improved the corporate distress resolution process in India. It was enacted as a pivotal element in India's transition towards a mature market economy.
The IBC effectively addresses the need for a comprehensive law to manage the insolvency of debtors, while also maximizing asset value for creditors and facilitating the closure of unviable businesses.

Since its launch in December, 2016 until December 2023, a robust insolvency ecosystem has been established, comprising of 4409 Insolvency Professionals, 118 Insolvency Professional Entities, 1 Information Utility, 5489 Registered Valuers, 90 Registered Valuer Entities, 16 Registered Valuer Organizations, NCLT (16 benches), NCLAT (2 benches), IBBI, and the Government Judicial System.

Together, these elements form the backbone of the insolvency ecosystem and have developed a vibrant process for the smooth operation of the insolvency proceedings.

As of December 31, 2023, this integrated system has collectively handled 7325 Corporate Insolvency Resolution Process with 1899 cases closed and 5426 resolved through approval of resolution plans (891 cases), commencement of liquidation plans (2376 cases), or withdrawal U/s 12A (1035 cases) or settlement (1124 cases). In the 891 resolution cases, creditors have successfully realized INR 3.21 Lakh Crores against their combined claims of INR 10.07 Lakh Crores, resulting in a recovery rate of 31.86%.

According to a report titled “Trend and Progress of Banking in India 2022-23” published by the Reserve Bank of India on December 27, 2023, the Insolvency and Bankruptcy Code (IBC) emerged as the dominant mode of asset recovery for banks accounting for 43% to the total amount recovered in 2022-23. Furthermore, the realization against claims under IBC improved to 40.3%, up from 23.9% recorded in 2021-22.

A study conducted by IIM Ahmedabad on measuring the achievements of resolution process under IBC reveals that a significant number of firms that underwent resolution experienced substantial improvements in both operational and financial performance.

The Insolvency and Bankruptcy Code, 2016 is a very dynamic and continuous evolving law with various amendments introduced since its inception. These amendments focus on areas such as individual insolvency, group insolvency, cross-border insolvency, real-estate insolvency, mediation, pre-packaged insolvency, and more. The effectiveness of the IBC code lies in its ability to ensure overall efficiency, maximizing value, and maintain fairness and equity for all stakeholders.

Despite all, the code is not a magic wand. It may have shortcomings, and the regulatory body, IBBI, is continuously considering numerous changes to rejuvenate the Code.

In this context, CII & Sumedha have prepared this knowledge series covering technical notes on Innovative and Hybrid Mechanism of Restructuring, Judicial Interpretation of Fairness and Equity, Opportunities and Challenges for Enhancing Fairness and Equity Within the IBC Framework, Future Directions, and Selected Judgements.

Vijay Maheshwari
Chairman, Sumedha Fiscal Services Ltd
&
Director, Sumedha Management Solutions Pvt Ltd

01

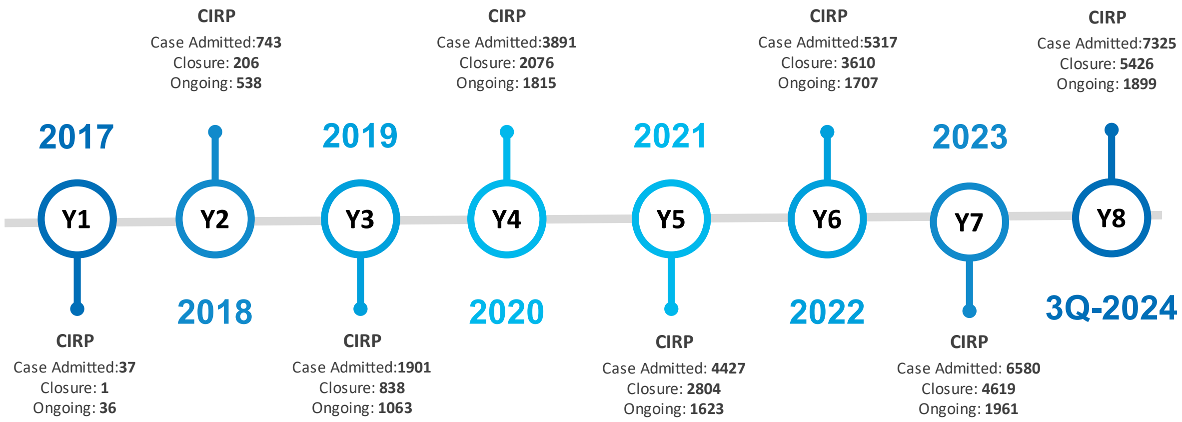
A Glimpse into the CIRP's Progress

Since the introduction of the Code in December 2016, India has made remarkable progress in stressed assets resolution. Throughout this period, a significant improvement has been witnessed in both collection efficiencies and the speed at which disputes are resolved. Despite all the positives, the code has its limitations. In this evolving state the resolution process is often delayed beyond the prescribed timeline due to litigation occurring at different stages of the CIRP process, as well as inadequate regulatory infrastructure.

As on December 31, 2023, a total of 7325 corporate debtors had undergone the CIRP. Out of which, 5426 cases were closed either through approval of the resolution plans, commencement of liquidation or due to appeal/review/withdrawal U/s 12A of the Code.

During the financial year 2022-23, there were 1263 new cases admitted in CIRP and another 745 new cases were admitted during the first nine months of the financial year 2023-24. The continuous admission of such a significant number of cases reflects the effectiveness of the code in the resolution of the stressed assets. As of December 31, 2023, a total of 1899 cases are active and are at various stages of the CIRP process.

Progress in the Corporate Insolvency Resolution Process (Cumulative Cases)



Source: IBBI

Outcome of CIRP Initiated Stakeholder-wise, as on December 31, 2023

		CIRPs initiated by				
Outcome	**Description**	**FCs**	**OCs**	**CDs**	**FiSPs**	**Total**
Status of CIRPs	Closure by **Appeal/Review/Settled**	336	779	9	0	1124
	Closure by **Withdrawal** u/s 12A	292	735	8	0	1035
	Closure by Approval of **Resolution Plan**	511	308	69	3	891
	Closure by Commencement of **Liquidation**	1095	1036	245	0	2376
	Ongoing	1066	728	104	1	1899
	Total	**3300**	**3586**	**435**	**4**	**7325**
Resolution	**Realisation by Creditors** as % of Liquidation Value	177.6	129.5	149	160	169
	Realisation by Creditors as % of their Claims	33.8	18.7	17.9	42.4	31.9
	Average Time Taken for Closure of CIRP	677	686	569	632	671
Liquidation	Liquidation Value as % of Claims	5.7	9.3	8.5	-	6.5
	Average Time Taken for Closure of CIRP	496	492	414	-	486

Source: IBBI

Resolution of Claims Amounting to INR 10.07 Lakh Crores

As of December 31, 2023, there had been a total of 891 CIRP cases that were ended with the approval of the resolution plan. In these cases, creditors successfully realized INR 3.21 Lakh Crores against their combined claim of INR 10.07 Lakh Crores. Creditors' collective realizations were 68.64% higher than the liquidation values determined by the valuers. The cumulative collecting efficiencies from concluded resolution cases stood at 31.86%, therefore creditors saw only 31.86 cents returned for every dollar they had claimed. Notably, around 39% of these corporate debtors were either under BIFR or had become defunct. In such instances, the debtors managed to realize as much as 21.81% of their admitted claims and 156.24% of liquidation value.

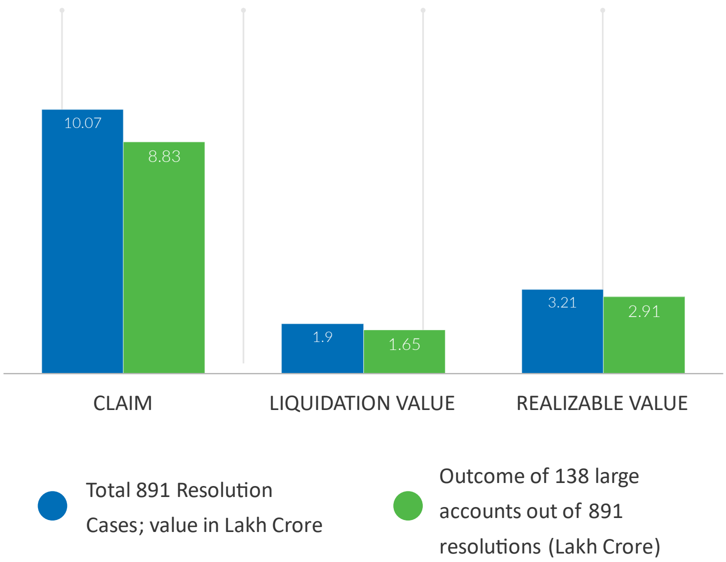
Closure by Liquidation Dominates

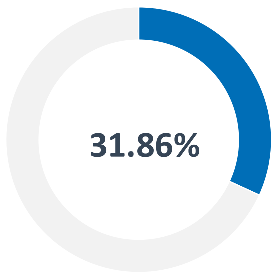
From all closed cases, it is seen that liquidation dominates over resolution, where 43.79% cases resulted in initiation of liquidation as against 16.45% cases concluded with the approval of resolution plan.

In the majority of instances involving liquidation, the Committee of Creditors (CoC) opted for liquidating the corporate debtor instead of approving a resolution plan. Many of these corporate debtors were so fundamentally weak that they did not receive any resolution plan from applicants. Approximately 77% of the liquidation cases involved corporate debtors that were either into BIFR and/or defunct, and the economic value of those businesses had been completely eroded before admission into CIRP. On average, the assets of these companies were valued at only 7.00% of the outstanding debt amount.

As of December 31, 2023, a total 2376 CIRPs resulted in the initiation of liquidation process. Final reports have been submitted in 830 cases, while 1546 companies are still undergoing liquidation. Out of the INR 1,06,469.40 Crore total admitted claim, INR 3,840.11 Core from the 830 closed liquidation cases were distributed to stakeholders, representing a recovery of only 3.61%. Notably, 43 of these cases were closed by sale as going concern, with cumulative claims of INR 43,955.31 Crore and realization amount of INR 1,964.27 Crore.

891 CIRPs Ended with Approval of Resolution Plans

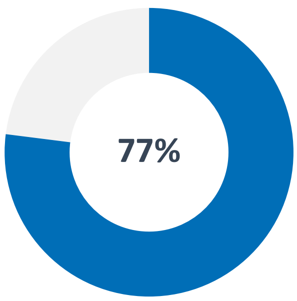




Realization by Creditor as % of their Claims

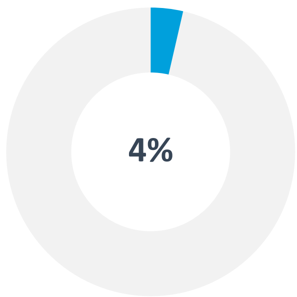
The cumulative collecting efficiencies from concluded resolution cases stood at 31.86%.

Cases of Liquidations



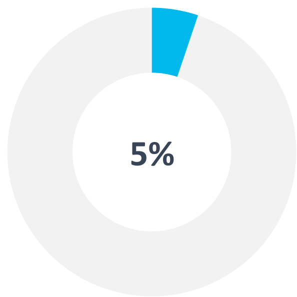
Liquidation- BIFR/Defunct

Approx. 77% of CIRPs resulted liquidation were earlier with BIFR and/or defunct



Liquidation- Recovery

INR 3,840.11 Crore were distributed from 830 closed cases against claim of INR 1,06,469.40 Crore, approx. 4% recovery



Sale as Going Concern under Liquidation

43 CDs out of 830 closed liquidation cases were closed by sale as going concern, approx. 5% of the total.

Source: IBBI

A Delay in the Process

Among the 1899 ongoing CIRPs, about 68% of cases have been continuing for over 270 days. According to regulations, CIRP is required to be completed within 330 days from the insolvency commencement date. Data provided by IBBI reveals that, on average, the closure of CIRP that ended with the approval of the resolution plan took approximately 858 days (including excluded time). Similarly, for liquidation, the average duration is around 661 days (including excluded time).

In summary, since its introduction, the Code has resolved claims amounting to INR 22.13 Lakh Crore, and in many cases, the recovery rate has fallen short of creditors' expectations. However, the overall recovery rate is relatively low due to several reasons. Many corporate debtors undergoing CIRP were either under BIFR or had minimal assets to monetize before the process. The recovery rate has gradually decreased over the years. A worrisome concern is the delay in completing the process, often exceeding the time stipulated by the Code.

02

Innovative & Hybrid Mechanisms of Restructuring (Mediation, Pre-Insolvency, Schemes and Pre – Packs): Comparative Analysis and Way Forward

The Insolvency and Bankruptcy Code, 2016 (**"Code/ IBC"**), is the primary legislation governing insolvency and restructuring in India. However, there are various other laws as well to govern the process of insolvency and restructuring in India such as –

i. Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (SARFAESI);
ii. Companies Act, 2013.

SARFAESI was introduced for banks or financial institutions in India or those notified by the government of India to recover non-performing assets without court intervention. Companies Act, 2013 deals with voluntary schemes of arrangement and compromise between debtors and their creditors. All of these laws provide various mechanisms of restructuring. Some of them are described hereinbelow:

A. **Mediation -** Mediation is the use of a neutral third party to facilitate the negotiated settlement of a dispute and resolve conflicts between two or more parties.

Typically, mediation is initiated by mutual consent of the parties, or by a pre-agreed contractual clause, or by reference of the court or tribunal, or by a mandatory requirement under the law. Mediation as an alternate dispute resolution (ADR) process is well known for improving the efficiency of dispute resolution and offering flexibility to the parties. It offers an opportunity to parties to reach mutually agreeable commercial solutions to business disputes without intervention of courts. Even though there have been instances of mediation of insolvency matters, the Code does not specifically provide for mediation.

B. **Schemes** - A debtor may reorganise under the Companies Act, 2013 by formulating a scheme of arrangement or compromise. The scheme can be:

- Between the debtor and any class of creditors; or
- Between the debtor and any class of shareholders.

A scheme may include a compromise or arrangement with creditors as well as shareholders. It provides a mechanism for companies to enter into arrangements such as mergers, amalgamations, demergers, acquisitions, or reorganizations.

C. **Pre-packs** - Pre-packaged insolvency process is an alternate and speedier resolution mechanism for micro, small or medium enterprises in financial distress. In pre-pack, various procedural requirements as applicable to Corporate Insolvency Resolution Process (CIRP) has much stricter timelines than CIRP to ensure quicker resolution. Further, it envisages a hybrid process, where pre-initiation phase is largely informal and post-initiation stage is formal. Pre-packaged insolvency process has the features, which make a CIRP sacrosanct, and has the rigour and discipline of the CIRP. It is informal up to a point and formal thereafter. It blends debtor-in-possession with creditor-in-control.

Comparative Analysis

All the above-mentioned modes of restructuring are detailed herein below:

A. **Mediation** as an alternative resolution practice will certainly be an aid to the existing IBC and reduce the burden on tribunals as well. As a matter of fact, one view is that even though there is no specific provision for mediation in IBC, the same is still not alien to the enactment and Rule 11 of the NCLT Rules, 2016 gives inherent powers to the tribunals (Adjudicatory Authority) to refer the matter to mediation.

In one of the matters namely V.K. Parvinder Singh v. Intec Capital Ltd. & Anr., (NCLAT No. 968 of 2019), the promoters were ready to settle the claims of Financial Creditors by appointment of Mediator by the Appellate Tribunal. The National Company Law Appellate Tribunal (NCLAT) allowed the mediation by consent of parties and settlement terms were entered which were placed before the Tribunal. NCLAT relied on Swiss Ribbons Pvt. Ltd. & Anr. v. Union of India & Ors., (Writ Petition (Civil) No. 99 of 2018) and in exercise of power conferred under Rule 11 of NCLAT Rules, 2016, set aside the CIRP.

Mediation can significantly reduce the rigid process as compared to litigation and result in a swift and satisfactory resolution among the parties which will also reduce the burden on the tribunals as well. Mediation allows both parties to work together with the help of a neutral third party to reach a mutually agreeable solution. This can save time, and money, and preserve the relationship between the parties.

Advantages of Mediation under the Code

✓ **Time and Cost Efficiency:** Mediation offers a quicker and more cost-effective alternative to traditional litigation. While the IBC sets a time limit of 180 days (extendable up to 270 days and with an outer limit of 330 days) for completing the CIRP, the actual resolution process often takes longer due to various factors such as delays in court proceedings, appeals, and settlement negotiations. Mediation can help parties resolve disputes more efficiently by engaging in facilitated discussions (with a timeline), thereby reducing the time and costs associated with lengthy court battles and the insolvency resolution process.

- ✓ **Flexibility and Party Autonomy:** Unlike litigation, mediation allows parties to tailor the dispute resolution process to suit their needs and preferences, subject to the contours of law. Parties can choose the mediator, the applicable rules, and the process for conducting the mediation, ensuring a more customized and effective resolution mechanism. This flexibility and party autonomy are particularly valuable in insolvency and bankruptcy matters, where parties often have unique interests and concerns that require tailored solutions.

- ✓ **Preservation of Business Relationships:** Mediation is a collaborative dispute resolution process that encourages open communication and mutual problem-solving, thereby fostering a more amicable resolution of disputes. This is particularly important in insolvency and bankruptcy matters, where preserving business relationships can be critical to the successful restructuring or resolution of the debtor company.

- ✓ **Confidentiality:** Mediation proceedings are typically confidential, ensuring that sensitive financial and business information is not disclosed to the public or competitors. This is especially important in insolvency matters, where the public disclosure of details of a company's financial difficulties may adversely impact its reputation and business operations. Confidentiality in mediation can help preserve the CD's value and protect the interests of the stakeholders involved.

Challenges/ Issues of Mediation under the Code

Within the interplay of the Mediation Bill and IBC, potential conflicts surface as a central concern. Notably, discrepancies may arise in terms of the enforceability of mediated settlements and the delineation of mediation's scope. The Mediation Bill, being a comprehensive legislative framework, seeks to govern a wide array of disputes encompassing civil matters, including contracts, familial conflicts, and more. In contrast, the IBC operates within the specific and specialised domain of corporate insolvency, focusing on the resolution of complex financial intricacies. These conflicts, often underpinned by jurisdictional challenges, pose questions about the hierarchy of these two legal frameworks when dealing with disputes that encompass elements of both legislations.
Furthermore, the distinct roles and responsibilities ascribed to Mediators in the Mediation Bill and Resolution Professionals in the IBC may create overlaps or contradictions, necessitating careful navigation to ensure a harmonious application of both. There is also the question of hierarchy and participation of various creditors in the mediation process.

B. **Scheme** - A debtor may reorganize under the Companies Act, 2013 by formulating a scheme of arrangement or compromise. The scheme can be either between the debtor and any class of creditors; or between the debtor and any class of shareholders.

A scheme may include a compromise or arrangement with creditors as well as shareholders. The scheme also requires NCLT approval, which is obtained by submitting an application in the prescribed format, together with the scheme and prescribed documents. Furthermore, the NCLT may order the convening of meetings of creditors or classes of creditors, or shareholders or classes of shareholders.

Government authorities and regulators can also make representations to the NCLT about the scheme. If a majority of persons representing three-quarters of the creditors or shareholders approve the scheme at the NCLT-convened meetings, a petition will be filed with the NCLT, which may then be sanctioned by an order.
From the debtor's perspective, the **advantages of restructuring proceedings/ Scheme** under the Companies Act include the following:

- ✓ This is a voluntary mechanism in which the debtor proposes the scheme.
- ✓ There are no predefined disqualifications; nor is there a competitive bidding process (which may result in a takeover of the debtor by a third party).
- ✓ The law governing schemes is well established, so there is little regulatory uncertainty.
- ✓ Once a scheme is approved, it is binding on all creditors (whose debts are being restructured).

The **disadvantages of scheme** are as follows:

- ✓ the lack of a moratorium;
- ✓ the relatively high approval threshold;
- ✓ the absence of a time-bound process; and
- ✓ the inability to achieve a cross-class cramdown.

Unlike Insolvency and Bankruptcy Code, 2016, in the scheme of Compromise and Arrangement under the Companies Act, 2013, the debtor suggests the plan and submits applications to the NCLT for its approval, together with any appropriate reports, statements and other documentation. The debtor is in charge of managing the entire procedure for getting the scheme approved, including notifying creditors.

C. Pre-Packs – Micro, small, and medium enterprises (MSMEs) are critical for India's economy. They contribute significantly to gross domestic product and provide employment to a sizeable population. The COVID-19 pandemic has impacted their business operations and exposed many of them to financial stress. Resolution of their stress requires different treatment, due to the unique nature of their businesses and simpler corporate structures. Therefore, it was considered expedient to provide an efficient alternative insolvency resolution process under the Code for corporate MSMEs, that ensures quicker, cost-effective and value maximising outcomes for all the stakeholders, in a manner which is least disruptive to the continuity of their businesses, and which preserves jobs.

Accordingly, President promulgated the Insolvency and Bankruptcy Code (Amendment) Ordinance, 2021 on 4th April, 2021 to introduce PPIRP under the Code for this purpose. PPIRP is built on trust and honours the honest MSME owners by enabling resolution when the company remains with them.

Advantages of Pre-Pack over Corporate Insolvency Resolution Process (CIRP)

- ✓ **Speedier resolution** process compared to CIRP as various time-consuming steps are eliminated;
- ✓ It facilitates swift and smoother resolutions, avoiding unnecessary adversarial litigations and is therefore, more **cost efficient** than CIRP;
- ✓ Under pre-pack, debtors and creditors can develop a resolution plan in collaboration before initiation of the process which results an inclusive process which **balances the interest of all stakeholders**;
- ✓ Easier to maintain the **going concern status** of the corporate debtor as it is essentially a debtor-in-possession model. This ensures that there are minimal disruptions to the debtor's business operations.
- ✓ It is one of the best forums for banks for recovery and vigilance as it involves seeking Court approval for a Resolution Plan.

Challenges/ Issues of Pre-Pack

- ✓ Banks, Financial Creditors and stakeholders in general are not well informed about the pre-pack process;
- ✓ Confusion in banks – whether the pre-pack insolvency process shall be handled by the Credit Department or the Recovery Department;
- ✓ One of the major challenges is the hesitancy on the part of the financial creditors (FCs) in approving the proposals under this mechanism, wherein the haircut is perceived as voluntary;
- ✓ Preference of CIRP over pre-pack by bankers as CIRP is more competitive.

Way Forward

The IBC transfers full control of the Corporate Debtors to the creditors during the CIRP period, through the resolution professional. The rationale for the same is to prevent any erosion of value during the process of resolution. Given the loss of saddle, it is seen that the promoters of the debtors in many cases resort to various litigatory tactics. While there could be bonafide reasons in some cases, other kinds of intent are also visible in the market. To minimize this friction, there has been an institutional attempt towards adopting the prepack schemes which is essentially a debtor-in-possession model. Globally, pre-packs have evolved organically without statutory interventions, because in those countries, the insolvency regimes had stabilized. In such predictable scenarios, the judiciary's role is rather limited because the Courts generally approve the resolution plans after verifying compliance with the laid down tenets.

In the Indian context, to start with, the Pre-Packaged Insolvency Resolution Process (PPIRP) has been rolled out for the MSMEs.

The response towards its adoption, however, seems to be relatively muted. One reason could be the hesitancy on the part of the financial creditors (FCs) in approving the proposals under this mechanism, wherein the haircut is perceived as voluntary. It may be stressed here that PPIRP will incentivise the promoters to constructively engage with the creditors, possibly even before occurrence of any default event. This would facilitate swift and smoother resolutions, avoiding unnecessary adversarial litigations. Overall, this could be a win-win situation for both creditors and debtors. Once this perception is established, there could be a greater acceptance of this mechanism for larger corporate debtors as well, as and when the statutory enablers are in place. Thus, in their own interest, the creditors and debtors may consider adopting PPIRP in applicable scenarios based on prudentially realistic cost-benefit evaluations.

Further, as per the Expert Committee's Report on framework for use of mediation under IBC, in the Indian insolvency regime, unlike many other jurisdictions, there is an overbearing need to balance the efficiency of the system with the public interest involved in distressed assets. This is especially true as most financial stakes are from public sector banks, who are the key creditors seeking to rescue corporate debtors. Mediation can provide a cost-effective way for quick resolution of disputes and make it more likely that parties voluntarily comply with agreements resulting from mediation. Further, this renewed paradigm of dispute resolution will shift the focus from NCLT to the private actors in the process (namely debtors, creditors, and all parties interested). This, in turn, will save precious time for the NCLT to focus on business rescue. In addition, an appointed mediator would play a key role in ensuring the proper functioning of negotiations and the efficient handling of procedures for the benefit of creditors as well as other stakeholders. Thus, it is essential that space for regulatory sandbox to operate mediation may be created through IBBI's formulation of regulations in line with the enabling provision under the Code.

It is expected that mediation will also reflect positively in effective litigation management through cost and delay reduction as well as cash flow management. It would augment procedural, operational and cultural changes in how India resolves insolvency. This is more so intended because, in essence, mediation places heavy reliance on 'human element' of the parties. It appeals to the common object of 'dispute resolution' (i.e., ending conflict and avoiding litigation) with the expectation of balancing all interests during the proceedings. Since mediation is 'party-driven' and outcomes are largely 'self-determined', the cultural mindset shift to explore the maximum possibility of resolution is the key. For instance, it is well recognized that enactment and implementation of IBC over the years has led to mindset change amongst debtors and improvement in debtor-creditor relationship.

The insolvency mediation framework must hence, rather than only being seen as a dispute resolution mechanism, expectedly become a way of introducing debtors and creditors to a new 'rescue culture', where they have the opportunity to 'amicably resolve' issues at the outset or once the insolvency process commences, at various stages within the timelines of IBC as the insolvency process runs parallelly.

In India, particularly in Delhi and Bengaluru, Civil Courts have been encouraging the use of mediation to divert appropriate cases for full, final and satisfactory resolution of all sorts of commercial disputes. While the prime motivator for judges was to decongest the dockets, many judges have themselves undergone mediation training and are now avid supporters of mediation even in complex matters. As mediation was paving its way in India to resolve the socio-economic and civil disputes, it was evident that insolvency and bankruptcy cases should also follow suite and explore the possibility of incorporating and employing mediation in insolvency proceedings. it is, in fact, protective of its well-being.

Authors suggest that it is advisable to identify the right kind of disputes to be referred to mediation. Disputes that involve debt restructuring (between FC and CD), employee claims, supplier-vendor disputes (between OC and CD), contract disputes or even preference actions are all fit cases where mediation can effectively help parties find mutually acceptable solutions to avoid insolvency or bankruptcy. However, cases that involve an element of fraud, extortionate credit transactions, regulatory compliance and payment of tax or has hostile and non-cooperating parties are disputes that are not ideal for mediation. In such cases, mediation should not be made compulsory.

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03

Pre-Packaged Insolvency Resolution Process – an Innovation within the IBC

The Corporate Insolvency Resolution Process (CIRP) under The Insolvency and Bankruptcy Code, 2016 (IBC, the Code) has been evolving since its launch in December 2016. One notable innovation within the Code has been the Pre-Packaged Insolvency Resolution Process (PPIRP), a hybrid mechanism poised to simplify proceedings and expedite the recovery process in a cost-effective manner.

Amid the Covid 19 pandemic, the business environment became unfavorable, leading to many corporates, particularly the MSMEs, face the financial challenges and become distressed. Given their unique nature, a distinct approach to debt resolution was necessary for these struggling MSMEs. Recognizing this need, the Insolvency Law Committee, a body operating under the Ministry of Corporate Affairs (MCA), under the Chairmanship of Dr. M.S. Sahoo recommended the genesis of the PPIRP to the Government.

Subsequently, the Government promulgated the Insolvency and Bankruptcy Code (Amendment) Ordinance, 2021 on April 04, 2021, incorporating PPIRP into the Code.

A Hybrid Model of Resolving Corporate Insolvency

The resolution process under PPIRP is informal during the initial phrase, after which it becomes formal. During the pre-initiation phrase, both the corporate debtors and the creditors have the flexibility to explore different options and negotiate to resolve the stresses. In addition to negotiation, the corporate debtor is entitled to prepare a base Resolution Plan, which serves as reference point. Any improved versions of Resolution Plan are sought from resolution applicants during the time of PPIRP process. Furthermore, prior to admission, a range of activities occur, including the identification of insolvency professionals (IPs), the passing of multiple board resolutions, updating of claims, and preparation of a preliminary information memorandum.

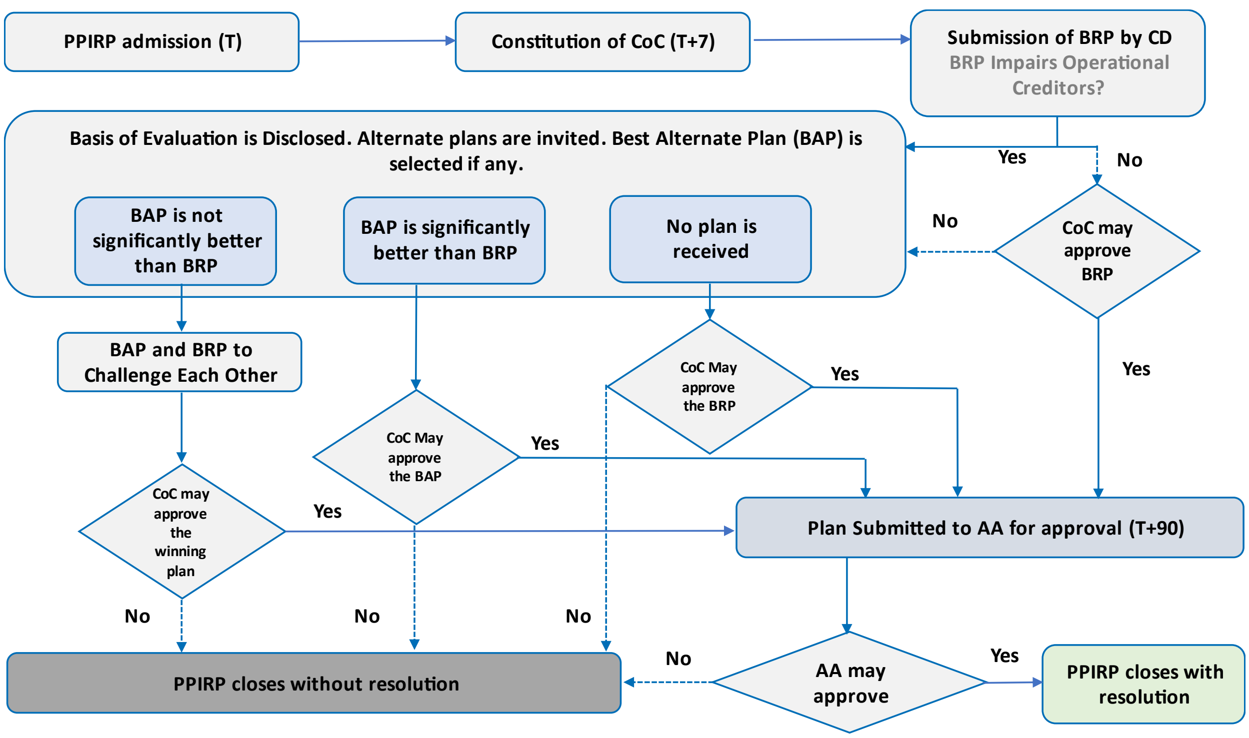
These pre-admission procedures are conducted to streamline the process and expedite proceedings.

Simplicity and Efficiency at the Core

Every feature of PPIRP has been designed with simplicity and efficiency at its core principles. Targeted towards financially stressed MSMEs, the PPIRP addresses the limitations of the complex CIRP, which may not be suitable for timely and cost-effective resolution for such entities. Unlike CIRP, PPIRP is targeted to complete within 120 days timeline from the date of admission into the process. The average time taken for a CIRP is over 600 days[1]. Many procedural practices under CIRP are either abolished or integrated into others to streamline the process under PPIRP.

In the PPIRP, the existing management continues to operate the business, in contrast to the CIRP where the RP assumes control. As a result, the involvement of the resolution professional (RP) is limited in the PPIRP. During the pre-initiation phase, the insolvency professional (IP) primarily acts as advisors, assisting in the application filing with the Adjudicating Authority. Following the initiation of the resolution process, the IP takes on the role of the RP with reduced involvement.
The judiciary involvement in PPIRP is comparatively limited, resulting in lower administrative expenses compared to CIRP. Furthermore, the PPIRP covers a wider range of MSMSs, as the threshold default limit for admitting into the process is only INR 10 Lakhs, compared to INR 1 Crore default limit set for admission into the CIRP.

A Typical Process Flow of a PPIRP[2]



[1] IBBI August 2023; (Source: Economic Times)
[2] Source: Pre-Packaged Insolvency Resolution Process, Information Brochure, IBBR

A blend of debtor-in-possession with creditor-in-control

Unlike the Corporate Insolvency Resolution Process (CIRP), the Code grants some additional control to corporate debtor under the Pre-Packaged Insolvency Resolution Process (PPIRP). Here, only the corporate debtor can initiate the resolution process. The corporate debtor (CD) is responsible for preparing the base resolution plan (BRP), and if it satisfies the financial creditors (FCs), then the BRP submitted by corporate debtor can be considered for resolution. In four out of five successful PPIRPs, the BRP submitted by corporate debtor is deemed final, allowing the corporate debtor to retain control of the company.

Throughout the resolution process, the existing management continues to operate the business, unlike in the case of CIRP where the resolution professional (RP) takes over. Despite this, the interests of creditors are well protected. Generally, any impairment of operational creditors (OCs) and workmen'/employees dues are not encouraged in this process. At every decisive stage of the resolution process, the voting of the creditors plays a crucial role.

No Opportunity for Misapplication

Given the corporate debtor's (CD) additional control in the resolution process under PPIRP, there exists a potential for the code to be misused for personal gain. The CD may artificially portray financial distress and enter PPIRP to obtain relief.

However, code is not without safeguards, and the final judgements are thoroughly reviewed by competent adjudicating authorities before being issued. It's worth noting that unlike in countries such as the USA, Indian regulations lack provisions to distinguish between fraudulent and honest defaulters[3].

Current Status

According to the information available from the Insolvency and Bankruptcy Board of India, a total 10 applications were filed for admission into PPIRP under part IIIA of IBC. Out of these, five cases were resolved with acceptance of resolution plan, two cases are currently admitted and pending, two cases were withdrawn either before or after admission and one case was dismissed. *We have summarized the five successful resolution cases and attempted to glean insights from them.*

[3] Pre-Packaged Insolvency in India: A progressive adaptation meeting the objective standards of a good insolvency regime. Aaradhya Mandloi

Parameters	GCCL Infra[4]	Enn Tee[5]	Amrit[6]
Date of Admission	14-Sep-21	10-Oct-22	28-Nov-22
Date of Resolution	05-Sep-23	19-Oct-23	03-May-22
Time taken for Resolution	721 Days	374 Days	156 Days
Time taken – Pre-admission	70 Days	124 Days	75 Days
Debt Outstanding (INR L)	Total: 111.24 Lakh FCs' Claim: 56.19 Lakh OCs' Claim: 55.05 Lakh	Total: 1,588.63 Lakh FCs' Claim: 1,196.00 Lakh OCs' Claim: 392.63 Lakh	Total: 38.33 Lakh FCs' Claim: 12.70 Lakh OCs' Claim: Nil Contingent Claim: 38.33 Lakh
Cause of Default	Pandemic Related Stress	Dumping of yarn from China hampered the business	Trust deficit between CD and FC; Defunct
Features of Base Resolution Plan (BRP)	▪ The CD agreed to cover FCs' and OCs' dues and PPRIP costs without impairment ▪ The submitted plan complied with Section 30(2) of the IBC ▪ All current employees are considered for employment	▪ The CD agreed to cover FCs' and OCs' dues and PPRIP costs without impairment ▪ The CD outlined the roadmap for funding the resolution, along with proper schedule of payment ▪ The submitted plan complied with Section 30(2) of the IBC	▪ The CD proposed a BRP with a 90% debt haircut for FCs and 100% impairment for contingent creditors ▪ Given this, CoC asked CD to enhance the BRP and to invite resolution plans from the public
PPIRP Cost / Remuneration of RP	INR 3.50 Lakh (Total PPIRP Cost)	INR 6.00 Lakh (Total PPIRP Cost)	Actual Amount
Best Alternate Plan (BAP)	NA	NA	Plan given by applicant Aquarius Fincap; which agreed to pay 39.37% due of FC and 8.58% contingent claims
Final Outcome	Ahmedabad Bench of NCLT approved the resolution plan submitted by the CD GCCL Infra;	Principal Bench of NCLT (New Delhi) approved the resolution plan submitted by the CD Enn Tee;	Principal Bench of NCLT (New Delhi) approved the resolution plan submitted by Aquarius Fincap;
Remarks	▪ The CD retained ownership in the Company ▪ The CD's BRP covered the interests of OCs, FC, and Employees. ▪ The plan provided 100% recovery for FC and OCs, coupled with a well-defined implementation roadmap. ▪ Although the BRP was submitted within 14 days, the process lasted 721 days	▪ The CD retained ownership in the Company ▪ The plan provided 100% recovery for FC and OCs. ▪ The process lasted for 374 days, although it was delayed by 51 days for procedural reason ▪ Total plan value exceeds total infusion due to contributions from the ECLGS scheme and annual renewal of cash credit limit on existing terms	▪ Aquarius Fincap; whose bid was significantly better than the CD, became the new owner of the company ▪ Although the offer of Aquarius is better than the CD, the haircut is quite high ▪ The process lasted for 156 days, this included three adjournments at the request of CD

[4] GCCL Infrastructure and Projects Limited
[5] ENN TEE International Limited
[6] Amrit India Limited

Parameters	Shree Rajasthan Syntex[7]	Sudal Industries[8]
Date of Admission	19-Apr-23	20-Apr-23
Date of Resolution	22-Aug-23	10-Aug-23
Time taken for Resolution	125 Days	112 Days
Time taken – Pre-admission	267 Days	228 Days
Debt Outstanding (INR L)	Total: 11,167.00 Lakh FCs' Claim: 10,008.00 Lakh OCs' Claim: 996.00 Lakh Others: 163 Lakh	Total: 15,647.18 Lakh FCs' Claim: 15,073.74 Lakh OCs' Claim: 573.44 Lakh
Cause of Default	Regulation of pet coke in Rajasthan	Not Available
Features of Base Resolution Plan (BRP)	▪ The CD agreed to cover 30.10% of FCs' due and 100% OCs' and workmen's due ▪ The CD outlined the roadmap for funding the resolution, along with proper schedule of payment ▪ Interest of 120 days towards period prior to NCLT approval shall be paid to Financial Creditors	▪ The BRP provided by the CD was not approved by FCs initially, and they sought for resolution application. However, did not receive any, and therefore considered the BRP by majority of 77.72% of CoC members. ▪ The resolution plan provided, sought for a hair-cut of 67% for secured FCs (1st charge), 73% (2nd charge) and a massive 99% haircut for unsecured FCs. ▪ OCs and workmen's dues are fully covered
PPIRP Cost / Remuneration of RP	Actual & INR 10,000/Month for RP	Actual & INR 10,000/Month for RP
Best Alternate Plan (BAP)	NA	NA
Final Outcome	Jaipur Bench of NCLT approved the resolution plan submitted by the CD Shree Rajasthan Syntex.	Mumbai Bench of NCLT approved the resolution plan submitted by the CD Sudal Industries.
Remarks	▪ The Company, listed publicly, had previously negotiated loan restructuring with banks despite losses ▪ Pre-admission into PPIRP was delayed by 367 days due to Bank of Baroda admitting the CD into CIRP under section 7 of IBC ▪ CD filed a PPIRP application, approved by over 66% of FCs ▪ FCs took a 70% haircut in resolution, while dues of OCs and workmen were fully covered	▪ The Company is a publicly listed entity. At the time of admitting to PPIRP, two applications for initiating CIRP were pending for the CD. However, Canara Bank, the single largest FCs (77.72% voting share), consented the CD to PPIRP ▪ The time taken for resolution is 112 days, due to complexities, the pre-admission period was as high as 228 days ▪ Although OCs and workmen's interest were protected, the FCs' recovery was very low at 26.45%

[7] Shree Rajasthan Syntex Limited
[8] Sudal Industries Limited

Salient Findings

- Out of five cases, three were completed within a reasonably shorter period, while in two cases, time required for resolution was unreasonably high. The duration of pre admission period varied from 70 days (GCCL Infra) to 267 days (Shree Rajasthan Syntax). Both Shree Rajasthan Syntex, and Sudal Industries were listed entities, and in both cases, the appeal for initiating CIRP was filed by FCs. However, in both cases, the CIRP was adjourned, upholding the decision to admit them into PPIRP.

- In case of Enn Tee International, it was noted that after admission into PPIRP, the matter should have been transferred to the Stressed Asset Wing of the concerned bank. However, it was initially routed through the branch, causing a delay before being transferred to the appropriate division. Furthermore, internal negotiations within the bank also contributed to the delay in this case.

- In case of GCCL Infra, it took 721 days to complete the resolution process from the date of admission. Throughout this period, there were multiple adjournments, many of which were caused by time constraints or absence of the regular bench[9].

- In the case of Shree Rajasthan Syntex, one of the three corporate debtors, Bank of Baroda filed it CIRP application, despite knowing that the corporate debtor (CD) was attempting to file a PPIRP application. Other two financial creditors (FCs) SBI and IDBI Bank, who together hold 73.91% voting share, approved the PPIRP scheme filed by the CD[10]. As per the Section 11A of the IBC, an application under Section 54C of the code is filed after 14 days of filing application under Section 7, 9, or 10, and in such cases, the application under section 7,9 or 10 shall be adjudicated first. However, in this case, the adjudicating authority found that the PPIRP filed by the CD was in the interest of all stakeholders, despite being filed after the 14-day period following the CIRP application. Therefore, it was considered as PPIRP application.

- In case of Sudal Industries, prior to the corporate debtor (CD) filing a PPIRP application, two applications had already been submitted to admit the CD into CIRP. Canara Bank, one of the financial creditors (FCs) seeking CIRP admission, had also consented to the CD's PPIRP application. However, another FC requested the Tribunal to consider the CIRP case as mandated under section 11A (4) of the code. Despite this request, the Tribunal dismissed both section 7 petitions, as Canara Bank, with a 77.72% voting interest, had consented.

[9] With input from the article "Lessons from Pre-Packaged Insolvency Cases in India: A Long Road Ahead", by Mr. M.P. Ram Mohan and Mr. Sriram Prasad
[10] With input form the article "Lessons from Pre-Packaged Insolvency Cases in India: A Long Road Ahead", by Mr. M.P. Ram Mohan and Mr. Sriram Prasad

- In four out of five cases, the CD emerged as successful resolution applicant, and in two cases, the FCs recovered the total dues along with full realization of OCs dues. In fact, in all five cases, OCs and workmen's/employees' due were settled without any impairment.

- The costs associated with PPIRP are minimal. In certain cases, the monthly remuneration of the Resolution Professional (RP) is as low as INR 10,000. Additionally, there is very little delay attributed to the actions of the NCLT throughout the entire resolution process.

Concluding Thought

The concept of pre-packaged insolvency process has been adopted in different jurisdictions in different name and forms. In India, PPIRP represents a novel approach of resolving stressed assets, particularly targeting MSMEs. PPIRP stands as a hybrid mechanism for addressing distressed companies. It involves a series of preparatory activities conducted before formal admission to expedite and streamline the resolution process, aiming for cost-effectiveness.

However, despite these limitations, the actual time taken, including the pre-admission phase, often results in a considerable duration for resolution, although it remains lower compared to the time required under the traditional Corporate Insolvency Resolution Process (CIRP).

In the PPIRP framework, the corporate debtor gains additional control during the proceedings, with a scope of retaining ownership rights. Nevertheless, creditors maintain a significant influence throughout, bolstered by the oversight of the adjudicating authority.
Despite such positives, the uptake of PPIRP has been limited, with only ten companies opting for this route since its inception in April 2021. Considering the relaxation of threshold limits for MSMEs, this figure is extremely low.
Understanding the dynamics further, the majority of the CIRPs are initiated by creditors (either FCs or OCs) accounting for 94.06% of cases, while corporate debtors initiate a mere 5.94% of CIRPs. This disparity arises from corporate debtors' reluctance to relinquish control under CIRP. In the context of PPIRP, only a corporate debtor has the authority to admit it's company for resolutions. However, during the resolution process, the CD has a fair chance to lose the control of its own company. Consequently, the number of admissions under PPIRP remains low.
Looking ahead, as experience grows, there will be opportunities to refine the process and incorporate new features. This could involve extending PPIRP beyond MSMEs to include companies of varying sizes, ultimately strengthening the procedure.

Further bottlenecks remain due to –
- ✓ Clarity to whether such exercise would be done by credit or recovery department of banks;
- ✓ Proper circular and training to executives for propagating PPIRP exercises.
- ✓ Effective monitoring of the filed applications.

04

Judicial Interpretation of Fairness and Equity Under the IBC

Some of the important case laws/ amendments related to IBBI that promote the concept of fairness and equity under IBC are listed hereinbelow:

1. **Entitlement of wages/salaries of the workmen/employees during the CIRP period and the amount due and payable to the respective workmen/employees towards Pension Fund, Gratuity Fund and Provident Fund.**

The Hon'ble Supreme Court in the matter of Sunil Kumar Jain and others V/s. Sundaresh Bhatt and others held that-if during the CIRP the corporate debtor was a going concern, the wages/salaries of such workmen/ employees who actually worked, shall be included in the CIRP costs and in case of liquidation of the corporate debtor, dues towards the wages and salaries of such workmen/employees who actually worked when the corporate debtor was a going concern during the CIRP, being a part of the CIRP costs are entitled to have the first priority and they have to be paid in full first as per Section 53(1)(a) of the IB Code.

The wages and salaries of all other workmen/employees of the Corporate Debtor during the CIRP who actually have not worked and/or performed their duties when the Corporate Debtor was a going concern, shall not be included automatically in the CIRP costs. However, the wages and salaries of the workmen/employees of pre-CIRP period will have to be governed as per the priorities mentioned in Section 53(1) of the IB Code.

Further, Section 36(4)(iii) of the IB Code specifically excludes "all sums due to any workman or employee from the provident fund, the pension fund and the gratuity fund", from the ambit of "liquidation estate assets". Considering Section 36(4) of the IB code and when the provident fund, gratuity fund and pension fund are kept out of the liquidation estate assets, the share of the workmen dues shall be kept outside the liquidation process and the concerned workmen/employees shall have to be paid the same out of such provident fund, gratuity fund and pension fund, if any, available and the Liquidator shall not have any claim over such funds.
Reference: Judgment of Hon'ble Supreme Court dated 19.04.2022 in CIVIL APPEAL NO. 5910 OF 2019– In the matter of Sunil Kumar Jain and others V/s. Sundaresh Bhatt and others

2. **Rights of a Secured Creditor who do not fall under the category of Financial Creditors or Operational Creditors as per the IBC**

In this matter, the Corporate Debtor had created a first ranking exclusive security by way of pledge in favour of Vistra ITCL (India) Ltd. over the equity shares held by it in the capital of JMT Auto Ltd. and a Security Trustee Agreement was executed between the parties. Vistra ITCL (India) Ltd. had filed its claim as a secured creditor of the Corporate Debtor on the basis of the pledged shares, which was rejected by the Resolution Professional. The Resolution Plan was already approved by the Hon'ble NCLAT and the Hon'ble Supreme Court.

The Hon'ble Court observed that the person in whose favour the security interest is created need not be the creditor who avails the credit facility, and can be a third person. Security interest can be created for credit facilities/loan advanced to another person. It is accepted and admitted that Vistra has security interest in the pledged shares.

The Hon'ble Court provided a two-fold solution in this matter. First is to treat the secured creditor as a financial creditor of the Corporate Debtor to the extent of the estimated value of the pledged share on the date of commencement of the CIRP. This would make it a member of the CoC and give it voting rights, equivalent to the estimated value of the pledged shares. However, in the present case, the said solution may not be viable as the resolution plan has already been approved by the CoC without Vistra being a member of the CoC.

Therefore, we would opt for the second option. The second option is to treat the Vistra as a secured creditor in terms of Section 52 read with Section 53 of the Code. In other words, we give the option to the successful resolution applicant to treat Vistra as a secured creditor, who will be entitled to retain the security interest in the pledged shares, and in terms thereof, would be entitled to retain the security proceeds on the sale of the said pledged shares under Section 52 of the Code read with Rule 21A of the Liquidation Process Regulations. The second recourse available, would be almost equivalent in monetary terms for Vistra, who is treated as a secured creditor and is held entitled to all rights and obligations as applicable to a secured creditor under Section 52 and 53 of the Code.

Reference: Judgment of Hon'ble Supreme Court dated 04.05.2023 in CIVIL APPEAL NO. 3606 of 2020 – In the matter of M/s Vistra ITCL (India) Ltd & Ors. V/s. Mr. Dinkar Venkatasubramanian & Anr.

3. **Treatment of the Government Dues under IBC**

Rainbow Papers Judgment is a very well-known and one of the most remarkable judgments pronounced under IBC. In this matter, it was contented that the Government cannot claim first charge over the property of the Corporate Debtor, as Section 48 of the Gujarat Value Added Tax, 2003, hereinafter referred to as the "GVAT Act", which provides for first charge on the property of a dealer in respect of any amount payable by the dealer on account of tax, interest, penalty etc. under the said GVAT Act, cannot prevail over Section 53 of the IBC.

The short question raised by the appellant in this appeal was, whether the provisions of the IBC and, in particular, Section 53 thereof, overrides Section 48 of the GVAT Act?

The Hon'ble Court observed that if the Resolution Plan ignores the statutory demands payable to any State Government or a legal authority, altogether, the Adjudicating Authority is bound to reject the Resolution Plan. They further expressed their views, that the Committee of Creditors, which might include financial institutions and other financial creditors, cannot secure their own dues at the cost of statutory dues owed to any Government or Governmental Authority or for that matter, any other dues.

In the Hon'ble Court's view, the NCLAT clearly erred in its observation that Section 53 of the IBC over-rides Section 48 of the GVAT Act.

Section 48 of the GVAT Act is not contrary to or inconsistent with Section 53 or any other provisions of the IBC. Under Section 53(1)(b)(ii), the debts owed to a secured creditor, which would include the State under the GVAT Act, are to rank equally with other specified debts including debts on account of workman's dues for a period of 24 months preceding the liquidation commencement date.

As observed, the State is a secured creditor under the GVAT Act. Section 3(30) of the IBC defines secured creditor to mean a creditor in favour of whom security interest is credited.

Such security interest could be created by operation of law. The definition of secured creditor in the IBC does not exclude any Government or Governmental Authority.

Reference: Hon'ble Supreme Court Judgment dated 06.09.2022 in Civil Appeal No. 1661 of 2020 in the matter of State Tax Officer V/s. Rainbow Papers Limited

Note: Various review petitions were filed against the abovementioned judgment but they were dismissed. However, the said judgment cannot be relied upon for every case and the treatment of Government dues shall be on the basis of the particular State Government / Central Government acts/ laws as applicable.

4. **Amendment in IBBI (Liquidation Process) Regulations, 2016, dated 12.02.2024 brings a huge relief to Homebuyers**

The Insolvency and Bankruptcy Board of India has vide its Notification No. IBBI/2023-24/GN/REG112 dated 12.02.2024, issued various amendments to the Insolvency and Bankruptcy Board of India (Liquidation Process) Regulations, 2016. One of the latest amendments has been issued in favour of Homebuyers which is stated herein below:

"wherever the corporate debtor has given possession to an allottee in a real estate project, such asset shall not form a part of the liquidation estate of the corporate debtor."

[11]This latest amendment comes as a relief to homebuyers who had been given possession of their homes but were left in a lurch after the builder's company was declared insolvent. As per this amendment, the properties where the allottee has taken possession should be excluded from the liquidation estate.

[11] Source: Hindustan Times

This means that a house already allotted/given possession to a buyer will remain with him even if the builder faces liquidation. Prior to this amendment, the buyer who had received possession of the property was left with no remedy except being entitled to a refund in case of liquidation.

To iron out this anomaly, the IBBI has come up with this amendment that will ensure that such flats (for which possession has already been offered, but no conveyance deed has been executed or registered) are kept out of the liquidation estate.

Experts said that this amendment provides certainty to buyers that completed projects will not form part of liquidation. It takes care of buyers who have already received possession of their units.
These amendments are important as thousands of homebuyers have in the past been stuck in a long-drawn and complicated legal battle after the builder went bankrupt. The amendment is likely to benefit homebuyers who have been allotted the units/flats and are in possession of the same. Their interest shall not be impacted (even if possession is without registration with the registrar) and their units will not be made the part of the liquidation estate even if the corporate debtor/builder/developer goes into liquidation, says experts. The regulation is in the nature of beneficial legislation and therefore it will have retrospective effect which means that the corporate debtor for which liquidation process is still on/ not completed as yet, the liquidator will have to re-draw the liquidation estate and exclude those flats that are in possession of the allottees, ensuring that the homebuyers cannot be asked to give up their flats.

In the current real estate scenario, it has become commonplace for builders to give possession to the allottees without actually executing the conveyance for the same. In this twilight period, if the builder goes into insolvency, such allottees are in a precarious position as the asset does not belong to them. In the event of the company going into liquidation, a homebuyer is left with no remedy and is at best entitled to a refund.

This issue has already been highlighted by various NCLAT judgments as the value of these assets might not be much to the secured creditors but to an allottee it means his/her entire life savings. Hence, all attempts must be made to protect the interest of the homebuyers and also see that stuck projects are completed.

5. **The provisions of the IBC are not meant to defeat slum redevelopment and similar or allied statutes – Protection of interests of individual citizens for whom that welfare statutes are intended.**

Facts of the case – This Writ Petition was filed seeking an order of the Hon'ble High Court at the instance of the Resolution Professional (RP) staying an acquisition process under the Slum Rehabilitation Act, 1995. The developer, Truly Creative Developers Pvt Ltd ("Truly Creative") bought the plot under question in March, 1997 sought to implement a slum redevelopment proposal. However, Truly Creative failed to implement this scheme. Between 2006 and 2018 there was no progress in the implementation of the slum rehabilitation scheme. Many slum dwellers were deprived of transit rent. The Slum Rehabilitation Authority (SRA) initiated proceedings under Section 13(2) of the Slum Act.

However, Truly Creative was given an opportunity and were allowed to continue to implement this scheme. The society being aggrieved filed an application before the Apex Grievance Redressal Committee (“AGRC”). That application succeeded and Truly Creative’s appointment was terminated. The society was permitted to appoint another developer. The eligible members of the society appointed another developer. Meanwhile, Truly Creative challenged the AGRC order of 25th October 2019 in Writ Petition (L) No 3512 of 2019. On 18th December 2019, a Single Judge of this Court declined any interim relief. Truly Creative did nothing. Ultimately, its Writ Petition was dismissed on 17th January 2024 for a failure to cure filing defects.

Truly Creative was not only a developer but also was an owner. Consequently, the society had to ensure that title to the property was validly acquired to continue with slum rehabilitation. Therefore, the society applied on 18th November 2021 to the SRA to initiate steps in acquisition and for a declaration of the slum plot as a slum rehabilitation area (a distinct concept) under the provisions of Section 3C of the Slum Act.

Shortly thereafter, SRA issued a Notification dated 23rd May 2022 saying that there was a policy decision to declare all slums on public and private lands and which existed prior to 1st January 2011 and which had been declared as slums under Section 4 of the Slum Act to be “deemed slum rehabilitation areas” under Section 3C. On 11th November 2022 that the National Company Law Tribunal (“NCLT”) admitted a proceeding under the Insolvency and Bankruptcy Code, 2016 (“IBC”) against Truly Creative for a Corporate Insolvency Resolution Process (“CIRP”).

The RP filed this Petition on 31st January 2024 only on the basis that the Section 14 moratorium declared by the NCLT meant that the acquisition could not proceed.

Issue in hand – Whether the provisions of the IBC and specifically the pendency of a CIRP meant to protect the assets of a potentially insolvent corporate debtor can ever prevail over the considerations of a welfare statute and the concerns of individual citizens for whom that welfare statute is intended, such as the Slum Act?

The Hon’ble High Court noted that until the entire gamut of the CIRP process is completed, and whatever be the final outcome, the society members must continue to suffer. They will not receive transit rent. They will not see any construction activity on site. The statutory promise of redeveloped premises will be denied to them and this will continue for an indefinite period of time. All this because the corporate debtor’s ‘asset’ must be ‘preserved’. At whose cost, we have to ask? And for what fault of the slum dwellers?

The Hon’ble Court held that the provisions of the IBC are not meant to defeat slum redevelopment and similar or allied statutes and a defaulting corporate debtor cannot use the golden parachute of the IBC to secure through the RP a restraint against the welfare of slum dwellers.

Reference: Hon’ble Bombay High Court Judgment dated 03.04.2024 in Writ Petition No. 1398 of 2024 in the matter of Rajan Garg, Resolution Professional of Truly Creative Developers Pvt. Ltd. V/s. Chief Executive Officer, Slum Rehabilitation Authority & Ors.

05

Discussing Opportunities for Enhancing Fairness and Equity Within the IBC Framework

The Insolvency and Bankruptcy Code, 2016 **(Code/IBC)** was introduced with one of its objectives being balancing the interest of stakeholders. The insolvency of a corporate impacts a diversity of interests, including but not limited to creditors, employees, customers and the community at large. Now, Section 53 of the Insolvency and Bankruptcy Code, 2016, describes the waterfall mechanism for distribution of assets on liquidation of a company. Once the insolvency resolution process costs and liquidation costs have been paid in full, the workmen's dues for a period of 24 months preceding the liquidation commencement date and the debts owed to a secured creditor who have relinquished their security, are ranked equally and is payable. Employees' dues (other than workmen) for 12 months preceding liquidation commencement date come next, following which financial debts owed to unsecured creditors become payable. In the fifth position are government dues (unless secured by operation of law) and dues to secured creditors, for any amount remaining unpaid after enforcement of security interest. Remaining debts and dues (which include unsecured operational debts) come in the sixth position, just before preference shareholders and equity shareholders, who take the last share.

Notably, the Code makes a two-fold distinction in relation to the distribution of liquidation assets, firstly, in relation to the nature of the debt, i.e., whether a debt is secured or unsecured and secondly, in relation to the nature of the stakeholder, i.e., whether the creditor is an operational creditor (OC) or a financial creditor (FC). For secured debt, the Code does not distinguish between whether such debt is due to an OC or a FC, and secured debt to both these types of creditors may be paid simultaneously. However, for unsecured debt, unsecured FCs are ranked higher in the fourth place over unsecured OCs who take sixth place in the hierarchy of the liquidation waterfall and are paid only after FCs and government dues have been paid. Recently, in the matter of Damodar Valley Corporation Vs. Dimension Steel and Alloys [Company Appeal (AT) (Insolvency) No. 62 of 2022], the Hon'ble NCLAT expressed concerns towards nil and almost negligible payment to operational creditors generally made under the resolution plans, to both the Central Government and the IBBI.

The Hon'ble NCLAT urged the Government and the Board to find out whether there are any grounds for considering a change in the legislative scheme towards the payment to the Operational Creditors, which also consist of Government dues and other statutory dues.

However, there is a notable transparency under IBC: The formation of the Committee of Creditors, comprising of all financial creditors, ensures that decisions are made collectively, thereby minimizing undue influences and biases. Every major decision, including the selection of resolution plans, requires a specified majority of the CoC, ensuring that no single creditor can unduly influence the outcome. This ensures collective decision making and promotes transparency. The Code also introduced section 29A to keep away errant promoters from gaining access to the Corporate Debtor (CD) by making them ineligible to submit resolution plans in the insolvency process. The Board also comes out with periodic updates through quarterly newsletters, annual reports, etc. by which stakeholders are able to gauge the efficacy of the process and its outcomes.

Further, there is the idea of enhancing stakeholder engagement wherein regular consultations with stakeholders, from financial institutions to corporate entities, can provide valuable feedback, ensuring that the IBC remains responsive to their needs. Another important amendment that can enhance fairness and equity under IBC is implementation of Code of Conduct for Committee of Creditors (CoC). The creditor-in- control regime under the IBC has entrusted the CoC with a challenging task of giving a new life to the distressed CD.

However, the AA on several occasions, highlighted deficiencies in the decision-making process of the CoC. The AA has observed instances where representatives of creditors participated in meetings without the necessary authorization to make decisions, marking undue delays even in routine matters. This raise concerns not only about the competence of the representatives but also about the effectiveness of the CoC from the perspective of financial institutions.

Presently, the conduct and decision making of the CoC is not subject to any regulations, instructions, guidelines etc. Many stakeholders have expressed the need of a Code of Conduct for the CoC. The 32nd Report of the Parliamentary Standing Committee on finance had also recommended the same stating that, 'there is an urgent need to have a professional code of conduct for the CoC, which will define and circumscribe their decisions, as these have larger implications for the efficacy of the Code'.

In view of the vital role of the CoC and duties entrusted upon it, the IBBI came out with a discussion paper in August, 2021 wherein a Code of Conduct was proposed to be brought in for the members of CoC (yet to be implemented), that shall elevate accountability and responsibility of CoC. It has been argued that as the primary decision-making body for the resolution process, the CoC acts as the custodian of public trust, ensuring that the interests of all stakeholders, including creditors, shareholders, and employees, are protected and preserved. In performing its role, the CoC must balance the competing interests of various stakeholders and act in the best interests of the public at large. The proposed Code of Conduct draws from the ethical norms on which a CoC is expected to function and act as the guiding light for the CoC while conducting itself.

However, the Hon'ble Delhi High Court in the matter of Kunwer Sachdev Vs. IDBI Bank and Ors. (Judgment pronounced on 12.02.2024) has directed IBBI to frame/finalise a code of conduct/guidelines in accordance with its stand set out in this case, principles mentioned therein and as per other relevant considerations, within a reasonable period of time, preferably, within three months from the date of the passing of this judgment, for the effective functioning of the CoC, without diluting the sanctity of the "commercial wisdom" of the CoC and the legislative intent of the IBC.

Insolvency resolution of CDs in real estate sector is a different ball game than of other CDs and need a different or modified version of IBC. Allottees or applicants of a real estate project are now treated as financial creditors (FCs). However, their position and interests are different than other FCs such as lenders in nature, rights, and quantum, with their life savings and aspirations at stake, though amount involved may be small unlike FCs. Their interest lies in possession of house and not in recovering of amount deposited with the developer. Another issue is whether or not, and, if yes, under what circumstances one or more projects by the same developer should be considered for stress resolution in a particular project. To protect the interests of allottees, several judicial interventions have been made such as 'reverse CIRP' and 'project-specific resolution'. However, for want of clarity and regulatory provisions on the subject, many CIRPs of real-estate cases are languishing in courts. It is, therefore, necessary that IBC should provide for a specialised framework for real estate projects. Further, there have been various judicial pronouncements under IBC that deals with promoting the concept of fairness and equity by balancing the interest of all stakeholders.

Furthermore, there has been recent amendment in IBBI (Liquidation Process) Regulations, 2016, which brings a huge relief to Homebuyers wherein if the corporate debtor has given possession to an allottee in a real estate project, such asset shall not form a part of the liquidation estate of the corporate debtor.

Further, the Insolvency and Bankruptcy Board of India (IBBI) had issued a Notice on 18.01.2023 inviting public comments on changes being considered to the Insolvency and Bankruptcy Code, 2016 which proposes to bring the following amendments to IBC for promoting fairness and equity:

- ✓ The concept of waterfall mechanism in CIRP to provide an equitable scheme of distribution of proceeds received pursuant to a resolution plan(s).

- ✓ For improving recoveries for operational creditors in liquidation, it is being considered that all unsecured creditors (FCs, OCs and any government or authority) other than the workmen and employees shall be treated equally for distribution under section 53.

The said proposed changes are yet to be notified/ implemented. However, if the same is implemented, it will provide a fair treatment to other classes of stakeholders as well. Further, it is anticipated that with time IBC will be reformed further to promote the concept of equity and to fulfil one of its objectives i.e., balancing the interest of stakeholders.

Sources –

1. *IBBI – Expert Committee Report on Framework for Use of Mediation under the Insolvency and Bankruptcy Code, 2016 (January 2024)*
2. *IBC Evolution, Learnings and Innovation 2023.*

06

Identifying Challenges Faced by Stakeholders, Including Creditors, Debtors, Resolution Professionals and Regulatory Authorities

Some of the major challenges being faced by various classes of stakeholders under IBC, 2016 are as listed hereinbelow:

- ✓ **Low Repayment Percentage and Haircuts in recovery rate:** It has been observed that the Resolution Plan approval process typically involves about 15% payment by the Resolution applicants. In some cases, the haircuts rates have even gone up to 95% and the creditors do not recover much under IBC. Further, according to the financial stability report (FSR) issued by the Reserve Bank of India in 2023, the Repayment can take years without any further interest collected by the Banks.

- ✓ **Initial surge in cases:** One of the immediate challenges post the IBC's introduction was the sudden influx of cases. This was a testament to the pent-up demand for a streamlined insolvency process.

  The National Company Law Tribunal (NCLT) and subsequently, the National Company Law Appellate Tribunal (NCLAT), found themselves at the forefront of this surge, tasked with handling a volume of cases that was unprecedented. This sudden increase underscored the need for robust infrastructure, efficient processes, and a well-trained cadre of professionals to manage and adjudicate these cases effectively.

- ✓ **The challenge of infrastructure and process enhancements:** The existing infrastructure, both physical and technological, was initially overwhelmed by the sheer volume of cases.

- ✓ **The challenge of complexity of cases:** The multifaceted nature of many insolvency cases posed another challenge. Cases involving intricate financial structures, cross-border elements, or large conglomerates demanded a nuanced understanding of not just domestic laws but also international insolvency practices and conventions.

The NCLAT, in its role as an appellate authority, often found itself navigating these complexities, ensuring that judgments were both legally sound and economically prudent.

- ✓ **The challenge of training and skill development:** The IBC's introduction also highlighted the need for continuous training and skill development. Resolution professionals, legal practitioners, and even the judiciary needed to familiarize themselves with the intricacies of the new code. Workshops, seminars, and training programs became essential to ensure that all stakeholders were well-equipped to handle IBC-related proceedings.

- ✓ **The challenge of evolution and adaptation:** Over the years, as the IBC's implementation progressed, it became evident that the Code itself, while robust, would need periodic revisions to address emerging challenges and to plug any gaps. The Hon'ble Supreme Court, High Court and NCLAT played a crucial role in highlighting areas of the IBC that required clarity or amendment, ensuring that the Code remained dynamic and responsive to the evolving landscape.

- ✓ **Limited Judicial Bench Strength:** The IBC resolution process is impeded by a shortage of judges, resulting in a deceleration of case processing. This, in turn, contributes to prolonged resolution times, delay in the entire process and reduction in the realization of value to the stakeholders.

- ✓ **Limited Benches of NCLAT:** Currently NCLAT is operating out of New Delhi and Chennai only. With few benches – plethora of cases are piling up and cases hearing being deferred due to paucity of time. It's time now to consider additional benches in West and East as well.

Sources:

1. *Keynote Address for the 7th Annual Day of the Insolvency and Bankruptcy Board of India*
2. *Keynote Address by Shri Shaktikanta Das, Governor, Reserve Bank of India at a Conference on Resolution of Stressed Assets and Insolvency and Bankruptcy Code (IBC) organised by the Centre for Advanced Financial Learning (CAFRAL), Mumbai, January 11, 2024*

07

Future Directions: Towards a More Equitable Insolvency Regime

While approving a resolution plan under section 31 of the Code, the Adjudicating Authority (AA) must confirm whether the Committee of Creditors (CoC) approved the resolution plan with the requisite majority and whether the mandatory requirements under section 30(2) of the Insolvency and Bankruptcy Code, 2016 (IBC) are fulfilled. If these requirements are not fulfilled, the AA is required to reject the resolution plan. Section 30(2) provides for two types of requirements: the manner of distribution and the minimum entitlement for the Operational Creditors (OCs) and dissenting Financial Creditors (FCs), and other implementation-related requirements. It is observed that several objections regarding the distribution of proceeds are raised when the resolution plan is pending approval before the AA. Since this requirement is a pre-condition for a plan's approval, the process cannot move forward, or the successful resolution applicant ("**SRA**") cannot take over the Corporate Debtor's (CD) management unless these disputes are settled. As a result, a substantial amount of time is wasted in these proceedings, which results in value deterioration.

The time lag often makes the negotiation between the CoC and the SRAs infructuous. Various issues have been raised in CIRP and liquidation matters with regards to unequitable approach towards distribution of realisations to various classes of stakeholders and no law in place to promote equality and fairness in distribution. In this regard, the Insolvency and Bankruptcy Board of India (IBBI) had issued a Notice on 18.01.2023 inviting public comments on changes being considered to the Insolvency and Bankruptcy Code, 2016. Some of the important changes being considered to promote equality and fairness are listed hereinbelow:

1. **Waterfall Mechanism in CIRP**
   It is felt that during the Corporate Insolvency Resolution Process (CIRP), many disputes have raised in relation to the distribution of proceeds, and there are concerns regarding inequitable distributions amongst the creditors. To alleviate these concerns, an objective formula may be devised to distribute proceeds during the CIRP, which shall be fair and equitable towards all creditors.

Therefore, it is proposed that the Code may be amended to statutorily provide an equitable scheme of distribution of proceeds received pursuant to a resolution plan(s) through a separate waterfall mechanism in the CIRP. As per this scheme, creditors will receive proceeds up to the CD's liquidation value for their claims in the order of priority provided in section 53. Any surplus over such liquidation value will be rateably distributed between all creditors in the ratio of their unsatisfied claims. Finally, any remaining amount or further surplus would be distributed to the shareholders and partners of the corporate debtor, as the case may be. It is expected that this will make the distribution process fairer and more equitable for all the stakeholders.

2. **Improving recoveries for operational creditors in liquidation**

There have been several judicial opinions in favour of granting equitable distribution to OCs under the processes of the Code. The recoveries made by OCs under liquidation are seemingly inadequate, even compared to unsecured FCs. Thus, to improve their position in the priorities for distribution under a plan or in liquidation, **it is being considered that all unsecured creditors (FCs, OCs and any government or authority) other than the workmen and employees shall be treated equally for distribution under section 53**. The order of priority for the secured creditors, workmen and employees shall be retained as stipulated under section 53.

3. **Clarity in the treatment of security interests created by statutes**

Section 3 (30) defines a 'secured creditor' as a creditor in favour of whom security interest is created. In *State Tax Officer v. Rainbow Papers Limited* (Civil Appeal No. 1661 of 2020), the Supreme Court interpreted the definition of 'secured creditor' to hold that any government or governmental authority shall be a secured creditor as the charge created by a statutory law can be considered as a 'security interest'. The definition of 'security interest' under the Code means that a right, title or interest or a claim to property, created in favour of, or provided for a secured creditor by a transaction, which secures payment of performance of an obligation. It is intended to be restricted to 'transactions', which means that the security interest should be created pursuant to an agreement on the part of the asset holder while giving rights to the other party. Further, 'transaction', as defined under section 3 (33), includes an agreement or arrangement in writing to transfer assets, funds, goods, or services from or to the CD. **Thus, it is clear that the concept of security interest was intended to cover a consensual transaction between parties (and not any similar interest created through mere operation of a statute).** Thus, it is being considered that all debts owed to Central Government and the State Government, irrespective of whether they are secured creditors pursuant to a security interest created by a mere operation of statute, shall be treated equally with other unsecured creditors. Further, it will be clarified that only where the security interest is created pursuant to a transaction of the Central Government or a State Government with CD, the Government in question will continue to be treated as a secured creditor in the order of priority.

However, the above proposed changes have a very mixed reaction from the industry experts. India's banks and bondholders stand to recover less in insolvency resolutions under the proposed changes in law that would apportion more to junior creditors, such as unpaid vendors and the government, according to restructuring and insolvency professionals. Further, as per the insolvency professionals, secured creditors, who are generally paid out before those with unsecured claims, may be less amenable to the IBC if the above-mentioned proposed changes are ultimately put into effect. Secured creditors, typically banks and bondholders, would continue to have first claim on proceeds of an insolvency resolution plan, but only up to the liquidation value of the corporate debtor. Any recovery beyond liquidation value would be shared ratably among all creditors, including unsecured financial creditors, unpaid vendors and statutory dues owed to government, according to the discussion paper.

The proposed changes may promote fairness in treatment of various classes of stakeholders but is believed to be unfair treatment of secured creditors. Overall recoveries under the IBC — which has already been mired in delays and litigation — have been roughly one-third of claims or less. Under those circumstances, the government's proposal may turn off lenders, ranging from Indian banks to international private credit funds, even more. Currently, other classes of stakeholders such as operational creditors, government etc. barely recover anything under the waterfall mechanism as they are placed quite below in the order of priority. Secured Creditors in spite of being placed at higher order suffer huge haircut in their recoveries which goes up to 95% in certain cases. Therefore, a more balanced approach needs to be adopted to ensure equitable treatment of all stakeholders under IBC without any stakeholder suffering major losses and to maintain the faith of all the stakeholders on IBC.

However, since its introduction in 2016, IBC has evolved to a great extent to promote equitable treatment of other classes of stakeholders. For an instance, the Hon'ble Supreme Court in the matter of Sunil Kumar Jain and others V/s. Sundaresh Bhatt and others held that if during the CIRP, the corporate debtor was a going concern, the wages/salaries of such workmen/employees who actually worked, shall be included in the CIRP costs and in case of liquidation of the corporate debtor, dues towards the wages and salaries of such workmen/employees who actually worked when the corporate debtor was a going concern during the CIRP, being a part of the CIRP costs are entitled to have the first priority and they have to be paid in full first as per Section 53(1)(a) of the IB Code. The wages and salaries of all other workmen/employees of the Corporate Debtor during the CIRP who actually have not worked and/or performed their duties when the Corporate Debtor was a going concern, shall not be included automatically in the CIRP costs. Only with respect to those workmen/employees who actually worked during CIRP when the Corporate Debtor was a going concern, their wages/salaries are to be included in the CIRP costs and they shall have the first priority over all other dues as per Section 53(1)(a) of the IB Code.

However, the wages and salaries of the workmen/employees of pre-CIRP period will have to be governed as per the priorities mentioned in Section 53(1) of the IB Code. Further, Section 36(4)(iii) of the IB Code specifically excludes "all sums due to any workman or employee from the provident fund, the pension fund and the gratuity fund", from the ambit of "liquidation estate assets". Considering Section 36(4) of the IB code and when the provident fund, gratuity fund and pension fund are kept out of the liquidation estate assets, the share of the workmen dues shall be kept outside the liquidation process and the concerned workmen/employees shall have to be paid the same out of such provident fund, gratuity fund and pension fund, if any, available and the Liquidator shall not have any claim over such funds.

Further, in the matter of Sikander Singh Jamuwal V/s. Vinay Talwar & Ors., the Hon'ble NCLAT, New Delhi observed that Resolution Applicant is also liable to pay the contribution and other sums due from the employer under any provisions of this act as the case may be in respect of the period up to the date of such transfer. All this requires that the explicit provisions of the above said PF Act needs to be complied with. This aspect is justiciable as a duty has been casted on the Resolution Professional/Adjudicating Authority/ on this Tribunal. This is not a commercial wisdom as compliance of law is a must. Further, PF dues are not the assets of the CD as amply made clear by the provisions of Section 36(4)(a)(iii) of the I& B Code, 2016. Therefore, the Hon'ble Tribunal directed the Successful Resolution Applicant to release full provident fund dues in terms of the provisions of the Employees Provident Funds and Miscellaneous Provident Fund Act, 1952.

There have been various other judgments on the same issue wherein it has been ruled out that Provident Fund dues have to be released and they are to be treated on priority basis under a Resolution Plan.

The IBC has also brought forth a paradigm shift in debtors' behaviour. Knowing that there is a robust mechanism in place prompts business owners to better manage their finances and avoid insolvency proceedings. This is evident from the fact that 26,518 applications for initiation of CIRPs having total underlying default of INR 9.33 lakh crore which were withdrawn before admission, till August 2023. Thus, IBC has brought about credit discipline amongst businesses and there is a positive behavioural change amongst promoters. The credible 'threat of insolvency' ignited by the Code has strengthened the negotiating powers of the creditors, in the absence of which it is most likely that those defaults would have lingered for much longer, resulting in value destruction. It has to be stated here that the IBC should not be seen as merely a loan recovery instrument; it has to be seen as an instrument which facilitates preservation of economic value of assets through effective resolution or unlocking of capital which is stuck in unviable businesses.

Further, as per the data made available by IBBI, as on 31.12.2023, out of 3,586 CIRP cases initiated by Operational Creditors, 779 cases were closed by Appeal/Review/Settlement and 735 cases were closed by withdrawal u/s 12A and 308 cases were closed by approval of Resolution Plan. This implies that the Operational Creditors has recovered some amount or their dues were settled to some extent after filing of application for initiation of CIRP. The 'threat of insolvency' had worked in favour of operational creditors in certain cases.

Further, as per the extracts from the **Keynote Address for the 7th Annual Day of the Insolvency and Bankruptcy Board of India**, the following are some of the anticipated future challenges and the evolving landscape that need consideration:

- ✓ **Global economic uncertainties:** The global economy is increasingly interconnected. Events like trade wars, pandemics, or financial crises in one part of the world can have ripple effects in India. The IBC will need to be agile to address challenges arising from such global uncertainties, ensuring timely and effective resolution of insolvencies.

- ✓ **Technological disruptions:** Rapid technological advancements can render certain industries or business models obsolete. The IBC will need to cater to insolvencies arising from such disruptions, ensuring that resources are reallocated efficiently.

- ✓ **Cross-border insolvencies:** With Indian businesses expanding globally, cross-border insolvencies will become more common. The IBC will need to align with international frameworks and conventions, ensuring seamless coordination between jurisdictions.

Moreover, some other important issues/ challenges of IBC were addressed by **Shri Shaktikanta Das, Governor, Reserve Bank of India** at a conference**.** Some of them are listed hereinbelow:

- ***Reaffirming the financial creditor's role***
  Through the course of last seven years of implementation of the Code, the jurisprudence on the role of the Committee of Creditors (CoC) has evolved. The CoC has a fiduciary responsibility to safeguard the interests of all stakeholders.
  The success of the Code is linked to an active involvement of the CoC in driving the resolution process forward. On several occasions, however, the Adjudicating Authorities (AA) have raised concerns regarding the conduct of the CoC in the insolvency proceedings. This includes lack of participation in the CoC meetings; lack of engagement or effective coordination among creditors; disproportionate prioritization of individual interest of creditors rather than their collective interest while designing the resolution plans which can be detrimental to the resolution plan itself, etc.
  Given these shortcomings on the part of CoC, there appears to be a trend in recent years towards balancing the rights of Operational Creditors (OCs) with those of Financial Creditors (FCs) under the Code. While the focus on ensuring equity among all stakeholders may be appreciated, there needs to be some distinction in weightage attributed to different category of creditors, depending upon the degree of risk absorbed ab initio. It has to be recognized that the financial creditors take the maximum risk and hence their risk needs to be commensurately compensated and with priority. Accordingly, any amendments to the Code and its evolution thereof may continue to lay emphasis on a financial creditor-led resolution framework, in an overarching manner.

The Insolvency and Bankruptcy Board of India had proposed for setting up a Code of Conduct for the Committee of Creditors. However, the same is yet to be implemented.

- ***Envisaging a Group Insolvency Mechanism***
  While the insolvency mechanism has been graduating towards a zone of stability through various concerted measures, one visible impediment seems to be the absence of a clear framework for group insolvency.

Globally, there are two diverse facets of Group Insolvency. Some jurisdictions have adopted either procedural coordination or substantive consolidation. Substantive consolidation pertains to the consolidation of assets, liabilities, and operations of multiple entities within a group, disregarding their separate legal entity status. On the other hand, under procedural coordination, the approach is limited to aligning procedural aspects like filing requirements, timelines, coordination, etc., and not mingling the entities per se.

In the Indian context, in the absence of a specified framework, the group insolvency mechanism has been so far evolving under the guidance of the Courts. Perhaps the time has come for laying down appropriate principles in this regard through legislative changes. There has been quite a bit of brainstorming on this issue in the policy circles for some time now. The task now is to move forward through appropriate legal changes.

While a legal framework cannot envisage all plausible real world scenarios, given the complicated group structures at the ground level including cross border linkages, it may be in the fitness of things to formally conceive a framework to start with. There would be challenges in this journey like intermingling of assets, devising a definition of 'Group', addressing cross-border aspects, etc. It would still be preferable to see the opportunity here and put in place a workable framework for group insolvency.

Large conglomerates often have intricate corporate structures with multiple entities. Addressing group insolvencies, where multiple entities of a group are undergoing insolvency, will be a challenge.

The IBC needs a clear framework to address group insolvencies, ensuring that insolvency proceedings for conglomerates with multiple entities are handled holistically.

Further, the Insolvency and Bankruptcy Board of India has vide its Notification No. IBBI/2023-24/GN/REG112 dated 12.02.2024, issued various amendments to the Insolvency and Bankruptcy Board of India (Liquidation Process) Regulations, 2016. One of the latest amendments has been issued in favour of Homebuyers which is stated herein below:

"Wherever the corporate debtor has given possession to an allottee in a real estate project, such asset shall not form a part of the liquidation estate of the corporate debtor."

This latest amendment comes as a relief to homebuyers who had been given possession of their homes but were left in a lurch after the builder's company was declared insolvent. As per this amendment, the properties where the allottee has taken possession should be excluded from the liquidation estate. This means that a house already allotted/given possession to a buyer will remain with him even if the builder faces liquidation. Prior to this amendment, the buyer who had received possession of the property was left with no remedy except being entitled to a refund in case of liquidation.

To iron out this anomaly, the IBBI has come up with this amendment that will ensure that such flats (for which possession has already been offered, but no conveyance deed has been executed or registered) are kept out of the liquidation estate.

Experts said that this amendment provides certainty to buyers that completed projects will not form part of liquidation. It takes care of buyers who have already received possession of their units.

These amendments are important as thousands of homebuyers have in the past been stuck in a long-drawn and complicated legal battle after the builder went bankrupt.

The amendment is likely to benefit homebuyers who have been allotted the units/flats and are in possession of the same. Their interest shall not be impacted (even if possession is without registration with the registrar) and their units will not be made the part of the liquidation estate even if the corporate debtor/builder/developer goes into liquidation, says experts. The regulation is in the nature of beneficial legislation and therefore it will have retrospective effect which means that the corporate debtor for which liquidation process is still on/ not completed as yet, the liquidator will have to re-draw the liquidation estate and exclude those flats that are in possession of the allottees, ensuring that the homebuyers cannot be asked to give up their flats.

In the current real estate scenario, it has become commonplace for builders to give possession to the allottees without actually executing the conveyance for the same. In this twilight period, if the builder goes into insolvency, such allottees are in a precarious position as the asset does not belong to them. In the event of the company going into liquidation, a homebuyer is left with no remedy and is at best entitled to a refund.

This issue has already been highlighted by various NCLAT judgments as the value of these assets might not be much to the secured creditors but to an allottee it means his/her entire life savings. Hence, all attempts must be made to protect the interest of the homebuyers and to see that stuck projects are completed.

Conclusion

Thus, it is apparent that IBC is perhaps one of the most critical legislations introduced in the preceding decade impacting the ‘ease of doing business in India’ in a positive manner and has proved to be an effective catalyst in accelerating the pace of the Indian economy. Going forward, IBC is destined to face a monumental challenge and equally monumental expectations in terms of consistent and speedier execution. Given the progress made by the IBC thus far, it is strongly expected that it will overcome all challenges and usher the Indian economy further on the path of fairness, stability and prosperity.

Sources:

1. *Hindustan Times*
2. *Keynote Address for the 7th Annual Day of the Insolvency and Bankruptcy Board of India*
3. *Keynote Address by Shri Shaktikanta Das, Governor, Reserve Bank of India at a Conference on Resolution of Stressed Assets and Insolvency and Bankruptcy Code (IBC) organised by the Centre for Advanced Financial Learning (CAFRAL), Mumbai, January 11, 2024*

08

Selected Judgements

1. **whether the Corporate Debtor not having an MSME status at the time of commencement of CIRP proceedings would disqualify the resolution applicant under section 29A of the Code as benefit of section 240A would not be available?**

In this matter, the Hon'ble Supreme Court observed that the Code is clear that default of INR one lakh or above triggers the right of a financial creditor or an operational creditor to file for insolvency. Thus, the financial creditor or operational creditors of MSMEs may take it to insolvency under the Code. However, given that MSMEs are the bedrock of the Indian economy, and the intent is not to push them into liquidation and affect the livelihood of employees and workers of MSMEs, the Insolvency Law Committee sought it fit to explicitly grant exemptions to corporate debtors which are MSMEs by permitting a promoter who is not a wilful defaulter, to bid for the MSME in insolvency. The rationale for this relaxation is that a business of an MSME attracts interest primarily from a promoter of an MSME and may not be of interest to other resolution applicants.
The Hon'ble Court held that for submission of a Resolution Plan by the promoter of a corporate debtor, the cut-off date for obtaining the MSME status for availing the exemption under Section 240A shall be date of submission of resolution plan and not the date of commencement of CIRP proceedings i.e., the promoter can obtain MSME certificate after commencement of CIRP but before submission of resolution plan to be eligible to become a Resolution Applicant.

Reference: *Hon'ble Supreme Court Judgment dated 29.11.2023 in Civil Appeal No. 4422/2023 in the matter of Hari Babu Thota*

2. **Whether NCLT has jurisdiction to direct the ED to release the attached properties, invoking section 32A of the IBC, 2016, since section 32A provides that all attachments over properties of a corporate debtor would cease once a resolution plan in respect of the said corporate debtor is approved?**

The issue raised in this matter was in regard to the implications of Section 32A of the Insolvency and Bankruptcy Code, 2016 ("IBC, 2016") for corporate debtors and their assets, upon approval of resolutions, and indeed for enforcement agencies that have attached assets of such corporate debtors. Section 32A of the IBC, 2016 provides for immunity to corporate debtors and their assets, upon approval of a resolution plan, subject to certain conditions stipulated in that provision.

The Hon'ble Court upheld the decision of the Hon'ble NCLT and observed that the Hon'ble NCLT was well within its jurisdiction in declaring that the corporate debtor would stand discharged from the offences alleged to have been committed prior to the CIRP and that the Attached Properties as identified in the Approval Order became free of attachment from the time of approval of the resolution plan eligible for benefit of Section 32A. On facts, it is evident that the NCLT was accurate in the valid exercise of its explicit jurisdiction;

As a consequence of Section 32A of the IBC, 2016, the Hon'ble Court directed the ED to necessarily release the attachment on the Attached Properties.

Reference: *Hon'ble Bombay High Court Judgment dated 01.03.2024 in the matter of Shiv Charan & Ors. V/s. Adjudicating Authority under the PMLA, 2002 & Ors.*

3. Whether financial debt can be proved on the basis of MoU and ledger extract filed by a claimant before the RP?

In this matter, Claim Form was filed by the Claimant/ Appellant along with Memorandum of Understanding ("MoU") and Ledger extracts attached therein. The Appellant submitted that on the basis of MoU and Ledger extract, which were annexed with the Claim Form, the RP ought to have admitted the claims. No further documents were submitted to substantiate the claims.
The Hon'ble NCLAT upheld the decision of the RP and the Hon'ble NCLT and observed that the RP has rightly communicated to the Appellant that documents submitted are insufficient to accept their claim as financial debt and no error has been committed. The Hon'ble Tribunal further stated that the MoU, which is a basic document evidencing the transaction does not qualify as a financial debt and the RP has rightly taken the view that the documents filed, i.e. MoU and Ledger statement are insufficient to accept the Claim as financial debt.

Reference: *Hon'ble NCLAT Judgment dated 03.01.2024 in the matter of D S Kulkarni & Associates V/s. Manoj Kumar Aggarwal*

4. Resolution Professional cannot file an appeal against the order of NCLT/NCLAT

In this matter, the Hon'ble Supreme Court held that the Resolution Professional cannot file an appeal against the order of NCLT/NCLAT as they are appointed by the Tribunals itself to assist in conducting the corporate insolvency resolution process and that they should maintain a neutral stand. It is for the aggrieved parties, such as Committee of Creditors to take appropriate proceedings or file an appeal before the Court/ Tribunal.
Reference: *Hon'ble Supreme Court order dated 25.09.2023 in the matter of Regen Powertech Private Limited V/s. Giriraj Enterprises & Anr.*

5. A claim if verifiable but submitted in a different form has to be considered and accorded due consideration in the category to which it belongs even if the form is not as per CIRP regulations

The Hon'ble Court observed that – "*The use of the words "a person claiming to be an operational creditor" in the opening part of Regulation 7, and the words "a person claiming to be a financial creditor" in Regulation 8, indicate that the category in which the claim is submitted is based on the own understanding of the claimant. Thus, there could be a situation where the claimant, in good faith, may place itself in a category to which it does not belong. However, what is important is, the claim so submitted must be with proof. As to what could form proof of the debt/ claim is delineated in sub regulation (2) of Regulations 7 and 8 of the CIRP Regulations, 2016.*"

It was further observed that even if any creditor submits its claim against the corporate debtor in a Form not as specified in the CIRP Regulations, 2016, the same has to be given due consideration by the IRP or the RP, as the case may be, if it is otherwise verifiable, either from the proof submitted by the creditor or from the records maintained by the corporate debtor.

Further, if a claim is submitted by an operational creditor claiming itself as a financial creditor, the claim would have to be accorded due consideration in the category to which it belongs, provided it is verifiable.

Reference: *Hon'ble Supreme Court order dated 12.02.2024 in the matter of Greater Noida Industrial Development Authority V/s. Prabhjit Singh Soni & Anr.*

6. The protection of the moratorium is only for the corporate debtor and is not available to the directors/officers of the corporate debtor

In this matter, the Hon'ble Court approved the view taken in the case of P. Mohanraj(supra) that notwithstanding moratorium, the liability, if any, of the directors/officers will continue even after declaration of moratorium. The Hon'ble Court further observed that only because there is a moratorium under Section 14 of the IBC against the corporate debtor, it cannot be said that no proceedings can be initiated against the directors for execution of any decree, provided that they are otherwise liable to abide by and comply with the order, which is passed against the corporate debtor. The protection of the moratorium will not be available to the directors/officers of the corporate debtor.

Reference: *Hon'ble Supreme Court Judgment dated 17.01.2024 in the matter of Ansal Crown Heights Flat Buyers Association V/s. M/s. Ansal Crown Infrabuild Pvt. Ltd. & Ors.*

7. The suspended board of directors/ officers of the corporate debtor cannot undertake any loan repayment and other bank transactions even if there is a stay on CIRP proceedings

In this matter, CIRP was commenced and thereafter stay order was pronounced by the Hon'ble NCLAT.

Later on, the stay order was vacated. The suspended board of directors during the intermittent period from stay order to vacation of stay order, made payments towards loan repayment to their Group Companies under the impression that the moratorium was not in existence during such period.

The Hon'ble Tribunal relied on the judgment of the Hon'ble NCLAT in Ashok Kumar Tyagi v. UCO Bank in which it was held that stay on CIRP process is not the same as the quashing of the CIRP order and hence the former situation does not make the Corporate Debtor in charge of the business in the manner as it was before the applicability of the order initiating CIRP which is passed by the Hon'ble NCLT. The Hon'ble Tribunal further clarified that after a stay order is given on the CIRP, the Resolution Professional cannot discharge any function. Further, stay of admission order/CIRP does not mean that the Corporate Debtor should be put back in the management of day-to-day affairs of the company and allowed to function as such. Interim Order putting a stay on CIRP clearly means that no further process shall be taken in CIRP and the Resolution Professional shall not take any further action. The Corporate Debtor can no longer be permitted to function as it was functioning prior to the date of admission order. Therefore, any loan repayment and other bank transactions undertaken by the Suspended Directors during such period are untenable as per law.

Reference: *Hon'ble NCLT, Mumbai Bench order dated 18.12.2023 in the matter of State Bank of India V/s. Arshiya Northern FTWZ Limited*

8. State tax officer vs. Rainbow Papers Ltd judgement is not applicable for all statutory dues- central excise cannot be treated as a secured creditor under IBC

The Assistant Commissioner of Central Tax filed an appeal against the Resolution Plan approval order passed by the Adjudicating Authority as only 0.13% has been earmarked towards Government Dues which was stated to be unfair and that the dues of Central Excise shall be treated as Secured Creditor as per the Judgment laid down by the Hon'ble Apex Court in the matter of State Tax Officer Vs. Rainbow Papers Ltd.

The Hon'ble NCLAT, Chennai Bench while disposing the said appeal observed that Section 11E of the Central Excise Act, 1944 is distinct from the provisions of GVAT Act, 2003. It is also pertinent to mention that the Master Circular No.1053/02/2017-CX, issued by the Ministry of Finance, Department of Revenue, Central Board of Excise and Customs specifies that dues under Central Excise Act, 1944 would have first charge only after the dues under the Provisions of the Code are recovered.

Keeping in view, the Section 11E of the Central Excise Act, 1944 is quite different from the GVAT Act, 2003 and Clause 20 of the afore noted Circulation, this Tribunal is of the considered view that the Appellant herein, cannot be treated as a Secured Creditor.

Reference: *Hon'ble NCLAT, Chennai Bench order dated 02.08.2023 in the matter of the Assistant Commissioner of Central Tax Vs. Mr. Sreenivasa Rao Ravinuthala RP Samyu Glass Pvt. Ltd.*

9. Date of default in case of guarantee

The Hon'ble Appellate Tribunal while dismissing the appeal observed that the Date of Default in case of invocation of Corporate Guarantee shall be from the date when the corporate guarantee has been invoked.

When the Financial Creditor has invoked the corporate guarantee of the corporate guarantor by the notice dated 16.10.2020 and asked the corporate guarantor to make the payment within seven days from the receipt of the notice, the default has occurred during the 10A period and the default dated 02.07.2019 which is default alleged against the Principal Borrower cannot be put to a default for corporate guarantor. Liability of corporate guarantor although is coextensive of the Principal Borrower but when the Guarantee requires invocation of the guarantee deed, default on the guarantor shall be the date when corporate guarantee has been invoked.

Reference: *Hon'ble NCLAT Principal Bench, New Delhi order dated 26.07.2023 in the matter of Mudhit Madanlal Gupta Vs. Supreme Constructions and Developers Pvt. Ltd.*

10. Advances given by property buyers to real estate developer shall be considered as financial debt and termed as Financial Creditor

The Appeal was filed to determine whether Mr. Vermuri Ravi Kumar (Homebuyer) is a Financial Creditor or not and secondly whether interest accrued can be added to the principal amount and claimed as Financial Debt. The Appellant submitted that Financial Creditor is not a genuine homebuyer but is a speculative investor as he sought to sell five plots out of the 10 plots to third parties for higher consideration and shall not be entitled to be termed as the Financial Creditor.

The Hon'ble Appellate Tribunal emphasised on the applicability of Section 5(8)(f) of the Code, advances given by Property buyers to real estate developer will be considered as a "borrowing" and such amounts raised from allottees falls within the scope of Section 5(8)(f) of the Code and observed as follows:
The Code is thus a beneficial legislation which can be triggered to put the corporate debtor back on its feet in the interest of unsecured creditors like allottees, who are vitally interested in the financial health of the corporate debtor, so that a replaced management may then carry out the real estate project as originally envisaged and deliver the flat/apartment as soon as possible and/or pay compensation in the event of late delivery, or non- delivery, or refund amounts advanced together with interest. Thus, applying the Shayara Bano v. Union of India (2017) 9 SCC 1 test, it cannot be said that a square peg has been forcibly fixed into a round hole so as to render Section 5(8)(f) manifestly arbitrary i.e. excessive, disproportionate or without adequate determining principle. For the same reason, it cannot be said that Article 19(1)(g) has been infracted and not saved by Article 19(6) as the Amendment Act is made in public interest, and it cannot be said to be an unreasonable restriction on the Petitioner's fundamental right under Article 19 (1) (g). Also, there is no infraction of Article 300-A as no person is deprived of its property without the authority of a constitutionally valid law.

Reference: *Hon'ble NCLAT, Chennai Bench order dated 04.09.2023 in the matter of Venkat Rao Marpina Vs. Vemuri Ravi Kumar*

11. An agent who has paid to principal supplier the outstanding amount due from Corporate Debtor is an Operational Creditor, an application u/s 7 is not maintainable

The Appeal was filed by the Agent being a Del Credere Agent (*A Person or company that acts as a salesperson and guarantor of credit for the buyer, while receiving commission for selling goods or services for another person or company and becomes liable to pay the principal if the buyer defaults on payment*) aggrieved by the Order of Hon'ble NCLT, Chennai Bench for dismissing the application u/s 7 on the grounds of non-maintainability and not falling under the purview of Financial Debt as per Section 5(8) of the IBC, 2016.
The Hon'ble Appellate Tribunal observed while dismissing the appeal that Going by the objective and scheme of the IBC, this Tribunal on the basis of surrounding facts and circumstances of the instant case in the teeth of Clause 15 of the `Del Credere Agency Agreement' and keeping in mind of a prime fact that the default which took place pertaining to the supply of goods comes within the definition of Operational Debt as per Section 5(21) of the Code, 2016 and hence, Section 9 of the Code, 2016 attracts in an unambiguous manner. Viewed in that perspective, the debt in the present case, cannot be termed as Financial Debt, as per Section 5 (8) of the Code, 2016, in the considered opinion of this Tribunal.

Reference: *Hon'ble NCLAT, Chennai Bench order dated 28.08.2023 in the matter of Madras Chemicals & Polymers Vs. Vijay Aqua Pipes Pvt. Ltd.*

12. If a wilful defaulter proceeding does not come within the wider purview of Section 14 of the IBC, Section 96 of the same cannot be a bar to such a proceeding

In Atibir Industries Company Limited & Ors. Vs. Indian Bank, the Hon'ble High Court stated that with respect to Section 96 of the IBC, it was clearly observed in Gouri Prasad Goenka (supra) that the moratorium envisaged in Section 14 of the IBC creates no hindrance to a wilful defaulter declaration proceeding, which, as held by the Supreme Court in several judgments, is "to disseminate credit information pertaining to wilful defaulters for cautioning banks and financial institutions so as to ensure that further bank finance is not made available to them" and not for recovery of debts or assets of the corporate debtor, which could hamper the corporate insolvency resolution process.

Thus, a wilful defaulter proceeding does not come within the contemplation of Section 14 or Section 96 of the IBC, which primarily pertains to legal actions to foreclose, recover or enforce security interest, or recovery of any property of the debt-in-question.

In P. Mohanraj (supra), the Supreme Court has repeatedly highlighted that the moratorium concerns not merely recovery of debt but any legal proceeding even indirectly relatable to recovery of any debt. Hence, the moratorium applies to recovery proceedings and proceedings which directly or indirectly "relatable" to such recovery. A wilful defaulter proceeding cannot, by any stretch of imagination, be said to be even remotely relatable to recovery of debt but is merely an off-shoot of the debt. The corpus of debt is not the subject-matter of a wilful defaulter proceeding, unlike a recovery proceeding, but is a mere stimulus to spur the wilful defaulter proceeding into motion.

Thus, the argument of the petitioners that the pendency of a proceeding under Section 95, IBC automatically entails a moratorium under Section 96 on a wilful defaulter proceeding is also not tenable in the eye of law.

Reference: *Hon'ble Calcutta High Court Judgment dated 20.03.2024 in the matter of Atibir Industries Company Limited & Ors. Vs. Indian Bank*

13. Clarity on the right to claim set-off in the Corporate Insolvency Resolution Process, when the resolution professional proceeds to take custody and control of all the assets of the Corporate Debtor

The Hon'ble Supreme Court observed that the expression 'mutual dealings' for the purpose of Regulation 29 of the Liquidation Regulations, is wider than the statutory set-off postulated under Order VIII Rule 6 of CPC, as well as, equitable set-off under the common law as applicable in India. Insolvency set-off applies when demands are between the same parties. There must be commonality of identity between the person who has made the claim and the person against whom the claim exists. Even when there are several distinct and independent transactions, mutuality can exist between the same parties functioning in the same right or capacity. Mutual dealings are not so much concerned with the nature of the claims, but with the relationship and apposite identity of the parties giving rise to the respective claims, such that it would offend one's sense of fairness or justice to allow one to be enforced without regard to the other.

Insolvency set-off as a proposition mitigates against the doctrine of pari passu. Insolvency set-off gives primacy and an overriding effect to the creditor who is entitled to set-off mutual credits. When cross demands are set-off, the assets available for distribution amongst the general body of creditors, would be depleted in favour of a single creditor with a set-off entitlement. This consequently results in reduction of the dividend payable. In other words, The principle of pari passu though not explicitly mentioned in the IBC, is apparent as the edifice of Section 53 read with Section 52 of the IBC, as these provisions create a liquidation hierarchy with the stipulation that each class of creditors shall rank equally among each other. The same class of creditors should be given equal treatment. As set-offs can mitigate against the pari passu principle, they should be allowed when mandated, or can be justified by law.

Given the aforesaid legal position, we do not think that the provisions of statutory set-off in terms of Order VIII Rule 6 of CPC or insolvency set-off as permitted by Regulation 29 of the Liquidation Regulations can be applied to the Corporate Insolvency Resolution Process.

The aforesaid rule would be, however, subject to two exceptions or situations –The first, if at all it can be called an exception, is where a party is entitled to contractual set-off, on the date which is effective before or on the date the Corporate Insolvency Resolution Process is put into motion or commences – The reason is simple – The Corporate Insolvency Resolution Process does not preclude application of contractual set-off – The second exception will be in the case of 'equitable set-off' when the claim and counter claim in the form of set-off are linked and connected on account of one or more transactions that can be treated as one – The set-off should be genuine and clearly established on facts and in law, so as to make it inequitable and unfair that the debtor be asked to pay money, without adjustment sought that is fully justified and legal – The amount to be adjusted should be a quantifiable and unquestionable monetary claim, as the Corporate Insolvency Resolution Process is a time-bound summary procedure.

Reference: *Hon'ble Supreme Court Judgment dated 03.01.2024 in the matter of Bharti Airtel Limited and Another v. Vijaykumar V. Iyer and Others*

14. Hon'ble Bombay High Court judgment dated 04.04.2024 in the matter of Amit Gupta v/s. IBBI & Ors.

The Insolvency and Bankruptcy Board of India issued a Circular on 28th September, 2023 to provide Clarification w.r.t. Liquidators' fee under clause (b) of sub-regulation (2) of Regulation 4 of IBBI (Liquidation Process) Regulations, 2016.

Regulation 4 of the IBBI (Liquidation Process) Regulations, 2016 ("**Liquidation Regulations"**) provides for Liquidator's fee. Sub-regulation (1) and (1A) provide that the fee payable to the liquidator be decided by the Committee of Creditors (CoC) or Stakeholders' Consultation Committee (SCC), as the case may be. If liquidators' fee is not fixed under sub-regulation (1) and (1A), clause (b) of sub-regulation (2) of Regulation 4 provides that the liquidator shall be entitled to a fee as a percentage of the amount realised net of other liquidation costs, and of the amount distributed, for the balance period of liquidation, as mentioned therein. The following clarifications were issued-

Amount realised: Regulation 4(2)(b) provides that the fee shall be "as a percentage of the amount realised net of other liquidation costs, and of the amount distributed, for the balance period of liquidation...."

Clarification: "Amount realised" shall mean amount realised from assets other than liquid assets such as cash and bank balance including term deposit, mutual fund, quoted share available on start of the process after exploring compromise and arrangement, if any.

Other liquidation costs:

Clarification: The "other liquidation cost" in regulation 4(2)(b) shall mean liquidation cost paid in priority under section 53(1)(a), after excluding the liquidator's fee.

Amount distributed to stakeholders:

Clarification: "Amount distributed to stakeholders" shall mean distributions made to the stakeholders, after deducting CIRP and liquidation cost.

Amount of Realisation /Distribution:
Clarification: "Amount of Realisation /Distribution" shall mean cumulative value of amount realised/ distributed which is to be bifurcated in various slabs as per column 1 and thereafter the same is to be bifurcated into realisation/ distribution in various periods of time and then corresponding fee rate from the table is to be taken.

Period for calculation of fee
It has been observed that the liquidators are suo-moto excluding various time periods such as stay by court on sale of a particular asset, delay in relinquishment by secured creditor, for the purpose of calculating the fee. However, since the liquidator works under the overall guidance of the Adjudicating Authority, any such exclusion should have stamp of judicial authority and should be only for the asset for which such exclusion has been granted.
Clarification: Exclusion for purpose of fee calculation is to be allowed only when the same has been explicitly provided by the Hon'ble NCLT/ NCLAT or any other court of law and will operate only for the asset which could not have been realised during the excluded period.

The Hon'ble High Court held that *Paragraph 2.1 and Paragraph 2.5 of the Impugned Circular are hereby struck down as being ultra vires the LP Regulations and the IBC. They introduce substantive amendments to statutory legislation even while purporting to be mere clarifications. The changes they seek to bring in are not even covered by the IBC and the LP Regulations. Due process by way of compliance with the statutory requirements of the Law Making Regulations is missing. Therefore, in the course of conducting the quasi-judicial proceedings, the IBBI is prohibited from placing any reliance on Paragraph 2.1 and Paragraph 2.5 of the Impugned Circular in determining if any fee charged by the Petitioner in the liquidation assignments in question, was in excess of permissible thresholds;*

Paragraph 2.2 is upheld in its terms since it does not stipulate any new standard and rightly clarifies the legal position under Section 5(16) of the IBC read with Regulation 2(1)(ea) of the LP Regulations in discerning the meaning of the term "liquidation cost". The definitional content of Regulation 2(1) (ea) of the LP Regulations is only illustrative of the types of "liquidation cost" that are covered by the term "any cost incurred" under Section 5(16) of the IBC;
Paragraph 2.3 and Paragraph 2.4 are upheld. Payments to those doing business with the Corporate Debtor in the course of keeping the business running as a going concern pending liquidation, would not constitute a "distribution" to "stakeholders" from the proceeds of realisation, if they are paid in priority as "liquidation costs". If any business counterparty is willing to wait in queue to be paid as part of the eventual waterfall mechanism (potentially, in itself, a theoretical and impractical proposition), then such counterparty may be an operational creditor who is a stakeholder to whom proceeds from realisation have to be distributed. But a counter-party who is paid for the purpose and while the business of the Corporate Debtors is running as a going concern during liquidation, and that too ahead of all others (only possible because such payment is a "liquidation cost") would not be a "stakeholder" waiting for "distribution" of the liquidation proceeds realised. Any reliance on Paragraph 2.3 and Paragraph 2.4 of the Impugned Circular in the proceedings, must be in accordance with the declaration of the law on the respective subjects as articulated above;

Thereafter, the IBBI issued a Circular on 18th April, 2024 by modifying the earlier circular dated 28th September, 2023 partially to the extent of para 2.1 and para 2.5 of the said circular of 28th September 2023 are being withdrawn.

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Registered Office
8B, Middleton Street, 6A Geetanjali Apartment,
Kolkata-700071
T: +91 33 6813-5920
E:kolkata@sumedhamanagement.com
W:www.sumedhamanagement.com
Bangalore I New Delhi I Mumbai

/SumedhaFiscal | @SumedhaFiscal | /sumedha-fiscal-services-limited

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Confederation of Indian Industry
Eastern Region Headquarter
6, Netaji Subhas Road, Kolkata-700001, India
T: 91 033 22307727/28/1434/3354, F: 91 033 22301721, 22312700
E: ciier@cii.in **W**: www.cii.in

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Reach us via our Membership Helpline Number: 00-91-99104 46244
CII Helpline Toll Free Number: 1800-103-1244