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Efficient Corporate Governance in the Aftermath of Corporate Insolvency Resolution Process

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ABSTRACT

The Indian Insolvency regime had seen a major setback since 2016 when the IBC – Insolvency and Bankruptcy Code was brought into. This can be called one of the biggest reforms in the history of the Indian insolvency regime. This Code has been passed by both the Houses of Parliament under the suggestive measures of a joint committee of the Parliament. For clearing and improving the credit markets, the government has taken this huge step. The Insolvency and Bankruptcy Code, 2016 is a combination of all the insolvency laws, though these laws have been changed from the already existing laws, which are very scattered. The uniqueness of this Code comes from the Corporate Insolvency Resolution Process because it keeps in mind the time management and no interference by the court, which was missing earlier. The legislation of this Code is historical in itself. The present paper is intended to analyze the corporate insolvency resolution process. The paper aims to give a brief overview of the main issues in this area. The paper tries to examine the gaps in the current system. The paper includes all the stages that are involved in the insolvency resolution process. The author also tries to figure out the recent judicial pronouncements that involve the insolvency process. The objective of this paper is to critically analyze the current legislation and to give some recommendations in this regard.

Keywords: *Corporate Insolvency Resolution process, Insolvency and Bankruptcy Code, Legal Regime, Adjudicating authority, 2016.*

I. INTRODUCTION

Before the passing of the Insolvency and Bankruptcy Code, 2016, the companies which were facing financial stress were not governed by particular laws. As discussed earlier, the laws were somewhat present, but they were scattered. There were different laws for different companies and creditors like an act called sick industrial companies act, 1985 was only meant for the industrial companies, likewise for corporate organization, companies ac, 1956 was followed.

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For debt and security things from banks and institutions, other acts called SARFAESI, 2002 and RDDBFI Act,1993 were there.[2] But the main problem was that there was no structured law; everything was scattered, there was the proper legal framework.

Since there was no legal framework, it was quite possible that there would be delays, confusion and conflicts amongst the legal flora. The already established efforts proved to be very ineffective, and the want of speedy structuring in this field demotivated both the debtors and creditors. According to the reports of the "World Banks Ease of Doing Business Index, India was ranked 137 out of 189 countries in 2015 just because it was not speedy in providing justice to those who become the victims of insolvency, and it could be because of several factors like costs, the recovery rate for creditors, participation and most importantly due to the weakness of legal framework in insolvency laws."[3]

Now when the year 2014 was about to end, efforts were seen to be made by the Ministry of Finance. The first step in this regard was setting up of "Bankruptcy Law Reform Committee", which was headed by Mr T.K Viswanathan. [4] During the budget speech of 2015-16, the finance minister made it very clear that their topmost priorities would be some insolvency laws. This statement was given a thumbs up when BLRC has mentioned in its report the draft of the Insolvency and Bankruptcy Bill, 2015, which was then introduced into Lok Sabha and obviously with some changes. This bill was then handed over to the Joint Parliamentary committee, and it revised the above-mentioned bill and came up with a new version of it that was finally passed.[5]

Now Insolvency and Bankruptcy Code, 2016 is a consolidated law that has provided new structural reforms for easy functioning and smooth functioning of the various entities in the country. For example, now there is a regulator, which is the Insolvency and Bankruptcy Board of India, then there are various insolvency professionals and agencies, and also some information outputs where there is collection of debts and defaults. All the regulations were jotted down in IBC 2016 and helped the corporate debtors and partners and unincorporated entities very much. Also, there has been set up of NCLTs – National Company law Tribunals and DRTs, Debt Recovery Tribunals for a speedy justice in case of insolvencies occur at any point of time. Ince, a scholar, said, "in the absence of a bankruptcy law, a firm's assets would

[2] Samvad Partners, Insolvency and Bankruptcy Code, Mondaq India, Septmeber 2017. https://www.mondaq.com/india/insolvencybankruptcy/627706/insolvency-and-bankruptcy-code
[3] Pawan Nahar, Ease of doing business: India slips, ET, October 28, 2015.
[4] Report of the Bankruptcy Law Reforms Committee, Vol 1: Rationale and Design, November 2015.
[5] Report of The Bankruptcy Law Reforms Committee, Vol 2, 2015. https://www.mondaq.com/india/insolvencybankruptcy/627706/insolvency-and-bankruptcy-code

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be sold as scrap, and value would be lost." Now since we have particular legislation and Code for these economic resources are fully and wised used, and as compared to the earlier time, the value of the assets don't get depleted, and they are used to make profits through some economic activity.

II. Relevance of Corporate Insolvency and Resolution Process (CIRP)

Whenever there is insolvency, it not only hampers the debtor company but also hampers stakeholders creditors, which are related to that company and eventually affects the economy as a whole. In this chapter, the relevance of having such an efficient process in the economy and issues dealing with it will be discussed.

IBC has been very intelligently framed now; it allows the corporates not to go through the liquidation process directly. Here it is important to note that the liquidation and resolution process are two different things. Before getting into Liquidation, the corporates have the option of undergoing a resolution process. If the company fails to prove itself right under the resolution process, then only it moves to the liquidation side. As discussed earlier, the objective of CIRP is to maximize the value of assets, promotion of entrepreneurship, making sure the availability of credit, and, most importantly, balance the interests amongst the stakeholders. Whenever a corporate comes into a distressed position, the corporate insolvency resolution process plays a crucial role. Corporate may be destroyed either financially or because of business failure. Basically, CIRP "fundamentally preserves the viable companies, instead of going through liquidation and to liquidate the unviable companies."[6] This is the main reason why there is a need for such a resolution process so that whenever such circumstances occur, it gets resolved at the most initial stage and in a good manner.

Now understanding the provisions in the IBC, firstly resolution process is given under Chapter 2 of Insolvency and Bankruptcy Code, 2016. It comes into the game whenever the corporate Debtor is at default. IBC also differentiate between the types of creditors as financial creditors and operational creditors. So as mentioned earlier, CIRP can be initiated either by financial creditors, operational creditors or by corporate Debtor himself. Financial creditors initiate this insolvency process under section 7[7] or by an operational creditor under section 9[8] and by corporate Debtor itself under section 10 of IBC. Here, it is important to note that "the money

[6] Insolvency and Bankruptcy Code, 2016.
[7] Id. Section 7 (a person to whom financial debt has been legally assigned).
[8] Id. Section 9 (a person to whom operational debt has been legally assigned).

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was given by the home-buyers for a period of time, so that good utility of money is produced within the ambit of Financial Creditor."[9] NCLT -National Company Law Tribunal acts as an adjudicating authority whenever the company has defaulted payment of creditors.[10] The whole resolution process starts from the initial stage of application which is requested by the stakeholders to the NCLT; then, it is the NCLT who has to determine whether the defaulted payment can be repaid or not. But before all of this, the applicant has to prove if the creditor belongs to the financial category or operational category.

(A.) CIRP by Financial Creditor-

If a financial creditor wants to initiate the resolution process, he may alone or, with the help of other financial creditors, can move the application for the process to the authority. The process can be initiated only when the defaulted money is above 1 lakh. As per the current scenario, the financial creditor has to pay a draft amount f Rs 25,000 in favour of the Ministry of Corporate Affairs and the application has to be attached with Form -1 of the Insolvency and Bankruptcy Code.[11] Then upon receiving the application from the creditor, it is the NCLT who has to tell if there is any sort of default of payment within 14 days. NCLT may give its two-fold opinions; firstly, it may either get convinced in the first place that there is default of payment and gives a clear nod to the application; secondly, if the adjudicating authority is not convinced and it thinks that the application is either incorrect or there is no default of payment the authority may decline the application or also it may give a time period of 7 days to the creditor to make changes in its application and then come up with the new application. However, the whole resolution process needs to be completed within 180 days. The resolution professional who is looking after or heading this process can ask for an extension of not more than 90 days, and such an extension must be passed by 75% of voting by the Committee of creditors.

(B.) CIRP by operational creditors-

The initial stages for the start of resolution plans for both financial creditors and operational creditors are the same as the whole process starts when there is the failure of payment of the debt of any types of goods and services. The operational creditors can either file an application by issuing a demand notice to the Corporate Debtor[12] or by directly filing an application to NCLT.[13] Under section 4 of the act, if the defaulted payment is 1 lakh rupees, then the

[9] Anil Mahindroo & Anr. V. Earth Organics Infrastructure, NCLT 74/2017.
[10] Insolvency and Bankruptcy code, 2016, section 5(1).
[11] Supranote 5.
[12] Insolvency and Bankruptcy code, 2016, section 8.
[13] Id. Section 9

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operational creditors can go to the adjudicating authority by the filing of the application. However, this default limit of 1 lakh is now raised to 1 crore rupees.[14](amendment)

Here M/s Krystal Integrated Services Pvt. Ltd v. M/s Indiaontime Express Pvt. Ltd. is an important ruling to cite. In this case, the court ruled that "if the demand notice is not provided to the corporate debtor, then the operational creditor cannot seek to receive admissibility of his application for CIRP under section 9 of the Code."[15] This proves the earlier statement of filing an application is the first step by creditor correct. After 10 days of delivery of demand notice and still, the creditor doesn't get his defaulted payment back, then the creditor is empowered to file an application before adjudicating authority. Unlike financial creditors, the operational creditors have to attach Form 5 along with a copy of Form 3[16] as per the Insolvency and Bankruptcy Rule, 2016. After that, it is the responsibility of NCLT to tell the applicants whether there is a default of payment or not within 14 days. The proceedings for the insolvency and resolution process begins with the acceptance of the application by NCLT.

III. STAGES OF CIRP

Since the initial stage has been discussed above for the resolution process, there are certain stages of Insolvency and Resolution process once it starts. Following are the stages of CIRP:

1. Moratorium: This stage is stated under section 14 of the Code. Generally, it means "suspension of certain remedies" According to Black Law Dictionary, "A period of permissive or obligatory delay, a period during which an obligor has a legal right to delay meeting an obligation". In context to the insolvency, when the adjudicating authority gives the nod to start the insolvency process, and it gets convinced that there is a default of payment, then NCLT can issue an order of moratorium. By this order, many of the activities like foreclosing recovering security interest get prohibited. This stage remains in effect until the proceedings are completed.

2. Publication of Notice: Under section 15 of the Code, there is a provision which states that "the resolution professional will issue a notice in the newspapers to call for submission of claims against the Company Debtor by a predetermined, with a period of time."[17] It is basically an announcement to the public in general. To be very precise, under the insolvency and resolution process, the issued notice must contain the Name and the place of living of the

[14] Ministry of Corporate Affairs, Notification No. S.O. 1205 (E), March 24, 2020.
[15] Krystal Integrated Services Pvt. Ltd v. India on time Express Pvt. Ltd. NCLT CP 223/16.
[16] Shivam Goel, The Insolvency and Bankruptcy Code, 2016: Problems and Challenges, Imperial Journal of Interdisciplinary Research, Vol 3, Issue 5, 2017.
[17] Insolvency and Bankruptcy Code, 2016, Section 15.

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Corporate Debtor, all the evidence that the resolution professional found out till that date and all the fines and penalties for the defaulted payment.

3. Processing of Claim: After collecting all the claims, in this stage, the resolution professional has to make sure that the claims are genuine from the books of the Debtor. Resolution Professional is bound with the responsibility of verifying the claims from information utility, and all these claims are to be supported by some evidence like the financial statements.

4. Information Memorandum: Section 29 of the Code provides that "a memo has to be prepared by the resolution professional in which he has to share each and every detail of assets and liabilities of a debtor under the guidelines by the board for the formulation of a resolution plan."[18] In this stage, the resolution professional has to keep in mind that this information is not shared with any third person, and all the protocols should be adhered to protect the corporate Debtors from being exposed.

5. Meeting of Committee of Creditors: After the verification is done by the resolution professional now, this information is shared and discussed with all the financial creditors of the Debtor. These are all those creditors whose claims have been gathered by the professional. This is known as the meeting of creditors, and mostly all the meetings are leaded by the professional either person to person or via an electronic mode.

6. Call for Resolution Plan: A call is made for the resolution plan by the resolution professional through a newspaper from the applicants to carry out the CIRP of the defaulter. This resolution plan is described under Section 5 (26) of the Code. After receiving the plans from various applicants, it becomes the duty of the professional to approve them within 30 days and to present the plan in front of the Committee.

7. Acceptance and Rejection of Plan: This is termed to be the most important stage as the stage of moratorium cease to effect after this stage is approved. But for this, if the resolution plan presented by the professional before Committee is passed by 66% majority of creditors. This plan is followed throughout by the debtors and all the connected members that are involved. But this plan can also be rejected by the authority if it is not convinced. To accept the plan, the Committee of creditors is given 180 days, and if this is not done in this period, then the professional has the power to ask for an extension of up to 90 days, but this extension is only granted if the adjudicating authority is given valid reasons for the same.

[18] Id. Section 29.

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As mentioned above, if all the efforts went in vain, like a rejection of the plan failure of the resolution process, then the LIQUIDATION process is adopted. Under this, the "company's assets are liquidated, and then the debt is repaid to the creditors."

IV. Judicial Views on the Insolvency and Bankruptcy Code 2016, and Interpretations of CIRP

Since the corporate insolvency and resolution process is out of the hands of the judiciary, and there is just involvement of adjudicating authority and no role of the judiciary as such, there are several landmark judgements and pronouncements by various courts which are discussed below to give a better clarity as to how to eliminate the challenges faced during the CIRP.

The general rules of the Resolution process included that the process should 'mandatorily' be completed in 330 days even after the extension time is over, and then this failure of the process would throw the debtors into the process of Liquidation. This thing was majorly discussed in a landmark case of **Committee of Creditors of Essar Steel India Ltd. through Authorized Signatory vs Satish Kumar Gupta & Ors.** "The SC struck down the word mandatorily and stated that the time taken during the legal proceedings should not affect the interests of the litigant."[19]

In the same case, S.C. also talked about the Committee of Creditors. The court stated that since 66% majority of the creditors is taken for the passing of the resolution plan, then COC should be the main authority to look into the default of the debtors. COC alone should be empowered to make alterations and can give suggestions in the resolution plan.

The judicial contentions have been changed over time regarding the role of the resolution professional, some think of it as an adjudicating authority, and some do not. The provision in the Code under section 30 states, "Once the resolution plan is approved by the COC, the plan is forwarded to adjudicating authority by resolution professional, and the professional examines the plan".[20] But Supreme Court in the case of ArcelorMittal India Pvt. Ltd. Vs. Satish Kumar Gupta & Ors. had made discussions on the work and role of resolution professionals. The court came up with an analysis and stated, "The professional inspect plans, doesn't make decisions and give opinions to the creditors. So the resolution professional does not have the power to decide whether the resolution plan is violative of any provision or not. Its role is just

[19] Committee of Creditors of Essar Steel India Ltd. through Authorised Signatory vs. Satish Kumar Gupta & Ors, Civil Appeal No. 8766-67, 2019.
[20] Supranote 5, Section 30(2), Section 30(3).

to examine and is not the sole adjudicating authority."[21]

Then comes the relation between the Financial Creditors and Operational Creditors. There were a lot of questions and debates regarding the two types of creditors and also a fight between the two as to who will be a part of the Committee of Creditors. "The distinction made between financial and operational creditors was violative of Article 14 of the constitution."- this statement was pronounced in the case of Swiss Ribbons Pvt. Ltd. & Anrs. Vs. Union of India.[22] When this statement was made Supreme Court took the help of Insolvency and BLRC report and then got to a particular decision thought. The court said they had found an intelligible difference, but it is a big thing. The court was of the view that the presence of financial creditors in the assets of debtors make a huge difference. And since the financial creditors are known for their finance skills and are the banking institutions, they can make an impact in going through the resolution plan, and that is why there is no discrimination by not adding operational creditors in the Committee of creditors. The Supreme court finally held that there is no violation of article 14 of the constitution and there is no discrimination as to the addition of operational creditors in COC. In the same case, the court also gave its opinion about the constitutional validity of section 29A(j). The court ruled out that "the person acting jointly or in concert must be related to the business activity of the resolution applicant. Therefore, the relative mentioned in the definition must be related or connected to the business activity of the resolution applicant. In the absence of such a connection, a person cannot be disqualified under Section 29A(j) of the Code."

In the case of ArcelorMittal India Pvt. Ltd. vs Satish Kumar Gupta & Ors., Section 29A of the Code was a question there were many doubts and questions on the eligibility of the applicants who can present the resolution plans, it is very complicated though. However, Supreme Court ruled out these issues and came up with a judgement that "the disqualification of a person from submitting a resolution plan under Section 29A (c) is attracted when the plan is submitted and not before that. It can be, however, removed under Section 29A(c) if the person submitting the plan pays all the dues along with the charges and interest related to said non-performing asset before submitting the plan."[23]

V. CONCLUSION

To conclude this research, after going through all the brief history of the Code and CIRP and also about the aftermath theory or the after-effects story of the resolution process, it is very

[21] Arcelormittal India Pvt. Ltd. Vs. Satish Kumar Gupta & Ors, (2019) 2 SCC.
[22] Swiss Ribbons Pvt. Ltd. vs. Union of India. (2019) 4 SCC 17.
[23] Supranote 20.

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evident that Insolvency and Bankruptcy Code, 2016, came up as a revolutionary reform in the insolvency laws. The process to get over insolvency has been made very clear and easy. Before this Code and reform, there was no provision and a process as such to deal with companies and corporates who were the victims of bankruptcy and earlier, everything was scattered, and no proper framework was present to deal with this thing. So, a big change is that the process is now easier and simple than before. Since the inclusion of this provision, especially the Resolution process, the Code has made certain promises like ending up everything in a fine manner and in a time-bound manner. If we see the process, it is quite a creditor friendly as all the decisions relating to the resolution process are taken by them only. The above-mentioned amendments and landmark judgements that we discussed make the system more effective and efficient. Also, it should be kept in mind the whole resolution process will produce good results only if there are high-quality professionals. So, the insolvency and resolution process is a gift by the drafters who drafted this Code as it helps the financially distressed companies to preserve value as well as it helps to restructure debts. According to the data till 2019, "the insolvency resolution process has helped in recovering 1.6 lakh crore of defaulted payments back to the creditors and as many 200 companies have been benefitted by this process." This is enough evidence to prove that Insolvency and resolution process's success rate is very high, and the scope of this provision, if it gets widened, then it may help more companies and institutions to get benefitted and eventually will help the economy to grow smoothly and without any problems.

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