

SHODH SAMAGAM

ISSN : 2581-6918 (Online), 2582-1792 (PRINT)



Deciphering Corporate Insolvency: An Analytical Exploration of Resolution Dynamics

Y Papa Rao, Ph.D., Centre for Banking and Insurance Law

Ankit Awasthi, Ph.D., Centre for WTO-WIPO Studies,

HNLU, Raipur, Chhattisgarh, , INDIA

Sadhana Prabhat, Legal Consultant

Anheuser Busch Inbev India Limited, Andheri Kurla Road, Andheri (East) Mumbai, Maharashtra, INDIA

ORIGINAL ARTICLE



Authors

Y Papa Rao, Ph.D.

Ankit Awasthi, Ph.D.

Sadhana Prabhat

E-mail : dr.yamala@hnluc.ac.in

shodhsamagam1@gmail.com

Received on : 17/05/2024
 Revised on : 09/07/2024
 Accepted on : 19/07/2024
 Overall Similarity : 01% on 11/07/2024



Plagiarism Checker X - Report

Originality Assessment

Overall Similarity: **1%**

Date: Jul 11, 2024

Statistics: 82 words Plagiarized / 6131 Total words

Remarks: Low similarity detected, check with your supervisor if changes are required.

ABSTRACT

The Indian financial crisis of 1991 along with the emergence of globalization in the Indian economy during the 1990s necessitated the convergence of existing economic and commercial laws. The inflating issues of the Non-performing Assets ('NPAs') in the Indian economy and the absence of a robust insolvency legal regime to deal with the same was duly highlighted by several expert committees formed by the Indian Government to deal with it. In furtherance, desperate reforms were released to liberate the economy and get on a new journey. Amongst the economic reforms of India, the reforms in the Indian banking sector formed a crucial part. The Indian insolvency regime, henceforth, underwent a major transformation. The "United Nations Commission of International Trade Law" ('UNCITRAL') suggested international standards formed the basis for it. In light of recommendations floated by committees to amend "the Companies Act, of 1956" to form a proper insolvency regime in India, it was replaced with "the Companies Act of 2013" and a uniform "Insolvency and Bankruptcy Code, 2016" ('Code'). Since the Code was enacted, we have observed ongoing challenges that the legislative body is actively addressing. This paper aims to research certain such crises faced during "the Corporate Insolvency Resolution Process" ('CIRP').

KEY WORDS

Deciphering, Corporate, Finance.

July to September 2024 www.shodhsamagam.com

A Double-Blind, Peer-Reviewed, Referred, Quarterly, Multi Disciplinary
and Bilingual International Research Journal

INTRODUCTION

The Code aims to ensure timely insolvency resolution for maximizing the value of a Corporate Debtor's assets. However, figures of pending cases implicate the unceasing failure to meet the aims and objectives of the Code. The Insolvency and Bankruptcy News in its *January-March, 2022 Issue* stated that around 1852 applications of CIRP and more than one thousand liquidation applications were pending to be resolved as of March 2022.¹ It further, revealed that only 14% of the filed applications result in a successful CIRP, whilst 47% of matters end up in liquidation.² Moreover, the journal revealed that 66% of the CIRP matters take more than 270 days to conclude.³ Time is a crucial factor under the Code, which often seems to be violated in practicality due to several challenges that the Code faces in its implementation.⁴ A few of such other challenges have been discussed at length in this chapter.

Creditors in Control Model

Under the Code, CIRPs for CD take place under a "creditors in control" model.⁵ The CIRP starts with the admission of the application and ends with the approval of the resolution plan by the "Adjudicating Authority". A moratorium period is imposed upon CIRP commencement and an *Interim Resolution Professional* ('IRP') is appointed to govern the management of the debtor's entity.⁶ The IRP has been conferred to constitute the *Committee of Creditors* ('CoC').⁷ The said committee either retains the appointed IRP as the RP or appoints a new insolvency professional as the RP.⁸ Once the CIRP commences, "the moratorium" or "the calm period" initiates, and, consequently, an automatic stay is imposed upon all legal action against the CD up till the end of the CIRP.⁹ Under the general supervision of the CoC, the IRP operates the CD like a "going concern" and performs several responsibilities as outlined under the Code and the associated CIRP Regulations.¹⁰

The CoC has a crucial role in the CIRP proceeding but in an unregulated environment.¹¹ The CoC is recognized as the supreme decision-making body during CIRP under the Code. Section 21(2) of the Code states that the CoC shall comprise of Financial Creditors ('FC') only, which makes the CoC a "heterogenous body". The Operational Creditors ('OC') stand discriminated against, thereby.¹² The said committee has a wide range of power. It is empowered to make all important financial decisions regarding the CDs' assets.¹³ It is empowered to appoint the RP and can also decide to replace the RP. Although the RP is bestowed with administrative duties and functions, the committee decides upon crucial and critical financial matters related to the entity in distress. However, the RP has been mandated to seek prior approval of the committee to perform its duties such as raising interim finance, creating security interest over the CD's assets, management of the corporate person, and the like for ensuring commercially prudent actions to protect the value of assets of the entity.¹⁴ The CoC's main role is to evaluate the CD's business sustainability, assess future operational feasibility, and analyze costs and expenses. and make a decisive determination. This decision may involve either continuing the resolution process, potentially extending the timeline if necessary, or choosing to initiate immediate liquidation if the CoC determines that the resolution process is unlikely to succeed.¹⁵ Furthermore, the applicant may only request to withdraw the insolvency case once it has been admitted with the consent of 90% of the CoC's creditors.¹⁶ Once the CoC approves a resolution plan with the requisite majority, the RP is bound to present it to the AA for its approval.¹⁷ Hence, the CoC is considered as "the custodian of public trust" during the resolution process.¹⁸ It has a key role in concluding the insolvency resolution of the CD in the stipulated timeframe.

With the wide range of power comes a wide range of responsibilities. The CoC is conferred with both. A paramount importance is given to the committees' decision-making abilities. The AA relies on the "commercial wisdom" of the committee to decide upon the matters of resolution plan. It does not look into the merits of the decision, rather just see if the said plan has been duly approved by the requisite majority of the CoC or not. Hence, it becomes imperative for the CoC to utilize its "commercial wisdom"¹⁹ or the financial prudence in its decision-making role.²⁰ However, in practicality, we often witness that such power is exploited by the CoC. They construe such decision-making power arbitrarily due to minimal intervention of the judiciary in it. Hence,

a transparency and accountability measure is very much required in the decision-making procedure of the committee. Additionally, the committee shall be made to follow a “code of conduct”²¹ to make any decision that concerns the assets of the CD’s entity.

..... *K Shashidhar v. Indian Overseas Bank and Ors.*²², It was determined that the AA lacks authority to intervene in the CoC’s judgment regarding the “commercial wisdom” and has only minimal judicial review at its disposal. In the matter of “*The Committee of Creditors of Essar Steel Limited v. Satish Kumar Gupta*”²³, the Supreme Court of India reaffirmed that the AA’s limited judicial review can be invoked only if the CoC fails to take into account crucial factors including the necessity to maximize asset value, the CD’s ability to continue as a going concern²⁴, in the interests of all stakeholders, etc.

The decisions of the Supreme Court of India in “*Arcelor Mittal India Pvt. Ltd. v. Satish Kumar Gupta and Ors.* and *Swiss Ribbons Pvt. Ltd. and Anr. v. Union of India*”²⁵ underscores the CoC’s authority to evaluate the practicality and sustainability of a resolution plan, verify the qualifications of the resolution applicant, prioritize efforts to maintain the CD’s ongoing operations, consider liquidation only as a final option, and protect the interests of all stakeholders. Furthermore, it emphasizes the necessity for the resolution plan to ensure fair and impartial treatment of OCs.²⁶ The court observed that while the commercial wisdom of the CoC is protected from judicial scrutiny²⁷, the decisions made by the CoC during the CIRP, even while carrying out other duties, are open to scrutiny and potential challenge. In the matter of *M/s. Andhra Bank Vs. Sterling Biotech Ltd. and Ors*²⁸, the promoter of the company was attempting to take over the corporate entity under the insolvency regime. They got the resolution plan approved by the CoC with a 90.32% majority. The promoters of the CD are, however, statutorily barred and are declared ineligible to participate in the revival of the debtor company.²⁹ The NCLT in the light of the given facts of the case observed that “*This raises doubt about the functionality of the CoC as such an act of CoC can never be treated as an act of commercial wisdom.*”

Similarly in the case of “*Bank of Baroda, Vs. Mr. Sisir Kumar Appikatla, & Ors*”³⁰, the resolution plan, which was duly approved by the CoC, was rejected by the AA. The tribunal observed that under the given set of facts of the case, it is apparent that the CoC is acting arbitrarily. The resolution plan was submitted by an ineligible applicant³¹ under the Code but was duly considered and approved by the committee. It is an act in violation of the Code to give control of the company to the person who is defined as ineligible persons to become a resolution applicant under the Code. While rejecting the resolution plan, the appellate tribunal held that “*The approval of the Restructuring Plan camouflaged as Resolution Plan emanating from an ineligible person renders the role of the Committee of Creditors questionable*”.

The CoC has great potential to rehabilitate distressed CDs. Hence, it is worth exploring the area of challenges attached to the committee to undertake adequate measures to further fill the gap lacuna and strengthen the framework. A proper mechanism shall be devised to maintain the transparency and accountability of the committee to prevent them from acting arbitrarily.³² A possible way through which such a suggestion could be attained is by considering enacting and adopting a “code of conduct”³³. The said code of conduct would comprise guiding principles for the CoC to be mindful of when making any decision This would ensure the application of the commercial wisdom within the four walls of these guiding principles. Any abnormalities would be required to be adequately justified by the committee. Hence, The legislative shall consider amending section 196 of the Code to include an obligation upon the CoC to follow a “code of during the CIRP to have transparency during the proceeding.

The Code, in India, imposes the duty to maintain transparency in the CIRP fundamentally on the CoC.³⁴ The CoC is obliged to use its commercial wisdom or ordinary prudence to approve the resolution plan and make other decisions.³⁵ Ensuring transparency and fairness in the CIRP could be brought with a well-crafted

and drafted "code of conduct" for CoC members to be complied with. The CoC's ability to apply its business acumen for the good of the CD could be enhanced by the implementation of principles and practices like transparency, prior due diligence, and disqualification for wrongdoing.³⁶ In summary, implementing a "code of conduct" as described above could greatly enhance the effectiveness of the CIRP, optimize asset value for all involved parties through robust procedural standards, and align Indian insolvency law with well-established international practices.³⁷

CIRP in a Timebound Manner

The Code provides for "*insolvency resolution and reorganization of distressed corporate persons for procuring maximized value of its assets*". The Code is distinct from the previous insolvency regime due to its time-stringent provision. Section 12 of the Code mandates completing the CIRP within 180 days of the insolvency application's admission by the AA, with a possible one-time extension of 90 days approved by the AA under specific conditions.³⁸ *Time is of the essence* for matters governed under the Code. A prolonged CIRP period has the potential to negatively impact the asset's value in the event of liquidation.³⁹ Such delays accrue high expenses for the parties involved.⁴⁰ In addition, stakeholders' faith in the process wanes as delays mount. Hence, the CIRP timeline demands to be strictly adhered to.

Up until June 30, 2021, there have been 4541 CIRPs admitted since the enforcement of the Code.⁴¹ Where 653 matters were resolved through appeal, review, settlement, or other means; 461 applications were withdrawn under Section 12A; 1349 were liquidated; and 396 had their resolution plans approved.⁴² As of the 30th of June, 2021, about 1264 CIRPs failed to meet the 270-day deadline required by the Code.⁴³ There are certain obstacles to meeting the required deadline. Delays in the CIRP have been caused by a variety of factors, such as delayed response to expressions of interest, extensions of the deadline for resolution plan submissions, revisions to previously submitted plans that were not requested, negotiations with resolution applicants, the receipt of resolution plans that were not requested, and so on.⁴⁴

1. Admission of CIRP Application

The Code stipulates that "default" occurs when the CD is unable to make payment of debt to creditors. It stands as a mandatory criterion for filling out a CIRP application with the AA. On filing of application, the AA has to conduct the "*default test*"⁴⁵ to determine whether the CD is unable to make payment of debt when "it became due and payable". The AA is required to admit the application if it stands assured with the occurrence of default by the CD. However, this determination of default by the AA consumes a substantial amount of time.⁴⁶ The major factors that add to the consumption of time are the contesting arguments by the parties, production of evidence to support the argument, and proving of pre-existence of dispute in the case of OC, amongst other factors.⁴⁷ If only the necessary information or material fact is presented before the AA, relevant for the determination of the presence of a default on the part of CD or the presence of a legitimate conflict relating to it, then the time spent on these tasks can be minimized. Moreover, the AA is not bound to admit the application of FC, unlike other creditors, even if there is a default on the part of the CD. Section 7(5)(a) uses the term "may", which gives the AA discretionary power to admit the insolvency resolution application of the FC, whereas in the case of OC, under section 9(5) the term "shall" has been used, wherein if the OC satisfies the AA about the occurrence of the debt, then the AA must admit such application.⁴⁸ This again consumes much time to decide the application of the FC in light of the discretionary power of the AA.

Information Utilities⁴⁹ ('IUs') forms one of the cornerstones of the Code which is described as a "repository of financial information database".⁵⁰ It stores data on debt and defaults concerning entities such as corporate debtors. In light of the significance of the IUs, the applicant who desires to initiate a CIRP against the CD should ascertain the relevant information concerning the occurrence of such default or related dispute with the IUs. In light of this, although, the Code does have the provision of Section 215 which mandates the FCs to submit the financial data to IUs, it is merely a directory for the OCs who wish to file for CIRP. Hence, the said shall be modified to include all categories of CIRP applicants to mandatorily submit all sorts of

relevant financial data with the IUs, which can then be authenticated or verified by the IUs supplemented with the view of the CD under Section 215.⁵¹ Such financial records duly obtained, authenticated, and maintained by the IUs shall be considered or declared by the parliament by an amendment to be conclusive proof. This will allow the AA to conduct the “default test” to determine the default expeditiously. Such a step, to align the CIRP proceeding within the statutory stipulated timeline, would be a right step in the right direction.

2. Moratorium

It is specified under Section 14 of the Code that as soon as the CIRP application gets admitted by the AA, the AA shall order the operation of a moratorium period, which is also popularly known as the “calm period”. An application of moratorium preserves and duly maintains the “status quo”⁵² of the CD by prohibiting any legal action to be instituted or continued against the CD and its assets.⁵³ Protection is provided to the CD by suspending or staying the ongoing legal action. This provision is prohibitory. The purpose of the moratorium is to prevent the creation of any new right relating to CD while maintaining its status quo.⁵⁴ The said moratorium period exists until the conclusion of CIRP proceedings. It helps in preserving the assets of the CD for the unpaid creditors.⁵⁵ This provision seems to be an advantageous provision for the creditors. But, interestingly, the moratorium period does not apply during certain circumstances⁵⁶ which causes inordinate delays in moving further during the CIRP proceeding eventually defeating the goal of the Code, that is, essentially to bind up the insolvency resolution in the stipulated time frame of a maximum of 330 days. A few of them are:

- i. The provision of moratorium provides that the moratorium order shall not disrupt the “supply of essential goods and services”. It forms an essential element for the RP to keep running the CDs under the insolvency resolution as a going concern.⁵⁷ However, for continued essential supplies, OCs need their debt to be paid, otherwise they would be hesitant to make the supplies.⁵⁸ This stands as a challenge. What if the existing OC doesn't intend to make the supply in light of the unpaid due credit with the least assurance of recovery? Also, what if no new OC wishes to invest in a company that is under insolvency resolution? This issue needs to be looked into.
- ii. Courts several instances have held that an arbitration proceeding cannot be initiated⁵⁹ against the CD during the moratorium. However, proceedings under Section 34 of “the Arbitration and Conciliation Act, 1996” will not be suspended⁶⁰, meaning thereby that the moratorium will not apply in this case.
- iii. Any legal action taken against the appointed IRP or the RP will again not attract the calm period⁶¹, leading to a delay. The Code is silent upon this issue and not much discussion has taken place concerning this.
- iv. The moratorium period does not apply to the proceedings under the “Prevention of Money Laundering Act, 2002.”⁶²

3. Resolution Plan

Regulation 36B of the “Insolvency and Bankruptcy Board of India (Insolvency Resolution of Corporate Persons) Regulations, 2016” Allows submission of a resolution plan within 30 days of request, extendable with CoC approval.⁶³ The revision of the resolution plan is duly allowed subject to an additional thirty days timeline.⁶⁴ However, if the CoC is not satisfied with the received resolution plan, it can get the resolution plans re-issued through the RPs. An inordinate delay is caused towards the completion of the CIRP due to the time-consuming approval process of a suitable resolution plan by the CoC.⁶⁵ As per the *IBBI Newsletter, as of September 2021*, the approval of the resolution plan on average takes around 584 days against the 330 statutory days.⁶⁶ Moreover, there is no capping to the number of revisions that could be done to the prospective resolution plans.⁶⁷ This loophole allows the resolution applicants to amend and modify their resolution plan numerous times causing delays. In response to this, the “Swiss Challenge Method”⁶⁸ could be the right choice. The “Swiss Challenge” method is described as a process of bidding, wherein the original bidder submits an unsolicited bid to the auctioneer against which a counter-proposal is sought by the auctioneer. Amongst several proposals, the auctioneer tends to choose the most suitable bid. The original bidder is generally

conferred with the “right to first refusal”.⁶⁹ This method has stood as an extremely effective method in ensuring transparency, time-efficiency, and value maximization of assets of CD during the insolvency procedure, as per “*The Report of the Sub-Committee of the Insolvency Law Committee on Pre-packaged Insolvency Resolution Process (‘PIRP’)*”⁷⁰

In the matter of “*Bank of Baroda v. Mandhana Industries Ltd.*”⁷¹, Hon’ble NCLT, Mumbai Bench directed the RP to adopt the “Swiss Challenge” method on the application of resolution applicant which turned out to be a success. However, in the matter of “*Saket Tex Dye Private Limited v. Kailash T. Shah*”⁷², Hon’ble NCLT, Mumbai Bench observed that the “Swiss Challenge” method fails to have a statutory backup of the Code or the CIRP Regulations. Hence, it prohibited the use of the said method during the CIRP stating that it would hurt the “commercial wisdom” of the CoC.

The Code along with the CIRP Regulations promulgated thereunder, allows for a hybrid approach to value maximization of the debtor’s asset during the PIRP.⁷³ The hybrid strategy takes cues from the Swiss challenge, with some modifications to ensure its success in the regime of PIRP. Under this dual approach, a settlement plan by CD acts as a benchmark for competing plans from the other resolution applicants. The calculated benchmark along with the parameters of the evaluation for the base resolution plan are disclosed to third-party resolution applicants. The resolution applicant for the chosen resolution plan which is set as a benchmark, thereby, loses “the right of first refusal”, if after both sets of plans have been received, and the other plan is determined to be significantly better.⁷⁴ The applicants of the set benchmark plan and the best alternate plan to it are given repeated opportunities to compete against each other via an electronic platform if the best alternate plan does not practically stand out from the base plan.⁷⁵ They have many chances to refine their submission up to the point when one contributor decides to withdraw. However, the number of times the resolution plan could be updated is limited. Within a fixed time, frame not exceeding the legal window, the aforementioned process of approving the plan must be completed.

Considering the PIRP resolution process, the “Swiss challenge” method could be adopted to improve the inordinate delays while deciding the resolution plan by the CoC during CIRP.⁷⁶ However, the request for revision of the resolution plan, if required, should be allowed for a specific number of times. Also, a proper criterion⁷⁷ for the approval of the resolution, the plan should be formulated and made known to the applicants rather than approving the plans as per the whims and fancies of the CoC. The proposed change would not only bring time and cost efficiency in the CIRP along with value maximization of the debtor’s assets but also will bring transparency in the procedure and will consequently boost the confidence of the stakeholders.

Time is described as the essence of the Code. Hence, the timely admission of insolvency resolution application by the AA and timely approval of resolution plans by the CoC will allow the system involved in the insolvency ecosystem to analyze and focus on other attached challenges affecting the CD, such as the “flow of credit” to “value maximization by way of exit”.⁷⁸ A non-expeditious or delayed process only has the potential to ensure the deterioration of the will of the buyers and the investors under the process.⁷⁹

Single Resolution Plan

As soon as the CIRP application is admitted by the AA, the IRP is appointed and the CoC is constituted to look into the financial affairs and feasibility of the CD to rehabilitate, if possible, it at the earliest. On the appointment of RP or turning the IRP into RP, the Expression of Interest (‘EOI’)⁸⁰ is issued inviting the prospective resolution applicants to come up with their resolution plan. The significance of the said plan is that it shall mandatorily provide for the “insolvency resolution” of the CD as “a going concern”.⁸¹ Additionally, the resolution plan may provide provisions for the restructuring of the CD. The Code allows approval of a single resolution plan by the CoC for the revival of the CD.⁸² The CoC in no circumstance is to approve more than one resolution plan, such as, to run the CD’s entity as a going concern and, separately, to deal with its assets.

Identifying a single resolution plan that covers and deals with all the issues attached to the financially distressed CD in its entirety is a difficult task. Finding such a resolution applicant willing to take over the CD

altogether stands as an impediment in the way of CIRP.⁸³ As a result, a substantial delay in binding up the CIRP occurs resulting in erosion of the value of the assets of the company whilst, consequently, pushing the CD into the liquidation process. Delay in concluding the CIRP due to non-approval of an appropriate resolution plan leads the CD into dissolution and is one major concern presently. Also, due to the value deterioration of the CD due to the inordinate delays, the negotiation between the successful resolution applicant and the CD becomes infructuous.⁸⁴

The CIRP mechanism in the present insolvency and bankruptcy legal regime does not provide for separate resolution plans for specific matters, such as varied assets of the CD.⁸⁵ Hence, in light of this existing issue, the legislation shall consider empowering the CoC under the Code and the CIRP regulation to approve different resolution plans for different assets of the CD, to maximize the value of the assets of the CD.⁸⁶ For instance, a resolution plan approved for viable assets and another to deal with the unviable assets. This will allow the CD to rehabilitate and stay in the market rather than getting liquidated. However, there shall be a restriction to this. There must be one resolution plan approved dealing with running the CD as a going concern during its insolvency resolution.⁸⁷ Similarly, another resolution plan might be approved for the corporate restructuring of the CD and other matters such as dealing with the management of the CD, subject to the approval of the AA.⁸⁸ Also, on approval of any of several resolution plans by the CoC with the majority of 66%⁸⁹ and thereafter by the AA, the said plan shall be implemented, while other plans still being under scrutiny for approval.⁹⁰ However, once all the proposed resolution plans are duly approved both by the CoC as well as the AA, the CIRP shall stand terminated.⁹¹

1. Separation of Resolution Plan and the Distribution of Proceeds

Section 30(2) of the Code provides for the CoC to comply with two requirements, namely, fulfilling the essentials for implementation of the resolution plan and the manner of distribution of the proceeds along with other entitlement for OCs and the dissenting FCs. It has been observed that several objections and concerns are raised during the pendency of the approval of the resolution plan by the AA regarding the “distribution of proceeds” and “inequitable distribution of the same amongst the creditors”.⁹² These matters are to be determined as a pre-requisite condition for the resolution plan approval by the AA. This practically causes a delay in insolvency resolution but only on such determination or settlement of conflict arising out of such determination, the resolution plan could be successfully approved by the AA.⁹³ Hence, it is only upon settlement of said disputes that the successful resolution applicant can move forward with the plan and take over the CD’s management.⁹⁴ Hence, a change must be brought in the Code for segregating the plan of the distribution of the proceeds from the primary resolution plan by the resolution applicants.⁹⁵ The primary resolution plan should ideally comprise the provisions for the flow of credit to the CD and/or other provisions for restructuring the CD. Additionally, a separate plan should be drafted for the distribution of the proceeds under the primary resolution plan by the SRA. Both of these plans should be duly approved by the CoC with a majority while fulfilling other implementation requirements of the resolution plan.⁹⁶ Nonetheless, on the approval of the said two separate plans, that is, “the resolution plan” and “the plan of distribution of proceeds”, by the CoC, they should be consequently approved by the AA.⁹⁷

Now, the question arises how can the “distribution of proceeds” be determined equitably? Regarding this, an objective formula could be devised, in line with fair and equitable principles, to distribute proceeds during the CIRP.⁹⁸ To make an equitable distribution of proceeds, a separate waterfall mechanism⁹⁹ could be devised, wherein the creditor being in order of priority under the “waterfall mechanism” under Section 53 of the Code would receive proceeds up to CD’s liquidation value regarding their claims.¹⁰⁰ Their unsatisfied claims could be satisfied by the surplus over the liquidation value. Then the remaining surplus could be finally distributed amongst the equity shareholders. This would make the process for the “distribution of proceeds” a fairer process and would consequently boost the enthusiasm of the stakeholders.¹⁰¹

Classified Creditors

Anyone to whom a debt by CD is due is referred to as a creditor under the Code.¹⁰² Creditors could be categorized as financial creditors, secured creditors, operational creditors, unsecured creditors, and decree holders. The Code majorly deals with the FCs and OCs and distinguishes the two. Where an FC has been defined to be someone¹⁰³ who has a purely financial contractual relationship¹⁰⁴ with the CD, namely, a loan or debt security. On the other hand, an OC has been defined to be someone¹⁰⁵ who provides for the operation¹⁰⁶ of the CD. The Code also recognizes a creditor who could be both an FC as well as an OC.

1. Homogenous Default Amount

Sections 3(11), 5(8), and 5(21) of the Code define debt, financial debt, and operational debt.¹⁰⁷ A default, meaning, debt due to be paid by the CD is described as the trigger point for the commencement of CIRP. The IBC defines 'default' in quite uncontroversial terms as, "*the non-payment of debt when whole or any part or installment of the amount of debt has become due and payable and is not paid by the corporate debtor*".¹⁰⁸ However, the Code is distinct in the meaning of the term 'default' in respect of the OCs as against the FCs. The homogenous nature of the default for both the FCs and OCs with their differential rights in terms of the voting rights that the FC enjoys during the meeting of the CoC against the OCs stands discriminatory.¹⁰⁹ The debt that is being defaulted on the part of OCs is often of small amounts in comparison to the FCs. Also, a FC are allowed under the Code to file a CIRP application jointly with other FCs which allows them to default amount criteria easily. As against this, an OC is only permitted to file the CIRP application individually. Time and again the judiciary has looked into this aspect¹¹⁰ and has justified the homogenous amount of default for different types of creditors based on intelligible differentia. However, a heterogenous default amount for different categories of creditors will facilitate a better manner to achieve the goals of the Code.¹¹¹ Another way could be stipulating different default amounts to initiate a CIRP proceeding for different categories of companies, such as, based on the annual turnover of the company or a company in the MSME sector, etc.

2. Differential Treatment Between Creditors

The Code establishes several variations to deal with FCs and OCs, namely, for filing of insolvency resolution applications with NCLT; rights available during CoC meetings; distribution of proceeds under the resolution plan, and rights to benefit from CD's liquidation.¹¹²

The certain distinctions between the two classes of creditors are the following:

- i. **Filing of CIRP application:** Concerning filing of the insolvency resolution application, FCs can directly file a CIRP application with the AA on the occurrence of "default", either jointly or individually.¹¹³ In contrast, when it comes to OCs, it has to individually, firstly, comply with a pre-condition to put forward a "demand notice"¹¹⁴ to the CD, to file a CIRP application. Ten days is provided to CD to answer the said notice. Only on the expiry of the said ten period, wherein, if OC does not receive either the claimed payment or any notice of dispute, the OC gets a right to file for CIRP with the AA. This pre-requisite for the OCs for the filing of CIRP applications often pushes them to the verge of becoming insolvent.
- ii. **Withdrawal of CIRP application:** Section 12 A of the Code allows for withdrawal of CIRP application filed under sections 7, 9, and 10 with approval of 90% majority of the CoC. Now, we know that OCs are expressly barred from participating in CoC meetings, and even if allowed, under certain conditions,¹¹⁵ they are not given any voting rights. Hence, this implicates the due prominence given to FCs. It is at the behest of FCs, to withdraw the CIRP application.
- iii. **Participatory rights in the working of CoC:** When we talk about the participation rights of the creditors in the CoC, the OC's participation is expressly barred in the CoC meetings as per Section 21(2) of the Code. Hence, the most important document, the resolution plan, which not only provides for an insolvency resolution scheme but also the repayment plan is approved only at the behest of the

FCs. Section 24(3)(c) further restricts the OCs rights. It states that the Resolution Professional is not required to give even the notice of the meetings of CoC to OCs if the amount due to OCs is less than 10% (aggregately) of the debt due to the CD. Section 24(4), further, creates discrimination by providing not providing any voting rights to OCs.

- iv. **Proposing IRP and providing financial information:** Another point of discrimination relates to “proposing the IRP name”. The FCs must furnish the name of IRP.¹¹⁶ Whereas the same is made optional for the OCs.¹¹⁷ Similarly, concerning the “submission of financial information related to assets related to which any security interest has been created” to the “Information Utility” “it has been made mandatory for the FCs whereas optional for the OCs.”¹¹⁸
- v. **The order of priority under the waterfall mechanism:** Payment of debts and dues made to creditors is let alone discrimination. It has been held on several instances by the court that the minimum payment shall be done to OCs under the resolution plan. A “fair and equitable distribution” of the amount shall be made amongst the creditors. However, in the waterfall mechanism¹¹⁹, in the sequence of priority, the FCs stand before the OCs. Where a large sum is distributed amongst the FCs, the amount left for OCs stands almost minimal to nil.¹²⁰ This again brings to the surface the disparity amongst creditors under the Code.

The Supreme Court of India in the case of *Essar Steel*¹²¹ observed that the “equality for all” principle¹²² concerning creditors under the Code cannot be applied effectively due to the inequitable treatment of the creditors under the Code. The two fundamental categories of creditors under the Code are classified on certain parameters and are equally significant for the business of an entity.¹²³ The court further observed that if all the creditors are treated equally, the FCs, who have the authority in the CoC working, will try to push for liquidation rather than working towards the rehabilitation of the entity, which will result in the defeat of the objective of the Code.¹²⁴ Taking this observation of the Supreme Court into account, we understand that the FC and OC are treated differently within the ambit of the Code. However, there is one aspect where there is no differential treatment, that is, regarding the “default amount”¹²⁵ for the filing of an application for commencing the resolution of insolvency with the AA. The amount of default is homogenous while the rights which are conferred thereafter are completely varied. This leads to absurdity. The Parliament shall either create a difference in the default amount also or confer equitable rights to every creditor.

Way Forward

It has been established in several existing literature that the CIRP procedure is structured in a manner so that the RP can keep the CD running as “a going concern” during the CIRP and simultaneously obtain creditors’ approval, wherever required. Several crucial details must be paid attention to during CIRP, namely, filing of the CIRP commencement application, operation of the moratorium, role of the RP, constitution of the CoC, approval of most competent resolution plan, etc.¹²⁶ There are several practical issues attached to these factors. For instance, what if the resolution plan is not approved in the given timeline and the value of the assets of the CD deteriorates, or what if the CoC approves the resolution plan without applying its commercial wisdom, then can the AA reject the same? Certain other challenges which is being faced in practicality during the CIRP that need to be considered, including interim financing which is required for the CD to be run as a going concern during the CIRP; interim moratorium which provides for the operation of moratorium during the pendency of the CIRP application with the AA; timely resolution of conflicts arising out of the proposed resolution plan and strengthening the insolvency ecosystem to deal with unusual circumstances, for instance natural disaster such as COVID 19.¹²⁷ All such practical challenges shall be duly considered and addressed by the legislative and appropriate amendments regarding them shall be introduced. The insolvency ecosystem of India is still in its evolving stage and with diligent steps of the legislative it has the potential to be one of the most comprehensive and robust legal regimes in India.

Footnotes

1. Gupta, Mani; Chaudhry, Aman and Upadhyay, Saumya, (2022) *Overview of India's Insolvency and Bankruptcy Code*, GRR, <https://globalrestructuringreview.com/review/asia-pacific-restructuring-review/2023/article/overview-of-indias-insolvency-and-bankruptcy-code>, Assess on March 24, 2023, 8:05 PM.
2. Insolvency and Bankruptcy News, IBBI 22, 14 (2022).
3. *Id.*
4. M. S. Sahoo, *Insolvency Reforms, A Road Under Construction*, IBBI (2020).
5. *Supra* note 2.
6. Chugh, Bharat and Singh, Advaya Hari (2020) *A to Z of the Insolvency and Bankruptcy Code: A Beginner's Guide* (Part II), June 8, 2020, <https://bharatchugh.in/2020/06/08/a-to-z-of-the-insolvency-and-bankruptcy-code-a-beginners-guide-part-ii/>, Assess on March 24, 2023, 1:09 PM.
7. "Insolvency and Bankruptcy Code, 2016", § 21(1), No. 31, Acts of Parliament, 2016 (India).
8. "Insolvency and Bankruptcy Code, 2016", § 22(2), No. 31, Acts of Parliament, 2016 (India).
9. "Insolvency and Bankruptcy Code, 2016, § 13(1) and 14, No. 31, Acts of Parliament, 2016 (India)".
10. "*Understanding the IBC: Key Jurisprudence and Practical Considerations*, A Handbook", IBBI, October 2020.
11. Shrijita Kesharwani, *Analysis of Corporate Insolvency and Laws Related To It*, [2021] 1132 TAXMANN.COM 4 (Article), November 1, 2021.
12. "Insolvency and Bankruptcy Code, 2016, 24, No. 31, Acts of Parliament, 2016 (India)".
13. "Insolvency and Bankruptcy Code, 2016, 28, No. 31, Acts of Parliament, 2016 (India)".
14. "Insolvency and Bankruptcy Code, 2016, 25, No. 31, Acts of Parliament, 2016 (India)".
15. D'Souza, Christian and Das, Priankta, (2022) *The proposed code of conduct for CoC: A forestall of creditors' supremacy?* 139 TAXMANN.COM 218 (Article), June 9, 2022
16. Insolvency and Bankruptcy Code, 2016, 12A, No. 31, Acts of Parliament, 2016 (India).
17. "Insolvency and Bankruptcy Code, 2016, 30(6), No. 31, Acts of Parliament, 2016 (India)".
18. "Insolvency and Bankruptcy Board of India", *Discussion Paper*, Aug 27, 2021.
19. "Essar Steel India v Satish Kumar Gupta" (CA No. 8766-67/2019 & others).
20. Singh, Gaargi (2022) *Need for Judicial Scrutiny of the Commercial Wisdom*, *Indian Review of Corporate* and CL, June (2022), <https://www.ircl.in/post/need-for-judicial-scrutiny-of-the-commercial-wisdom-of-coc>, Assess on March 24, 2023, 5:24 PM.
21. D'Souza, Christian and Das, Priankta, (2022) *The proposed code of conduct for CoC: A forestall of creditors' supremacy?* 139 TAXMANN.COM 218 (Article), Assess on June 9, 2022.
22. Civil Appeal No. 10673 of 2018.
23. CA No. 8766-67/2019 & others.
24. *Supra* note 10.
25. (2019) 2 SCC 1 [116].
26. *Supra* note 10.
27. *K Sashidhar v. Indian Overseas Bank* [2019] 102 taxmann.com 139/152 SCL312 (SC); "*Andhra Steel India Ltd v Satish Kumar Gupta* [2019] 111 taxmann.com 234 (SC); *Maharashtra Seamless Ltd v. Padmanabhan*", Venkatesh [2020] 113 taxmann.com 421/158 SCL 567 (SC), Assess on March 20, 2023, 2:33 PM.
28. Company Appeal (AT) (Insolvency) No. 612 of 2019.
29. Insolvency and Bankruptcy Code, 2016, 29A, No. 31, Acts of Parliament, 2016 (India).

30. Company Appeal (AT) (Insolvency) No. 579 of 2020.
31. “Insolvency and Bankruptcy Code, 2016, § 29A, No. 31, Acts of Parliament, 2016 (India)”.
32. SBI v. Videocon Industries Ltd (2019) SCC Online NCLT 23720; IDBI Bank Ltd v Siva Industries and Holdings Ltd [2019] 109 taxmann.com 255 (NCLT - Chennai) (SB), Assess on March 23, 2023, 9:21 PM.
33. *Supra* note 18.
34. *Supra* note 10.
35. State Bank of India v. Ushdev International Ltd. 2018 SCC OnLine NCLT 173.
36. D’Souza, Christian and Das, Priankta (2022) The proposed code of conduct for CoC: A forestall of creditors’ supremacy? [2022] 139 TAXMANN.COM 218 (Article), Assess on June 9, 2022.
37. Jain, Shraiya and Jhalani, Palak (2022) Accountability of the CoC: Formulating a Standard Code of Conduct, *NLIU Journal of Business laws*, Volume 3, December 29, 2022, p. 5-9.
38. Singh, Jyoti & Shriram, Vishnu (2017) *Insolvency And Bankruptcy Code, 2016: Concepts and Procedures*, Bloomsbury India Professional, 2nd edition, p. 5-15.
39. Mukesh Chand, Bankruptcy Code Dilemma and Challenges, LiveLaw (2022), <https://www.livelaw.in/library/hnl/remotexs.in/columns/insolvency-and-bankruptcy-code-nclt-allahabad-english-bankruptcy-act-corporate-insolvency-ibbi-cirp-personal-insolvency-203333>, Assess on March 24, 2023, 6:22 PM.
40. *Id.*
41. Anand, Saurav (2023) *Insolvency cases up 25% in Q3, but recoveries still on downtrend: Report*, LIVEMINT, <https://www.livemint.com/news/india/insolvency-cases-up-25-in-q3-but-recoveries-still-on-downtrend-report-11676889990257.html>, Assess on March 24, 2023, 7:53 PM.
42. *Id.*
43. *Id.*
44. Chugh, Nidhi S.(2021) *Delay in resolution raise questions on IBC regime, ETBFSI (2021)*, <https://bfsi.economictimes.indiatimes.com/news/banking/delay-in-resolutions-raise-questions-on-ibc-regime/86250618>, Assess on March 25, 2022).
45. “Ministry of Corporate Affairs, *Invitation of comments from the public on changes being considered to the Insolvency and Bankruptcy Code, 2016, F*”. No. 30/38/2021-Insolvency, Notified on January, 18, 2 (2023).
46. Perumal, Venkateshwara and Das, Paulomi (2023) Time vs. Value: A Tug of War in IBC Concerning Reliance Capital, 147 TAXMANN.COM 575 (Article), Assess on February 28, 2023.
47. *Supra* note 10.
48. Gaur, Yatin and Kumar, Ashutosh (2022) Walking the tightrope: Addressing the legal conundrum vis-a-vis Vidarbha Industries judgment and what lies ahead, *Insolvency and bankruptcy Journal*, ICSI IIP 9, 7, 141 TAXMANN.COM 284 (Article), Assess on August 17, 2022.
49. Insolvency and Bankruptcy Code, 2016, § 3(21), No. 31, Acts of Parliament, 2016 (India).
50. *Supra* note 10.
51. *Supra* note 41.
52. “M S Sahoo, Here’s How IBC 2016 Has Taken Corporate Governance to New Heights, Financial Express”, Feb. 30, 2020, www.financialexpress.com/opinion/heres-how-ibc-2016-has-taken-corporate-governance-to-new-heights/1866199/, Assess on March 10, 2023, 1:10 PM.

53. Alchemist Asset Reconstruction Co. Ltd. v. Hotel Gaudavan (P.) Ltd. [2017] 88 TAXMANN.COM 202/[2018] 145 SCL 428 (SC), Assess on March 22, 2023, 5:05 PM..
54. “M/s Embassy Property Developments Pvt. Ltd. v. State of Karnataka and Others, 2019 SCC OnLine SC” 1542.
55. *Supra* note 10.
56. *All about Moratorium under Section 14 of IBC, 2016 including judicial pronouncements*, Rajat Jain & Associates (2022), https://carajput.com/learn/all-about-moratorium-us-14-of-ibc-2016-including-judicial-pronouncements.html#heading_3, Assess on March 24, 5:34 PM.
57. Gujrat Urja Vikas Nigam Limited v. Amit Gupta & Ors. Civil Appeal No. 9241 of 2019.
58. Ghish, Shalin (2023) *Secured Creditors vis-à-vis Debt Recovery: A Positive Step*, LiveLaw, February 10, 2023, <https://www.livelaw-in.elibraryhnluremotexs.in/columns/secured-creditors-vis-vis-debt-recovery-a-positive-step-221277>, Assess on March 24, 2023, 6:33 PM.
59. Alchemist Asset Reconstruction Co. Ltd. v. Hotel Gaudavan (P.) Ltd. [2017] 88 taxmann.com 202/[2018] 145 SCL 428 (SC).; P.Mohanraj and Others v. Shah Brothers Ispat Pvt. Ltd. (2016) 7 SCC 221, Assess on March 02, 2023, 07:09 PM.
60. Power Grid Corporation of India Ltd. v. Jyoti Structures Ltd. [2017] 88 taxmann.com 124/[2018] 145 SCL 449 (Delhi), Assess on March 09, 2023, 10:16 AM.
61. Insolvency professional: A Key to resolution Information Brochure, IBBI (2021).
62. Deputy Director, Office of the Joint Directorate of Enforcement vs. Asset Reconstruction Company of India Ltd. and others (Writ Petition No. 29970 of 2019 and WMP Nos. 29872 and 34971 of 2019).
63. *Frequently Asked Questions on the Insolvency and Bankruptcy Code, 2016*, Committee on Insolvency & Bankruptcy Code, ICAI (2022).
64. Pallavi Mishra, “*RP and CoC Can Request Resolution Plan for a Second Time: IBBI Notification*”, LIVE LAW (2023), <https://www.livelaw.in/news-updates/insolvency-and-bankruptcy-board-of-india-ibbi-insolvency-resolution-process-for-corporate-persons-regulations-insolvency-and-bankruptcy-code-209640>, Assess on March 25, 2023, 10:20 AM.
65. Ghanashyam Mishra and Sons Private Limited through the Authorized Signatory v. Edelweiss Asset Reconstruction Company Limited through the Director and Others (CIVIL APPEAL NO.8129 OF 2019).
66. *Quarterly Newsletter For Jul-Sep. 2021*, IBBI (2021).
67. Insolvency and Bankruptcy Code, 2016, 27, No. 31, Acts of Parliament, 2016 (India).
68. *Supra* note 18 at 5.
69. Borkatakya, Samiron and Angirish, Kritika (2022) *India: Swiss Challenge Method: A Brief Discussion*, MONDAQ, <https://www.mondaq.com/india/insolvencybankruptcy/1232462/swiss-challenge-method-a-brief-discussion>, Assess on March 25, 2023, 2:02 PM.
70. *Supra* note 18 at 6.
71. C. P. No. 1399/I&BP/2017.
72. C.P.1981(IB)/MB/2019.
73. *Supra* note 18.
74. *Id.*
75. *Id.*

76. *Id.*
77. Regulation 2(1)(ha), *The Insolvency and Bankruptcy Board of India (Insolvency Resolution of Corporate Persons) Regulations, 2016*".
78. *Quarterly Newsletter For Jul-Sep. 2021*, IBBI (2021).
79. *Supra* note 41.
80. Insolvency and Bankruptcy Code, 2016, § 25(2)(h), No. 31, Acts of Parliament, 2016 (India).
81. Deshmukh, Amitesh (2023) *Understanding Challenges In CIRP While Managing Business As Going Concern*, *Insolvency Tracker*, <https://insolvencytracker.in/2023/03/05/understanding-challenges-in-cirp-while-managing-business-as-going-concern/>, Assess on March 25, 2023, 2:09 PM.
82. *Supra* note 10.
83. Garg, Prithu and Singh, Shailendera (2020) *Resolution Plan Under IBC: An Albatross Around The Resolution Applicant's Neck*", *LIVELAW*, <https://www.livelaw.in/law-firms/articles/resolution-plan-under-ibc-an-albatross-around-the-resolution-applicants-neck-161708>, Assess on March 25, 2023, 3:40 PM.
84. *Id.*
85. *Supra* note 10.
86. *Supra* note 18.
87. *Id.*
88. *Id.*
89. Insolvency and Bankruptcy Code, 2016, § 30(2), No. 31, Acts of Parliament, 2016 (India).
90. *Supra* note 18.
91. *Supra* note 10.
92. *Supra* note 41, at 10.
93. *Supra* note 10.
94. *Id.*
95. *Supra* note 41.
96. Insolvency and Bankruptcy Code, 2016, § 30, No. 31, Acts of Parliament, 2016 (India).
97. *Supra* note 41.
98. *Id.*
99. Insolvency and Bankruptcy Code, 2016, § 53, No. 31, Acts of Parliament, 2016 (India).
100. Das, Awstika (2023) *NCLAT Chairperson Calls for IBC Amendment to Ensure Due Share for Operational Creditors; Stresses on Need to Train IRPs*", *Live Law*, <https://www.livelaw.in/top-stories/nclat-chairperson-calls-for-ibc-amendment-to-ensure-due-share-for-operational-creditors-stresses-on-need-to-train-irps-219654>, Assess on March 25, 2023, 6:17 PM)
101. *Supra* note 41.
102. IBC, 2016, § 3(10), No. 31, Acts of Parliament, 2016 (India).
103. IBC, 2016, § 5(7), No. 31.
104. IBC, 2016, § 5(8), No. 31, Acts of Parliament, 2016 (India).
105. IBC, 2016, § 5(20), No. 31.
106. IBC, 2016, § 5(21), No. 31, Acts of Parliament, 2016 (India).
107. *Supra* note 38.
108. *Supra* note 10.
109. *Id.*

110. Swiss Ribbons v Union of India (2019) SCC Online SC 73; “Akshay Jhunjunwala and Anr. v. Union of India” [W.P. No. 672 of 2017].
111. *Supra* note 41.
112. *Supra* note 10.
113. Insolvency and Bankruptcy Code, 2016, § 7(1), No. 31, Acts of Parliament, 2016 (India).
114. IBC, 2016, § 8, No. 31, Acts of Parliament, 2016 (India).
115. IBC, 2016, § 24(3)(c), No. 31, Acts of Parliament, 2016 (India).
116. IBC, 2016, § 7(3)(b), No. 31, Acts of Parliament, 2016 (India).
117. IBC, 2016, § 9(4), No. 31, Acts of Parliament, 2016 (India).
118. IBC, 2016, § 215, No. 31, Acts of Parliament, 2016 (India).
119. IBC, 2016, § 53(2), No. 31, Acts of Parliament, 2016 (India).
120. Justice Bhushan at the book launch of the second edition of Eastern Book Company’s ‘Insolvency and Bankruptcy Code’ by A.K. Mittal, while highlighting the need for amendment of section 53 of the Code said, “The maximum casualty is of the operational creditor who are at the very bottom of the distribution chain. The financial creditors take the major share, while the operational creditors get nothing”, <https://www-livelaw-in.elibraryhnl.u.remotexs.in/top-stories/nclat-chairperson-calls-for-ibc-amendment-to-ensure-due-share-for-operational-creditors-stresses-on-need-to-train-irps-219654>, Assess on March 25, 2023, 10:23 PM.
121. Committee of Creditors of Essar Steel India Limited (through authorized signatory) v. Satish Kumar Gupta and Others, (2020) 8 SCC 531.
122. India Resurgence Arc (P.) Ltd. v. Amit Metaliks Ltd [2021] 127 taxmann.com 610 (SC)
123. Sethi, Rajat and Agarwal, Aditi (2021) *India: Case Note: Judgement Of The Supreme Court In The Essar Steel Case*, Modaq, <https://www.mondaq.com/india/insolvencybankruptcy/1058270/case-note-judgement-of-the-supreme-court-in-the-essar-steel-case>, Assess on March 25, 2023, 10:49 PM.
124. *Id.*
125. IBC, 2016, § 4, No. 31, Acts of Parliament, 2016 (India).
126. Manhas, Anupam (2022) *Corporate Insolvency Laws: A Critical Analysis*, 5 INT’I J.L. MGMT. & HUMAN. 1378.
127. *Supra* note 81.
