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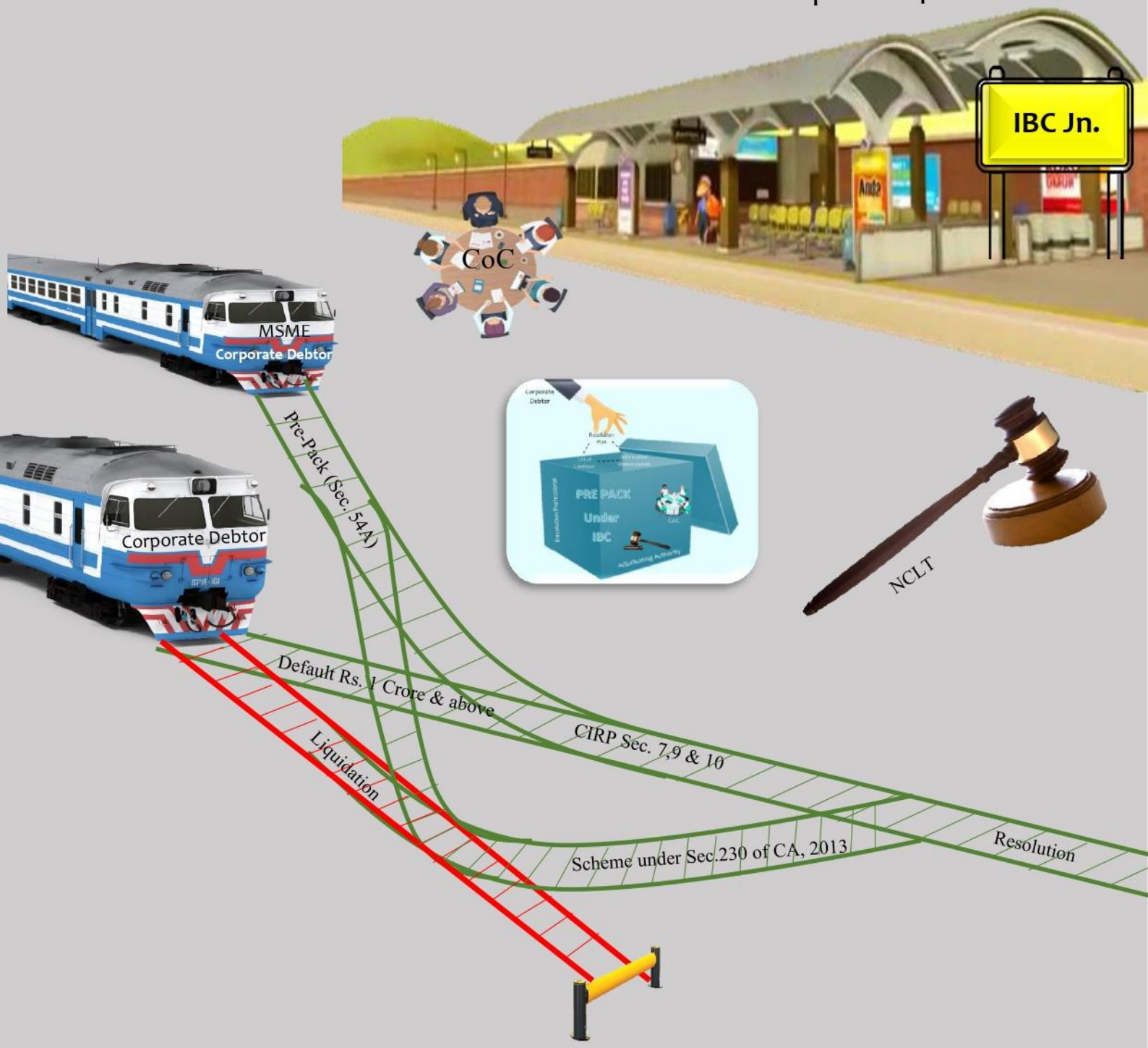

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குறள்: 385
இயற்றலும் ஈட்டலுங் காத்தலும் காத்த வகுத்தலும் வல்ல தரசு.

Thirukural: 385

He is a king who is able to acquire(wealth), to lay it up, to guard, and to distribute it.

From the Editor's Desk

Dear Readers of CGRF SandBox

We have great pleasure in wishing the esteemed readers of CGRF SandBox a brand-new financial year 2021-22. There is no doubt that the stark memories of lock-downs during 2020-21 will linger for some time for the unprecedented havoc it wrecked on the global economy. However, the Governments all over the world have taken proactive steps to cure the deeper wounds and infuse fresh blood. It's our pleasure to bring out the April 2021 Issue of CGRF SandBox on a very positive note as our economy is limping back to normalcy, or a new normal rather, showing strong signs of recovery.

True, there is a worrying trend of "second wave" of Covid-19 cases in a few States like Kerala, Karnataka, Maharashtra, etc. where the administration is battling to curb the spike in infection while at the same time keeping their fingers away from pressing the "lock-down" button.

Curtains are down on interest-on-interest? Not exactly...

Well, the Supreme Court has finally come out with its verdict that no interest on the unpaid interest shall be charged to the customers who availed moratorium on servicing their loans during the pandemic. The question – who has to foot the bill – is still unanswered. Lenders are seeking the Government support to bear the loss – estimated to be in the range of Rs.13,500 – Rs.14,000 crores (ICRA estimates). It makes sense for the Government to bear this cost as part of the several packages it announced for revival of the economy rather than leaving the banks to lick their wounds.

**** Stop Press ****

Pre-pack Insolvency Resolution for MSME

As we are getting ready for the launch of this issue, the Government has come out with an Ordinance on 4th April 2021 to introduce **"pre-packaged insolvency resolution process"** (PPIRP) for companies and LLPs coming under the definition of MSME sector.

A new Chapter IIIA has been introduced under Part II of Insolvency and Bankruptcy Code, adding 16 Sections, namely, 54A to 54P, to lay down the criteria for a corporate debtor to take this shorter and quicker route of pre-packaged insolvency resolution process. In addition, several other provisions have been amended in relation to PPIRP.

A quick glance reveals that "PPIRP" can be initiated only by a corporate debtor who is a MSME with default amount not exceeding Rs. 1 crore (to be notified), and who is eligible under Sec.29A to submit a resolution plan. On receipt of an application for such initiation and on approval by unrelated financial creditors with not less than 66% of financial debt, a resolution professional will be appointed. Stricter time-lines have been provided, like within 120 days, the entire PPIRP should be completed and that the resolution professional shall submit a resolution plan duly approved by the financial creditors within 90 days of the PPIRP commencement.

The devil is always in the detail. The fine-print of the PPIRP scheme needs to be seen in greater detail to appreciate the intent of the Government to bring about quicker resolution process for the distressed MSME sector. The rules and regulations are expected to be notified shortly. The attention of CGRF SandBox readers is invited to our issue for the month of February 2021 in which a write-up on PPIRP, (prior to the present ordinance) has been brought out. We are planning to hold a conference on PPIRP shortly, the details of which will be informed to our readers.

The will to succeed

Challenges do come in the way of every single living species on the earth. Those who have the indomitable spirit and the will to succeed only survive and march forward. CGRF SandBox Team believes that the new financial year has a lot more exciting things in store for the banking community, corporates and professionals. The only thing required is the will to succeed against all odds. All the very best to the readers for a wonderful fiscal year ahead.

Yours truly

S. Rajendran

Tax liability on sale of assets during liquidation under IBC

N. Nageswaran,
Insolvency Professional

Sale of immovable properties held as security interest either under statutorily provided auctions or by way of private sale to third parties by financial creditors has rampantly increased. This has been happening more under SARFAESI as a matter of fact and lesser under the provisions of Liquidation under IB Code. Naturally this has given rise to the questions on incidence of taxations on the property sold such as Tax Deducted at Source (TDS), Long Term Capital Gains Tax (LTCG) etc. We will, in this article, look into these aspects along with the relative provisions under SARFAESI Act and IB Code as well as select judicial pronouncements in this regard.

1. Tax Deducted at Source (TDS)

As per Finance Bill of 2013, TDS is applicable on sale of immoveable property wherein the sale consideration of the property exceeds or is equal to ₹ 50,00,000 (Rupees Fifty Lakhs). Sec 194 IA of the Income Tax Act, 1961 states that for all transactions with effect from June 1, 2013, Tax @ 1% or 0.75% should be deducted (depending upon the Date of Payment/Credit to the Seller) by the purchaser of the property at the time of making payment of sale consideration. Tax so deducted should be deposited to the Government Account through any of the authorised bank branches. The attempt was to find out whether the new provisions of the Income Tax u/s 194-IA introduced through the Finance Bill of 2013 are inconsistent with Section 53(1)(e) of the Code.

As it could be seen, it is the duty of the purchaser of any property worth more than Rs. 50 lacs to deduct 1% of the total value of the property and remit it to government account. The purchaser of the property need not have a Tax Account Number for reporting/remitting the TDS sale of property. However, PAN numbers of the seller (in this case the Corporate Debtor) and buyer are mandatory and the buyer need to have the same before entering into the purchase. Hence, the liquidator should ensure compliance of the deduction of TDS by the buyer. Of course, a question was raised by the Liquidator himself in the matter of Om Prakash Agarwal Vs. Chief Commissioner of Income Tax (TDS) who filed an application before NCLT, Principal Bench, New Delhi seeking direction against the successful bidder and the Income Tax Authority not to deduct TDS from the sale value of assets. The ground made out was that tax dues cannot be collected by the Government in priority to the waterfall mechanism under Section 53 and Section 238 has an overriding effect upon other enactments. The Tribunal declined to issue such directions observing that the deduction of tax at source under Section 194A of the IT Act does not mean assessment and raising demand for collection of tax by the Department. Collection of tax will arise only after passing orders under the IT Act subsequent to filing of Income Tax Return by the assesses. The deduction of TDS does not tantamount to payment of Government dues in priority to other creditors because it is not a tax demand for realization of tax dues. It is the duty of the purchaser to credit TDS to the Income Tax Department. It also observed that the liquidator is not asked to pay TDS; it is the duty of the purchaser to credit TDS to the Income Tax Department.

(Image source: website)

The liquidator went on appeal to NCLAT. During the hearing the Appellate Authority went in detail into every related aspect of both IT Act and the Code and finally declared on 8th feb 2021 that the orders of the NCLT asking the purchaser to deduct and remit the TDS is erroneous. The order of NCLAT confirmed that the deduction of Tax at source is in fact raising of a demand for collection of tax by the Department. Actually TDS under Section 194 IA, is an advance capital gain tax, recovered through transferee on priority with other creditors of the corporate debtor which is into liquidation. Thus it is inconsistent with the provision of Sec 53 (1) (e) of the Code and by virtue of Section 238 of the Code, the provision of Sec 53 (1) (e) shall have overriding effect.

The position of law is that the purchaser of a property need not deduct TDS equivalent to 1% of the bid value he is putting in.

2. Long Term Capital Gains Tax (LTCG)

Three questions normally arise while the assets of the corporate debtor are sold under liquidation as to whether there will be an incidence of tax on the capital gains. If the answer is in affirmative, further question arises whether that payment to tax authorities is to be treated as a cost of liquidation and paid before taking up the distribution of the sale proceeds to the creditors or such payments need to be treated as a claim and put in

appropriate place as per the water fall mechanism suggested under Sec 53 of IB Code. The related provisions of Income Tax Act are spelt out under Sections 178 and 179. It may be worthwhile to nation that the IBC while enacted in 2016 amended Sec 178(6) of IT Act giving an overriding position to IBC.

The above questions are settled in the matter of Ms. Pooja Bahry, Liquidator and Anr. Vs. Gee Ispat Pvt. Ltd. where the liquidator sold certain properties relinquished by the secured creditors. The question was whether the liquidator is required to deposit the capital gains tax on sale of the secured assets and include it in the liquidation cost. It was noted that a secured creditor is entitled to effect sale under the SARFAESI Act and appropriate the entire amount towards its dues, without any liability to first pay capital gain tax. If the capital gain tax is first to be provided for, and then be included as liquidation cost, it would create an anomalous situation in the secured creditor getting a lesser remittance than what it could have realised had it not relinquished its security interest for adding it into the Liquidation Estate. Hence the AA held vide order dt. 22nd oct. 2019 that "the tax liability arising out of the sale shall be distributed in accordance with the provisions of Sec 53 of the Code. The applicability of Section 178 or 194 IA of the IT Act will not have an overriding effect on the water fall mechanism provided under Section 53 of the Code, which is a complete Code in itself, and the capital gain shall not be taken into consideration as the liquidation cost."

Conclusion

In conclusion, the issues discussed above show that the nitty-gritties of the taxation system vis-à-vis the objective of the IB Code are the next line of challenges that may require a conclusive position of law. One thing is certain that the breadth of the tax laws and the traditional priority of the claims under it have certainly taken a subordinate position in a lot of issues post the enactment of the IB Code.

MCA Amendment

MCA has, vide notification dated 18th March 2021 amended Section 149, Section 247 and Schedule V of the companies Act 2013, which paves way for companies to provide remuneration to non-executive directors including Independent Directors in case of loss or inadequate profit also.

LLP vs Private Limited Companies – pros and cons from a lender's perspective

CGRF Bureau

Private Limited Company vs Limited Liability Partnership (LLP) – A Comparison

A growing business needs the right business structure. With so much to consider in building a business such as preparing a business plan, analysing, setting up a team, competition, raising capital, etc., the ease of commencing a sole proprietorship can be felt as a relief. Also item one can begin business without formal registration with minimal upfront costs.

Sole Proprietorship & Partnership

Though sole proprietorship is a simple and flexible way to scale up operations, there are risks associated, too. The personal liability of a sole proprietor represents risk, and, for this reason, banks can be hesitant to lend money or issue credit under this business structure. It is also more difficult for a sole proprietor to generate funds from investors, as the business structure is not formally recognized and is not designated to have shareholders.

Partnership firms registered or unregistered have their own shortcomings when legal issues crop up.

(Image source: website)

Private Limited Companies and LLP

Smaller business ventures had the only option of forming a private limited company till 2008. Since the adoption of the Limited Liability Partnership Act, 2008, there is now more flexibility for corporate organizations. It is therefore critical not only for the entrepreneurs but also banks to know the pros and cons of each business enterprise in order to understand their legal characteristics, compliance issues and managerial perspectives.

Comparing the advantages and disadvantage of these two business structure is especially important in selecting the suitable structure by an entrepreneur.

S. No.	Particulars	Private Limited Company	Limited Liability Partnership (LLP)
a)	Applicable Law	Companies Act, 2013	Limited Liability Partnership Act, 2008
b)	Minimum Share Capital/ Contribution	Nil	Nil
c)	No. of Members/ Partners	Minimum: 02 Maximum: 200	Minimum: 02 Maximum: No Limit
d)	No. of Directors / Designated Partners	Minimum: 02 Maximum 15	Minimum: 02 Maximum: No Limit
e)	Meeting for Management Decisions	Minimum 2 or 4 Board Meetings in a Financial Year & An Annual General Meeting for every Financial Year	No requirements for Meetings. Decision can be taken as per LLP Agreement
f)	Statutory Audit	Mandatory	Not compulsory unless partners' contribution exceeds Rs.25 lakhs or Annual Turnover Exceeds Rs.40 lakhs
g)	Annual Filing	Annual Audited Financial Statement (in Form AOC-4) & Annual Return (in Form MGT-7) with Registrar of Companies	Statement of Accounts and Solvency (in Form 8) and Annual Return (in Form 11) with Registrar of Companies
h)	Cost of setting up including fees to professionals	Rs. 50,000/- approximately	Rs. 25,000/- approximately
i)	Compliance Cost per annum	Depends on the volume of business. Rs. 25,000 to Rs. 50,000 p.a. approximately	Depends on the size of business Rs. 15,000 to 50,000 p.a. approximately
j)	Liability of Shareholders / Partners	Limited	Limited
k)	Transferability of shares	In compliance with the restrictions, if any, imposed in the Articles of Association, shares may be transferred	By mutual consent between the Partners, the capital contribution can be changed.
l)	Name	Should end with "Private Limited"	Should end with "LLP"
m)	Status	Recognised as Separate Legal Entity	Recognised as Separate Legal Entity
n)	Registers and Records	Required to maintain certain Statutory Registers, Records and to keep Minutes of Board Meetings and General Meetings from time to time	Not required, unless specifically mandated by LLP Agreement
o)	Tax Rate	Company is taxable at 25% - 30% on Net Profit (plus surcharge and cess)	LLP is taxable at 30% on Net Profit (plus surcharge and cess)
p)	Dividend Distribution Tax	Dividend distributed to Shareholders are taxable in the hands of the Shareholders. There is no DDT.	Share of Profits to Partners is not taxable in the hands of Partners
q)	Penalties for non-compliance in respect of annual compliances	Penalty of Rs. 100 per day for delay	Penalty of Rs. 100 per day for delay
r)	Legal Authority for filing application, Appeal etc.,	Jurisdictional NCLT, NCLAT	Jurisdictional NCLT, NCLAT

Advantages for banks in dealing with companies

Banks also face problems in funding to sole proprietorships since the owners' personal financials are tied directly to the business. This means that if the business goes bankrupt, so does the business owners. This makes the sole proprietorship a lot more riskier from lenders perspective.

Banks have now been shifting focus in funding to Private Companies and LLP compared to funding to Sole Proprietorships.

Apart from their individual income tax return filing, there is no requirement for the sole proprietorship to maintain any statutory records. Since there is no separate audit procedures / filing of returns with Registrar, the Banks are kept in dark and find difficult to monitor and track the performance of the sole proprietorship concern. Hence, Banks should have some threshold limit for funding to the sole proprietorships and beyond that threshold limit the Banks should insist the sole proprietorship to restructure their business either into Private Company or LLP enabling them to monitor and take corrective actions in time.

IBC Amendment

The Insolvency and Bankruptcy Board of India (IBBI) has issued notification dated 15th March 2021 to further amend the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 by inserting a new Regulation 12A. This regulation provides for updating of claims by the creditors, as and when the claim is satisfied, partly or fully, during the CIRP. To monitor the progress in line with the regulation 40B (1A), the IRP/RP is required to report the status of CIRP in Form CIRP-7.

Filing of Secretarial Audit Report in XBRL mode with Stock Exchanges

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Introduction

eXtensible Business Reporting Language (XBRL) is a software standard that was developed to improve the way in which financial data is communicated, making it easier to compile and share the data.

XBRL is a data-rich dialect of XML **(eXtensible Markup Language),** the universally preferred language for transmitting information via the Internet. It was developed specifically to communicate information between businesses and other users of financial information, such as analysts, investors and regulators. XBRL provides a common, electronic format for business reporting. It does not change what is being reported. It only changes how it is reported.

Currently, financial statements along with board's report and its annexures are filed in XBRL mode with the Registrar of Companies by listed companies and certain class of other companies. The stock exchanges i.e. BSE and NSE both have now come out with notification that they are also adopting the XBRL taxonomy as issued by the Ministry of Corporate Affairs for filing the compliance documents for listed companies. This will greatly enable the companies for ease of filing since the format being the same. With the recent notification issued by stock exchanges, all the listed entities can submit to the stock exchange(s), the annual report prepared using the XBRL taxonomy of Ministry of Corporate Affairs, itself.

Provisions under Companies Act 2013 on secretarial audit report

Section 204 of the Companies Act 2013 mandates that listed companies and certain other companies to conduct the secretarial audit. As we are all aware, the secretarial Audit is a process to check compliance with the provisions of various laws and rules/ regulations/ procedures, maintenance of books, records etc., by an independent practising Company Secretary to ensure that the company has complied with the legal and procedural requirements and also followed due processes. It is essentially a mechanism to monitor compliance with the requirements of stated laws and processes and the secretarial audit helps to detect any non-compliance by

the Company following which, the company could take necessary rectification action.

Appointment of secretarial auditor / intimation to ROC

The companies who are covered for the provisions of secretarial audit are required to appoint a secretarial auditor, each financial year for carrying out the secretarial audit. The appointment of the secretarial auditor is required to be done in a duly convened board meeting and the secretarial auditor needs to be appointed. After the appointment is done, the listed companies and also unlisted public companies are required to file MGT 14 form with the Ministry of Corporate Affairs within a period of 30 days. The private companies are exempted in filing the form MGT-14.

Secretarial audit report and its format

The secretarial auditor, upon conducting the audit of the company's secretarial and related records for the particular financial year would submit his report.

The secretarial audit report is issued by the practicing company secretary pursuant to section 204(1) of the Companies Act 2013 and Rule 9 of the Companies (Appointment and Remuneration of Managerial Personnel) Rules 2014 in the specified form MR-3.

Secretarial Audit Report is annexed to Board Report

The secretarial audit report forms part of the board's report as an annexure and it is required to be sent along with the annual report to the members of the company. Upon adoption of the financial statements along with the board's report, the annexures are also required to be filed with MCA.

Time limit for filing the secretarial audit report with MCA

As per the provisions of sub-section (1) section 137 of the Companies Act 2013, the financial statements, including consolidated financial statement if any along with all the documents which are required to be attached to such financial statements are required to be filed within thirty days of the date of annual general meeting with the Registrar of Companies.

Prescribed form for filing with ROC

The financial statements, board's report and its annexures all are required to be filed in XBRL format in the prescribed Form AOC-4 in the case of listed companies and certain other class of companies. Secretarial audit report is one of the annexures to the board report.

Provision under LODR on secretarial audit report for listed companies

As per Regulation 24A of the SEBI (Listing obligation and Disclosure Requirement) Regulations 2015, every listed company and its material unlisted subsidiaries are required to undertake secretarial audit and required to annex with its annual report, a secretarial audit report, given by a company secretary in practice.

Filing requirement of secretarial audit report for listed companies under LODR

Securities and Exchange Board of India vide its Circular CIR/CFD/CMD1/27/2019 dated 8th February 2019 has, (earlier) prescribed the format on annual secretarial compliance report issued by the practicing company secretary, which is required to be filed with the stock exchange(s) where the company's securities are listed. The companies are required to file the secretarial audit report (Regulation 34 of LODR) in PDF mode with the stock exchanges where the company's securities are listed till now.

Latest notification by SEBI

On 31st March 2021, Bombay Stock Exchange (BSE) has issued a notification bearing no 20210331-2 on filing of annual secretarial compliance report in XBRL mode by companies. Similar notification has also been issued by National Stock Exchange (NSE). As per these circulars, the listed companies are now required to file the annual secretarial compliance report in XBRL mode under the provisions of Securities and Exchange Board of India (Listing Obligation and Disclosure Requirements) Regulations 2015 and the effect of this notification is said to be with "immediate effect". XBRL format is the one which is used for filing the annual financial statements at the MCA site as seen earlier.

(Image source: website)

Filing in XBRL mode is in addition to filing of PDF mode

The notification issued by the Stock Exchange (s) spells out that the XBRL filing of the annual secretarial compliance report is in addition to filing the same in PDF mode. This means, the companies are required to file the annual secretarial compliance report through XBRL mode, in addition to the filing in PDF mode which is already in existence.

Time limit for filing the annual secretarial compliance report

The annual secretarial compliance report is required to be filed with the stock exchange(s) by the listed companies within 60 days of end of the financial year.

Conclusion

Earlier, the stock exchange(s) have prescribed customized and distinct electronic compliance filing platforms for the listed companies. Listed companies are required to adhere to the specified format by the stock exchange(s) and ensure the filing of the documents. It may be noted that listed companies are also required to file the documents with MCA separately under the provisions of the Companies Act 2013 and the annual financial statements filing mode is XBRL.

This has resulted in duplication of efforts for the listed companies i.e. XBRL format for MCA filing and customized format filing for stock exchange(s). By and large this issue is now being addressed by stock exchanges by following an identical and standardized structures for compliance filings and adopt filing structures of MCA.

Since both the National Stock Exchange and Bombay Stock Exchange have decided to introduce XBRL based compliance filing mechanism featuring identical and homogenous compliance data structures between Stock Exchanges / MCA, this would help listed companies to use the compliance data generated in XBRL format with MCA as well as with the stock exchanges.

Lastly, the XBRL mode of filing would also increase efficiency and accuracy and enhance reliability for the users. By presenting its statements in XBRL, a company can facilitate collation of data by the regulators for meaningful analysis by using computer algorithms.

Credit Guarantee Scheme for Subordinate Debt (CGSSD) extended upto 30.09.2021

A Scheme (Credit Guarantee Scheme for Subordinate Debt) was approved by the Government of India, was launched on 24th June 2020 to provide credit facility through lending institutions to the promoters of stressed MSMEs, who are eligible for restructuring as per RBI guidelines. This scheme was to expire on 31.03.2021. Government of India has now extended the Scheme for six months from 31.03.2021 to 30.09.2021

Interplay of Section 230 of Companies Act, 2013 with IBC

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Insolvency Professional

Backdrop

The provisions of Sec.230 of Companies Act, 2013 deal with measures for: -

- restructuring of companies by way of compromise or arrangement with creditors and members, and/or
- merger and amalgamation.

Prior to the enactment of Insolvency and Bankruptcy Code in 2016, Sections 230 to 240 of Chapter XV of Companies Act, 2013 were widely used for restructuring of healthy as well as ailing companies. Afterwards, with the landmark judgment by Hon'ble National Company Law Appellate Tribunal (NCLAT) in Shivram Prasad Vs. S. Dhanapal & Others on 27th Feb. 2019, Sec.230 of Companies Act got itself entangled with the provisions of Insolvency and Bankruptcy Code, 2016 (IBC).

Interestingly, while merger and amalgamation of companies were resorted to for restructuring, aiming at certain tax advantages and other benefits, the NCLAT order referred above, brought to the fore the amendment made in 2016 in Sec.230 of Companies Act, 2013 by which the liquidator appointed under IBC may also file an application to the National Company Law Tribunal (NCLT) in the case of a compromise or arrangement proposed between a corporate debtor and its creditors or members in order to revive the corporate debtor.

Section 230 of CA 2013 empowers the NCLT to make an order on the application of the company or creditor/member or in the case of company being wound up by the liquidator for the proposed compromise or arrangements including Corporate Debt Restructuring (CDR). Under this Section, a compromise or an arrangement may take place between a company and its creditors or any subset of creditors; or between a company and its members or subset of members. Prior to November 15, 2016, an application for compromise or arrangement could be moved before the Tribunal by (i) the company; (ii) a creditor; (iii) a member of the company; and (iv) in the case of a company which is being wound up, by the liquidator. However, with the amendment to Section 230 of the Act which came into effect from November 15,

2016, an application under Section 230 of the Act could be presented by a liquidator who has been appointed under the Act of 2013 or under the IBC. A liquidator appointed under the IBC, when invoking the provisions of Section 230 of the Act, attempts for revival of the corporate debtor to save it from the likelihood of a corporate death. Section 230 allows the liquidator of a company undergoing liquidation to file an application before the NCLT to seek sanction for a scheme of arrangement between the company and its creditors and, where applicable, its members. While some argue that a compromise or arrangement scheme under Sec.230 can be given only by a creditor or a member, a larger perspective has been that even a person other than a creditor or member can also propose a scheme for compromise or arrangement.

This article examines the context in which provisions of Sec.230 of Companies Act, 2013 are now brought into play under an IBC regime and the spate of amendments in IBC as well as the IBBI Regulations pursuant to the abovesaid NCLAT order.

Challenges faced after NCLAT order dt. 27th February 2019

After the NCLAT order, questions were raised at various forums whether resorting to Sec.230 of Companies Act, 2013 will undermine the IBC process inasmuch as the ineligibility under Sec.29A was not applicable and the defaulting promoters would be able to wrest control of the company in liquidation through backdoor. In this context, it would be relevant to examine the amendments brought in subsequently, addressing the above questions and validating the Sec.230 process.

Core objective of IBC

The preamble to IBC captures the objectives as reorganisation and insolvency resolution of corporate persons in a time bound manner for maximisation of value of assets of such persons, to promote entrepreneurship, availability of credit and balance the interests of all the stakeholders. In many a decision of the courts, this preamble has been highlighted to say that **insolvency resolution is the primary objective and liquidation is the last resort.** This view has been in the minds of NCLAT when the order was pronounced in Shivaram Prasad case.

At this juncture, it is important to remember that the Appellate Authority in the matter of *Y. Shivram Prasad vs S. Dhanapal and Ors. Comp. Appeal AT Ins. 224 of 2018 dated 27.02.2019,* raised the question as to what steps should a liquidator take during the liquidation process. In the said case, an order of liquidation had been passed by the Adjudicating Authority as there was no CoC approved resolution plan at the end of the expiry of the 270 days. The former promoters of the corporate debtor had challenged the order of liquidation, whereby, the Appellate Authority for the first time held that the intention of the Code is revival of the corporate debtor and therefore the liquidator is required to take steps under Section 230 of the Companies Act, 2013 inviting a scheme of compromise or arrangement in terms of the aforesaid order. The Appellate Authority further held that on failure to achieve a compromise, the liquidator may proceed to sell the assets of the corporate debtor.

The Insolvency Law Committee in its Report of February, 2020 stated that, for companies under liquidation, the inviting of schemes of compromise of arrangement under Section 230 to 232 of the Companies Act, 2013, was not part of the original framework. The order in *Y. Shivram Prasad vs S. Dhanapal and Ors.*, had led to multiplicity of proceedings such as the inconsistency between the dual roles of NCLT as a supervisory under the IBC and a driving Tribunal under the Companies Act, 2013. However, the judicial intervention by the NCLAT along with the introduction of a new regulation in terms of Regulation 2B of the IBBI (Liquidation Process) Regulations, 2016 by the IBBI have led to some streamlining in the two frameworks, the Committee noted. The introduction of Regulation 2B of the IBBI (Liquidation Process) Regulations, 2016 was a result, in the nature of clarification, issued by the IBBI, as the ambiguity in the application of these two frameworks became clearer.

(Image source: website)

The Committee further noted that introduction of such schemes will lead to enormous delays, as it did under the Sick Industrial Companies Act, 1985, and if at all the benefits of such schemes are intended to be to be brought it, they should be introduced under the IBC itself and not under the Companies Act.

Amendments in IBC and Regulations regarding merger, amalgamation and demerger during Corporate Insolvency Resolution Process (CIRP)

In this context, it would be relevant to take note of the amendment made to Sec.5(26) of IBC which defines a resolution plan. As per this clause, "resolution plan" means a plan proposed by resolution applicant for insolvency resolution of the corporate debtor as a going concern in accordance with Part II (dealing with corporate persons' insolvency resolution). With effect from 16th Aug. 2019, an explanation was added to Sec.5(26) as below:

> *"Explanation: For the removal of doubts, it is hereby clarified that a resolution plan may*

include provisions for the restructuring of the corporate debtor, including by way of merger, amalgamation and demerger."

As a follow up measure, the Reg.37 of IBBI (IRPCP) Regulations was amended with effect from 27th Nov. 2019 in the context of the measures which a resolution plan shall provide for insolvency resolution of the corporate debtor for maximisation of value of its assets:

> "*(ba) restructuring of the corporate debtor, by way of merger, amalgamation and demerger."*

It is significant to note that these amendments came much after the NCLAT order in Shivram Prasad Vs. S. Dhanapal & Others. However, in none of these amendments, the provisions relating to Sec.230 of the Companies Act were invoked or referred.

Amendments in IBC and Regulations regarding merger, amalgamation and demerger during liquidation

It is interesting to note that there has been no amendment in IBC with reference to restructuring by way of merger, amalgamation and demerger during liquidation process while at the same time, a few amendments have been notified in the IBBI Regulations. Let us examine them now.

Reg.39D of IBBI (IRPCP) Regulations, inserted with effect from 25th July 2019, speaks about the fee of the liquidator. This Regulation stipulates that the Committee of Creditors (CoC), while approving a resolution plan under Sec.30 or deciding to liquidate the corporate debtor under Sec.33, may, in consultation with the resolution professional, fix the fees payable to the liquidator, for the period, if any, used for: -

- **compromise or arrangement under Sec.230 of Companies Act, 2013;**
- sale under clauses (e) and (f) of Reg.32 of IBBI (Liquidation Process) Regulations, i.e. sale of corporate debtor as a going concern and sale of the business of the corporate debtor as a going concern; and
- the balance period of liquidation.

Reg.2(ea) of IBBI (Liquidation Process) Regulations which was inserted with effect from 25th July 2019, while defining liquidation cost, states that the cost if any, incurred by the liquidator in relation to compromise or arrangement under Sec.230 of Companies Act, 2013 shall not form part of liquidation cost.

Further, Reg.2B has been inserted with effect from 25th July 2019 which deals with **"Compromise or arrangement"**. It says that where a compromise or arrangement is proposed under Sec.230 of the Companies Act, 2013, it shall be completed within ninety days of the order of liquidation. Interestingly, a proviso has been added in this Regulation with effect from 6th Jan. 2020 to say that "a person, who is not eligible under the Code to submit a resolution plan for insolvency resolution of the corporate debtor, shall not be a party in any manner to such compromise or arrangement".

Reg. 4 of IBBI (Liquidation Process) Regulations, amended with effect from 5th Aug. 2020, provides that where the liquidator fee has not been decided as per Reg.39D of IBBI (IRPCP) Regulations, the liquidator shall be entitled to a fee at the same rate as RP was entitled during the CIRP for the period of compromise or arrangement under Sec.230 of Companies Act, 2013.

It is apparently clear that after the NCLAT judgment in Feb. 2019 showing the way for a liquidator to proceed under Sec.230 of Companies Act, 2013, amendments have been made in several provisions.

Sec.230 scheme in the matter of M/s.Nagarjuna Oil Corporation Ltd.

In the matter of Liquidation Process of Nagarjuna Oil Corporation Limited, the Adjudicating Authority vide orders dated 19.03.2021 in CP/546/CAA/2020 allowed the application filed by the liquidator under Section 230 of the Companies Act, 2013 whereby, the scheme of compromise between the corporate debtor and its creditors for takeover of its assets and properties by M/s. Haldia Petrochemicals Limited was approved. It is pertinent to note that the scheme of compromise approved was received from one of the bidders during the resolution process of the corporate debtor.

Why there is no provision in IBC for the RP to file an application under Sec.230

During CIRP, resolution plans are invited which can contain provisions for restructuring including merger, amalgamation and demerger. In those cases, the resolution plan duly approved by the CoC is filed under Sec.30(6) of IBC by the RP with the Adjudicating Authority for its approval. Hence, there is no separate provision made in the Code for moving such an application under Sec.230 since the Authority under Companies Act, 2013 is the same NCLT which is approving the resolution plan under Sec.31 of IBC.

When approved by the NCLT, the scheme binds the company, its members and its creditors. It is also possible for third parties to propose and contractually agree to be bound by a scheme of compromise or arrangement.

In this regard, it would be pertinent to examine the recent decisions of NCLAT and the Supreme Court.

NCLAT, in Gujarat NRE Coke case, ruled on 24th Oct. 2019 that ineligible promoters cannot reclaim control via scheme of arrangement under the Companies Act.

Section 29A was inserted in the IBC to keep out errant and wilful defaulters from buying back stressed assets. This was essential to prevent chronic defaulters and

fraudulent promoters from gaming the system and taking back control of their company at a fraction of what they owed to lenders. The provision has served the intended purpose in many cases (as in the Essar Steel case). But there was lack of clarity on how the provision will apply in liquidation proceedings in the case of scheme of arrangement under Section 230 of the Companies Act.

When resolution fails and the debtor goes into liquidation, the adjudicating authority has, in the past, directed the liquidator to consider provisions of Section 230 of Companies Act, 2013, which deals with 'Power to Compromise or Make Arrangements with Creditors and Members'. It had been unclear whether promoters ineligible under Section 29 A of the IBC can participate in the scheme of arrangement under Section 230 of the Companies Act.

In its order in the Gujarat NRE Coke case, the NCLAT has removed the ambiguity around this and held that promoters ineligible under Section 29A of the IBC cannot participate in the scheme of arrangement under Section 230 of the Companies Act.

The Supreme Court, in the oft-quoted Swiss Robbins case, had observed that "the Preamble does not, in any manner, refer to liquidation, which is only availed of as a last resort, if there is either no resolution plan or the resolution plans submitted are not up to the mark. Even in liquidation, the liquidator can sell the business of the corporate debtor as a going concern". Hence, the NCLAT ruling in the the SC Sekaran vs Amit Gupta case (January 2019 order) had cited the Meghal Homes vs Shree Niwas Girni KK Samiti case, in which the Supreme Court upheld the provisions under Section 391 of the Companies Act, 1956, and Section 230 of the Companies Act, 2013. These provisions give the liquidator (resolution professional under IBC) the right to propose a compromise or arrangement with creditors and members (shareholders) even in the case of a company which is being wound up. Section 230 of the Companies Act, in effect, deals with 'Power to Compromise or Make Arrangements with Creditors and Members', which may include reconstruction or amalgamation/merger/demerger of companies or reduction of share capital or even corporate debt restructuring. While Section 29 A debars errant promoters from bidding in the resolution process, it was unclear if it specifically precluded them from participating in the scheme of arrangement under Section 230 of the Companies Act.

In the Gujarat NRE Coke case, the question raised was whether Arun Kumar Jagatramka (promoter of Gujarat NRE Coke Ltd.), ineligible under Section 29A of the Code to be a resolution applicant (buyer), could ask for a financial scheme of comprise and arrangement under Section 230 of the Companies Act. NCLAT held that "even during the period of liquidation, the 'Corporate Debtor' is to be saved from its own management, meaning thereby that the promoters who are ineligible under Section 29A are not entitled to file application for compromise and arrangement in their favour under Section 230 to 232 of the Companies Act."

Hence, a promoter, ineligible under Section 29A of the Code, cannot make an application for compromise and arrangement for taking back the immovable and movable property or actionable claims of the debtor. Aggrieved by the order of NCLAT, Mr. Arun Kumar Jagatramka filed an appeal before the Apex Court.

Final say of Supreme Court in Arun Kumar Jagatramka Case on 15th March 2021

Recently, SC examined the interplay between liquidation proceedings under IBC and Section 230 of the Companies Act, 2013. The issue before the Supreme Court was to decide whether a person ineligible to submit resolution plan under Section 29A of the IBC is barred from proposing a scheme under Section 230 of the Companies Act. ***The Supreme Court held that a person who is ineligible under Section 29A of the Insolvency Bankruptcy Code to submit a resolution plan, cannot propose scheme of compromise & arrangement***

The Hon'ble Supreme Court stated that primarily, the IBC is a legislation aimed at re-organization and resolution of insolvencies. Liquidation is a matter of last resort. These objectives can be achieved only through a purposive interpretation which requires courts, while infusing meaning and content to its provisions, to ensure that the problems which beset the earlier regime do not enter through the backdoor through disingenuous stratagems.

(Image source: website)

The Hon'ble Supreme Court went through its various judgments on the subject and observed that it had been held that Section 29A has been enacted in the larger public interest and to facilitate effective corporate governance. It was further held that Parliament rectified a loophole in the Act which allowed backdoor entry to erstwhile managements in the CIRP. (In another case, the Hon'ble Supreme Court had held that the norm underlying Section 29A continues to permeate Section 35(1)(f) when it applies not merely to resolution applicants, but to liquidation also. The plea that Section 35(1)(f) is ultra vires was also rejected.)

The Hon'ble Supreme Court further observed that under Sub-section (6) of Section 230, the comprise or arrangement has to be agreed to by a majority of persons

representing three fourth in value of the creditors, members or a class of them. Upon the sanctioning of the compromise or arrangement by the NCLT, it binds the company, all the creditors or members or a class of them, as may be, or in the case of a company being wound up, the liquidator appointed under the Act of 2013 or the IBC and the contributories.

The Hon'ble Supreme Court further noted that there is no reference in the body of the IBC to a scheme of compromise or arrangement under Section 230 of the Companies Act 2013. Sub-section (1) of Section 230 was however amended in 2016 to allow for a scheme of compromise or arrangement being proposed on the application of a liquidator who has been appointed under the provisions of the IBC.

The Hon'ble Supreme Court observed that NCLAT in the course of its decision observed that during the liquidation process the steps which are required to be taken by the liquidator include a compromise or arrangement in terms of Section 230 of the Companies Act 2013, so as to ensure the revival and continuance of the corporate debtor by protecting it from its management and from "a death by liquidation". The decision by NCLAT took note of the fact that while passing the order under Section 230, the Adjudicating Authority would perform a dual role: one as the Adjudicating Authority in the matter of liquidation under the IBC and the other as a Tribunal for passing an order under Section 230 of the Act of 2013. Following the decision of NCLAT, an amendment was made in 2019 to the Liquidation Process Regulations by the IBBI so as to refer to the process envisaged under Section 230 of the Act of 2013.

The Hon'ble Supreme Court stated that it is difficult to accept the submission of the appellant that Section 230 of the Companies Act 2013 is a standalone provision which has no connect with the provisions of the IBC. It stated that undoubtedly, Section 230 is wider in its ambit in the sense that it is not confined only to a company in liquidation or to corporate debtor which is being wound up under Chapter III of the IBC. Obviously, therefore, the rigors of the IBC will not apply to proceedings under Section 230 of the Companies Act 2013 where the scheme of compromise or arrangement proposed is in relation to an entity which is not the subject of a proceeding under the IBC. But, when, as in the present case, the process of invoking the provisions of Section 230 traces its origin or, as it may be described, the trigger to the liquidation proceedings which had been initiated under the IBC, it becomes necessary to read both sets of provisions in harmony. A harmonious construction between the two statutes would ensure that while on the one hand a scheme of compromise or arrangement under Section 230 is being pursued, this takes place in a manner which is consistent with the underlying principles of the IBC because the scheme is proposed in respect of an entity which is undergoing liquidation under Chapter III of the IBC. As such, the company has to be protected from its management and a corporate death. It would lead to a manifest absurdity if the very persons who are ineligible for submitting a resolution plan, participating in the sale of assets of the company in liquidation or participating in the sale of the corporate debtor as a 'going concern', are somehow permitted to propose a compromise or arrangement under Section 230 of the Companies Act 2013.

The Hon'ble Supreme Court held that prohibition placed by the Parliament in Section 29A and Section 35(1)(f) of the IBC must also attach itself to a scheme of compromise or arrangement under Section 230 of the Companies Act 2013, when the company is undergoing liquidation under the auspices of the IBC. As such, Regulation 2B of the Liquidation Process Regulations, specifically the proviso to Regulation 2B (1), was also held to be constitutionally valid.

(Image source: website)

When the IBC was introduced, the provisions did not contain any restrictions for any person in submitting a resolution plan or participating in the acquisition process of the assets of a company at the time of liquidation. However, certain concerns were raised that individuals (who were the cause for the default) could take advantage of the situation and participate in the resolution or liquidation process. In fact, there were couple of instances were with huge haircuts to creditors, the promoters have acquired the corporate debtor. As a result, Section 29A was introduced in IBC to ensure individuals, who by their misconduct contributed to the defaults of the corporate debtor were prevented from gaining or regaining control of the corporate debtor. This Section 29A was inserted with retrospective effect (from 23/11/2017) containing almost an exhaustive list of individuals/entities who were ineligible to be resolution applicants to prevent backdoor entry under CIRP and liquidation.

The liquidator under IBC is vested with several powers and duties. The liquidator exercises several functions which are of quasi-judicial in nature. However, under Section 35(1)(f), a restriction is placed on him that the liquidator cannot sell the immovable and movable property or actionable claims of the corporate debtor in liquidation to any person who is not eligible to be a resolution applicant.

Whether the schemes can provide for retention of existing promoters/management

This question becomes relevant in the context to understand how and in what manner the schemes can impact section 29A persons. Generally, such persons would be majority shareholders of the corporate debtor. Is it possible to contend that even though a section 29A person will not qualify to propose a scheme under section 230, the rights of such persons as shareholders/directors can remain intact under the scheme? Is it possible to maintain status quo and/or retain substantial shareholding and management rights of the former promoters under the scheme?

Say for instance, there is a proposed scheme which envisages one-time settlement such that 'A', an outsider, infuses loan into the company to pay-off its existing lenders, without any substantial change in existing shareholding/management structure of the company. Assuming that the scheme gets requisite approval(s) from creditors/members, can the scheme be rejected by the NCLT?

Retention of existing management/promoters might not be directly hit by section 29A; however, the question as to its tenability is yet to be examined. In any case, it must be emphasised that the objective of the Code is not to oust the management, who might have failed for purely no fault of their own, but to revive the company, and promote entrepreneurship. While in general, an incoming resolution applicant/scheme proposer would induct fresh equity and managerial resource into the company, there might be cases where the resolution applicant/proposer of scheme requires continued presence of existing management for the latter's expertise, which might be necessary for revival of the business. Further, section 29A or any other provision of the Code no-where debars continuation of existing management/promoters. Hence, each case will have to be assessed separately.

Participation by ineligible promoters under Sec.29A in the class meetings under Sec.230

Another interesting question is whether persons ineligible under section 29A can **participate and vote** in the class meetings. Will such persons be entitled to notice of the meetings and a copy of the schemes?

In our view, applying the principles of natural justice, the promoters need to be involved in the process, much like Sec.24 of IBC where the directors (whose powers stand suspended during CIRP) can participate in the meetings of the CoC.

Immunity under Sec.32A of I BC – is it available for a Sec.230 scheme?

One more question being asked is whether the immunity provided under Sec.32A of IBC shall be available for the corporate debtor in the event it is taken over by a person under Sec.230 of Companies Act, 2013. Logically it makes sense that any person taking over the company under sec 230 by virtue of a scheme duly applied by NCLT should also be entitled to the immunity under sec 32A which is available to a successful resolution applicant. However, the provisions of sec 32A speak only about the situation of protection against prior offences.

Conclusion:

While the Supreme Court's decision has provided ample clarity that the provisions of Section 29A of IBC will be applicable for a scheme proposed under Sec.230 of Companies Act, 2013, there are a few critical issues such as participation and consent, voting thresholds, immunity under Sec.32A, etc. that need further clarification in the framework during the liquidation proceedings.

When the courts have recognised the fact that before the corporate debtor is consigned to the deathly hallows, all efforts should be made to revive it, there seems to be redundancy in the thought process. This is because, 90 days' time is given from the date of liquidation commencement date to consider a scheme proposed under Sec.230 of Companies Act, 2013, which is more like sale as a going concern. After exhausting this option, the liquidation process starts. During this period, how a liquidator should proceed is stipulated in Reg.39A of IBBI (IRPCP) Regulations which took effect from 25th July 2019. As per this Regulation, the CoC may recommend that the liquidator may first explore the sale of the corporate debtor as a going concern under Reg.32(e) or sale of the business of the corporate debtor as a going concern under Sec.32 (f) of IBBI (Liquidation Process) Regulations.

While it is laudable that all efforts should be taken to revive the ailing corporate debtor, at the same time, doing multiple rounds for Sec.230 scheme or sale as a going concern would cost heavily on the corporate debtor as such processes take time and cost and more importantly, in the process the value of assets goes down the spiral.

Do You Know??

Finance Minister Smt.Nirmala Sitharaman on 25th March 2021 launched the Central Scrutiny Centre (CSC) and Investor Education and Protection Fund Authority (IEPFA) Mobile App to leverage digital solutions to achieve the vision of 'Digitally empowered India'. The CSC will scrutinize certain Straight Through Process (STP) Forms filed by the corporates on the MCA21 registry and flag the companies for more in-depth scrutiny. The IEPFA App will have the facility of tracking the status and progress of refund of claim under IEPF.

Role of Adjudicating Authority in approving a resolution plan

M. Savitha Devi
Advocate, Madras High Court

The Hon'ble Apex Court on occasions, more than one, has held the scope of judicial review of the Adjudicating Authority in approving a CoC approved resolution plan as limited and has confined the scope to simply to check if the requirements set out under Section 30(2) of the Code are met.

Although the Adjudicating Authority cannot interfere on merits with the commercial decision of the CoC, in the words of the Hon'ble Supreme Court in *Swiss Ribbons Pvt Ltd. and Anr vs Union of India [W.P. (C) No. 99 of 2018],* the limited scope available in judicial review to the Adjudicating Authority is to examine whether the CoC has taken into consideration the fact that the corporate debtor during the CIRP is kept as a going concern, asset value maximization of the corporate debtor, and whether the interests of all stakeholders including the operational creditors is taken into account.

Effective implementation

The Code, in Section 31(1), clearly lays down that for final approval of a resolution plan, the Adjudicating Authority has to be satisfied that the requirement of Section 30 (2) of the Code has been complied with. However, the other point on which the Adjudicating Authority needs to be satisfied is laid down in the proviso to Section 31(1) of the Code. That factor is that the resolution plan has provisions for its effective implementation as laid down in *Committee of Creditors of Essar Steel vs Satish Kumar Gupta [C.A. No 8766-67 of 2019].*

In a matter under Section 31(1) of the Code, the statutory mandate of the Adjudicating Authority is to determine whether a resolution plan meets the requirement of Sections 30 (2) and 30 (4). So long as there is no breach of the said provisions and the resolution plan is otherwise compliant, the Adjudicating Authority may not be in a position to disapprove a resolution plan in light of the limited scope of the power of judicial review available to it.

If the Adjudicating Authority finds that the aforesaid parameters have not been considered by the CoC, an opportunity to reconsider the plan has to be given by the Adjudicating Authority, whereby the CoC would have to re-submit the resolution plan after satisfying the aforesaid parameters. It has been held in the case of *Swiss Ribbons Pvt Ltd. and Anr vs Union of India [W.P. (C) No. 99 of 2018],* that the reasons given by the CoC while approving the resolution plan would have to be looked at by the Adjudicating Authority only from this point of view, and if the Adjudicating Authority is satisfied that the CoC has given heed to these key factors, then it must pass the resolution plan assuming the resolution plan is otherwise proper.

(Image source: website)

Resolution plan below Liquidation value

Interestingly, in *Maharashtra Seamless Ltd vs Padmanabhan Venkatesh [C.A No. 4242of 2019],* the question that arose for consideration of the Bench was whether the Adjudicating Authority could reassess a resolution plan approved by the Committee of Creditors, even if the same is otherwise compliant with the requirements under Section 31 of the Code. In the aforesaid case, the CoC had approved a resolution plan with a value much lesser than that of the liquidation value. The Hon'ble Apex Court upheld the decision of the Adjudicating Authority, in approving the resolution plan as approved by the CoC, thereby holding that the liquidation value is simply a result of a valuation process carried out by the resolution professional to assist the CoC to take a decision on a resolution plan properly. Moreover, there is no prescription either in the Code or in the Regulations, that the resolution plan value has to match the liquidation value arrived at.

The exercise of appointing registered valuers, for evaluating the assets of the corporate debtor, carried out by the resolution professional, is merely to ascertain the value of the assets of the corporate debtor and is definitely not an indicator to the creditors to judge a resolution plan based on its value in comparison to that of the liquidation value. The liquidation value cannot be made a benchmark figure, for the CoC to analyze the resolution plan, but

simply as a guiding factor to understand what could be expected in terms of a resolution plan amount, and that cannot be the factor influencing the decision of the CoC in approving a resolution plan.

Commercial Wisdom

In essence, what is to be seen by the Committee of Creditors while approving a resolution plan under IBC, is not the parity in payment to the creditors or the liquidation value, or equitable perception but the commercial angle involved in the revival of the corporate debtor. The tool that the CoC is expected to employ in the process of approving the resolution plan is the majority commercial wisdom as held in *K. Sashidhar vs Indian Overseas bank and Ors. [C.A. No. 10673 of 2018]*, where Hon'ble Court has dealt with the paramount importance attached to it.

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Your materials for publishing may please be sent to

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in 'MS Word'.

Central Government amends Insolvency and Bankruptcy Code, 2016

Govt of India, Ministry of Law and Justice through an Ordinance amends the Insolvency and Bankruptcy Code, 2016 (IBC) by inserting the provisions relating to 'Pre-Packaged Insolvency Resolution Process (PPIRP)' for Corporate Debtors classified as MSMEs under the Mirco, Small and Medium Enterprises Development Act, 2006, with effect from 4th April 2021.

PPIRP is a process by which the debt of a distressed MSMEs may be resolved by an informal resolution plan worked out between non-related financial creditors and corporate debtor and allows the approval of such plans by NCLT.

Salient features of PPIRP:

1. Reduced timeline of 120 days to complete the PPIRP
2. Management control retained by CD (unless there has been gross mismanagement or affairs conducted in fraudulent manner during PPIRP)
3. Involvement / Co-operation by CD
4. Cost effective

The following are the criteria for classification of Micro, Small and Medium Enterprises, with effect from 1st July, 2020

Classification	Threshold limit not exceeding	
	Investment in Plant & Machinery	Turnover p.a.
Micro Enterprise	Rs.1 crore	Rs.5 crores
Small Enterprise	Rs.10 crores	Rs.50 crores
Medium Enterprise	Rs.50 crores	Rs.250 crores

Court Orders

CGRF Legal Team

(Image source: website)

A. Navinchandra Steels Pvt. Ltd.
vs
Srei Equipment Finance Limited. and Ors.
CIVIL APPEAL NOs.4230-4234 OF 2020
Decided on 1st March, 2021
(Supreme Court)

Whether proceedings under IBC can be 0initiated/continued when winding up petitions are admitted by the Company Court and the Official Liquidator has been appointed?

The present appeal arises out of an order of stay of Section 7 IBC proceedings before the NCLT by the Hon'ble Supreme Court. The issue for consideration before the Bench was whether proceedings under IBC can be initiated/continued when winding up petitions are admitted by the Company Court and the Official Liquidator has been appointed.

The Hon'ble Supreme Court while deciding the above issue restated certain fundamentals such as the object of the IBC as described in *Swiss Ribbons (P) Ltd. v. Union of India, (2019) 4 SCC 17* at paragraphs 25 to 28, that sets out IBC as a special statute dealing with revival of companies where winding up is the last resort when all attempts to revive fails. In contrast, the Companies Act, which is a general statute dealing with all aspects of the companies, including debt ridden companies. The IBC being a special statute which would prevail in the event of conflict, has also a non-obstante clause in Section 238, which makes it even clearer that in case of conflict, the provisions of the IBC will prevail the Court held.

The Court referred to its decision in *Allahabad Bank v. Canara Bank, (2000) 4 SCC 406,* where the Court dealt with the question whether the Recovery of Debts Due to Banks and Financial Institutions Act, 1993 [RDB Act] was a special statute qua the Companies Act, 1956. It was held that the Companies Act being a general Act does not prevail over the RDB Act, "which was a later Act and which has a non-obstante clause that clearly excludes the provisions of the Companies Act in case of conflict".

The Court went on to distinguish general law from special law and discussed the case in *Madras Petrochem Ltd. BIFR, (2016) 4 SCC 1,* where the question whether a predecessor statute to the IBC, which has been repealed by the IBC, i.e., the Sick Industrial Companies (Special Provisions) Act, 1985, would prevail over the SARFAESI Act to the extent of inconsistency. This Court noted that "in the case of two statutes which contain non-obstante clauses, the later Act will normally prevail".

The Court disagreeing with the arguments of the appellants that, given Section 279 of the Companies Act, 2013 / Section 446 of the Companies Act, 1956, once a winding up petition is admitted by the Company Court, the winding up petition should supersede any subsequent attempt at revival of the company through petition filed under Section 7 or Section 9 IBC. "While it is true that Sections 391 to 393 of the Companies Act, 1956 may, in a given factual circumstance, be availed of to pull the company out of the red, Section 230(1) of the Companies Act, 2013 is instructive" the Court held.

Section 230 of the Companies Act, 2013 was taken into account while noting that a compromise or arrangement can also be entered into, if liquidation is ordered in an IBC proceeding. The key difference being that under the Companies Act, only an order of winding up can be issued, whereas under the IBC, the prime emphasis is on revival of the corporate debtor, the Court noted.

In the present case, Indiabulls, a secured creditor of the corporate debtor, has, outside of the winding up sold the mortgaged property, in enforcement of its debt by mortgage. This sale is subject matter of proceedings before the Bombay High Court filed by the provisional liquidator. If the said sale is set aside, the asset of the corporate debtor that has been sold will go back to the provisional liquidator for the purposes of winding up. If the sale is upheld, the Court noted, that the other assets of the corporate debtor which continue to be in control of the provisional liquidator for the purposes of winding up shall remain. The Court also observed that although no application was filed for transfer of the winding up proceeding pending in the Bombay High Court, the Bombay High Court itself, by the orders dated 28.11.2019 & 23.01.2020, directed the provisional liquidator to hand over the assets and records of the corporate debtor to the IRP in the Section 7 proceeding that is pending before the NCLT. As the IRP has not been able to pay to the provisional liquidator the requisite amount for his expenses, the handover has not yet been done.

The arguments of the appellant that SREI has in its application under Section 7 of the IBC before the NCLT, suppressed the winding up proceeding and has resorted to Section 7 only as a subterfuge to evade filing an application of transfer before the High Court in the pending winding up proceedings did not hold good before the Court for the simple reason that Section 7 is an independent proceeding, as has been held in a series of judgments of this Court, which has to be tried on its own merits. The Court further held that "any suppression of the winding up proceeding would, therefore, not be of any effect in deciding a Section 7 petition on the basis of the provisions contained in the IBC. Equally, it cannot be said that any subterfuge has been availed of for the same reason that Section 7 is an independent proceeding that stands by itself." The Court further held that "a discretionary jurisdiction under the fifth proviso to Section 434(1)(c) of the Companies Act, 2013 cannot prevail over the undoubted jurisdiction of the NCLT under the IBC once the parameters of Section 7 and other provisions of the IBC have been met". For all of the above reasons, the appeal was dismissed and the interim order that was passed by the Hon'ble Court on 18.12.2020 was vacated with immediate effect.

P. Mohan raj
vs
Shan Brothers Ispat P Ltd
Decided on 1st March 2021
(Supreme Court)

Section 138/141 proceedings under the Negotiable Instrument Act against a corporate debtor is covered by moratorium under Section 14(1)(a) of the IBC.

The Corporate Debtor, Diamond Engineering Chennai Pvt. Ltd. (DECPL) was admitted into CIRP pursuant to an Application filed by the Respondents, Shan Brothers Ispat P Ltd. In the meantime, criminal complaints were lodged against the DECPL and Mr P. Mohan raj as its directors Appellants herein (the Corporate Debtor & its directors/ promoters) to initiate proceedings u/s 138 of the Negotiable Instrument Act.

The Appellants stated above approached the Hon'ble NCLT and obtained a stay on the said criminal complaints which was turned down by the Hon'ble NCLAT taking a view that no criminal proceedings can be covered under the moratorium relief provided by the Code.
Thus, the Appellant approached the Hon'ble Supreme Court and the question before it was,

1. "whether the institution or continuation of a proceeding under Section 138/141 of the Negotiable Instruments Act (N I Act) can be said to be covered by the moratorium provision, namely, Section 14 of the IBC?"

The Hon'ble Supreme Court observed that a Section 138 proceeding being conducted before a Magistrate, would certainly be "a proceeding" in "a court of law" in respect of a transaction which relates to a debt owed by the corporate debtor, as the provision uses the terms, "proceedings against the corporate debtor" … "in any court of law". Therefore, sec 138 proceeding is covered under moratorium and relief provided u/s 14 of the Code. However, any other criminal proceeding, which are not directly related to transactions evidencing debt or liability of the corporate debtor would be outside the scope of the expression, "proceedings" and not be provided with relief under moratorium.

2. The next question was, "whether natural persons (here directors/ promoters) are covered by Section 14 of the IBC?"

The Hon'ble Bench was of the view that, although Sec. 141(1) of the N I Act, states that "every person who, at the time the offence was committed, was in charge of, and was responsible to the company for the conduct of the business of the company, as well as the company, shall be deemed to be guilty of the offence and shall be liable to be proceeded against and punished accordingly.", no proceeding can continue or be initiated against the corporate debtor because Sec. 14 of IBC is a statutory bar. However, such proceedings can be initiated or continued against the persons mentioned in Section 141(1) and (2) of the N I Act. This being the case, it is clear that the moratorium provision contained in Section 14 of the IBC would apply only to the corporate debtor; the natural persons mentioned in Section 141 continuing to be statutorily liable under Chapter XVII of the Negotiable Instruments Act.

In view of the above, other similar Appeals that were pending before the Hon'ble Supreme Court were also dismissed in favour of the Corporate Debtor or granted liberty to proceed against the directors, accordingly. However, in the present case since the moratorium ended and the CIRP of the Corporate Debtor did not result in taker over of a new management, (i.e approval of resolution plan), the Hon'ble SC held that the Section 138/141 proceedings in this case will continue both against the company as well as the Directors.

Thus, it can be concluded that criminal proceedings cannot be initiated /continued against the Corporate Debtor, by virtue of Sec. 14 during CIRP and Sec 32A in case of take over of the Corporate Debtor by a new management resulting out of a resolution plan approval.

Arun Kumar Jagatramka
vs
Jindal Steel And Power Ltd.
Decided on 15th March, 2021
(Supreme Court)

Whether the Promoter is eligible to file application for Compromise and Arrangement under Section 230 of the Companies Act, 2013, while he is ineligible under Section 29A of the IBC to submit a Resolution Plan?

The present appeal arises out of an order of the Appellate Tribunal dated 24.10.2019 holding that a person who is ineligible under Section 29A of the Insolvency Bankruptcy Code, 2016 to submit a resolution plan, is also barred from proposing a scheme of compromise and arrangement under Section 230 of the Companies Act, 2013.

Mr Arun Kumar Jagatramka, who is a promoter of the corporate debtor had submitted a scheme of compromise under Section 230 of the Companies Act, 2013 which was allowed by the NCLT. Against which, an unsecured creditor filed an appeal before the NCLAT, where the order of NCLT was reversed. Challenging the same, the promoter by way of the present appeal stood before the Hon'ble Supreme Court assailing the order dated 24 October 2019 of the NCLAT. The Amendment to the Liquidation Process Regulation by way of insertion Section 2B was also challenged by way of a separate appeal.

Among other grounds of challenge, the appellant highlighted that Section 230 of the Act of 2013 does not place any embargo on any person for the purpose of submitting a scheme.

According to the them, in the absence of a provision for disqualification under Section 230 of the 2013 Act, the NCLAT ought not to have read the ineligibility under Section 29A of the IBC into Section 230 of the Act of 2013. This, according to the appellant, amounts to "a judicial reframing of legislation by the NCLAT, which is impermissible".

The NCLAT had formulated two principal issues:

i. Whether in a liquidation proceeding under IBC, the Scheme for Compromise and Arrangement can be made in terms of Sections 230 to 232 of the Companies Act?
ii. If so permissible, whether the Promoter is eligible to file application for Compromise and Arrangement, while he is ineligible under Section 29A of the IBC to submit a Resolution Plan?

The first of the two questions was answered in favour and therefore the second of the two questions was before the Court to decide.

Whether the ineligibility under Section 29A of the IBC can be read into the provisions of Section 230 of the Act of 2013?

The argument of the appellant was that, a disqualification which is not provided by the legislature cannot be introduced by a judicial determination. It was submitted that, Section 29A does not expressly provide that it extends to Section 230 of the Act of 2013. According to them, Section 230 is a different section in different enactment to which the ineligibility under Section 29A of the IBC cannot be attracted.

On the other hand, the respondents submitted that the correct question for determination is whether a person who is ineligible under Section 29A of the IBC is permitted to propose a scheme for revival under Section 230 of the Act of 2013 at the stage of liquidation either by themselves or in concert with others.

After elaborate arguments from both sides, the Hon'ble Court took note of the observations made by the Insolvency Law Committee in its Report of February 2020, the Committee acknowledged that the floating of schemes of compromise or arrangements under Sections 230 to 232 of the Companies Act, 2013 was not part of the framework under the IBC, including for companies undergoing liquidation.

The Committee further noted, that multiplicity of issues including the dual role of the NCLT (as a supervisory Adjudicatory Authority under the IBC versus the driving Tribunal under the Act of 2013) had arisen. The very question before the Court in this case is, whether the disqualification under Section 29A and proviso to Section 35(1)(f) of the IBC also attaches to Section 230 of the Act of 2013. However, the Committee had noted that judicial intervention by the NCLAT along with the IBBIs' introduction of new regulations have led to some alignment in the two frameworks.

The Hon'ble Court noted that "the explicit recognition of the schemes under Section 230 into the liquidation process under the IBC was through the judicial intervention of the NCLAT in *Y Shivram Prasad*. Since the efficacy of this arrangement is not challenged before us in this case, we cannot comment on its merits".

The Court went on to offer a note of caution to the NCLT and NCLAT, functioning as the Adjudicatory Authority and Appellate Authority under the IBC respectively, from judicially interfering in the framework envisaged under the IBC.

The Court emphasised that "the IBC was introduced in order to overhaul the insolvency and bankruptcy regime in India. As such, it is a carefully considered and well thought out piece of legislation which sought to shed

away the practices of the past. The legislature has also been working hard to ensure that the efficacy of this legislation remains robust by constantly amending it based on its experience. Consequently, the need for judicial intervention or innovation from the NCLT and NCLAT should be kept at its bare minimum and should not disturb the foundational principles of the IBC. This conscious shift in their role has been noted in the report of the Bankruptcy Law Reforms Committee."

Based on the above analysis, the Hon'ble Supreme Court held that the prohibition placed in Section 29A and Section 35(1)(f) of the IBC must also attach itself to a scheme of compromise or arrangement under Section 230 of the Act of 2013, when the company is undergoing liquidation under the auspices of the IBC.

As such, Regulation 2B of the Liquidation Process Regulations, specifically the proviso to Regulation 2B (1), which was also under challenge, was held to be constitutionally valid thereby disposing of the connected matters and deciding the issue.

(Image source: website)

Krishnan
vs
Stressed Assets Stabilization Fund (SASF)
CA (AT) (Insolvency) No.521 of 2020
Decided on 17th March 2021
(NCLAT)

Right to sue can be extended only when the debt is acknowledged by the Corporate Debtor within limitation of three years.

Brief facts of this case are that on 06.03.1998 Industrial Development Bank of India (IDBI) granted a term loan facility of Rs.6.50 crores to M/s.LSP Agro Limited (Corporate Debtor). Thereafter, in June 2000 IDBI granted another loan facility and disbursed Rs.4 crore to CD. As CD defaulted in repayment of said loans, IDBI issued recall notice on 15.01.2002 and thereafter on 06.02.2002, it had filed an OA before the DRT against the CD.

In the meantime, Central Government set up a Trust, Stressed Assets Stabilization Funds (SASF) for acquiring the stressed assets of the IDBI. Accordingly, the SASF took over the stressed assets of IDBI. On 23.01.2019 SASF filed an application for initiating CIRP against CD under Sec.7 of IBC with NCLT. During the pendency of the Sec.7 application with NCLT, DRT allowed the OA on 29.04.2019 and subsequently, issued a recovery certificate dated 16.01.2020 in favour of SASF.

On 25.01.2020 NCLT admitted the CIRP against the CD and observed that though SASF has not placed any material showing that the debt is not time barred, the application was admitted based on the DRT's Final Order. Against the order of NCLT admitting CIRP, an appeal was filed by Ex-Director of the CD before the Hon'ble NCLAT.

Hon'ble NCLAT after hearing the parties observed that the application under Sec.7 of the IBC for initiation of CIRP against a debtor is maintainable only when the default has occurred. It pointed out that Hon'ble SC in the case of *B.K. Educational Services Pvt. Ltd vs Parag Gupta & Associates (2019) 11 SCC 633* held that ***"the right to sue accrues" when a default occurs. If the default has occurred over three years prior to date of filing of the application under Sec.7 of IBC, the application would be barred under Article 137 of the Limitation Act. The date of right to sue can be extended only when the debt is acknowledged by the CD within limitation of three years*** *(emphasis added).*

The issue which fell for determination before the Hon'ble NCLAT in this appeal was whether the date of default can be shifted forward based on the order passed by the DRT.

Hon'ble NCLAT referring to the judgement of its Five Member Bench in the case of V.*Padamkumar vs Stressed Asset Stabilization Fund in CA (AT)(Ins) No.57 of 2020* under Para No.16 to 18 and 23, wherein it is stated "***that a Judgement or a decree passed by a Court for recovery of money by Civil Court / Debt Recovery Tribunal cannot shift forward the date of default for the purpose of computing the period for filing an application under Sec.7 of the IBC***" *(emphasis added).* It also observed that the NCLT had erroneously admitted the CIRP based on the direction given by DRT against the CD by taking the order passed by the DRT for initiation of CIRP into consideration.

Hon'ble NCLAT allowed the appeal and set aside the order dated 25.01.2020 admitting CIRP, stating that the loan account was declared as NPA before 2001 and thereafter, there is no acknowledgement of debt within limitation of three years, and the Judgement / Decree passed by the DRT on 29.04.2019 cannot shift forward the date of default for the purpose of computing the period for filing an application under Sec.7 of the IBC. Hence, application filed by SASF against the CD on 23.01.2019 is barred by limitation and was not maintainable.

Ram Ratan Kanoongo (RP)
vs
Veda Kumar Nimbagal
CA (AT) (Insolvency) No.906 of 2020
Decided on 17th March 2021
(NCLAT)

Whether AA can issue directions to erstwhile RP once the Resolution Plan has been approved, and the RP has been discharged of his duties?

Brief facts of the case are that an application under Sec.9 of the IBC was admitted against Sirpur Paper Mills Limited (Corporate Debtor) on 18th Sep 2017. An ex-Director of the CD filed his claim amounting Rs.13.50 lakhs towards payment of salary for the period from 23rd Jan 2017 till 20th Oct 2017. RP admitted the claim partially to the tune of Rs.5.40 lakhs as salary dues upto the date of commencement of CIRP (i.e, 18th Sep 2017). Aggrieved by the decision of RP in rejecting his claim, ex-Director filed an application with NCLT.

NCLT by its Order dated 19th Jul 2018 approved the Resolution Plan submitted by CoC, and in addition NCLT dismissed the application filed by ex-director and upheld the rejection of claim by the RP. NCLT while disposing the application observed that "***claim has to be filed by the employees only as on the date of commencement of CIRP period, and, it is open for the ex-director to claim his salary at an appropriate time, in an appropriate forum for the period 19th Sep 2017 to 20th Oct 2017***" (emphasis added).

Since ex-Directors were not co-operating in signing the financial statements of the CD for previous years from 2014-2018, RP as member of Monitoring Committee filed an application with NCLT. Ex-director has also filed an application inter-alia seeking for direction for release of salaries and other amounts aggregating Rs.20.38 lakhs due and payable to him. NCLT vide its Order dated 04.08.2020, directed the erstwhile RP to make payment of the salary to the ex-Director as acknowledged by him, in accordance with the provisions of IBC.

An appeal was preferred by RP in the NCLAT.

When the matter came before the Hon'ble NCLAT, *the issue which fell for determination was whether the AA can issue the directions to erstwhile RP once the Resolution Plan under Sec.31 of the IBC has been approved, and the RP has been discharged of his duties*?

NCLAT after analysing the case in detail, held that the AA has erred in issuing directions to the erstwhile RP to make payment of the salary to the ex-Director and allowed the appeal.

NCLAT observed that AA had dismissed the appeal of ex-Director and upheld the rejection of claim by RP vide its Order dated 19th Jul 2018. Ex-Director did not prefer any appeal against the said Order. As a result, the Order dated 19th Jul 2018 attains finality. No further, cause of action remains for ex-Director to raise the same issue again by filing a fresh application and without averment about the earlier application and its Order dated 19th Jul 2018.

Further, Hon'ble NCLAT pointed out that any claims for the CIRP period could have been raised before approval of a Resolution Plan. After the Resolution Plan's approval and implementation, no direction can be issued to erstwhile RP on account of any belated and settled claim. It also reiterated that given the law laid down by the Hon'ble SC in the case of Essar Steel, an approved Resolution Plan is binding on all the stakeholders and the Successful Resolution Applicant cannot be burdened with undecided claims / dues of the CD.

Feedback Matters

I am happy to receive and go through March 2021 issue of CGRF SandBox. Its comprehensive in its coverage and contains latest news on IBC laws including case laws. Kudos to the team behind such a wonderful magazine with useful content especially to corporates and banks.

- CA. IVSVB. Panchajanyam

Thanks for mailing me the March 21 issue of CGRF SandBox. The articles in this issue in particular, were very diverse, topical and lucid, ranging from Bad Bank to SPAC. Best wishes to you and your team to keep this great effort going.

- Mr H. Parmeswar
Management Consultant

I am working as a Chief Manager with Indian overseas Bank and the copy of CGRF SandBox is being received by our branch regularly. As I am very much impressed with the contents and the utility value of your magazine in day-to-day banking.

- Mr Pradeep Kumar Chief Manager, IOB Asset Recovery Management Branch

FIND THE WORDS

CLUES	WORDS
1. Minimum attendance required in a meeting to transact business	
2. Interest on interest	
3. A formal declaration of insolvency in respect of individuals	
4. The process of determining the intended meaning of a written document, such as the constitution, or a statute.	
5. People's Court	
6. A writ issued for quashing the order already passed by an inferior court, tribunal, or quasi-judicial authority.	

Note: The below group of letters can be used repeatedly for different clues.

KRUP	REST	QUO	BAN	LOK	ION
OUND	CERTI	INTE	COMP	INTE	ADA
TAT	RPRE	ORARI	RUM	LAT	TCY

Answers:

1.Quorum 2. Compound Interest 3. Bankruptcy 4. Interpretation 5. Lok Adalat 6. Certiorari

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- Assessing the viability of the businesses of the Corporate Debtor under CIRP
- Drafting of Resolution Plans / Settlement Plans/ Repayment /Restructuring Plans
- Implementation of Resolution Plan
- Designing viable Restructuring Schemes

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- Preparation of Request for Resolution Plans (RFRP) with Evaluation Matrix
- Evaluation of Resolution Plans / Settlement Plans / RepaymentPlans Scrutinizers for E-voting process
- Section 29A verification
- Framework for Resolution Plans
- Claims Processing

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- Validity of decisions taken by CoC
- Powers and duties of directors under CIRP
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- Due diligence report to banks on NPA/SPA Accounts
- Issue of Notice and filing application u/s 95 of IBC – PG to CDs
- Proxy advisory services for institutional shareholders

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