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CGRF®

CREATE & GROW RESEARCH FOUNDATION

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குறள்: 462

தெரிந்த இனத்தொடு தேர்ந்தெண்ணிச் செய்வார்க்கு
அரும்பொருள் யாதொன்றும் இல்.

Thirukural: 462
There is nothing too difficult to (be attained by) those who, before they act, reflect well themselves, and thoroughly consider (the matter) with chosen friends.

From the Editor's Desk

Dear Readers of CGRF SandBox

Heralding the arrival of south-west monsoon, the month of June generally turns out to be quite busy academically with schools and colleges commencing their new year with great enthusiasm. Last two years, "June" has come under "lockdowns" depriving the students of opportunities to collaborate and learn. Be that as it may, the opportunities for learning are manifestly huge these days, thanks to the new world of virtual learning. Admirably, the kids have taken to online classes like duckling to water.

In this context, even the adult population of the country has shown great resilience to adjust to the new demands of the corporates. Learning never ends; and when that happens, the growing stops. Therefore, wherever we are, whatever we do, there is always scope for learning and improvement.

(Image source: website)

5 years of IBC

Insolvency and Bankruptcy Code (IBC) was enacted in 2016 as a self-contained legislation to provide for revival of viable corporates which are saddled with defaults to lenders and in the process provide reasonable recovery to the lenders. Hailed as one of the path-breaking reforms, India's ranking in "ease of doing business" IBC pushed up by a huge leap. In spite of arguments heaped on both sides – for and against IBC - in the last five years of its journey, IBC has created a very good eco system for insolvency resolution and liquidation process. It has changed the equation from "defaulting debtor in possession of assets and management" to "creditors in control as the powers of board being suspended".

While the critics have drawn their swords to dismiss this relatively nascent law into the same old wilderness which was witnessed by its predecessors (RDBA, SICA, SARFAESI Act), the stakeholders have seen a mixed bag. Some of the ailing corporates with productive assets got a fresh lease of life, sustaining the livelihood of employees and other stakeholders. At the same time, the number of cases where successful resolution plans have been achieved is quite minimal. Conversely, several cases have been consigned to liquidation. Justifiably so, after exhausting all other avenues for a resolution. This only goes to signify that such companies had neither assets nor viability to survive and sustain. At least, the spoils would now be distributed to the stakeholders without further erosion in value.

Elsewhere in this Issue of SandBox, we have tried to highlight the proactive response from the Government at different points to bring amendments to the IBC – be it to prohibit backdoor entry of erstwhile promoters in the insolvency resolution process, legal recourse against the personal guarantors to corporate debtors, commercial wisdom of the committee of creditors, minimal protection for operational creditors, special scheme for MSMEs called "Pre-pack", etc.

We are glad that some interesting decisions by NCLT / NCLAT / Supreme Court have been brought out in this issue.

Semblance of normalcy

After a few more lockdowns in the months of May and June 2021, apparently the more severe second wave of Covid-19 seems to have been tamed. Again, the MSME sector had to bear the brunt. The increase in the rate of vaccination should bring some more comfort to the State and Central governments to relax the curbs and open up the economic activities.

I wish to sign off requesting all CGRF SandBox readers not to lower their guard against Covid-19. Countries like USA, France, Spain have shown that they could win the war against the virus and free up the economic activities. Thankfully, they were able to manage the crisis due to lesser population. For a country of 1.4 billion, it is not an easy task. Yet, we have time and again shown our resolve and resilience to fight back. Great times ahead!! Be safe!! Be strong.!!!

Yours truly

S. Rajendran

Importance of Board's Report for Bankers

S. Srinivasan, Senior Partner
SR *Srinivasan & Co* LLP

A couple of years before, I had the fortune of addressing a set of newly recruited officers of a nationalised bank in an interactive session as part of their induction programme. The topic for discussion was "*Legal intricacies in lending to corporates*". The participants were of a heterogeneous composition where some of them were hard core engineers, computer specialist, environmentalist, MBAs etc. And they had, by choice or compulsion, chosen banking as a career. I was not surprised that their knowledge on Company Law, SEBI Regulations etc which are relevant while lending to the corporate would be shallow. That goaded me to focus on a subject of great importance to these newly recruited officers, namely, "**Importance of Board's Report of a company**".

Introduction

It is not enough to study the financial health of the units being considered for funding or which are under review for renewal of limits or further funding only by scrutinising the Balance Sheets and Profit and Loss accounts along with Cash flow and the notes to accounts. **The Board's Report will give significant insight into the working and management of the company which are crucial in assessing whether the company is worthy of funding or continued funding or for recalling of the loans.** So also, are the Corporate Governance Report, Management Analysis and Business Responsibility Reporting, wherever applicable, in the case of listed companies.

There are several other crucial documents the banker has to scrutinise, such as: the Independent Auditor's Report, CARO, the Secretarial Auditor's Report, if applicable, the Diligence Report issued by a practising professional generally by a practising Company Secretary twice a year in respect of those units where RBI has mandated and more importantly, the Company's website wherever it is available. In case of listed companies, it would also be prudent for the banker to go through the BSE and NSE sites to follow information supplied by the Company to these Stock Exchanges. Not to be missed out are the Proxy Advisors' sites.

But standing tall among these, as far as the banker is concerned, is the Board's Report by which one can easily infer on the intentions of the management of the company. Also, it will not be enough to scrutinise the Board's Report of the previous year alone. The Banker has also to insist upon the company to furnish the Board's Report of the last two years to the previous year, which would reveal the consistencies or inconsistencies of the management's reporting.

Section 134 of the Companies Act, 2013, requires the Board of Directors of every company to attach to the financial statements to be laid before the members at the annual general meeting, a report of the Board of Directors. The Board's Report is an important means of communication by the Board of Directors of a company not only with its shareholders but also with all its stakeholders and more particularly with the Company's bankers and Financial Institutions. The Board's Report provides the stakeholders with both financial and non-financial information, including important events of the previous year having bearing on the Company's operation, the performance and prospects of the Company, relevant changes in the management and capital structure, recommendations as to the distribution of profits, future and on-going programmes of expansion, modernisation and diversification, capitalisation of reserves, further issue of capital and other relevant information.

The Companies Act, 2013, mandates certain disclosures to be made in the Board's Report. A listed company is also required to comply with certain additional requirements as stated under the Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015. Similarly, a company, whose securities are listed on an overseas stock exchange, is required to comply with additional requirements as may be specified by such stock exchange.

Further, a company which is regulated under other laws, may also be required to make additional disclosures in its Board's Report as stated in the respective applicable laws.

Essentially, the task of preparation of the Board's Report in consultation with the Managing Director or CEO, vests with the Company Secretary of the Company, who is expected to track the significant events which took place in the previous year and what the plans of the management are for the future. These two inclusions in the report, apart from what is mandatorily required u/s

134, will give to the banker a fair idea of the directions in which the Company is moving. The exercise of lending further or withholding lending by the banker depends largely on these two items.

Having said this, let us examine some of the important contents of the Board's Report as mandated u/s 134 which the banker must focus on.

Directors' Responsibility Statement

The Report shall include a Directors' Responsibility Statement stating the following:

> *(a) in the preparation of the annual accounts, the applicable accounting standards had been followed along with proper explanation relating to material departures;*
>
> *(b) the Directors had selected such accounting policies and applied them consistently and made judgments and estimates that are reasonable and prudent so as to give a true and fair view of the state of affairs of the company at the end of the year and of the profit and loss of the company for that period;*
>
> *(c) the Directors had taken proper and sufficient care for the maintenance of adequate accounting records in accordance with the provisions of the Act for safeguarding the assets of the company and for preventing and detecting fraud and other irregularities;*
>
> *(d) the Directors had prepared the annual accounts on a going concern basis;*
>
> *(e) the Directors had devised proper systems to ensure compliance with the provisions of all applicable laws and that such systems are adequate and operating effectively;*
>
> *(f) the Directors, in case of a listed company, had laid down internal financial controls to be followed by the company and that such internal financial controls are adequate and operating effectively.*

Section 134(3) of the Act provides that the Report shall include Directors' Responsibility Statement as per of section 134(5) of the Act.

Studying carefully the Directors' Responsibility Statement is very important for the Banker to ensure in particular, whether the company is a going concern. Material departure from the usual accounting norms would lead the banker to analyse the financial statements in proper perspective. The Banker will have comfort that the company has devised proper systems to ensure compliance with the provisions of all applicable laws and that such systems are adequate and operating effectively.

Reporting of frauds, if any

(Image source: website)

If the Auditor's Report has reported frauds, then the directors have to give details. The banker has to first go through the Auditor's Report for possibility of his report on fraud committed during the year.

Explanations/Comments on qualifications by auditors

If there are qualifications, reservations, adverse remarks, or disclaimers by the statutory/secretarial auditors, then the banker should look out for the explanations or comments of the Board in particular for those qualifications and the Board's comment have a bearing on lending.

Particulars of loans/guarantees/ investments

It is important for the banker to know if there are other secured and unsecured lenders to the Company which may impact the servicing of the bank's loans. So also, if guarantees have been furnished for not only the amounts advanced by these lenders but also guarantees provided by the company for loans advanced to third parties. This is also true of securities provided for these loans as the charges registered in favour of the bank may get diluted without the knowledge of the bank. This can be counter checked with the Statutory and Secretarial Auditors' Report as also from the Diligence Report referred to earlier.

State of Company's Affairs

The Board's Report should provide a brief about the operational highlights, growth in profits, if any, and loss, if any, along with graphs. Key ratios may have been included. The report may also indicate whether any new products have been introduced, fresh registration received from any regulatory authorities, business acquired during the previous year, company's plans to diversify, if any. The Board's Report may also give a brief performance of its subsidiaries and joint ventures. It would be prudent for the banker to study Board's Report of other companies in the same industry to make a comparative analysis.

Material Changes and Commitments, if any

The Board has to report on any material changes and commitments, if any, affecting the financial position of the company which have occurred between the end of the financial year of the company to which the financial statements relate, and the date of the report and such reporting will add to the basket of information which the banker already has which may affect the financial health of the Company.

Risk Management Policy

The Board's Report should contain a statement indicating development and implementation of a risk management policy for the company including identification therein of elements of risk, if any, which in the opinion of the Board, may threaten the existence of the company. In case the Board perceives that no risk is applicable to it, then it can state that in its opinion there are no factors which threaten the existence of the Company.

(Image source: website)

Further, risk management is the key function of the board of directors of every company, large or small, listed or unlisted. Whether the risk management is done through a separate risk management committee, or there is a formal risk management policy, or not, is a matter of differentiation based on type of company, but risk management per se is applicable to every company. Hence, the board should spell out how the board is tackling the key risks facing the company.

Vigil Mechanism

This is applicable to only listed company, companies accepting deposits from public and companies having borrowings from banks and financial institutions above Rs.50 crores. The details of establishment of vigil mechanism for directors and employees to report genuine concerns are to be disclosed which may be an eye opener for the banker.

Conclusion

What is spelt out here is not exhaustive of what a Board's Report should contain as per the Companies Act or SEBI Regulations. But in so far as a banker is concerned these are the alert points which the Banker has to be agile about. It would be advisable for the banker to go through the entire Board's Report to get a holistic view of what is happening in the Company. Not only that he should also go through Board's Report of other companies which are in the same industry to get a better grip of the affairs of the Company which he proposes to fund or continue to fund.

With a view to ensure enhanced disclosures and transparency, the Companies Act, 2013 and rules made thereunder, as well as the Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015, provide for pertinent disclosures in the Board's Report and other documents enclosed in the Annual Report. The matters to be reported in Board's Report require special focus. The purpose of this requirement is to ensure the inclusion of certain important information that should be presented to the stakeholders in a single document. There is, therefore, no doubt the Board's Report is an important tool in the hands of a banker which will play a significant role in his decision making.

Legal Maxim

Res Judicata also known as "a matter decided".

The thing has been judged by the court, the issue before a court has already been decided by another court and between the same parties. Hence, the court will dismiss the case as it has been decided by another court. Res judicata applies to both civil and criminal legal systems.

Genesis of Non-Performing Assets and the Role of Asset Reconstruction Companies

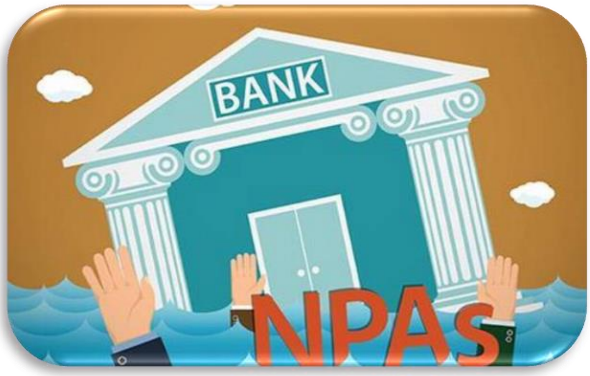
S. Venkataraman
Chief General Manager (Retd.) SBI
Insolvency Professional

(With inputs taken from multiple sources)

We all know that sound and healthy banks and financial institutions, play an important role in any vibrant economy. The Government and all other financial sector regulator's role is paramount in creating such an environment. For a Banking system to be sound, one of the major criteria is having a healthy loan books with the percentage of non-performing assets in their books being very low. Many economies in the last few decades had their own torrid stories of instances of high non-performing assets in their banking system and their efforts to address them through various means.

In India too, Banks were/are facing high incidences of NPAs at various times. High level of NPAs in banks and financial institutions has been a matter of grave concern as it becomes as a bottleneck for sustained credit flow. Mounting NPA shave created and is bound to create (on account of current ongoing pandemic) adverse repercussions on the economy. When the loans taken are not repaid, much of the funds go out of financial system and the cycle of lending-repaying-borrowing is not only broken but also may affect bank's ability to repay their depositors and others from whom they had borrowed. If the borrowers do not pay, the banks have to borrow funds to repay the depositors and creditors. This leads to a situation where banks are reluctant to lend to existing/new projects and also unable to meet the credit demand of the economy, thus affecting the economy adversely. This situation leads to slowdown in industrial output/productivity and fall in profit margins etc., which resultantly cause depression in the market.

High level of NPAs put strain on the bank's functioning as it leads to credit risk management assuming priority over other aspects of bank's operations. The bank's whole machinery would thus be pre-occupied with recovery procedures rather than concentrating on expanding business. A bank with a high level of NPAs would be



(Image source: website)

forced to incur carrying costs on non-income yielding assets. Other consequences would be reduction in interest income, high level of provisioning leading to profitability and capital adequacy stress, decline in ability to meet increase in various costs, put increased pressure on Net Interest Margin (NIM) thereby reducing competitiveness, steady erosion of capital resources and increased difficulty in augmenting capital resources. Thus, NPAs generate a vicious cycle of effects on the sustainability and growth of the banking system if not managed properly. To address this recurring problem of NPAs, in the recent times RBI has initiated certain bold measures like CRILC reporting, Asset Quality Review (AQR) etc., thus enforcing strict surveillance on Banks. Putting banks under Prompt Corrective Action (PCA) framework is part of the above approach.

Evolution of NPA recognition and recovery mechanism in banks

Until mid-eighties, management of NPAs was mostly left to the banks. In 1985, based on the recommendations of Ghosh Committee, the first ever system of classification of assets based on the health of the assets was introduced for the Indian banking system. This system, known as the 'Health Code System' (HCS), involved classification of bank advances into eight categories ranging from 1 (satisfactory) to 8 (bad and doubtful debt).

In 1991, the Narasimham Committee on the financial system felt that the classification of assets according to the HCS was not in accordance with international standards and suggested that for the purpose of provisioning, banks should classify their advances into four broad groups, viz. (i) standard assets; (ii) substandard assets; (iii) doubtful assets; (iv) loss assets. Following this, prudential norms relating to income recognition, asset classification and provisioning were introduced in 1992 in a phased manner.

An effective asset resolution mechanism is an integral part of a well-functioning financial system. It was with this understanding that the Recovery of Debts Due to

Banks and Financial Institutions (RDDBFI) Act* was passed in 1993 as part of financial sector reforms. With the enactment of the RDDBFI, Debt Recovery Tribunals (DRTs) were established as special tribunals to deal with loan recovery of cases involving Rs.20 lakh (increased from Rs.10 lacs in 2018). The DRTs were also authorised to form Lok Adalat to decide on cases involving an amount of up to Rs. 20 lakhs.

The passage of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act (SARFAESI Act) in 2002 empowered banks and financial institutions to recover secured loans by enforcing the security interest, and auctioning borrowers' property without any court intervention. As part of the SARFAESI Act, ARCs were set up as another institutional alternative for NPA resolution in India. The ARCs, regulated and supervised by the Reserve Bank, were institutions created for the sale of financial assets by banks and financial institutions. The creation of ARCs was an important financial sector reform following the recommendations of the Committee on Banking Sector Reforms (Narasimham Committee II), which was expected to speed up the process of resolution and recovery of secured assets. Finally, in 2016, came the Insolvency and Bankruptcy Code (IBC) that took the NPA resolution mechanism many steps further, as it is expected to streamline the insolvency resolution process for corporates and individuals, and protect the interests of not just secured but also unsecured creditors in the near future. (*The title of RDDBFI Act was amended by IBC as "Recovery of Debts and Bankruptcy Act, 1993".)

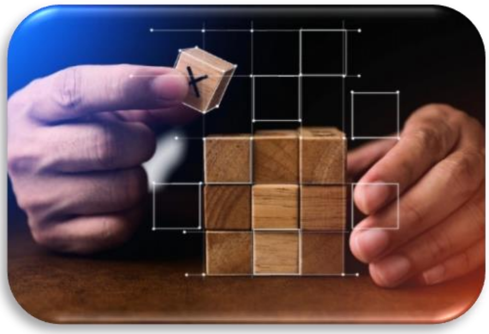
The ARCs, however, continue to be an important channel of loan recovery for banks and have a role to play in the field of asset management even in the post- IBC world. Their share in total amount involved across all four channels of recovery has ranged between 25 per cent and 35 per cent since the introduction of the IBC. Furthermore, they account for about 30 per cent of the total amount recovered through all channels.

Indian ARC Model and the Models in Other countries

The term ARC has been in usage in the Indian context; the common global parallel of it is an asset management company (AMC). AMCs can take two forms, those with a focus on bank resolution and those dealing with NPA resolution.

There have been several experiments of AMCs dealing with NPA resolution in other countries. Some of the successful ones include Securum of Sweden which was set up in 1992 and wound up in 1997, and which succeeded in recovering close to 86 per cent of the amount involved. Danaharta of Malaysia, set up following the Asian financial crisis and operational between 1998 and 2005, managed to recover about 58 per cent of the amount involved. Non-Performing Assets Trust (NPART) of Ghana that was in existence from 1989 to 1997 has also performed satisfactorily. While each of the above was a government-owned AMC, there have been experiments involving public- private partnership also. Spain created Sareb in 2012 with a lifespan of 15 years, involving private (including Spanish banks and financial institutions) and public equity in a ratio of 55:45. Similarly, Ireland set up National Asset Management Agency (NAMA) in 2009 with 51:49 state and private investors participation.

The Indian ARC model differs from the models in other countries in some fundamental ways. Firstly, ARCs in India were set up at a time when the NPA ratios of banks were significantly high; the gross NPA ratio was rising between 1998 and 2002 and was in the range of 10-14 per cent. While the increasing trend in NPAs could be deemed as a proximate cause for strengthening the asset resolution mechanism, the move to set up ARCs was part of the process of financial sector reforms and could be considered as being more proactive than reactive in nature. Secondly, as they were not strictly tasked with addressing any specific crisis, ARCs in India did not come into being for a pre-defined period. Thirdly, Indian ARCs have been private sector entities registered with the RBI. Public sector AMCs in other countries have often enjoyed easy access to government funding or government-backed funding. By contrast, capital constraints have often been highlighted as an area of concern for ARCs in India.



(Image source: website)

Coming back to our analysis of ARC, the growth of the ARCs has not been consistent over time and not always been synchronous with the trends in NPAs of banks and non-banking financial companies (NBFCs). The ARC industry began with the establishment of the Asset Reconstruction Company India Limited (ARCIL) in 2003. After remaining subdued in the initial years, a jump was seen in the number of ARCs in 2008, and then in 2016. Notwithstanding the increase in the number of

ARCs, the growth in their assets under management (AUM) has been largely trendless except for a major spurt in 2013-14. When compared with the volume of NPAs of banks and NBFCs, the AUM of ARCs has been on a declining trend except during the period of high growth in the AUM around 2013-14.

Although the number of ARCs has increased over time (currently over 220), their business has remained highly concentrated. Of the total AUM, about 60-70 per cent was held by the top-five ARCs in March 2020. Being private sector entities, the key shareholders of ARCs are banks and other financial institutions. In order to boost their capital base, ARCs were allowed to accept 100 per cent of foreign direct investment (FDI) through the automatic route in 2016.Notwithstanding the liberalisation relating to FDI, foreign entities account for a small portion of the total capital of these companies.

Business Model of ARCs

The business model of ARCs consists of three stages, which are discussed below:

Stage 1: The ARCs acquire NPAs from banks or financial institutions either through bilateral deals or auctions. After acquisition of the asset, they formulate schemes for inviting subscription to security receipts (SRs) by Qualified Institutional Buyers (QIBs) through one or more trusts set up exclusively for the purpose. The NPAs acquired are held in asset-specific or portfolio-specific schemes; the former is adopted when the size of the aggregate debt acquired from a bank or financial institution is large, while the latter type of scheme is invoked when the size of acquired debt is small, prompting the ARCs to create a portfolio of the debt from various banks or financial institutions. Debt can be acquired either through cash alone or a mix of cash and Security Receipts (SRs). To ensure that ARCs have more skin in the game of acquisition, they are required to invest a minimum of 15 per cent of the SRs under each scheme on an ongoing basis till the redemption of all SRs.

Stage 2: After asset acquisition, ARCs initiate the process of planning for resolution; the period for planning extends up to six months from the date of acquisition of assets from the originator. The resolution can take different forms, including change and takeover of the management of the business of the borrower, sale or lease of a part or whole of the business of the borrower, rescheduling of payment of debts payable by the borrower, enforcement of security interest, etc.

Stage 3: Following the resolution, ARCs start recovery of debt and work on the redemption of SRs. ARCs are allowed a period of five years to recover the dues. However, the period can be extended upto eight years subject to the approval of their Boards.

Acquisition of Assets

ARCs generally acquire assets from banks and financial institutions. While bilateral deals with sponsor banks are prohibited, no such restrictions exist for bilateral deals with financial institutions or for auctions conducted by the banks and financial institutions. Of the two modes, auctions have dominated the ARC deals till now.

(Image source: website)

Valuation of acquired assets is a critical business concern for ARCs in the process of acquisition. Considering that ARCs and banks are on two sides of the sale deal, a higher acquisition ratio (defined as acquisition cost to book value of assets) works in favour of banks. It has often been argued that a low acquisition ratio, and consequently a higher haircut, has hindered banks from getting stressed assets off their books. Over time, although the average acquisition ratio has gradually risen, it remains in the range of 30-35 per cent. Moreover, there continues to be a wide variation in the acquisition ratio across ARCs, with the variation too increasing over time.

Resolution of Assets

The acquisition of assets only marks the beginning of the operations of the ARCs; the second stage is about the resolution of acquired assets. More specifically speaking, the resolution methods of ARCs can be divided into five categories,

1. Rescheduling of payment of debt
2. Enforcement of security interest
3. Settlement of dues of borrower
4. Taking possession of assets
5. By sale of business

with ARCs preferring the method of rescheduling of the payment obligations over other methods. There has been a steady fall over time in the percentage of assets resolved by way of enforcing the security interest. Change in or takeover of management/taking possession of assets too has been used sparingly as a mode of resolution.

Recovery and Redemption of SRs

The third stage of operation of ARCs relates to the recovery and redemption of SRs. Recovery of SRs is a critical indicator of the performance of ARCs. As per the regulatory guidelines, ARCs have to disclose the NAV of the SRs issued by them, which are used for valuation of the SRs by investors. To determine the NAV, ARCs have to obtain a recovery rating from an accredited credit rating agency (CRA). The CRA generally decides its recovery rating based on an assessment of the resolution method adopted.

Recent developments regarding participation of ARCs under CIRP

Recently, the Reserve Bank of India stirred a debate regarding the role of an Asset Reconstruction Company in insolvency resolution by rejecting the bid submitted by an ARC for a distressed telecom player under **IBC**. UV Asset Reconstruction Company Limited **('UVARCL')** emerged as a successful resolution applicant in the Corporate Insolvency Resolution Process of Aircel Limited and its subsidiaries and received the nod of the National Company Law Tribunal in June 2020. Subsequently, RBI issued a show-cause notice to UVARCL on the ground that the acquisition did not conform to the guidelines under **SARFAESI Act.** Though RBI's notice has been currently stayed by the Delhi High Court, the debt industry is shrouded in doubts and speculations about an ARC's eligibility as a resolution applicant.

The interpretation could be that an ARC is formed for the purpose of carrying on the business of *asset reconstruction or securitisation or* both. In fact, section 10 of the SARFAESI Act prohibits an ARC from undertaking any other business without the prior approval of the RBI. The term 'asset reconstruction' has been defined as acquiring any right or interest of any bank or financial institution in any financial assistance (such as loans, guarantee, and credit facilities extended by such bank or financial institution) for repayment of such financial assistance. The statutory regime under SARFAESI Act is restrictive of the roles that an ARC can play in the realisation of outstanding dues. ARCs have to comply with certain conditions in order to hold more than 26% post-converted equity. Likewise, for taking over the management, ARCs are subject to eligibility conditions, procedural and reporting requirements under the RBI guidelines. Hence, the sphere of activities permitted to an ARC, remain a regulated affair and the language of the SARFAESI Act must be strictly construed.

Equity infusion does not fall within any permitted business of an ARC under SARFAESI Act, including asset reconstruction, and hence is barred. Asset reconstruction presupposes the acquisition of a right or interest in 'financial assistance' and not equity of the company. Besides, the object of an ARC currently contemplated under the statute is narrowly defined to mean the realisation of dues and not own and control stressed companies. Any equity investment by an ARC can be only in the manner envisaged under SARFAESI Act, that is, by way of conversion of debt and not the direct purchase of equity.

(Image source: website)

Concluding Observations

ARCs have been an integral part of the institutional infrastructure for asset resolution in India. Unlike many other countries that experimented with a public sector model of asset management companies marked by their existence for a pre-defined period following banking crises or crises-like situations, India introduced ARCs as private sector institutions as part of its financial sector reforms. Given the difference in the constitution and mandate, the course of evolution of Indian ARCs has been distinct in many ways as compared to their counterparts in other countries. The latest initiative of the Government of India, launching of National Asset Reconstruction Company Ltd (NARCL)is likely to start operations in the near future with equity participation from Banks/FIs and backed by government guarantee to address the problem of NPAs with public sector banks. Already efforts are on to identify and transfer NPA assets worth over Rs.80,000/- crores to NARCL. As stated earlier, the resolution efforts through the IBC process will also play a major role in bringing about satisfactory solution to the stressed portfolio of banks. Under the IBC process the recently introduced pre-pack resolution process, for MSMEs registered as Corporate or LLP, is expected to play a critical role in view of its inherent advantages over the CIRP.

Variable Capital Company (VCC) in India

CGRF Bureau

VCC is an alternative form of corporate vehicle which can be used for open-ended as well as closed-ended alternative and traditional fund strategies. It is a corporate vehicle with flexible capital because of which shares are created when investments are made, and shares are readily redeemable by shareholders. It has been designed for fund management industry.

The International Financial Services Centres Authority (IFSCA) a Statutory authority established by Government of India on April 27, 2020, under the International Financial Services Centres Authority Act, 2019 is a unified authority for the development and regulation of financial products, financial services and financial institutions in the International Financial Services Centre (IFSC) in India. At present, the Gujarat International Finance Tec-City (GIFT) IFSC is the maiden international financial services centre in India. Prior to the establishment of IFSCA, the domestic financial regulators, namely, RBI, SEBI, PFRDA and IRDAI regulated the business in IFSC.

IFSCA constituted a Committee of Experts under the Chairmanship of Shri K.P. Krishnan (retired IAS) for examining the suitability of the Variable Capital Company as a vehicle for fund management in the International Financial Services Centre in India.

The following were the terms of reference of the Committee:

- Comprehensive analysis of fund structures under Indian Trust Act and VCC. To examine VCC structure and suggest appropriate model/ framework that may significantly enhance the competitiveness of IFSC in India.
- Feasibility of introducing VCC as separate chapter in Companies Act, 2013 versus need of enacting a separate legislation.
- To explore alternative structures having characteristics like VCC.
- The Committee may also deliberate on any issues which may be considered necessary but not mentioned in the above terms of reference.

The IFSCA set up this Committee to explore the potential for allowing another legal structure – popularly known as a Variable Capital Company (VCC) – as an additional option through which asset managers could pool the investors' funds. The VCC structure dispenses with some of the key limitations of companies and LLPs and provides for higher regulatory standards than those applicable to trusts.

Fund management activities are an important pillar of the overall financial services ecosystem. In line with the mandate given to the Committee, it examined the relevance and adaptability of the VCC for the IFSC in India or alternative structures to attract fund business in the IFSC. Conventionally, pooling of funds in India is undertaken through three types of entities, namely, limited liability companies governed under the Companies Act, 2013; limited liability partnerships under the Limited Liability Partnership Act, 2008 and trusts governed under the Indian Trusts Act, 1882.

Recently, the Expert Committee on Variable Capital Company submitted its report to the International Financial Services Centres Authority (IFSCA).

The recommendations of the Committee are:

- Committee assessed the features of a VCC or its equivalent, in other jurisdictions such as Singapore, UK, Ireland and Luxembourg.
- Committee recommended the adoption of VCC-like legal structure for conducting fund management activity in IFSCs.
- Committee recognized that the legal framework governing entities that undertake fund management should provide for certainty and clarity to investors, effective segregation, and ring fencing of different pools of asset, the ability to issue different classes of shares, alterations to the funds' capital structure without regulatory approvals and the freedom to choose the appropriate accounting standards applicable to funds with different characteristics, the ability to wind up quickly.
- VCC structure dispenses with some of key limitations of Companies and LLPs. It provides for higher regulatory standards.

(Image source: website)

The full report of the Expert Committee on VCC is still not in the public domain and there is no clarity on the fiscal aspect. However, since globally VCC structures are tax-free and only end investors pay taxes in their home country, it is reported that Foreign Portfolio Investors (FPI) seek clarity on the tax implications of recently proposed VCC in financial centres such as Gujarat International Finance Tec-City (GIFT City).

Source:
https://pib.gov.in/PressReleasePage.aspx?PRID=1723511&s=08

Important Amendments in IBC in the Last 5 Years

B. Mekala,
Insolvency Professional

M.S. Elamathi,
Advocate, CS

S.No.	Date of Amendment	Amendment
1.	18th January 2018	✓ Insertion of Sec. 29A – Persons not eligible to be resolution applicant-- To prevent unscrupulous promoters to bid for their own Company. ✓ Amendment of Sec.35 that the Liquidator shall not sell the property of CD to the person is ineligible under Sec. 29A. ✓ Insertion of Sec.235A - Punishment where no specific penalty or punishment is provided
2.	6th February 2018	✓Amendment to Reg.35(1) –RP to Determination of Fair value and Liquidation value and provide to every member of CoC after obtaining confidentiality undertaking
3.	17th August 2018	✓ Insertion of Sec.12A - Withdrawal of application admitted under Sec.7,9 or 10. ✓ Amendment to Sec.21(8) that all decisions of CoC shall be taken by a vote of minimum 51% of voting share of FC. ✓ Amendment to Sec.22(3) which mandates Written consent from Insolvency Professional to act as RP of the CD. ✓ Amendment to Sec.30(1) that the resolution plan has to be submitted along with an affidavit stating that the applicant is eligible under section 29A. ✓ Insertion of Sec. 31(4) - To obtain the necessary approval required under any law for the time being in force within a period of one year from the date of approval of the resolution plan. ✓ Amendment to Sec.60(2) whereby an Application relating to insolvency resolution process, liquidation or bankruptcy of a corporate guarantor or personal guarantor as the case may be of the CD shall be filed before NCLT. ✓ Insertion of section 238A – Applicability of Limitation Act ✓ Insertion of section 240A - Application of IBC to MSME ✓ Insertion of the Twelfth Schedule regarding clause (d) of section 29A ✓ Amendment to Sec. 12/ Sec.22(2)/ Sec.27(2) /Sec. 30(4) /Sec. 33— The threshold of voting % of 75% got reduced to 66%, for Extension of CIRP/ Appointment of RP/Replacement of RP/Approval of Resolution Plan/To liquidate CD
4.	25th July 2019 (Notification)	✓ The liquidator shall liquidate the corporate debtor within a period of one year from the liquidation commencement date, (Prior to this it was 2 years) ✓ Model Timeline for Liquidation Process

5.	5th August 2019	✓ Amendment to Sec.12 that the CIRP process is to be completed within a period of 330 days. ✓ Amendment to Sec.30(2)(b) regarding payment of debt to operational creditors and dissenting financial creditors. ✓ Amendment to Sec.33 that the CoC may decide to liquidate the CD any time after its constitution and before the confirmation of resolution plan including any time before the IM
6.	15th November 2019 (Notification)	✓ Notified Sec. 94 to 187 so far as they relate to personal guarantors to corporate debtors. From 1st Dec. 2019 onwards, an application can be filed under Sec.95 of IBC by any of the creditors to whom an individual has given a personal guarantee in respect of the borrowings or dues of a corporate debtor (CD). A guarantor himself can also file an application under Sec.94. This is much like a Sec.10 application by the CD itself for corporate insolvency resolution. Applications have to be filed with the Adjudicating Authority which can be a National Company Law Tribunal (NCLT) or a Debt Recovery Tribunal (DRT).
7.	13th March 2020	✓ Amendment of Sec. 7- Financial Creditors who are allottees under a real estate project can initiate CIRP against a CD under IBC ✓ Amendment of sec. 11-CD may initiate CIRP against a CD under IBC ✓ Amendment of sec.14- License, permit registration etc. of the CD shall not be suspended on the ground of CIRP, there is no default in payment of current dues arising for the use or continuation of the license etc. ✓ Insertion of sec. 14(2A)-Supply of Essential goods and services shall not be terminated, except where such corporate debtor has not paid dues arising from such supply during the moratorium period or in such circumstances as may be specified. ✓ Amendment of section 16(1)- AA to Appointment IRP on the insolvency commencement date itself. ✓ Insertion of Sec. 32A- Liability for prior offences, etc. as this will give immunity to resolution applicant for qualifying against past offences.
8.	24th March 2020 (Notification)	✓ The minimum amount of default for the purpose of Sec.4 was increased to Rs.one Crore from Rs. One lakh keeping in view the covid19 pandemic difficulties faced by the MSME units.
9.	29th March 2020	✓ Insertion of Reg.40 C—Special Provision relating to time-line –Covid 19 Lockdown
10.	20th April 2020	✓ Insertion of Reg.47A-- Exclusion of period of lockdown (Liquidation)- Covid 19.
11.	5th June 2020	✓ Insertion of Sec.10A - Suspension of initiation of corporate insolvency resolution process for any default arising on or after 25th March 2020 for a period of six months. Got Extended for another six months and the suspension got lifted on 24th March 2021.
12.	4th April 2021 (Ordinance)	✓ Insertion of Chapter IIIA - Pre-Pack Insolvency Resolution Process. It consists of Sections 54A to 54P. Prepacks will be applicable to corporate debtor classified as MSMEs which meets the definition of MSME as per section 7 of the MSME Act and has committed a default of not less than Rs. 10 lakhs. ✓ PPIRP commences on the date of admission of application by AA and continues for a period of 120 (90 days for submission of plan to AA plus 30 days for AA to approve /reject the plan days thereof, without any provision for an extension.

Court Orders

CGRF Legal Team

India Resurgence ARC Private Ltd Vs Amit Metaliks Ltd & Anr.
Civil Appeal No.1700 of 2021
Hon'ble Supreme Court Order dated 13th May 2021.

Secured Creditors cannot contest the CoC approved Resolution Plan claiming that higher amount should be paid based on Security Interest held by them.

NCLT Kolkata Bench vide Order dated 07.08.2019 admitted M/s. VSP Udyog Private Limited into CIRP. During the CIRP, Resolution Plan submitted by M/s.Amit Metaliks Limited was approved by the Committee of Creditors (CoC) with 95.35% voting shares. Thereafter, the CoC approved Resolution Plan submitted by M/s.Amit Metaliks Limited (Successful Resolution Applicant) was also approved by NCLT on 20.10.2020.
India Resurgence ARC Private Limited (dissenting Financial Creditor) having a vote share of 3.94% and a CoC Member filed an appeal with NCLAT, primarily on the ground that the approved Resolution Plan failed to deal with the interest of all the stakeholders including the descending FC who was offered a meagre amount of slight over Rs.2 crores as against its admitted claim of amount exceeding Rs.13 crores without even considering the valuation of the security held by the dissenting FC in its Resolution Plan which had a valuation of approximately Rs.12 crores. It was contended by the dissenting FC that while approving the Resolution Plan value and quality of security interest of the Appellant was not considered by the Successful Resolution Applicant and the CoC. It was also contended that the manner of distribution and priority of share based on the value of security interest of a Secured Financial Creditor pursuant to Amendment in Section 30(4) of the Code has been over-looked.

NCLAT while dismissing the appeal observed that Section 30(4) of the Code provides that the CoC may approve a Resolution Plan by a vote which shall not be less than 66% of voting share of FCs. Such approval is to be done after considering the feasibility and viability of the Resolution Plan, the manner of distribution proposed therein having regard to the order of priority amongst the creditors in terms of the waterfall mechanism laid down in Section 53 of the Code including the priority and value of security interest of Secured Creditor besides other requirements specified by IBBI. *On a plain reading of this provision, it is manifestly clear that the considerations regarding feasibility and viability of the Resolution Plan, distribution proposed with reference to the order of priority amongst creditors as per statutory distribution mechanism including priority and value of security interest of Secured Creditor are matters which fall within the exclusive domain of CoC for consideration. These considerations must be present to the mind of the CoC while taking a decision in regard to approval of a Resolution Plan with vote share of requisite majority.* ***As regards amendment introduced in Section 30(4), be it seen that the amendment that it, introduced vide Section 6 (b) of Amending Act of 2019 vests discretion in the CoC to take into account the value of security interest of a Secured Creditor in approving of a Resolution Plan. It's a guideline and not imperative in terms, which may be taken into account by the CoC in arriving at a decision as regards approval or rejection of a Resolution Plan, such decision being essentially a business decision based on commercial wisdom of the CoC.*** *(emphasis added).* In this regard the observations of Hon'ble Apex Court in ***'Committee of Creditors of Essar Steel India Limited Vs. Satish Kumar Gupta and Others' (Supra)*** are significant. The Hon'ble Apex Court observed as under: -

"131. The challenge to sub-clause (b) of Section 6 of the Amending Act of 2019, again goes to the flexibility that the Code gives to the Committee of Creditors to approve or not to approve a resolution plan and which may take into account different classes of creditors as is mentioned in Section 53, and different priorities and values of security interests of a secured creditor. This flexibility is referred to in the BLRC Report, 2015 (see para 56 of this judgment). Also, the discretion given to the Committee of Creditors by the word "may" again makes it clear that this is only a guideline which is set out by this sub-section which may be applied by the Committee of Creditors in arriving at a business decision as to acceptance or rejection of a resolution plan. For all these reasons, therefore, it is difficult to hold that any of these provisions is constitutionally infirm."

It observed that is abundantly clear from Section 30(4) of the Code, that the considerations including priority in scheme of distribution and the value of security are matters falling within the realm of CoC. Such considerations, being relevant only for purposes for arriving at a business decision in exercise of commercial wisdom of the CoC, cannot be the subject of judicial review in appeal within the parameters of Section 61(3) of I&B Code. While it is true that prior to amendment of Section 30(4) the CoC was not required to consider the value of security interest obtaining in favour of a Secured Creditor while arriving at a decision in regard to feasibility and viability of a Resolution Plan, legislature brought in the amendment to amplify the scope of considerations which may be taken into consideration by the CoC while exercising their commercial wisdom in taking the business decision to approve or reject the Resolution Plan. Such consideration is only aimed at arming the CoC with more teeth so as to take an informed decision in regard to viability and feasibility of a Resolution Plan, fairness of distribution amongst similarly situated creditors being the bottom line. However, such business decision taken in exercise of commercial wisdom of CoC would not warrant judicial intervention unless creditors belonging to a class being similarly situated are not given a fair and equitable treatment.

(Image source: website)

Aggrieved by the decision of NCLAT, dissenting FC preferred an appeal with Hon'ble SC.

It was contended that the CoC could not have approved the resolution plan which failed to consider the priority and value of security interest of the creditors while deciding the manner of distribution to each creditor even though the legislature in its wisdom has amended Section 30(4) of the Code, requiring the CoC to take into account the order of priority amongst creditors as laid down in Section 53(1) of the Code, including the priority and value of the security interest of a secured creditor.

Hon'ble SC observed that the dissenting FC has not placed any objection before NCLT, while the Resolution Plan was under consideration for approval by NCLT. Hon'ble SC affirmed that regarding the question of fair and equitable treatment, though the NCLT and the NCLAT have returned concurrent findings in favour of the resolution plan yet, to satisfy ourselves, it had gone through the financial proposal in the resolution plan and no case of denial of fair and equitable treatment or disregard of priority is made out.

Hon'ble SC further observed that In ***Jaypee Kensington Boulevard Apartments Welfare Association and Ors V. NBCC (India) Ltd and Ors****, this Court repeatedly made it clear that a dissenting financial creditor would be receiving the payment of the amount as per his entitlement; and that entitlement could also be satisfied by allowing him to enforce the security interest, to the extent of the value receivable by him. It has never been laid down that if a dissenting financial creditor is having a security available with him, he would be entitled to enforce the entire of security interest or to receive the entire value of the security available with him. It is but obvious that his dealing with the security interest, if occasion so arise, would be conditioned by the extent of value receivable by him.*

The extent of value receivable by the appellant is distinctly given out in the resolution plan i.e., a sum of INR 2.026 crores which is in the same proportion and percentage as provided to the other secured financial creditors with reference to their respective admitted claims. Repeated reference on behalf of the appellant to the value of security at about INR 12 crores is wholly inapt and is rather ill-conceived.

The limitation on the extent of the amount receivable by a dissenting financial creditor is innate in Section 30(2)(b) of the Code and has been further exposited in the decisions aforesaid. ***It has not been the intent of the legislature that a security interest available to a dissenting financial creditor over the assets of the corporate debtor gives him some right over and above other financial creditors so as to enforce the entire of the security interest and thereby bring about an inequitable scenario, by receiving excess amount, beyond the receivable liquidation value proposed for the same class of creditors. (emphasis added)***

It needs hardly any emphasis that if the propositions suggested on behalf of the appellant were to be accepted, the result would be that rather than insolvency resolution and maximisation of the value of assets of the corporate debtor, the processes would lead to more liquidations, with every secured financial creditor opting to stand on dissent. Such a result would be defeating the very purpose envisaged by the Code; and cannot be countenanced.

While rejecting the appeal, Hon'ble SC referred the observations of SC in ***Essar Steel*** as follows: -

"85. Indeed, if an "equality for all" approach recognising the rights of different classes of creditors as part of an insolvency resolution process is adopted, secured financial creditors will, in many cases, be incentivised to vote for liquidation rather than resolution, as they would have better rights if the corporate debtor was to be liquidated rather than a resolution plan being approved. This would defeat the entire objective of the Code which is to first ensure that resolution of distressed assets takes place and only if the same is not possible should liquidation follow.

Kamla Industrial Park Limited vs. Monitoring Committee of
Metallica Industries Ltd & Registrar of Companies
IA No.1077 of 2020 in C.P.(IB) No.1329/MB/2017
NCLT Order dated 19th May 2021.

Successful Resolution Applicant cannot be held accountable for the continuing statutory non-compliances pertaining to the Corporate Debtor prior to date of approval of Resolution Plan by NCLT.

Metallica Industries Limited [Corporate Debtor (CD)] was admitted into CIRP by an order dated 13.04.2018. Under the CIRP, the resolution plan submitted by Kamla Industrial Park Ltd [Successful Resolution Applicant (SRA)] was approved by NCLT Mumbai Bench on 16.10.2019.

Annual Returns and Balance Sheets after 31.03.2013 had not been filed. As no authentic data was submitted by the disqualified directors to the SRA, SRA was not able to access any of the relevant documents of CD prior to 16.10.2019. The present directors were not able to sign any anterior document but could submit only returns and statements for the period after 16.10.2019.

SRA interacted with the Officials of Registrar of Companies (RoC) and made representation to explain the difficulties faced by SRA in getting the documents prior to 16.10.2019. However, RoC officials insisted that SRA must file all previous annual returns and balance sheet, as otherwise CD would continue to remain in default of its statutory obligations.

As SRA has facing difficulty in implementation of the Resolution Plan.

SRA filed an application with NCLT praying to direct the RoC not to insist upon compliance of any regulatory requirements of the Companies Act, 2013, pertaining to the period prior to the 16.10.2019, not take any coercive action against the CD arising out of the same and further to waive the requirement of filing of annual returns or balance sheets for the period of time prior to the 16.10.2019.

SRA further submitted that the CD initially used extensible business reporting language (XBRL) for the purpose of filing with the RoC. As the share capital of the CD has been reduced much below the threshold requirement for filing financials through XBRL under the approved Resolution Plan, the SRA should not be forced to file the accounts through XBRL, since as per rules, once XBRL is adopted it would not be possible for the Company to use another medium for filing.

RoC in its reply stated that it has no authority to waive the statutory compliances mandated in the Companies Act, 2013. Further, they emphasised that Section 17(2)(e) and Section 23(2) of the Code requires that the Resolution Professional shall comply with the requirements under any law for the time being in force and the same would accordingly apply to the SRA who takes over the CD. Besides, General Circular No. 08/2020 dated 06.03.2020 issued by the Ministry of Corporate Affairs (MCA), clarified that the Annual Returns in E-form no. MGT-7 and the Financial Statements in E-form No. AOC-4 and other documents as per the provisions of the Act shall have to be filed along with the required fees till such time the Company remains under CIRP. Therefore, the statutory requirements could not be waived, as sought for.

(Image source: website)

Though NCLT on 05.10.2020, considering the technical issues, instructed the SRA to take up the matter with the RoC for resolution of the issue. The matter could not resolve their intervention was sought again by SRA.

NCLT noted that as it would appear from the materials, the SRA has taking all possible steps in right earnest to get the Resolution Plan implemented. NCLT observed that "***The e-Filing of statements and returns obviously could not have envisaged all eventualities arising out of a successful resolution of a Corporate Debtor. It is settled that when the technical considerations are pitted against the substantial justice, cause of substantial justice would be preferred. Therefore, interest of justice requires that the Applicant shall have to be provided with all the support for getting the statutory compliances done***. *(emphasis added)"*

NCLT also noted that the new management of the CD could not be held liable and responsible for the malfeasance and misfeasance committed by the former promoters / directors of the CD in this regard.

Quoting the principles held up by the Supreme court in Essar Steel India Ltd, though in this case not related due to any new claim but echoing the same principle and sentimental NCLT.

NCLT after taking the facts and circumstances of the case into consideration and the principles, allowed the application and ordered that the present management of the Corporate Debtor shall not in any manner be held accountable for the default committed by the Corporate Debtor or its promoters / directors prior to 16.10.2019. Further, it directed the RoC or the appropriate authority should consider accepting Returns and Statements in physical form in case of incompatibility in online submission / e-filing.

Rakesh Kumar Agarwal vs Liquidator of M/s.Asis Logistics Ltd
Company Appeal (AT) (Insolvency) No.1034 of 2020
NCLAT Order dated 1st June 2021.

Promoters of the Corporate Debtors which is still under liquidation are eligible to file Scheme under Section 230 of the Companies Act, 2013, if the Corporate Debtor fall under MSME classification pursuant to change in the classification of MSME issued under MSME Act vide Notification dated 01.06.2020

Asis Logistics Limited [Corporate Debtor (CD)] filed an application for initiation of CIRP under Section 10 of the Code and the same was admitted by NCLT on 11.01.2018. As no resolution plan was received during CIRP, a resolution was passed by CoC with 97.37% voting share for liquidation of CD on 26.10.2018. An application for liquidation was filed with NCLT and accordingly Order liquidating the CD was passed on 28.08.2019.

(Image source: website)

During the liquidation process, the Promoters (Appellant) submitted Scheme of Arrangement under Section 230 of the Companies Act, 2013. The Scheme submitted by the Promoters was approved by stakeholders of the CD and an application for approval of the Scheme of Arrangement was filed before the NCLT. Subsequently, the said application for approval the Scheme of Arrangement was withdrawn in view of the amendment made in Regulation 2B of IBBI (Liquidation Process) Regulation, 2016, on 06.01.2020 by virtue of which the Promoters became ineligible to submit the Scheme of Arrangement under section 230 of the Companies Act, 2013 in the Liquidator Process of the CD.

Thereafter, the Central Government vide Notification dated 01.06.2020 amended the MSME Act wherein certain changes were made in the criteria for classification of an enterprises as Mirco, Small & Medium. In view of the said amendment in MSME Act, the Promoters again became eligible to submit the Scheme under section 230 of the Companies Act, 2013 in the Liquidation Process. Hence, the Promoters again filed an application with NCLT seeking permission to propose a Scheme and a direction to the Liquidator to consider the said Scheme.

NCLT rejected the application and held that the CD at this stage cannot claim it to be an MSME and take benefits of the MSME in view of the amendments vide notification dated 01.06.2020 with came into effect from 01.07.2020 by having its retrospective effect when admittedly on the date of filing of Application under Section 10 of the Code, the CD does not fall under the criteria of MSME.

Aggrieved by the decision of the NCLT, the Promoters filed this appeal with the NCLAT.

Learned Counsel for the Promoters (Appellant) admitted that in the present case when the Application under Section 10 was filed and CIRP initiated the Corporate Debtor was not falling in the criteria/classification of MSME. The amendment came during the liquidation process. He also submitted that the Hon'ble NCLT, grossly misunderstood the entire Application on the presumption that the Appellants have sought any relief on the basis of retrospective implementation of the notification dated 01.06.2020. On the contrary, the Appellants have sought implementation of the notification only prospectively knowing very well that the notification dated 01.06.2020 is effective prospectively and not retrospectively.

Further he submitted that the case of the Appellants is simple that at the time of filing the Application by the Corporate Debtor under Section 10 of the IBC on 11.01.2018 there was no restriction on the promoter to give the Resolution Plan and there is no restriction under Section 230 of the Companies Act, 2013. Since Section 29A of the IBC was not introduced and not in its existence at the time of filing of Application under Section 10. The notification of Section 29A of the IBC was issued by the Government of India only on 19.01.2018 whereby the restriction was imposed on the Promoter of the Corporate Debtor submitting the Resolution Plan. The Present case of the liquidation order of the Corporate Debtor was passed on 28.08.2019 and on which date also there was no restriction on the promoters to submit the scheme in terms of Section 230 of the Companies Act, 2013.

Learned Counsel submitted that for filing scheme under Section 230 of the Companies Act, 2013, the CD is not required to be MSME. The scheme under Section 230 of the Companies Act, 2013 can be filed at any stage of liquidation and if the promoters filing the scheme the relaxation is given, if it is MSME. As per the latest notification issued by the Government of India the Appellants being the promoters are eligible and there is no bar on the promoters at this stage for filing this scheme under Section 230 of the Companies Act, 2013 before the liquidator. He also submitted that the promoters had earlier complied the 90 day's limit when the liquidation order was passed.

Learned Counsel for the Promoter relied on the Judgement of the Hon'ble Supreme Court in the matter *'Swiss Ribbons Pvt. Ltd. vs Union of India' dated 25.01.2019 and 'Committee of Creditors of Essar Steel India Limited vs Satish Kumar Gupta & Ors.'* dated 15.11.2019, wherein the Hon'ble Supreme Court in both the judgements held that *"Preamble of the Code provide that liquidation is the last resort and it is duty of the RP/liquidator to explore all possibilities to keep the unit as going concern and take steps for revival within the ambit of the Code and liquidation of assets per- se would only be resorted if these steps are not possible."*

Decision of the Appellate Tribunal

Hon'ble NCLAT set aside the order of NCLT and held that it is settled law as per the decisions of the Hon'ble Supreme Court that the liquidation is only the last resort and as per the preamble of the IBC the main object of the Code is in resolving corporate insolvencies and not the mere recovery of monies due and outstanding. The Appellant being eligible to submit a scheme by virtue of an amendment to Section 7 of MSMED, Act 2006 vide notification dated 01.06.2020 and passed order that the Appellants are allowed to submit a scheme of arrangement to the liquidator of the Corporate Debtor and the liquidator shall consider the scheme of arrangement in accordance with the law.

Bank of India & Others Vs RP of Ferroy Alloys Corporation Ltd
Company Appeal (AT) (Insolvency) No.590 of 2020
NCLAT Order dated 28th May 2021.

Even if the CD had enough liquidity to run the Company as a going concern, the act of the Banks to adjust the credit balance in the CC Account towards the debit balance after CIRP commencement cannot be justified.

NCLT Kolkata Bench vide Order dated 06.07.2017 admitted Ferroy Alloys Corporation Limited [Corporate Debtor (CD)] into CIRP and the Resolution Plan for the CD was approved on 30.01.2020.

During CIRP, the Bills under Lender of Credit (LC) facility maturing during the CIRP were honoured by the erstwhile RP from the revenue generated by the CD which was making good profits and had accumulated enough cash balance. Hence, the erstwhile RP chose to reduce the utilization of the fund-based facilities and had squared off the Cash Credit Facilities with all the Banks.

The new RP after assuming charge requested the Banks to resume the working capital limits and to reimburse all the amounts which were appropriated. However, the

Banks took a stand that they did not maintain any current account from the date of commencement of the CIRP and hence the question of appropriation from the current account does not arise. They further added that since the company was a going concern and generating profits it did not have any issue in servicing the bills under LC.

Hence, the new RP filed an application with NCLT under Section 14 read with Section 17 and Section 60(5) of the Code seeking direction against the Banks to reimburse all the amounts appropriated by them after the insolvency commencement date, together with the amount appropriated towards interest payment and further resume the working capital limits as available to the CD as on the insolvency commencement date. NCLT vide its Order date 02.03.2020 has directed to reverse the appropriation of payments made by Banks during CIRP.

Aggrieved by the decision of NCLT Bench, Banks have preferred an appeal with NCLAT.

RP alleged that the amount received by the Appellants Banks were preferential in nature as defined under Section 43 of the IBC and that the Banks have violated Section 14 of IBC.

The Appellant Banks stated that the operation in the accounts was allowed as per the directions of this Tribunal vide an Order dated 09.08.2017 and the credit was received in the normal course of business. Appellant Banks further stated that amount received by the Banks were directly remitted by the erstwhile RP and there was a conscious business decision to reduce the interest expenses as a prudent business manager would do, the amount remitted by the erstwhile RP and received by the Appellant Banks during CIRP does not qualify to be treated as preferential transaction and hence, the amount of such credit is not reversible. Therefore, the amount utilized after the Insolvency Commencement Date is to be treated as Insolvency Resolution Process Cost and need not be reversed.

NCLAT after noting that the amounts were honoured partly by margin held as FDR and partly by funds of the CD deposited in its Cash Credit Accounts, ***opined that merely because the CD had enough liquidity to run the Company as a going concern, the act of the Appellant Banks to adjust the credit balance in the Cash Credit Account towards the debit balance after CIRP commenced, cannot be justified (emphasis added).*** It reiterated that IBC provides that Claims filed by the Creditors during the CIRP shall stand crystallized and will not be settled during the CIRP in preference over other Creditors. It observed that if the Appellant's argument is accepted, then the act of recovering receivables, under the garb of normal course of business will change the status of all the claims which would be in complete violation of Section 14 of the Code.

Hon'ble NCLAT is of the view that adjusting of the 'Claims' by the Appellant Banks during the CIRP out of the funds of the 'Corporate Debtor' results in unjust enrichment of the Banks and further, crediting amounts towards non-fund and fund-based accounts during the moratorium period is against the provisions of Section 14 of the Code.

Hon'ble NCLAT dismissed the Appeal as there is no illegality or infirmity in the Order of the NCLT.

A Winning Leadership Role

S. Rajendran,
Director-CGRF

There are numerous best-sellers in the world dealing at length on the role of a leader, the nuances of what he should and shouldn't do, et al. Hearing it from a person who has seen it and who has done it always make it special, isn't it?

Jack Welch, you might be knowing, was one of the best-known global leaders. He was a chemical engineer and started his career in General Electric (GE) in 1960's. He rapidly rose through the hierarchy, led the large business conglomerate as its CEO for about 20 years and retired in 2001. He made a famous thumb rule for GE's business: That GE will be either No.1 or No.2 in any business. No question of being a mediocre player in any industry.

He earned a nickname "**Neutron Jack" for** cutting thousands of jobs. He bought and sold scores of businesses, expanded GE into financial services and produced steadily rising profits. He passed away in March 2020, but he has left a big legacy in the leadership practices. **"Jack: Straight from the Gut" and "Winning"**, the books brought out by him would speak loud for years the clarity in leadership thinking.

I am glad to highlight some of the tried and tested leadership roles Jack Welch has brought out in his book "Winning". You won't miss the power and punch in each of these eight things the leader does.

1. **Leaders relentlessly upgrade their team, using every encounter as an opportunity to evaluate, coach and build self-confidence.**
2. **Leaders make sure people not only see the vision, they live and breathe it.**
3. **Leaders get into everyone's skin, exuding positive energy and optimism.**
4. **Leaders establish trust with candor, transparency, and credit.**
5. **Leaders have the courage to make unpopular decisions and gut calls.**
6. **Leaders problem and push with a curiosity that borders on skepticism, making sure their questions are answered with action.**
7. **Leaders inspire risk taking and learning by setting the example.**
8. **Leaders celebrate.**

Jack Welch goes on to say that **"performing balancing acts every day"** is leadership. How true it is in today's context!! Companies having healthy balance sheets are gone in no time when the Covid-19 pandemic hit hard.

There are conflicting demands in business – both short term results and long-term endurance. There are several paradoxes in the leadership traits. Like for example, the leader should be assertive and commanding while at the same time he should embrace people who takes risks especially when they fail. Leave alone business, each day in life is a challenge. So, it is a brand-new chance for you to get better at a job. Believe me, no one is perfect at that. As Jack says, **"You can only give it everything you've got."**

Right people in right jobs

(Image source: website)

In expounding his thoughts on leadership, Jack dwells at length on the importance of having right people in the right jobs. **"Hiring good people is hard. Hiring great people is brutally hard. And yet, nothing matters more in winning than getting the right people on the field. All the clever strategies and advanced technologies in the world are nowhere near as effective without great people to put them to work."**

It is remarkable to have such a simple but powerful insight on the role of right people in winning. He further drills it hard: "It is so easy to hire people you like, because you will be spending a lot of your waking hours with them. It is also easy to hire people with relevant experience as they will get the job done. But friendship and experience are never enough. Every person you hire has to have integrity, intelligence and maturity." He adds further: "Look hard for people with positive energy, ability to energize others, the courage to make tough yes-or-no decisions, ability to get things done and finally, the passion."

Well, if you think that these golden rules are more than a mouthful to digest, hold on. He has something more to offer. It's amazing when he says that while hiring a senior level person, in addition to the above tests, look for authenticity, foresight, the willingness to draw on others for advice and resilience."

If you are able to listen to his calls with an open mind, and put all these things together, you have a winning team!!

Tail piece

I have great pleasure to add here that in our very own organization, we have many brilliant leaders in their own right and it is a treat to watch them how they play their roles with elan in times of stress and challenge. And trust me, we are passively sowing the seeds of leadership in the minds of younger players and before long, they will bloom to the delight of the team!!

Feedback Matters

Nice issue covered almost all topics related to IBC. Congrats and best wishes.

- Mr. K. Sundarapandian
Registered Valuer

Do you Know

Draft of the Code on Social Security (Employee's Compensation) (Central) Rules, 2021 published inviting objections and suggestions from the stakeholders - reg.

Ministry of Labour and Employment, Government of India has published the draft rules relating to Employee's Compensation under the Code on Social Security, 2020 inviting public comments and suggestions from all stakeholders vide Notification dated 3rd June 2021. Objections and suggestions, which may be received from any person with respect to the said draft rules within a period of 45 days from 3rd June 2021, will be considered by the Central Government.

Do you Know

Government Simplifies Registration Process for MSMEs. Only PAN, Aadhaar Required for MSME Registration

Minister for Road Transport & Highways and Micro, Small and Medium Enterprises, Shri Nitin Gadkari announced simplification of process for registration of Micro, Small and Medium Enterprises. Addressing a webinar of SME Street Game Changers Forum, Shri Gadkari said that now only PAN and Aadhaar will be required for registration of MSMEs. *[Source: Press Release, PIB, dated 15th June 2021]*

MCA Cirular

MCA removes restrictions on matters to be dealt in Board & Committee Meetings through Video Conferencing (VC) or Other Audio-Visual Means (OAVM).

MCA vide Notification dated 15th June 2021 has omitted Rule 4 of the Companies (Meetings of Board and its Powers) Rules, 2014, which barred certain matters such as approval of financial statements, Board's report, prospectus etc. from being dealt with in a meeting held through Video Conference (VC) or Other Audio-Visual Means (OAVM).

It is to be noted that in the light of COVID-19 pandemic, MCA vide Notification dated 30th December 2020 allowed Companies to transact these items under the said Rule via VC/OAVM till 30th June 2021.

Do you Know

EPFO extends deadline for mandatory UAN-Aadhaar linking to 1st Sep.2021.

The EPFO had decided to make Aadhaar seeding compulsory after a labour ministry notification which mandated the ministry and bodies working under it to seek Aadhaar number from the beneficiaries under the Social Security Code.

The date of implementation for filing ECR (electronic challan cum receipt or PF return) with Aadhaar verified UANs has been extended from 1st June 2021 to September 1, 2021, vide Circular dated 15th June 2021 issued by the Employees' Provident Fund Organisation (EPFO). Earlier, the EPFO had set the deadline as June 1st, 2021.

IBC Help Line

CGRF is Proud to Launch
cgrfibchelpline@gmail.com

Please feel free to drop a mail for any query in IBC. Information shared will be kept confidential. CGRF team will respond within 24 hours.

CGRF offers online/class-room Awareness/Training sessions on Corporate Laws, IBC, and other Commercial Laws.

We are glad to share with you that **CREATE & GROW RESEARCH FOUNDATION (CGRF)** is a premier, not-for-profit research organization established as a Section 8 Company under the Companies Act, 2013. CGRF has been organizing seminars and Awareness programs on IBC and various other corporate laws to bankers, corporate professionals, faculty members of Universities, Colleges, Legal Professionals, Students, Government Organizations like EPFO, ESIC, Income Tax, GST, etc.

Training capsules are exclusively designed meeting specific client requirements on following domains:

Companies Act 2013
Insolvency & Bankruptcy Code 2016
Intellectual Property Laws
Competitions laws
Labour Laws
Excellence in Management
Contract Management
Proxy Advisory Services for Institutional shareholders

We have rich expertise on the abovesaid commercial laws with practical exposure in several industries. Our association with all the major banks gives an edge to provide professional training on practical aspects. We also provide classroom training for students on latest developments in business environment, regulatory domain and challenges faced, etc. Online sessions are also available for 2 hours / 4 hours.

Our training sessions to various educational institutions, bankers and Government departments have been received well with appreciable improvement in recognizing importance of updating knowledge in relevant fields.

Call for more information: Ms. Priya Karthick - Contact No: 044 - 2814 1604.

CREATE & GROW RESEARCH FOUNDATION
2nd Floor, Evalappan Mansion, No.188/87,
Habibullah Road, T.Nagar, Chennai - 600 017
(Near Kodambakkam Railway Station)
Phone: 044 2814 1604 | Mobile: 94446 48589 / 98410 92661
Email: create.and.grow.research@gmail.com
Website: createandgrowresearch.org

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- Assisting Corporates (MSME) in preparing Base Resolution Plan under Pre-Pack Scheme
- 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

Providing supporting services to IPs:

- Management of operations of the Corporate Debtor
- 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

Independent Advisory Service:

- Admissibility of Claims
- Validity of decisions taken by CoC
- Powers and duties of directors under CIRP
- Resolutions Plan / Settlement Plan
- Repayment Plan by Personal Guarantors to Corporate Debtors
- 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

Registered Office:

CREATE & GROW RESEARCH FOUNDATION

2nd Floor, Evalappan Mansion, No.188/87, Habibullah Road,
T.Nagar, Chennai - 600 017. (Near Kodambakkam Railway Station)
Phone: 044 2814 1604 | Mob: 94446 48589 / 98410 92661
Email: createandgrowresearch@gmail.com
Website: www.createandgrowresearch.org