COMMENTS ON THE PROPOSED CHANGES TO REDUCE DELAYS IN THE CORPORATE INSOLVENCY RESOLUTION PROCESS

MAY 2022

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PROPOSED BY CIFL - CENTRE FOR INSOLVENCY AND FINANCIAL LAWS

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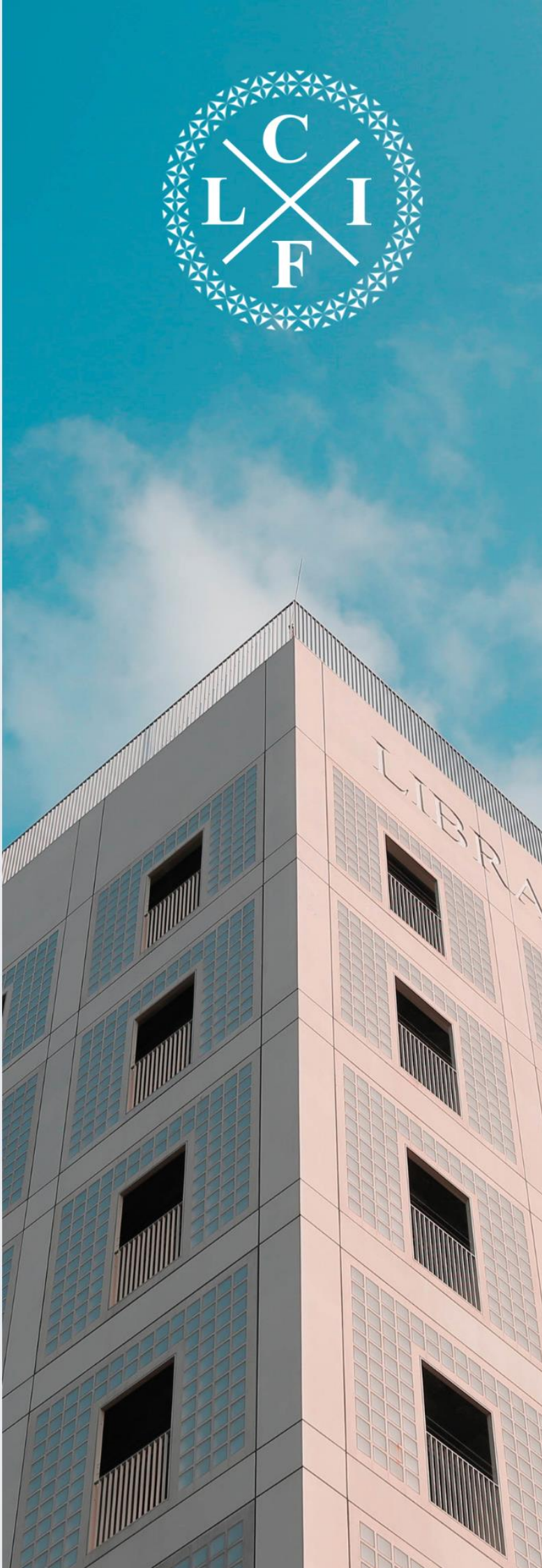

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The Centre for Insolvency and Financial Laws has given comments on the IBBI's discussion paper titled "Consultation paper on issues related to reducing delays in the corporate insolvency resolution process" ["**Consultation Paper**"] dated 13th April, 2022.

Table of Contents

PART 1: SUBSTANTIATING DEFAULT IN ADMITTING APPLICATIONS BY OPERATIONAL CREDITORS

The first part of Consultation Paper deals with documents required to be submitted by the operational creditor for proving their transaction and default by the corporate debtoe as under Section 9 of the Insolvency and Bankruptcy Code, 2016 ("IBC"). The primary aim of proposed amendment is to reduce delay in admission or rejection of application made by an operational creditor. This is sought to be achieved by including copies of GSTR-1 and GSTR3-B along with e-way bill for easier verification and admission of claims.

1. Time taken for admission of applications

Section 9 of the IBC prescribes a time period of 14 days for admission or rejection of application filed by an operational creditor. However, the Consultation Paper shows that average time period taken for admitting such applications in past financial year was 650 days. In 41% of the applications, this process took more than one year. Furthermore, the admission process extended beyond two years in 39% of the cases.

2. Proof of claim under the IBC and CIRP Regulations

Section 9(3) of IBC stipulates a list of documents that are to be furnished by the operational creditor along with the CIRP application. It includes: (i) demand notice sent to the CD (ii) Affidavit stating that the corporate debtor has not given any notice specifying dispute of the unpaid operational debt (iii) Copy of certificate from financial institution confirming that the operational debt is unpaid (iv) such other information as may be prescribed.

This additional information regarding proof of claims is contained in Regulation 7 of the Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 ("CIRP Regulations") which includes: (i) records available with Information Utility (ii) Contract for supply of goods or services (iii) invoice demanding payment (iv) order by court or tribunal (v) financial accounts.

Regulation 2A of the CIRP Regulations stipulates the category of documents that constitute evidence of default in applications filed by financial creditors. However, there is an absence of an equivalent provision for operational creditors even though 51% of CIRP applications are

filed by them.[1] The proposed amendment in para 8 of the Consultation Paper recommends addition of Regulation 2B that would specifically deal with record or evidence of transaction, debt and default for operational creditors. It mandates submission of GSTR- 1 and GSTR- 3B along with e-way bill wherever applicable.

This would bring in more certainty in the procedure for establishing proof of claim. Consequently, it would reduce delays occurring during the stage of admission of application as the claims would be easily verifiable. Therefore, this proposed amendment is a welcome step as it promotes timely resolution of debt. But, it should also be taken into consideration that this regulation would only be applicable to the operational creditors registered under GST. Other operational creditors such as workers, employees and statutory authorities are not included in its ambit. Hence, there is a need to add a provision regarding evidence of default in cases of statutory dues and employees' claims.

[1] IBBI Quarterly Newsletter Jan-March 2022, p.13. Available at https://www.ibbi.gov.in/uploads/whatsnew/08933bb5e16cab360074d3ef1640452a.pdf

PART 2: FACILITATING INFORMATION AVAILABILITY FOR THE PREPARATION OF INFORMATION MEMORANDUM AND PREPARATION OF AVOIDANCE APPLICATIONS

The proposed amendment in para 16 of the Consultation Paper implies that IRP or RP would be empowered to provide a time window for seeking information from the members, promoters, partners, board of directors and joint venture partners. This would be without prejudice to Section 19(2) under which an IRP can filed application before the adjudicating authority for necessary directions on account of non-cooperation from promoters of corporate debtor.

IRP or RP would be in a better position to streamline the insolvency resolution proceedings if they are entitled to fix a time window for information collection. Various stakeholders are more likely to abide by such timeline as the proposed amendment would impose such a specific legal obligation upon them. Along with the stakeholders mentioned in the proposed amendment, the obligation to share information in a swift manner should also be imposed upon other government agencies.

PART 3: DEALING WITH AVOIDANCE APPLICATIONS AFTER CLOSURE OF CIRP

The RP or IRP demits office when the resolution plan is approved. The committee of creditors also does not play an active role thereafter. However, some avoidance applications may still await adjudication. Under the present legal regime, it is unclear as to who would then continue these proceedings. The amendment proposed in para 23 of the Consultation Paper states that the resolution plan should specify the manner in which proceedings in respect of avoidance transactions or fraudulent or wrongful trading would be pursued after the approval of resolution plan.

But, it is pertinent to note that a few creditors may also be involved in the alleged avoidance transaction. The following excerpt from the UNCITRAL Legislative Guide on Insolvency law supports this possibility in para 151:

> "Transactions are typically made avoidable in insolvency to prevent fraud (e.g. transactions designed to hide assets for the later benefit of the debtor or to benefit the officers, owners or directors of the debtor); to uphold the general enforcement of creditors' rights; to ensure equitable treatment of all creditors by preventing favouritism where the debtor wishes to advantage certain creditors at the expense of the rest; to prevent a sudden loss of value from the business entity just before the supervision of the insolvency proceedings is imposed; and, in some States, to create a framework for encouraging out-of court settlement—creditors will know that last-minute transactions or seizures of assets can be set aside and therefore will be more likely to work with debtors to arrive at workable settlements without court intervention."

If the discretion to decide manner in which proceedings are to be conducted completely rests with the creditors, it may hinder its fair adjudication and timely completion. To avoid this, the adjudicating authority could scrutinise the manner of proceedings mentioned in the resolution plan by taking into account the creditors' involvement, if any, in the avoidance transaction.

PART 4: SIGNIFICANT DIFFERENCE IN VALUATIONS DURING A CIRP AND APPOINTMENT OF A THIRD VALUER

1. Present valuation system

Regulation 35 of the CIRP Regulations lays down that the fair value and liquidation value of the corporate debtor shall be determined by two registered valuers and the values should be computed in accordance with internationally accepted valuation standards. While arriving at this value if the two estimates of a value are significantly different, the RP may appoint another registered valuer who submits an estimate of the value computed in the same manner. The average of the two closest estimates of a value is deemed as the fair value or the liquidation value, as the case may be.

2. Proposed amendment adding threshold of 25%

Under the present regime, the RP enjoys discretion of appointing a third valuer if the estimates are significantly different. The proposed amendment sets a threshold of 25% which would be considered as a 'significant difference' for appointment of third valuer. This standard would increase objectivity and certainty in the valuation process. The appointment of a third valuer in case of marginal differences would be undesirable because it would act as an unnecessary burden on the liquidation estate. Similarly, accurate valuation of assets is crucial for maximisation of their value. Therefore, the proposed amendment is a positive step as it would balance the interests of all the stakeholders.

Specific Comments:

Sr. No.	Issue	Proposed Amendment	Comments
1.	Evidence of Default	It is proposed that GSTR-1 and GSTR-3 along with e-way bill shall be considered as evidence in case of application filed by operational creditors.	This is a welcome step as it would bring in more certainty in procedure for establishing proof of claim thereby reducing delays during the stage of admission. However, this amendment would only be applicable to operational creditors registered under GST. Hence, there is a need to insert provisions relating to proof of claim for applications filed by employees and government.
2.	Information availability	It is proposed that IRP or RP shall be empowered to prescribe a time window within which members, promoters, partners, board of directors and joint venture partners of the corporate debtor shall be obligated to provide the required information.	The IRP or RP would be in a better position to streamline the insolvency resolution proceedings if they are entitled to fix a time limit for information collection. Various stakeholders are more likely to abide by such timeline as the proposed amendment would impose such a specific legal obligation upon them. Along with the stakeholders mentioned in the proposed amendment, there must also be a mechanism to ensure swift sharing of information by other

			government agencies if necessary.
3.	Continuation of avoidance applications after the closure of CIRP	It is proposed that the resolution plan should mandatorily specify the manner in which avoidance proceedings would be pursued post the approval of resolution plan.	If the discretion to decide manner in which proceedings are to be conducted completely rests with the creditors, it may hinder its fair adjudication and timely completion. To tackle this, the adjudicating authority could scrutinise the manner of proceedings mentioned in the resolution plan by taking into account the creditors' suspected involvement, if any, in the avoidance transaction.
4.	Appointment of a third valuer	It is a proposed that a third valuer should be appointed if the difference in the two estimates is 25% in value.	This standard would increase objectivity and certainty in the valuation process. The appointment of a third valuer in case of marginal differences would be undesirable because it would act as an unnecessary burden on the liquidation estate. Similarly, accurate valuation of assets is crucial for maximisation of their value. Therefore, the proposed amendment is a positive step as it balances the interests of all the stakeholders.

ABOUT CIFL

The Centre for Insolvency and Financial Laws (CIFL) at MNLU Mumbai aims to act as a think-tank in furtherance of the principal objective of raising awareness about financial laws in theory and practice, as well as conducting high-quality research in the field to assist policymakers.

The Centre is premised on the objective of establishing a culture of financial laws by educating the next generation of lawyers and law students through seminars, conferences, workshops and symposiums. The Centre will conduct national and international insolvency and financial law policy and regulatory studies. The Centre aims to advise and analyze current policy approaches to financial law, as well as advocate for financial law reform and policy implementation.

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