

IBC Article Series: All about Resolution Plans

Understanding the framework of IBC and the resolution process

Insolvency is the state of being insolvent i.e. where the debtor is not able to pay its debts. Debtor may be a natural person or an artificial person. Previously, there were a number of laws dealing with such insolvencies directly or indirectly. IBC was introduced in 2016 to bring these under one head. IBC deals with corporate as well as personal insolvency. The Code aims to resolve these insolvencies i.e. give them a chance to come out of the insolvent state in a time bound manner, failing which, the artificial person goes into liquidation and the natural person is declared bankrupt. For the purposes of this article series, we will be dealing only with corporate insolvencies – primarily companies and LLPs.

The essence of the process under the Code is debt resolution i.e. to help the entity come out of the insolvency with external help in a time bound manner. This ensures that the value of the assets does not deteriorate further and creditors are able to get maximum realization.

Now the question is how does this process exactly work?

For understanding the process, it is necessary to understand certain terms generally used in the Code. Please note that these terms are very loosely explained below for ease of understanding. One may refer to the definitions in the Code for accurate meaning and scope of these words.

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| <ol style="list-style-type: none"> 1. <u>Creditor</u> – any person to whom the corporate debtor (CD) owes any money. 2. <u>Corporate Debtor</u> – company / LLP which is sought to be declared insolvent. 3. <u>Financial creditor (FC)</u> - to whom financial debt is owed – eg. banks, financial institutions, NBFC, debenture holders, deposit holders, homebuyers etc. 4. <u>Financial debt</u> – amount owed by the CD which is generally due towards loans, borrowings, debentures, advances, lease, Inter Corporate Deposits, deposits, guarantees, indemnity etc. 5. <u>Operational creditor (OC)</u> – to whom operational debt is owed. 6. <u>Operational debt</u> – amounts due towards supply of goods or services; amounts due towards government dues; amounts due towards employment dues. 7. <u>Default</u> – non payment of the debt in part or full. Minimum default amount prescribed for initiating action under the Code is <u>Rs. 1 crore</u> presently. | <ol style="list-style-type: none"> 15. <u>Moratorium</u> – On commencement of CIRP, NCLT directs a moratorium on certain actions to be taken against the CD, so that the RP can focus completely on the resolution process. This moratorium extends during the CIRP period. The moratorium is on dealing with any assets of the CD, initiating or continuing any litigation against the CD and on any recovery actions against the property of the CD or property occupied by the CD. 16. <u>Information Memorandum (IM)</u> – is like a prospectus; a document prepared by the RP giving all information about the CD – its assets, liabilities, financials, transactions, status of the entity, whether going concern, litigations etc – Purpose of this confidential document is to enable any person who receives it to get an idea about the state of affairs of the CD and to evaluate whether it is worth considering takeover / investment in the CD. 17. <u>Invitation for Expression of interest (EOI)</u> – Document inviting potential investors to participate in resolution of the CD and such investors should meet |
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<p>8. <u>NCLT</u> – National Company Law Tribunal, which has the jurisdiction to hear and decide cases under IBC.</p> <p>9. <u>Insolvency commencement date (ICD)</u> – date on which order for insolvency of the entity is passed by the NCLT.</p> <p>10. <u>CIRP</u> – Corporate Insolvency Resolution Process; generally 180 days</p> <p>11. <u>IRP / RP</u> – Interim / Resolution Professional who is an independent professional having requisite qualifications & who is appointed by the NCLT to run and manage the CD during the CIRP.</p> <p>12. <u>Claim</u> – amount outstanding towards a debt – financial or operational – as on the ICD.</p> <p>13. <u>COC</u> – Committee of Creditors – A committee formed by the IRP comprising generally of all unrelated financial creditors of the CD. The COC will take all decisions in respect of the fate of the CD. Voting share of each COC member is in proportion to their admitted claim. Decisions are generally taken through meetings of the COC.</p> <p>14. <u>CIRP costs</u> – Costs incurred during / on the CIRP process which may be met out of funds available with the CD or contributed by the COC members in proportion to their voting share.</p>	<p>the eligibility criteria decided by the COC and as prescribed by law.</p> <p>18. <u>Resolution Applicant (RA)</u> – a person who is declared by the RP as meeting the eligibility criteria and who submits a resolution plan for the CD.</p> <p>19. <u>Evaluation matrix</u> – criteria which may be fixed by the COC to compare resolution plans, in case more than one plan is received.</p> <p>20. <u>Request for Resolution Plan (RFRP)</u> – document prepared by the RP and approved by the COC. This document states the expectations of the COC as regards contents of the resolution plan and the legal requirements of the plan.</p> <p>21. <u>Resolution Plan</u> – a proposal submitted by RA for takeover / resolution of the CD and which includes the details of how much the RA proposes to pay to the FC, OC and how does the RA propose to resolve the CD.</p> <p>22. <u>Transaction audit</u> – Examination of the transactions entered into by the CD before the CIRP to find out whether the CD has been subject to any Preferential, Undervalued, Fraudulent or Extortionate credit (PUFE) transactions. Purpose is to determine the cause of insolvency of the CD and to bring back any amounts which may have been wrongfully siphoned out / diverted from the CD.</p>
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Now after having generally understood the meaning of the terms used in the process, let us try and understand the **insolvency resolution process** in simpler terms.

As one can imagine, this process explained below is a very broad macro level plain vanilla kind of situation where everything goes as per schedule, as prescribed in law and all parties involved work towards a common goal. Needless to say, that in real life cases, there will be host of issues, litigations, delays, complexities, conflicting interests which may arise in the process. There are many stakeholders and a lot is literally at stake for all of them.

These steps are given here only to familiarize us with the steps involved in the process so that once we move forward to discuss about the resolution plans, we are able to better relate to the process and technicalities. Without an introduction to the steps in the process, it may not be fruitful to directly get into the nitty gritty of the resolution plans.

CIRP

• Default

[Text]

• Application – FC/ OC/ CD

[Text]

• Admission or Rejection

• Moratorium

• Appointment of IRP

• Public Announcement

• Committee of Creditors (CC)

1. **Trigger:** Default is the trigger for any action proposed to be taken under the Code. Whenever a default of minimum Rs. 1 crore takes place, any creditor (FC / OC) can file the application with the NCLT to declare the CD as insolvent. Please take note that action is not to be initiated for recovery of the amount due. Hence, the creditor needs to prove that there is a default and the CD is unable to pay its dues. Here the OC is required to cross one more hurdle and prove that there is no pre-existing dispute between the parties due to which debt is unpaid.
2. Sometimes the CD itself may file an application stating that it is unable to pay its debts and hence should be declared insolvent.
3. **Admission:** On hearing the application filed by the FC / OC / CD, the NCLT will assess the merits of the case and if satisfied, admit it. The issues involved in the filing of applications and admission by NCLT is the subject matter of another article series by itself. The date of admission by NCLT is the date of ICD and triggers the moratorium. The IRP shall also be appointed on this date.
4. IRP shall manage the CD's affairs during the CIRP by taking control of the CD, its affairs, bank accounts etc. This means that the directors / partners of the CD lose their authority / powers almost overnight and the IRP takes over such powers.
5. **Public Announcement:** IRP shall make a public announcement to inform all stakeholders, including creditors and the general public, about the initiation of CIRP. Purpose of this is to invite claims from various creditors, so that the IRP can verify the claims and prepare lists of creditors of the CD. Claims are to be prepared as on the ICD.
6. **Formation of COC:** The FC, who are not related parties of the CD, shall be included in the COC. The COC shall function like the board of directors and make key decisions during the resolution process, including the approval or rejection of resolution plans. Hence, this process is also known as a 'Creditor in control' regime.

CIRP

- Appointment of Resolution Professional (RP)
- RP – conduct of CIRP
- Meeting of Committee of Creditors
- Preparation of Information Memorandum
- Preparation & Approval of Resolution Plan
- Resolution Plan – Successful or Unsuccessful
- Liquidation – If Resolution Plan is Rejected or Unsuccessful

- In its first meeting, the COC shall decide to continue the IRP as RP or appoint another person in place of the IRP to act as the RP. The RP shall conduct the CIRP hereafter.*
- RP shall also arrange for valuation of the assets of the CD (not valuation of the CD). The valuation shall not be disclosed to the COC members or any other person till the receipt of the resolution plans. This is to ensure maximum realization in the process.*
- RP shall prepare the IM based on the details of the CD available with her. IM is an extremely confidential document and can be shared only against a confidentiality undertaking.*
- The COC shall decide to issue the invitation for EOI by deciding the eligibility criteria for potential RA taking into consideration the nature, size, assets, claims, status of the CD. The law does not prescribe the criteria which are to be stipulated by the COC. The Code allows the market forces to decide. The Code only prescribes the legal criteria. The invitation for EOI shall be published in newspapers for maximum outreach.*
- PRA shall submit their EOI which will be examined by the RP to confirm that the PRA meet the eligibility criteria decided by the COC and those prescribed by law. On examination, RP shall declare the list of eligible PRA.*
- The eligible PRA shall be given the IM, Evaluation matrix and the RFRP. The PRA are expected to do their own due diligence while deciding whether or not to submit a resolution plan and on which terms.*
- Resolution Plan:** *PRA submit their plans to resolve the CD. Again, the law does not prescribe the quantum of amounts proposed to be paid under the plan; but only links it to the liquidation value of the CD. The resolution plan should ensure that the creditors are paid at least as much as they would get in the course of liquidation of the CD. The parties are free to decide the tenure of the plan, the manner in which the amounts shall be paid and so on by way of the plan.*
- The RP examines the plans for compliance and places all compliant plans before the COC for consideration and voting. The COC will vote on all the plans and the plan which garners at least 66% votes shall be declared as the approved plan.*
- Approval by NCLT:** *The RP shall submit the plan approved by the COC to the NCLT for its approval. The NCLT shall not generally go into the commercials of the plan; it is left to the commercial wisdom of the COC to decide which is the best plan for the CD. The NCLT shall*

generally check the compliance, whether any objections are received to the plan, compliance of CIRP process and if satisfied, approve the plan.

16. Implementation: On approval by the NCLT the plan shall be binding on all stakeholders and shall be implemented as provided in the plan. The CD is handed over to the new owner, and creditors receive payments as per the approved plan subject to monitoring.

17. Closure: The insolvency process concludes, and the CD resumes normal operations under new ownership. The new management is granted certain concessions like not being held liable for any non compliances by the CD during the tenure of the erstwhile management.

18. In case the CD does not receive any plans, or plans received are not approved by the COC / NCLT or if the COC decides during the CIRP, the CD shall be put into **liquidation**. This is to ensure that there is maximization of realization to the creditors in the process. Once liquidation starts, the CD is out of CIRP, moratorium ends and the liquidator shall proceed to realise all the assets and pay off the liabilities to the extent possible and as prescribed in the Code. On realization of all assets, the CD shall be dissolved by order of the NCLT.

Did you know?

As per The Economic Times, NCLT has approved 180 resolution plans in FY23, making it the highest-ever annual number so far. With this, NCLT has clocked in a total realization of Rs 51,424 crore from stressed assets. While, in terms of realisation of the amount for creditors, this is the second highest after FY19, when the total realisation was Rs 1.11 lakh crore after completing 77 insolvency proceedings including some big-ticket matters such as Essar Steel and Monnet Ispat.

From the next one, all about resolution plans.....