



Interpreting the Code

Corporate Insolvency
in India

November 2016

EY

Building a better
working world



Contents

Why is the Code imperative today?	5
About the Code	10
▶ What are the highlights of the Code?	11
▶ How does the Code change the legal landscape?	14
The Code on the ground	17
▶ How should lenders and borrowers adapt to the new Code?	18
▶ What are the potential challenges for Insolvency Practitioners?	21
▶ How does cross-border insolvency get impacted?	24
▶ What should be expected in the near-term?	26
Insolvency regime in other geographies	29
▶ How does the Code compare with other geographies?	30
▶ How does the Code measure with the UK?	32
Case studies:	33
▶ Insolvency resolution process	34
▶ Liquidation process	37
FAQs	40



Foreword

This is the year of landmark reforms: GST and the Bankruptcy Code (Code). While the former has been subject to much discussion and debate, the latter is just beginning to be scrutinized. Both are expected to get implemented around the same time and both have a high potential to change the way we do business – if implemented with the intent with which they have been drafted.

Since 2014, the Reserve Bank of India (RBI) has cracked down significantly on the bad loans situation accumulated in the banking system over time through an AQR process, bringing to light the seriousness of the problem. This has been supplemented by very progressive and constructive initiatives such as the Joint Lenders Forum (JLF), Strategic Debt Restructuring (SDR) – with and without change in control – and S4A. These frameworks, though unable to address all situations, are a step forward towards a resolution culture. Default resolution is and will always remain unique to each situation. The Code, from that respect, is timely as it focusses on a turnaround plan with a deadline, which, if not met, results in liquidation. This forces creditors to act in unison or face consequences (one of the significant drawbacks of the earlier schemes) and avoids arbitrages available due to multiple regulations.

While the Code is hailed as one of the best, the devil lies in the detail. Timely action by all stakeholders and dealing with owner-managers would underpin the success of the Code.

Timely resolution

No timely action by lenders is considered appropriate in an Indian environment, which destroys the overall value for most creditors. The law has provisions for such situations, but there are enough and more issues to deal with, including creditors taking quick decisions during the moratorium period, appeals to NCLT being resolved amicably and NCLT relying more on the IP to run the process for quicker disposition. The law is more an operational turnaround than a legal battleground. If that is understood by all the participants, it would solve problems than create them.

Dealing with owner-managers

The presence of owner-managers is a situation unique to developing economies such as India. In recent times, though, we have seen creditors take significant action to work with promoters in the best interest of the enterprise. The firmness of creditors supported by good execution can result in a win-win situation for enterprises and creditors. The Code further empowers this action, and there has been an increasing awareness among owner-managers to cooperate in the process.

While there is a long way to go in terms of filling all the holes, the Code is one of the best we have seen given our circumstances, and I am sure the law will amend itself as we gain maturity in behavior and experience unique situations that can be generalized. A good start with the right intent and a good infrastructure is half the battle won.

Abizer Diwanji

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1

Why is the Code imperative today?

The Insolvency and Bankruptcy Code, 2016 (the Code) is, undoubtedly, a significant reform. The speed at which the legislation was enacted and then subsequently, the supporting rules and regulations have been developed has surprised many.

How have banks dealt with stress commercially in the past?

Joint Lenders Forum (JLF)/Corporate Debt Restructuring (CDR)

Traditionally, banks have preferred to restructure the debt of stressed borrowers through the CDR or JLF mechanisms. While the CDR mechanism was used extensively, the objective seems to have been to provide temporary relief to the borrower rather than making active efforts to revive businesses. CDRs have met with limited success (only 17% exits as of June 2016) in reviving stressed assets due to poor evaluation of business viability and the lack of effective monitoring.

Strategic Debt Restructuring (SDR)

Until the introduction of the SDR in June 2015, the Reserve Bank of India (RBI) had largely stayed away from devising a mechanism that enabled the banks/lenders to play a direct role in the turnaround of stressed borrowers. SDR is a tool for lenders to acquire majority ownership in a borrower by converting a part of the outstanding loan (including overdue interest) into equity. At a later date, it can transfer the control to a new promoter. The SDR scheme (along with variations introduced in February 2016) provides banks significant relaxation from the RBI income recognition and asset classification norms.

Most importantly, SDR aimed to provide the lenders an option to initiate a comprehensive turnaround by taking control; giving them a fair shot at reviving these companies by partnering with a more capable promoter. There has been limited will, though, from banks to take on management of companies through the SDR route. Along with an apprehension that the existing legal system would not allow a change of management to take place smoothly, banks were sceptical of lack of protection from existing and imminent litigations. Lack of willingness of the banks to “right size” the debt and provide the “new” buyer with an appropriate capital structure to turnaround the assets has also impacted the success of SDR.

Scheme for Sustainable Structuring of Stressed Assets (S4A)

The lack of a positive response to SDR from banks have led the RBI to devise other measures such as S4A in June 2016. S4A is a reversal from the ‘creditor in control’ stance taken by the RBI. Under S4A, control remains with the existing promoter as long as 50% of their debt is “sustainable.” While the efficacy of the S4A is yet to be evaluated, it has found limited eligibility as it prescribes a short-term cash-flow visibility and does not allow change in repayment terms. Even as these challenges are being addressed, the lack of emphasis on a comprehensive turnaround could possibly result in the problem just being postponed.

Corporate stress needs a quick and decisive revival strategy rather than an indefinite deferral of the problem. If comprehensive turnaround plans had been implemented in a timely manner, the size of the problem could have been mitigated. Limited will from lenders to engender such a strategy and a judicial framework that did not entirely support them have hampered the efforts in this direction.

The current judicial framework

Until the Code, there was no single legislation that governed corporate insolvency and bankruptcy proceedings in India. Lenders had limited muscle when faced with default and promoters stayed in control. Only one element of a bankruptcy framework has been put into place to a limited extent, banks are able to repossess fixed assets which were pledged with them.

According to the Bankruptcy Law Reforms Committee (BLRC), “Corporate bankruptcy and insolvency is covered in a complex of multiple laws, some for collective action and some for debt recovery. These are:

1. Companies Act, 2013 - Chapter on collective insolvency resolution by way of restructuring, rehabilitation, or reorganisation of entities registered under the Act. Adjudication is by the NCLT. This chapter has not been notified.
2. Companies Act, 1956 - deals with winding up of companies. No separate provisions for restructuring except through Mergers & Acquisitions (M&A) and voluntary compromise. Adjudication is under the jurisdiction of the High Court.
3. SICA, 1985 - deals with restructuring of distressed ‘industrial’ firms. Under this Act, the Board of Industrial and Financial Reconstruction (BIFR) assesses the viability of the

industrial company, and refers an unviable company to the High Court for liquidation. SICA 1985 stands repealed, but the repealing enactment is yet to be notified.”

The significant number of legislations and the complex interplay between them have made the recovery of debts cumbersome for lenders. Different acts define the powers of lenders and borrowers in the case of an insolvency. The lack of clarity on jurisdiction and lack of commercial understanding have allowed stakeholders to manipulate the situation and stall progress.

Apart from Prime Minister Narendra Modi’s commitment that India will be among the top 50 countries in terms of ease of doing business within three years, the Code acquired urgency because of the following reasons:

- ▶ The stressed assets in the Indian banking system have peaked at ~US\$ 150 billion or over Rs 10 lakh crores (~15% of gross advances)
- ▶ There has been a heightened focus on the resolution of the problem by the Reserve Bank of India (RBI) and the Supreme Court. The previous RBI Governor had stated that “Our intent is to have clean and fully-provisioned bank balance sheets by March 2017”.
- ▶ There is a dire need of capital today – not just for stressed companies but for growth in general. It is not the most opportune time to tap capital markets nor are banks willing to provide liquidity; and most promoters are not in a position to infuse capital. Private capital would need to flow in and a strong legal framework would be a pre-requisite.

The average life of cases recommended for restructuring in 2002 was 7 years and the average life of cases recommended for winding up to the court was 6.5 years¹. Even as of October 31, 2015, only about 955 (out of 4,636) and 163 (out of 545) cases of court and voluntary winding up were resolved within 5 years. A significant number of such cases were pending for more than 20 years – 1,274 and 205 respectively².

In this environment, the outcomes are poor. For instance, the average time taken for insolvency proceedings in India is about 4.3 years, while it is only 1.7 years in high income OECD countries. The recovery rate (cents on the dollar) is 71.9 in high-income OECD countries as opposed to 25.7 in India.

Therefore, there is an immediate need to overhaul the insolvency framework.

How can the Code help?

The Code makes a clear distinction between insolvency and bankruptcy - the former is a short-term inability to meet liabilities during the normal course of business, while the latter is a longer term view on the business. As all businesses cannot succeed, it is perfectly normal for some businesses to fail, making it important to emphasise on corrective action.

The Code amply clarifies that insolvency or bankruptcy is a commercial issue, backed by law to enforce transparency and objectivity. It is not another law behind which the inevitable can be delayed.

As per the BLRC, the Code set out the following objectives to resolve insolvency and bankruptcy:

1. Low time to resolution.
2. Higher recovery.
3. Higher levels of debt financing across a wide variety of debt instruments.

The Code ensures certainty in the process, including what constitutes insolvency, the processes to be followed to resolve the insolvency, and the process to resolve bankruptcy once it has been determined.

Such a framework can incentivize all stakeholders to behave rationally in negotiations towards determination of viability, or in bankruptcy resolution. In turn, this will result in shorter recovery timeframes and better recovery, and greater certainty on lenders’ rights leading to the development of a robust corporate debt market and unlocking the flow of capital.

¹ Arvind Panagariya, India: The Emerging Giant, Oxford University Press, 2008.

² Report of the Joint Parliamentary Committee on Insolvency Code, 2016, p76-77 citing data from Department of Financial Services.

Why is the Code imperative today?



Why was the Code needed?

1. Reduce the time taken to resolve insolvency
2. Develop investor confidence
3. Eliminate confusion caused by a complex judicial framework
4. Address the NPA situation decisively
5. Develop credit and bond market



What the Code intends to change?


1. Single insolvency and bankruptcy framework
2. Provide a commercial solution to a commercial issue
3. Allow genuine business failures a second chance
4. Clear and unambiguous process to be followed by all stakeholders in a time bound manner
5. Provide confidence to lenders of their rights and their enforcement




What does it change for the lenders?

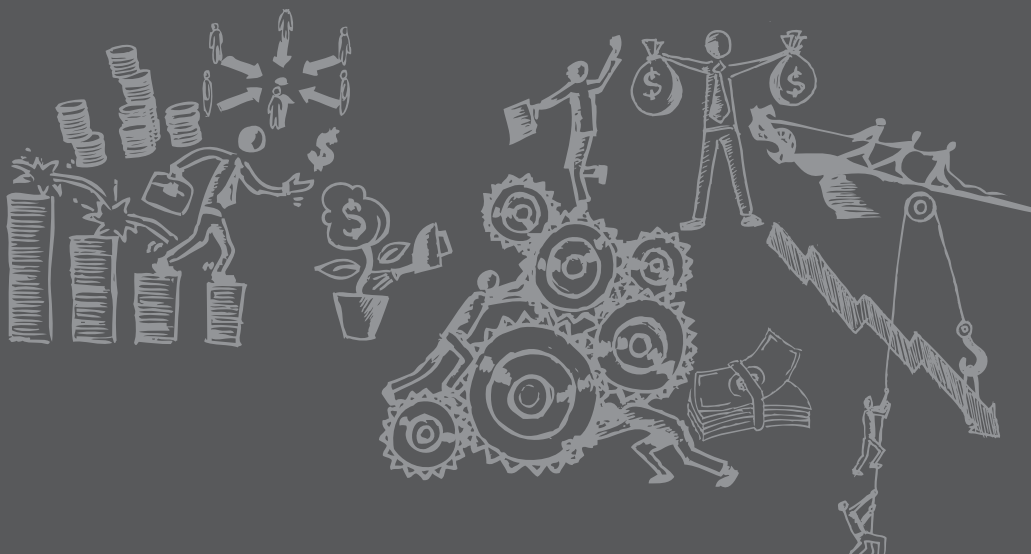
1. Right to control the borrower upon default and maximise recovery
2. Lender can initiate the process even if the default is in respect of the debt of another lender
3. Need for more robust monitoring systems to enable judicious exercise of powers
4. Lack of lender consensus on resolution plan can push the borrower into liquidation
5. Clear priority of distribution (waterfall) upon liquidation; government dues subservient to those of secured creditors and unsecured financial creditors

What does it change for the borrowers?

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1. Any creditor can file an insolvency petition on a default of INR1 lakh or more
 2. Insolvency Professional (IP) to take over the management and operations of the borrower during the CIRP
 3. Borrowers to focus on liquidity - ensure tight cash flow forecasting and monitoring to stay current on payments
 4. Need to be proactive in identifying issues, communicating with lenders and developing/ implementing a turnaround plan
 5. In case of fraudulent diversion of assets, personal contribution can be sought; imprisonment possible

How can the Code help fast-track resolution?

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1. Lender inertia during the CIRP would mean liquidation ~ invariably an economically inferior outcome as compared to resolution
 2. Clarity on the insolvency framework will attract investors to invest into stressed/ distressed situations
 3. Moratorium clause shall ensure smooth insolvency resolution process
 4. An 'open floor' for submission of resolution plans should facilitate the approval of the best plan
 5. The framework defines the role of the judiciary and leaves limited scope for a legal delay/ deferral of the problem





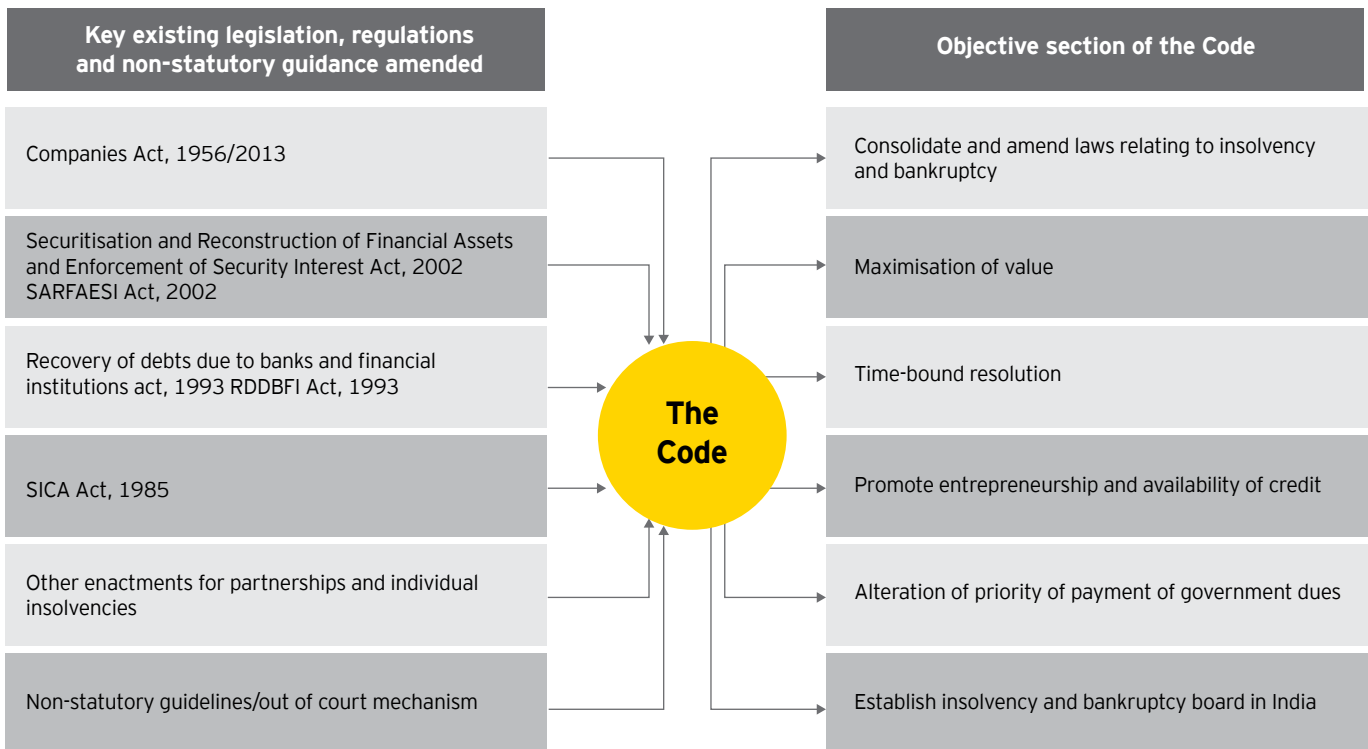
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About the Code

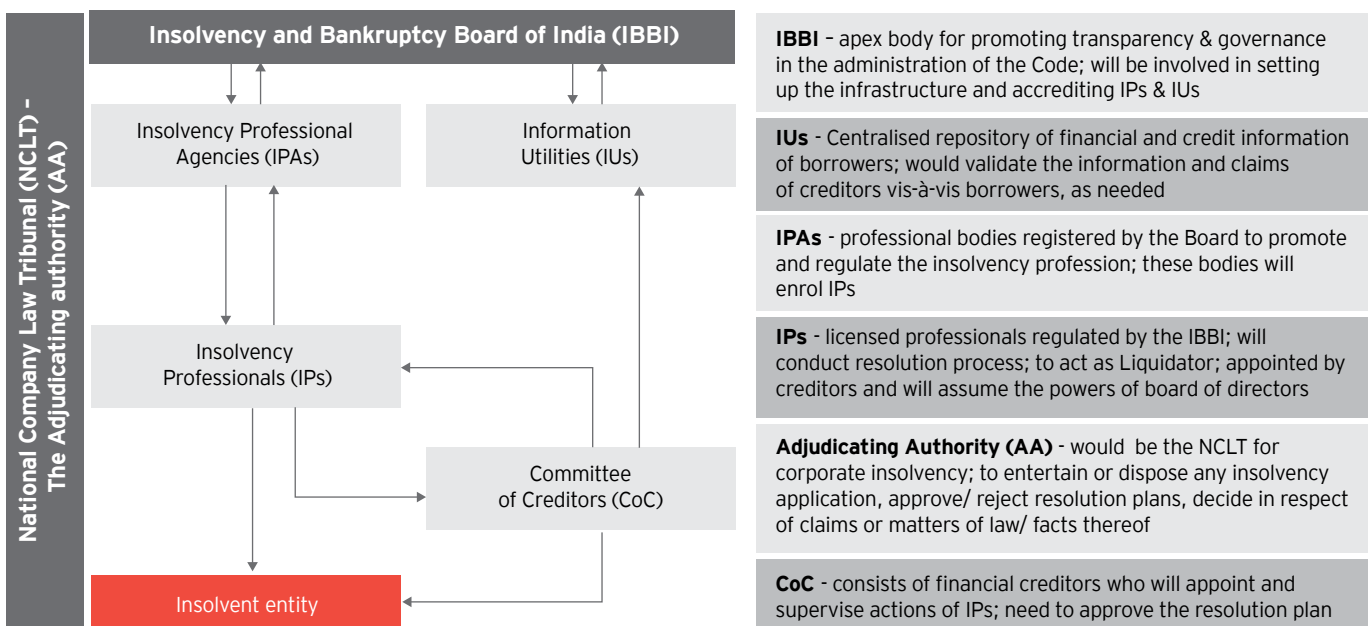
- ▶ What are the highlights of the Code?
- ▶ How does the Code change the legal landscape?

What are the highlights of the Code?

Changes after legislation

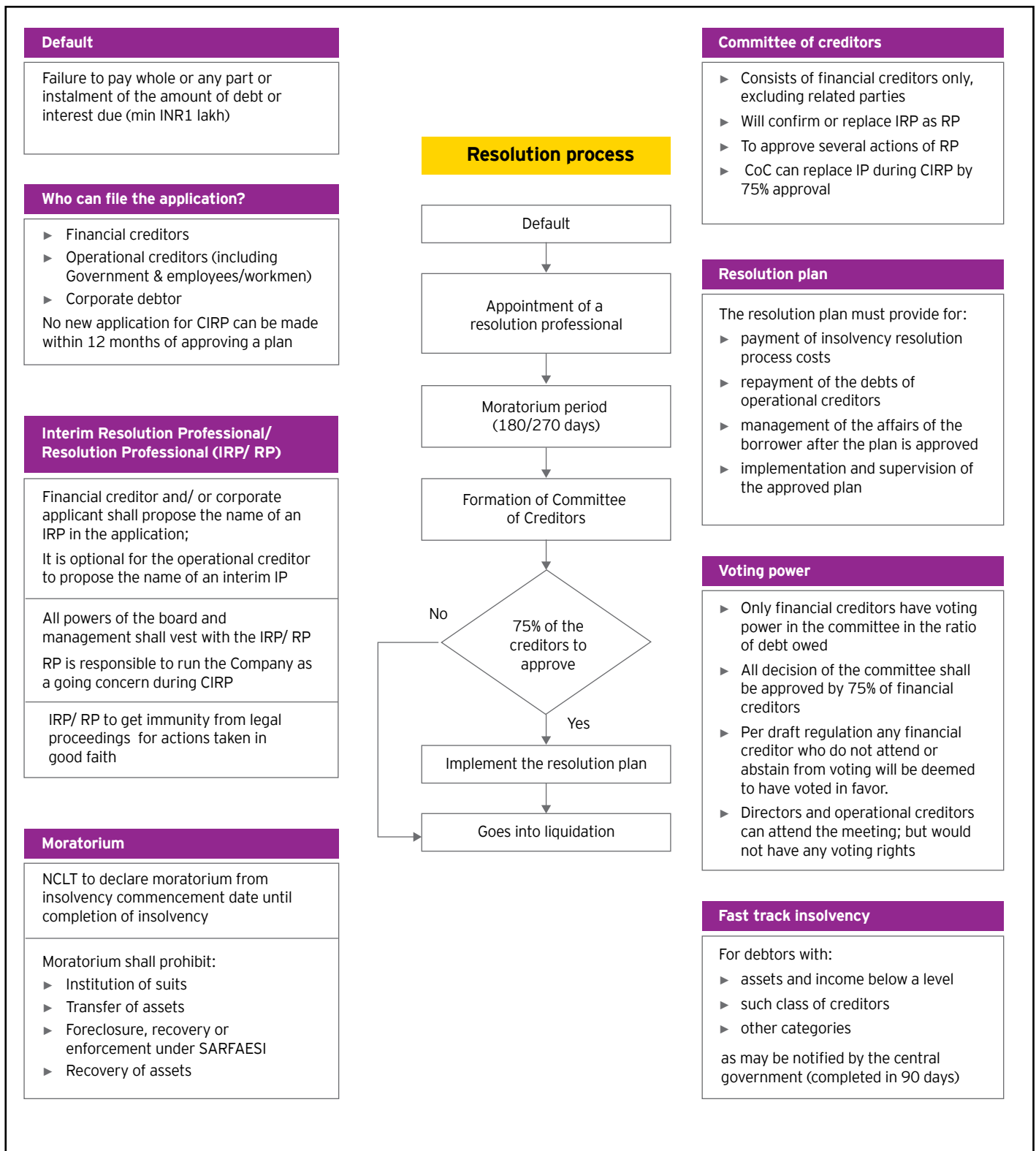


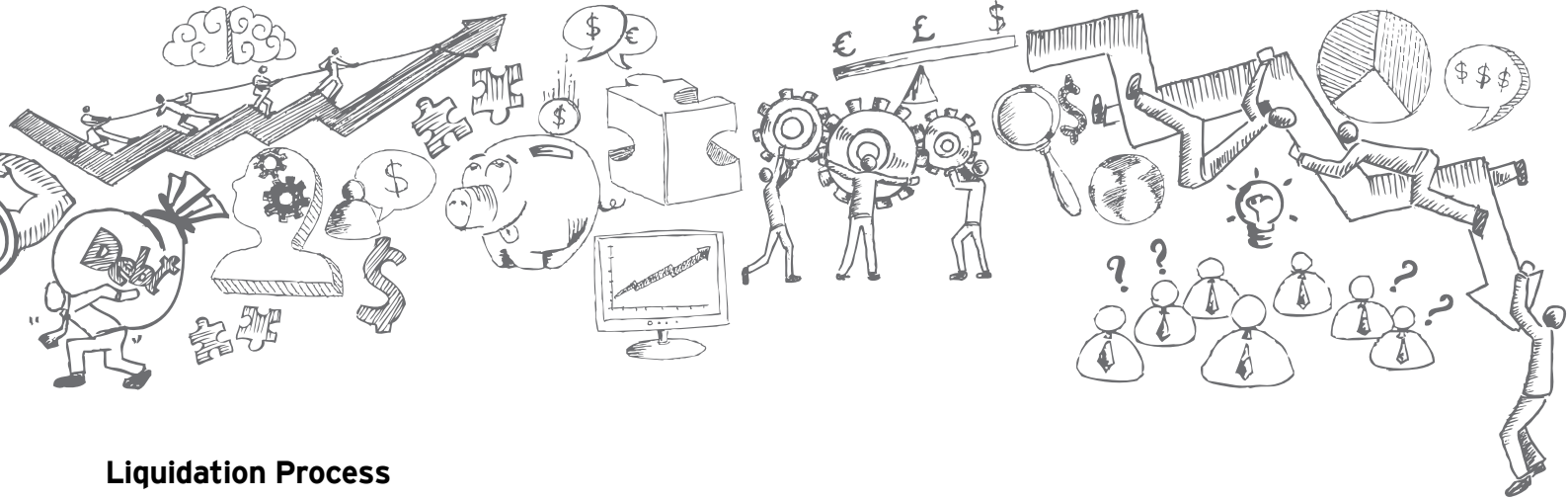
The Insolvency and Bankruptcy ecosystem



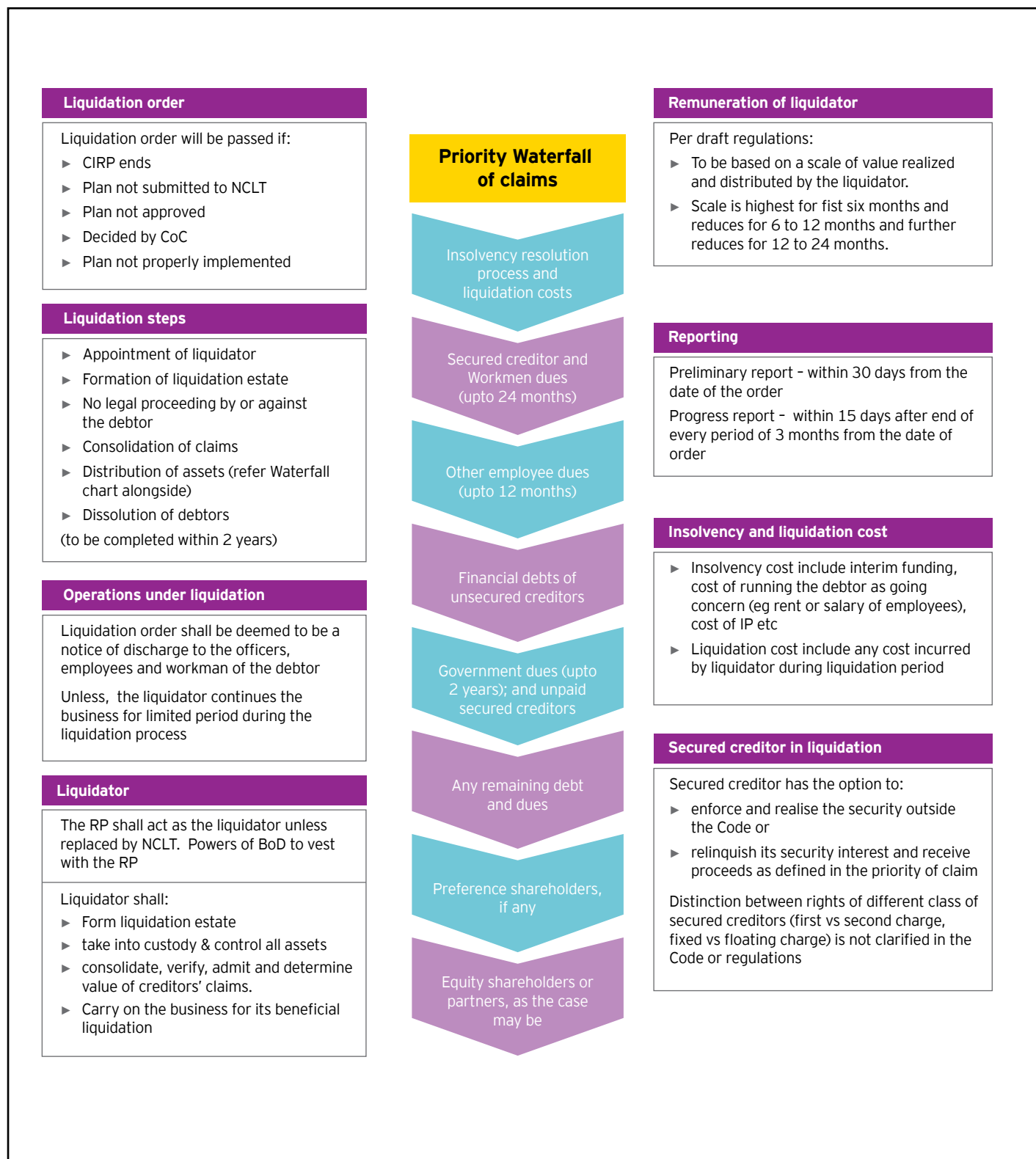


Corporate Insolvency Resolution Process (CIRP)





Liquidation Process





How does the Code change the legal landscape?

The Code consolidates and amends the laws relating to the reorganization and insolvency of corporations, partnerships and individuals. It seeks to achieve reorganization and, failing that, liquidation of the concerned entity. The Code makes some fundamental changes to the existing insolvency resolution process, procedurally as well substantively.

Shift from balance sheet to cash flow test

Unlike the SICA which relied on the test of erosion of net worth to determine sickness, the Code prescribes an objective test, that of payment default in respect of a debt. In effect, it applies a cash flow approach to insolvency. Under the Code, an application for CIRP can be filed upon the occurrence of a payment default in respect of a debt of at least INR1 lakh (or a higher amount as prescribed) before the NCLT. Though winding up proceedings could also be initiated upon a default on the ground of inability to pay debt under the Companies Act, however, the process was not efficient and was aimed for liquidation rather than resolution of insolvency.

New institutional framework

One of the distinguishing features of the Code is that it relies heavily on processes and administrative setup to ensure flow of information and resolution of issues in a time bound manner. The Code envisages the establishment of a new institutional framework including IUs, IBBI, IPAs and IPs. The IBBI administers the entire institutional framework including registration and regulation of each of each of these entities.

IUs are entities registered with the IBBI. Financial creditors are required to submit financial information and information relating to secured assets, as specified by the regulations, to the IUs. Further, along with an application for CIRP, financial

creditors have to furnish evidence of default recorded through the IUs (or such other evidence or record as prescribed) which the NCLT shall also refer to ascertain the existence of such default. A financial creditor can submit a claim to the liquidator by providing a record of such a claim with the IU. Therefore, records of Information Utilities will play a significant part in establishing default and help in minimizing disputes relating to default or security.

Initiation of CIRP

A financial creditor can file for CIRP even if the default is in respect of debt of another financial creditor. An operational creditor is required to deliver a notice of demand on the corporate debtor and the CIRP application can be filed only if the corporate debtor does not dispute the debt within 10 days of the delivery of such notice of demand. The corporate debtor can also file for CIRP. In each case, NCLT shall within 14 days of filing, admit or reject (after allowing 7 days for rectification of defects) the petition.

The CIRP has to be completed within a period of 180 days from the date of admission, which may be extended by a further period of 90 days by an order of the NCLT, upon application of a committee of creditors by resolution. The timelines, the requirement of notice for operational creditors and the ability of a financial creditor to file for CIRP even if the default is in respect of another financial debt, are new features incorporated under the Code. Earlier a statutory notice was required in the context of winding up. It is debatable whether in a two stage process for insolvency resolution and, thereafter, liquidation such notice and right of representation by the corporate debtor or the other creditors should also be required.

Moratorium

Upon the admission of application for CIRP, the NCLT shall by an order declare a moratorium in respect of the corporate debtor including, among others, in respect of institution/continuation of suits or proceedings or execution of any judgement or

order against the corporate debtor; any transfer, disposal or encumbrance of its assets by the corporate debtor; and any foreclosure or enforcement of security interest including those prescribed under the SARFAESI Act.

Though SICA also had moratorium provisions, SICA applied only to industrial undertakings (while the Code applies to all companies) and it had no finite end for such a moratorium.

It may be noted that the moratorium starts from the date of admission of application. Internationally, legislations typically provide for moratorium from the date of application itself rather than the date of admission to protect the assets of the debtor in the interim¹.

CIRP

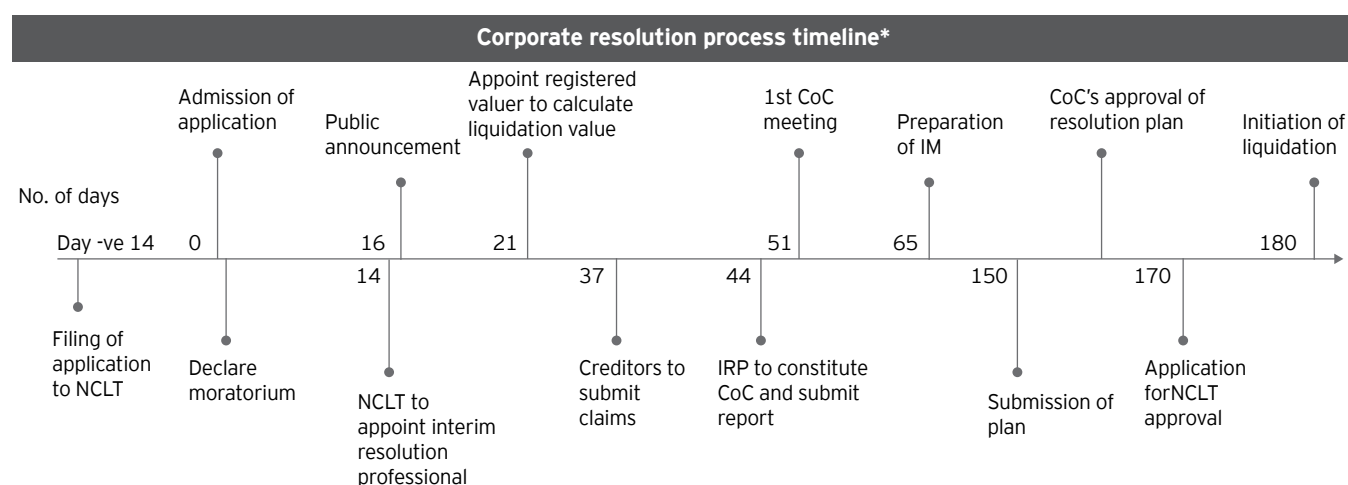
NCLT will appoint an IRP within 14 days of admission of an application. The IRP will have the power of management of the corporate debtor and takes control of the assets of the corporate debtor. The powers of the board of directors will be suspended. The IRP will constitute the CoC (comprising all financial creditors of the corporate debtor), which will, in turn, appoint an RP, who for certain decisions such as interim finance, change in capital structure etc. will require prior approval of the committee of creditors. Its meetings may be attended by representatives of the operational creditors

(holding at least 10% of debt), directors and partners of the corporate debtor and the RPs is required to notify them of the meetings.

The decisions of the CoC will be taken with a 75% voting share. The corporate resolution plan pursuant to CIRP, is required to be approved by the CoC. If in compliance with applicable laws, NCLT will approve such a plan and it will be binding on all parties. The appointment of RP and vesting of powers with the committee of creditors is a marked departure from the concept of the 'debtor in possession' during insolvency process under the existing regime.

Liquidation

If the corporate resolution plan is rejected or not approved/ received in a time-bound manner, if the resolution plan is not complied with, or if the CoC so recommends, NCLT shall order for the liquidation of the company and make a public announcement. In the current regime, the reorganization and winding up of corporate debtors are dealt with under separate laws. Once a liquidation order is passed by NCLT, the RP appointed for CIRP shall act as the liquidator (unless NCLT replaces the RP). The liquidator shall have the powers of the board and management. The liquidator has wide powers to act on behalf of the corporate debtor, including, among others, to



*Based on the Code and draft regulations in public domain

The Code proposes a time-bound resolution process, and provides aggressive timelines for each activity in the resolution process.

¹ See World Bank Principles for Effective Creditor/Debtor Rights Systems (2015) paragraph C 5. Interim moratorium also applies under the UK Insolvency Act

verify and settle claims of creditors, evaluate and sell assets of the corporate debtor, take measure to protect and preserve the assets and properties of the corporate debtor as he deems fit, institute or defend suits, and to carry on the business of the corporate debtor. The liquidator shall receive or collect the claims of creditors within a period of 30 days from the commencement of the liquidation process.

The liquidation estate has certain exclusions including assets held in trust, bailments, personal assets and assets in security collateral held by financial services provider that are subject to netting and set off in multilateral trading for clearing transactions.

Avoidance of transactions

The Code provides for avoidance of undervalued transactions and preferential transactions, which can be set aside upon application of the liquidator or resolution professional. Under the Code, the suspect period for such transactions with the related party is two years, while that of an unrelated party is one year. The Companies Act instead had the concepts of

“fraudulent preference” and floating charges before winding up, where the look-back period was six months and one year, respectively. The Code also introduces the concept of extortionate credit transactions², which can be set aside upon application of the liquidator or the resolution professional.

Preferential Payments

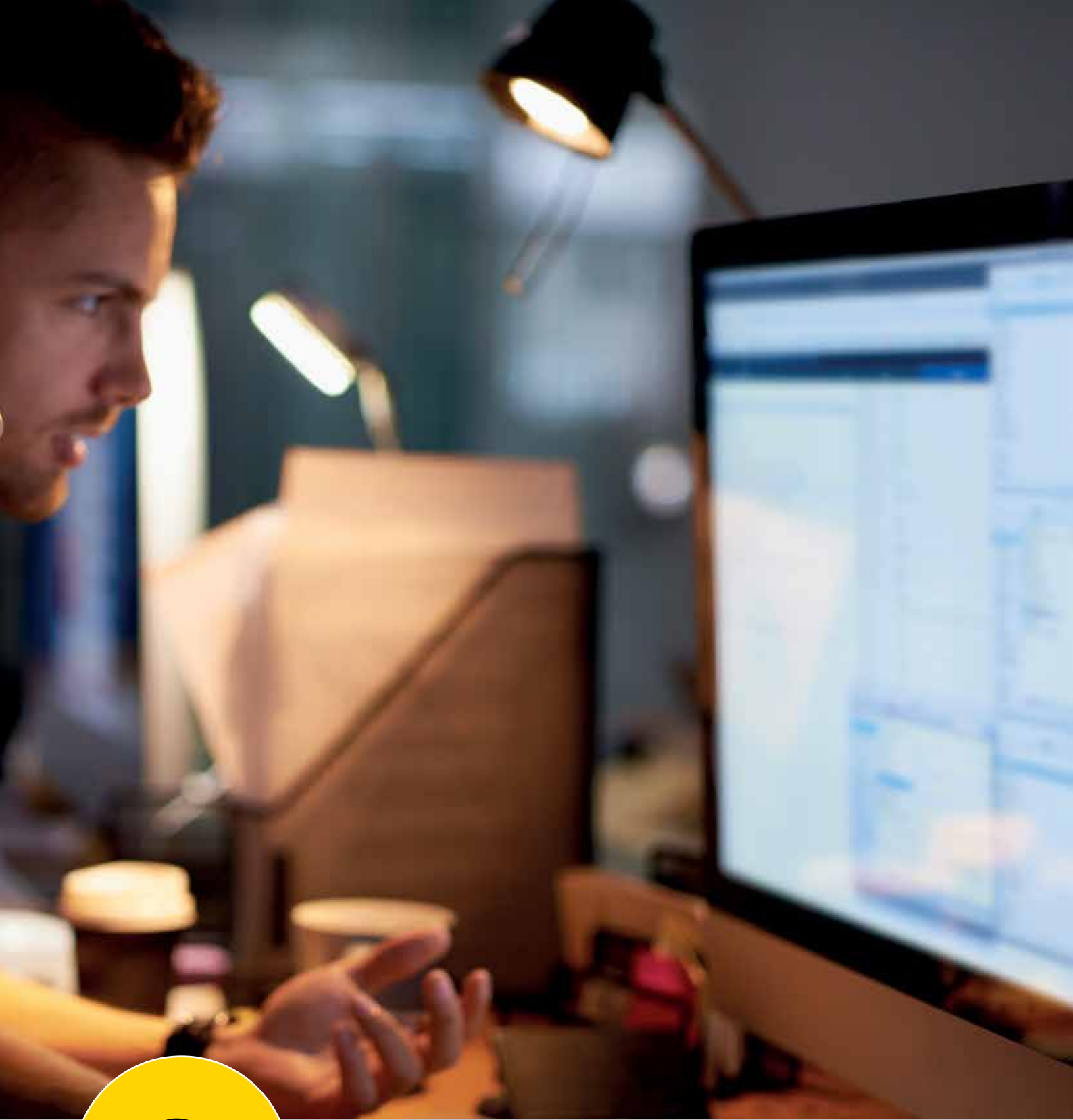
Under the Code, government dues and dues of secured creditors (for unpaid amounts after enforcement of security) rank after the financial debts owed to unsecured creditors. Government dues had higher priority under the Companies Act. Further, any contractual arrangement between the parties that are equally ranked will be disregarded by the liquidator if it disrupts the order of priority laid out in Section 53 of the Code.

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Key legal differences between the Code and the current regime

Topic	Current regime	The Code
What constitutes insolvency	Inability to pay debt/ erosion of net worth	Default of amount higher than INR1 lakh
Class of creditors	Secured and unsecured- separate classes recognised	Financial and operational - no subclasses. Committee of creditors consists of financial creditors only.
Management during CIRP	Liquidator	RP under supervision CoC
Preferential payments	Certain government dues had priority over secured debt	Government dues rank after financial unsecured debt. Trade creditors rank below financial creditors
Exclusions from liquidation estate	n/a	Netting and set-off recognized on financial collateral
Institutional framework	Fragmented. Spread across various authorities and forums.	Amends and consolidates laws relating to insolvency and reorganization of companies, partnerships and individuals. NCLT is the AA for CIRP. Also Envisages establishment of information utilities.

² Though not defined under the Insolvency Code, the concept is well recognised under the UK Insolvency Act.



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The Code on the ground

- ▶ How should lenders and borrowers adapt to the new Code?
- ▶ What are the potential challenges for Insolvency Practitioners?
- ▶ How does cross-border insolvency get impacted?
- ▶ What should be expected in the near-term?

How should lenders and borrowers adapt to the new Code?

The Code and its stakeholders

The Code establishes some very basic principles of borrowing and corporate insolvency resolution:

- ▶ It recognizes that all businesses cannot succeed; therefore, it emphasizes on decisive corrective action instead - on the part of all its stakeholders.
- ▶ Until now, multiple laws had often protected promoters and enabled “debtor in possession” to continue. The Code now unifies the legal framework to deal with insolvency.
- ▶ It also establishes that insolvency is a commercial issue and the law should not be left to decide if a business should be liquidated or revived- after it is insolvent. It is the creditors’ prerogative to decide. To this end, the Code prescribes a “creditor in control” regime with creditors exercising timely control in the event of a default in the repayment of any debt (including interest).

The intended benefits of the Code, however, will be realised only when all stakeholders contribute to creating an ecosystem conducive to an effective, fair and expeditious implementation of the Code.

How should the lenders gear up to the Code?

The Code unambiguously states that the trigger for an insolvency petition is a single default (more than INR1 lakh) which, if approved, will result in the lenders taking over the management of the defaulter through an IP.

Significant value can be preserved even in distressed situations, if the lenders act swiftly with a clear intent.

When to invoke the CIRP

A key issue that banks would need to address as the Code becomes operational is to determine if and when to invoke the CIRP which would entail ascertaining the nature and cause of the default. Banks will have to assess whether the default is on account of temporary problems or if there is probability of further default, and whether the entire loan outstanding

should be recalled and an insolvency petition should be filed. If the default is likely to be rectified, it may not be worthwhile to commence the CIRP. For assessing when to invoke CIRP, it may be necessary to define certain norms that take into consideration the following circumstances (only illustrative):

- ▶ Whether the default is one-off for valid and satisfactory reasons or recurring coupled with delays/defaults in the payment of other dues/ liabilities
- ▶ Whether the default is despite the capacity to pay and/or there are indications of diversion of funds and wilful default
- ▶ Whether the default is on account of delays in payment for supply of goods/services to government departments, other public authorities and public sector enterprises or large undertakings
- ▶ Whether the default is on account of some accident or force majeure, requiring a different treatment of default, including grant of debt relief
- ▶ Whether CIRP would result in a better realization for the creditors as compared to other options such as CDR, SDR and direct liquidation
- ▶ Whether invoking CIRP would have a negative impact on the borrower’s market image and potentially impact the going concern
- ▶ The cost implications of putting the borrower through CIRP (cost of IP, lawyers, new management etc.)
- ▶ The possibility of getting interim funding during the moratorium period to continue to run the borrower as a going concern
- ▶ The probability of 75% of the creditors approving the resolution plan
- ▶ The probability of reviving the business, or the creditors directly going into liquidation.

One size does not fit all; the Code cannot be looked upon as a single solution for all non-performing assets. Case by case commercial evaluation would be critical in finding the best solution.

The answers are not straightforward and would require a detailed set of internal policies and directives, which could be used as guidelines by banks when evaluating specific situations. In addition, banks would also need to develop a sharp commercial outlook and a deeper understanding of their borrowers’ economic environment before arriving at the appropriate

solution. This would need a significant strengthening of their credit monitoring and the development of early warning mechanisms.

In more developed economies, bankers specify a range of critical covenants linked to profitability and cash flows that are monitored rigorously and periodically. Any breach of such covenants leads to an immediate and independent business review (IBR) of the borrower by a specialized agency, resulting in an assessment of the short-term and long-term viability of the business. The outcome of such an IBR would provide banks an evaluation of various options – i.e., (a) allow the borrower to work out a revival or (b) agree with the borrower on an operational restructuring or (c) negotiate a financial restructuring or (d) to pull the trigger on the CIRP.

A few other matters that the Banks and RBI would need to consider include the following:

- ▶ What are the categories of loan accounts where the CIRP should be invoked? In cases of loans to small entities, it may not be feasible. Banks may consider restructuring the debt in these cases, if viable, and recover the debts via debt recovery laws, as required.
- ▶ The current provisioning norms as defined by the RBI may need to be aligned with the Code. One of the possibilities could be that the RBI continues with the existing classification norms such that for the first 90 days after default, the account can be treated as an SMA and after 90 days as an NPA. After approval of the resolution plan, the borrower can be classified as standard.
- ▶ Alternatively, a new category can be created for assets under the insolvency process and the provisioning can be stopped till the time a resolution plan is either approved or rejected by 75% of the creditors.
- ▶ Appropriate covenants would also need to be determined and included for each case in loan documents, empowering the bank to conduct an IBR when there is a breach. It should be incumbent on the borrower to inform the bank the reasons for default and the plan to mitigate it as soon as it realizes a likelihood of a loan default.

Appointment of IPs as RPs

Lenders (through the CoC) have to recommend the appointment of RPs under the Code.

During the CIRP, the powers of the Board of Directors of the corporate borrower will be vested with the RP. The RP would be

responsible for administering the corporate borrower as a going concern during this period and for evaluating the resolution plans submitted.

Considering the criticality of RPs to the process, the lenders should evolve appropriate processes and exercise professional judgment in appointing an RP. Such an appointment should consider, among other factors, the experience of the IP in working in similar stressed/distressed situations as chief restructuring officer/ interim management in driving turnaround plans and his reputation of professional integrity. Adequacy of staff, availability of technical/ sector experts and geographical presence could also be factors in choosing an IP commensurate with the size and complexity of the situation.

Along with competent IPs, lenders would also need to empanel experts across sectors that can assist the IPs in managing defaulting borrowers.

Approval of resolution plans

The plan would need to be holistic. It should not deal with just one aspect which is financial re-engineering, but should follow a multi-faceted approach that brings back the company to good health.

A resolution plan submitted by the RP to the CoC needs to be approved by a vote of at least 75% of the financial creditors. If no resolution plan is approved and submitted to the NCLT within the period of 180 days (or 270 days if extended), the NCLT shall order the liquidation of the corporate borrower.

Traditional resolution mechanisms (CDR, SDR, etc.) have not succeeded, partly, because of the lack of willingness and consensus of the banks to “right size” the debt and provide an appropriate capital structure to turnaround the borrower.

The Code would require lenders, based on a recommendation from the RP, to evaluate the resolution plan rationally with a focus on “maximizing recovery through turnaround and revival, “not on “minimizing provisioning.” Accordingly, lenders should develop internal norms to enable the approval of resolution plans on a timely basis.

The Code bestows tremendous powers to the lenders and a responsible exercise of these powers will require a complete transformation of their outlook. In addition, credit monitoring systems and loan recovery procedures in the Indian banking system would need to be overhauled.

Borrowers need to identify problems in advance and focus on a comprehensive turnaround

The Code envisages a 'creditor in control' regime with lenders exercising control upon a single default. This can be effected without any notice and the law is very stringent as compared to the existing laws.

This is a significant shift from a legal system that was heavily supportive of promoters and delayed recovery/ revival under the cover of public interest or saving organizational capital. As a result, bad (and badly run) businesses continued to operate to the benefit of their owners. On the other hand, the Code imposes jail terms of up to five years if "asset stripping" is noticed within 12 months before the default.

It is, therefore, inevitable for stressed businesses and their owners to proactively devise and implement a timely and effective turnaround plan to ensure that there are no defaults that trigger the Code. Such a turnaround plan should focus on

operational improvement, cash conservation and sale of non-core assets, as much as on right-sizing the capital structure.

Borrowers should also have a strong IT, finance and cash flow monitoring system to report any delayed payment or default.

The best people to make a difficult decision for a business facing difficulties are the people running the business, provided they work towards protecting the interest of all stakeholders.

Stressed/distressed businesses and their owners and managers should acknowledge the inefficiencies in their current business models in a timely manner and communicate any liquidity issues to financial creditors and other stakeholders well in advance - along with a turnaround plan.

Avoidance of historical transaction, which can be set aside by NCLT

Borrowers are personally liable to contribute where they have carried out any of the following transactions:

Section	Details	Time limit	Consequences
43	"Preferential transaction: If any person is given a preference in any transaction by the borrower with the effect of putting that person in a beneficial position"	"Related party - In the last two years Unrelated party - In the last one year"	NCLT can pass an order to make the borrower or the person given preference to restore, repay or account for any profit from such a transaction
45	"Undervalue transaction: If the borrower enters a transaction with any persons which were undervalued; and such a transaction did not take place in the ordinary course of business"	"Related party - In the last two years Unrelated party - In the last one year"	NCLT can pass an order to make the borrower or the person benefited from such a transaction to restore, repay or account for any profit from such transaction
49	"Transaction defrauding creditors: If any transaction is deliberately entered by the borrower to defraud a creditor"	No time limit	NCLT can pass an order to make the borrower or the person benefited from such a transaction to restore, repay or account for any profit from such a transaction
50	"Extortionate credit transaction: If the borrower has been party to an extortionate credit transaction and which is not in compliance with the law, and such that involved receipt of financial or operational debt"	In the last two years	NCLT can pass an order to restore the position, set aside the whole transaction, modify the term etc.

Conclusion

Most regulations, be it winding down under the Companies Act 2013, SDR, SICA or SARFAESI were all well-meaning to find a resolution in a systematic manner as much as the Code does. However, they were misused by making the processes prescribed in the regulation a mere formality to achieve the desired objective. If this is done with the Insolvency and

Bankruptcy Code, 2016, it will become just another piece of comprehensive legislation.

Positive involvement and participation of the key stakeholders – the borrower and the lender – and how they gear up for and contribute to the effective and intended functioning of the Code would be a critical factor for the success of the Code.



What are the potential challenges for Insolvency Practitioners?

An IP is defined by Section 3(19) of the Code as a person enrolled under Section 206 with an IPA as its member and registered with the IBBI as an IP under Section 207. Section 2(20) of the Code defines an “IPA” as any person registered with the Board under Section 201 as an IPA. If these provisions are compared with the Companies Act, 2013, there is a clear reference to names of company secretaries, chartered accountants, cost accountants and such other professionals notified by the central government, from a databank maintained by any institute or agency notified by the Government (Refer Section 259(1) and 275(2) of the Companies Act, 2013). The Company Law, therefore, permits the recognition of existing institutes of professionals as IPAs. The draft regulations under the Code, however, contemplates the establishment of a not-for profit Section 8 company with capital of INR5 crores and net worth of INR10 crores, which should apply for and obtain provisional or transitional registration as an IPA. The first challenge for the prospective IPs in India will be to establish a new association or institute of professionals to enrol, regulate and monitor working of IPs. This could have been avoided by recognizing existing professional agencies to operate as IPAs.

Professionals in India have been operating in an environment that protects industrial undertakings and large commercial enterprises from closure in spite of losses and inability to pay debts, by laws such as SICA or State Relief Undertakings Acts, which are still operative. From the freedom to pay the debts or other liabilities as and when you are able to do so, the law is changing to declare you insolvent if you have no money to pay the debt when it falls due for payment. The focus of the professionals advising business enterprises has to shift to prudent cash flow forecasting and management practices.

Although the definition of IP under the Code makes no reference to chartered accountants, cost accountants, company

secretaries and lawyers, it is clear that only such professionals (and other eligible professionals) will have to undertake the tasks of insolvency resolution and liquidation of corporates. The task of IPs will relate to the following categories of enterprises:

1. All companies with debt of INR1 lakh and above
2. Industrial undertakings and large commercial enterprises
3. Infrastructure projects
4. Medium, small and micro enterprises
5. Individuals and partnership firms (debts of INR1,000 and above)
6. Fresh start cases of individuals with annual income of INR60,000 or less

IPs will have to pick the category of insolvents from among these to focus on. If individual insolvencies and fresh start cases are to be taken up, it will require different kinds of enterprise and manpower to handle such cases. The Code provides that if there is no IP suggested by the creditor, the IBBI will nominate the IP. It is presumed that a panel of IPs to be maintained by the IBBI will be for different locations and types of insolvents, otherwise the system will be difficult to operate. In any case, IPs will have to decide their respective areas of operation and indicate them in their application for registration as IPs.

In certain economies (such as the US), the insolvency law has the concept of “debtor in possession” and on commencement of insolvency, a moratorium becomes operative and the debtor is allowed to remain in possession, formulate a resolution plan and obtain approval from all stakeholders. The Indian law prescribes a concept of “creditor in control,” and the IP is required to take possession of all assets and take over the management of the enterprise. This part of IPs’ responsibilities is the most challenging and could be eased if the insolvent enterprise extends cooperation to the IP and facilitates the takeover of assets and management. IPs will have to decide how possession of assets will be taken: whether each and every item will be included by making an exhaustive inventory or symbolic possessions will be taken, trusting the existing

personnel of the enterprise. Since there is a possibility of liquidation of the enterprise if a resolution plan is not worked out, it is expected that the company management will co-operate with the IP, and ensure that all assets are accounted for, preserved and protected, that no valuable assets are concealed or disposed of without the knowledge of the IP, and that the enterprise is allowed to be operated as a going concern.

Be that as it may, IPs are entrusted with the following tasks under the Code:

- ▶ Manage the affairs of the corporate debtors as a going concern
- ▶ Constitute the CoC, convene its meetings and conduct such meetings;
- ▶ Conduct the corporate insolvency resolution process
- ▶ Discharge various duties necessary to operate the enterprise as a going concern as listed out in Section 25 of the Code

- ▶ Prepare the information memorandum
- ▶ Submit a resolution plan to the adjudicating authority as approved by the CoC
- ▶ Conduct the liquidation process if the resolution plan is rejected or fails after approval

One important aspect of undertaking responsibility as an insolvency resolution professional is that the responsibility for operating the enterprise is of the IP and not the creditors at whose instance the IP is appointed. Hence, if there is a loss due to lack of timely sales of goods with a limited shelf-life or environmental damage as a result of leakage, the liability will be of the IP as the person in charge of the business enterprise. IPs will, therefore, need to empanel managerial experts in different fields who can be entrusted with the functions of a business enterprise.

Draft regulations on registration of IPs

IBBI has notified draft regulations on the registration of IPs for public comments. The salient features of the regulations are as follows:

- ▶ IP examination: IBBI shall form an examination committee to conduct an IP examination; the first such examination will be conducted within two years from the date of constitution of the board.
- ▶ Eligibility to register as a transitional IP: any person who:
 - ▶ Has a bachelor's degree
 - ▶ For not less than 15 years, has been a member of ICAI, ICSI, ICAI (Cost), Bar Council or IAI; working in the field of management of business or insolvency; or has been an officer of ICLS
 - ▶ For not less than three years, has been employed with or engaged in work pertaining to financial service, restructuring, NPA, fund raising and related advisory
- ▶ Transitional registration: Shall be valid for a period of two years
- ▶ Final registration: Professionals with transitional registration must appear for and pass the IP examination and apply for a final certificate of registration with the board. A partnership firm whereof a majority of partners practicing in India have received certificates of registration as IPs may also make an application for a certificate of registration. The certificate of final registration shall be valid for five years

When an insolvency resolution application is admitted and an IP is appointed, it is necessary that a CoC is constituted at the earliest so that the lenders providing working capital take a view on how and to what extent working capital funds will be provided and if they are not willing to continue to lend, whether loans are required to be raised from other lenders. It would be for the IP to make a quick assessment of the business and convince the lenders to continue lending limits so that the option of disposal of the enterprise as a going concern is explored or otherwise a resolution plan is worked out.

Lastly, the IPs need to note that the Code at every stage of the appointment of an interim or final IP or approval of change of IP requires that the IBBI certify that there are no disciplinary proceedings pending against the IP and give specific approval for appointment of IP. These provisions indicate a concern that IPs may deal with assets of the business enterprise for gaining pecuniary or other advantage for themselves or for other third parties to the detriment of other claimants and stakeholders. Professionals planning to undertake assignments as an insolvency resolution professional will have to ensure that the

officials selected are independent persons with no relationship with or interest in the business enterprise and are efficient, competent and honest with good reputation and character and integrity beyond any doubt.

Introduction of the Code in India involves total transformation of the mind-sets of the business community, judiciary and the professionals advising them. Smooth transition to the new norms will be a major challenge.

The article has been contributed by Mr. M. R. Umarji, Consultant, IBA. He was a member of the Bankruptcy Law Reforms Committee constituted by the Government of India to draft the Insolvency & Bankruptcy Code, 2016. Mr. Umarji has more than 45 years of experience in law specifically with respect to the banking sector. He has worked as Legal Assistant in Law & Judiciary Department of Government of Maharashtra, as Law Officer in Bank of Baroda and has worked on various committees and working groups set up by the Government.





How does cross-border insolvency get impacted?

Why has cross-border insolvency not been covered in the Code?

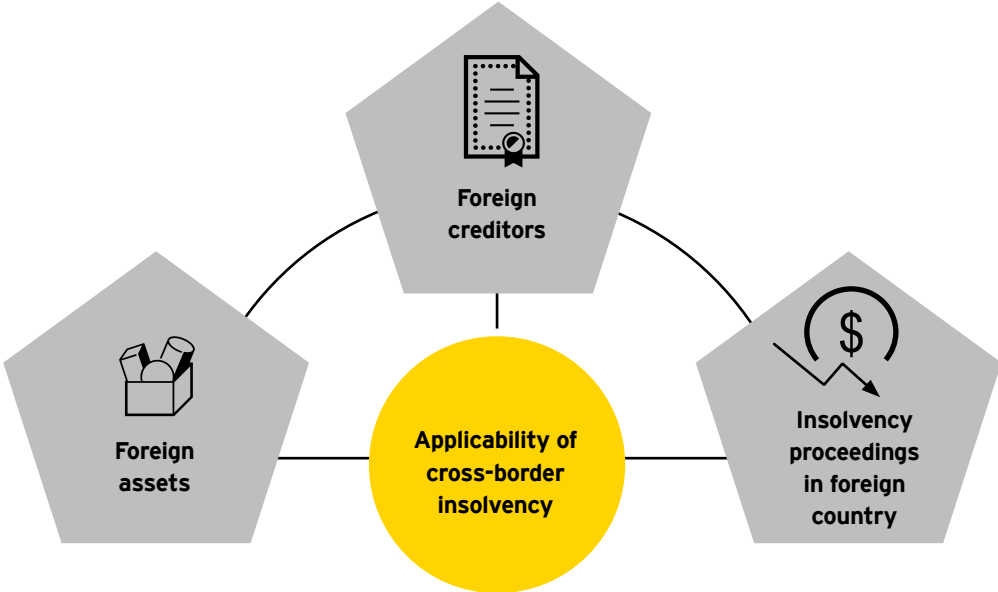
The Code has been widely acknowledged as a blend of some of the best practices across the world, but it just falls short of being truly global. Cross-border insolvency has not been adequately covered in the Code. While it accords the power to the central government to enter into an agreement with foreign countries for enforcing the provisions of the Code, the international community would have expected more.

Most of the previous law-reform committees had recommended that the UNCITRAL Model Law on Cross-Border Insolvency, which has already been adopted by over 41 countries, should be adopted in India. The Corporate Bankruptcy and Winding

up Code, 2001 proposed by the NL Mitra Committee laid out detailed provisions relating to the subject of cross-border insolvency, but it did not see the light of day. The BLRC, in its interim report, was of the opinion that *“Further thought and consideration is required before implementing the UNCITRAL Model Law. Such adoption should ideally take place only after the adoption of the Insolvency Code.”* It also noted that some other international approaches may also need to be considered while framing the cross-border insolvency laws, including EC Regulation on Insolvency Proceedings; American Law Institute’s NAFTA Transnational Insolvency Project and the International Bar Association Cross-Border Insolvency Concordat.

Given the complexity involved in cross-border cases and the absence of an effective domestic insolvency framework, it is probably prudent to take one step at a time.

Even while focusing on domestic insolvency, the BLRC acknowledged in its final report the need for cross-border insolvency.



Limited cross-border provisions in the Code

Cross-border insolvency has not been defined in the Code, but in general it may be understood as insolvency of borrowers who have assets or creditors in different jurisdictions, or are subject to insolvency proceedings in multiple jurisdictions.

The Joint Parliamentary Committee on the Code, while deliberating on the Code, conceded that not incorporating provisions relating to cross-border provisions will lead to an “incomplete code,” and accordingly added two new enabling sections: “Agreements with foreign countries (Sec 234)” and “Letter of Request to a country outside India in certain cases (Sec.235).”

Agreements with foreign countries: The Central Government is empowered to enter into bilateral agreements with foreign governments. It may also apply the Code in relation to assets or property of a corporate debtor (including a personal guarantor of a corporate debtor), situated at any place in a country outside India with which reciprocal arrangements have been made.

It is to be seen how effective the bilateral agreements turn out to be, since it would be contingent on long-drawn negotiations with each country; and agreements with each country would vary, resulting in chaos and litigation.

Letter of request to a country outside India in certain cases: The NCLT may, on receipt of an application from an RP, request a competent authority of a foreign country to seek evidence or action in relation to the foreign assets of the corporate debtor.

There are no specific provisions in the Code on how Indian authorities would give or seek assistance to or from foreign authorities; or how Indian authorities would recognize and deal with debtors that are undergoing insolvency proceedings in multiple proceedings.

Other provisions in relation to foreign assets/creditors:

- ▶ The RP may take control over the assets belonging to the corporate debtor but located in a foreign country.
- ▶ The Code does not make any distinction between domestic and foreign creditors, and therefore both category of creditors would have equivalent rights. However, it is not explicitly mentioned whether the representatives of foreign insolvency proceedings and creditors would have a right of access to the courts, as envisaged in the UNCITRAL Model Law.

“The next frontier lies in addressing cross-border issues. This includes Indian financial firms having claims upon defaulting firms which are global, or global financial persons having claims upon Indian defaulting firms.

Some important elements of internationalisation - foreign holders of corporate bonds issued in India, or borrowing abroad by an Indian firm - are dealt with by the present report. However, there are many other elements of cross-border insolvency which are not addressed by this report.”

Final report of BLRC: Volume I

Two new enabling sections: ‘Agreements with foreign countries (Sec 234)’, and ‘Letter of Request to a country outside India in certain cases (Sec.235)’



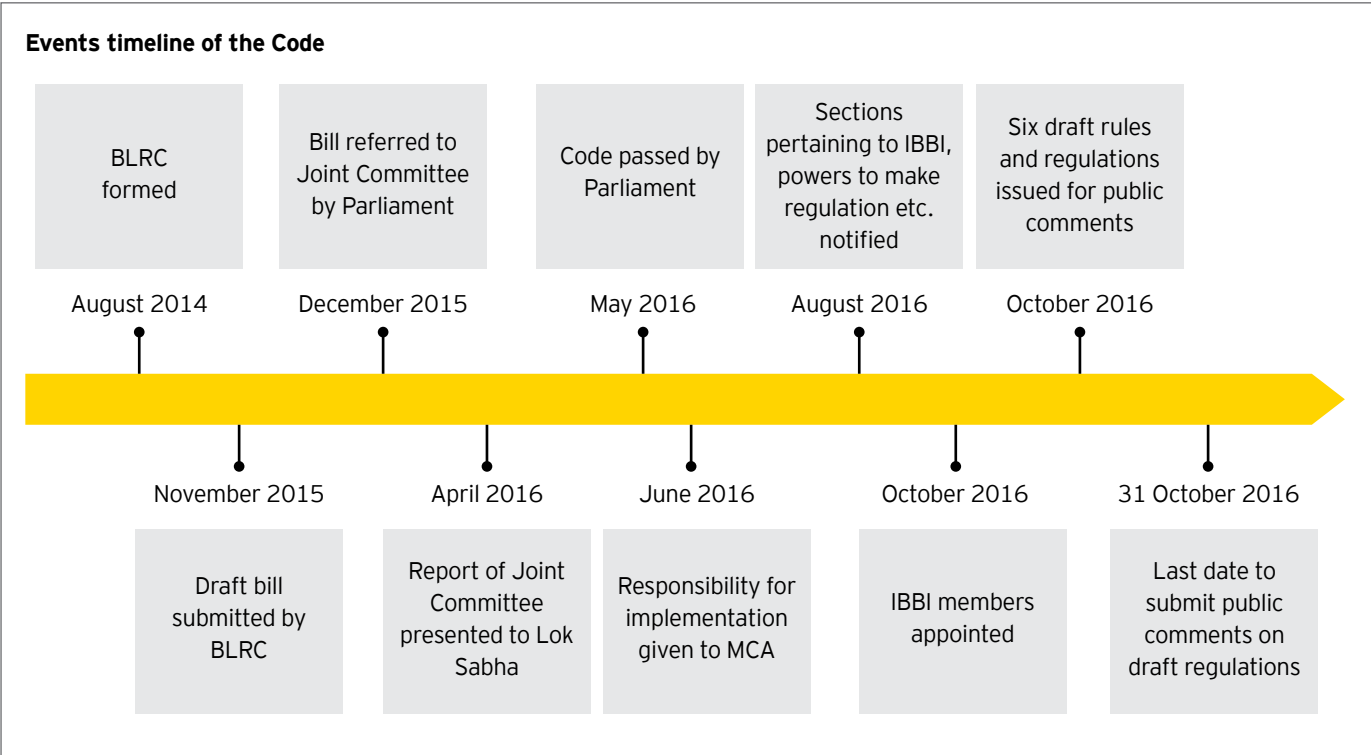
What should be expected in the near-term?

The government is moving at an unprecedented pace to operationalize the Code. The key activities that have been completed that would fast-track the implementation of the Code include:

- ▶ Notification of the constitution of the NCLAT and NCLT along with their locations (the NCLT has 11 functional benches already) in June 2016
- ▶ The enactment of the Enforcement of Security Interest and Recovery of Debts Laws and Miscellaneous Provisions

(Amendment) Act, 2016 in August 2016, which has amended provisions of the SARFAESI and RDDBFI

- ▶ Constitution of the IBBI as chairman and four other members in October 2016; three whole-time members and two other members are yet to be appointed
- ▶ Notification for public comments of draft regulations, rules and bye-laws supporting the Code



Draft regulations, rules and bye-laws

Draft regulations, rules and bye-laws notified

- ▶ Draft regulations for the registration of IPs and IPAs
- ▶ Draft regulations for the insolvency resolution process and liquidation process of corporates
- ▶ Draft rules for application to the adjudicating authority
- ▶ Model bye-laws for IPAs

The draft documents provide significant clarity and details with respect to the provisions of the Code. In particular, the following aspects have been amplified:

- ▶ Eligibility criteria for transitional certification of IPs and IPAs: Transitional IPs would need to be grandfathered to get the Code to operate until the requisite infrastructure (e.g., examinations) is ready
- ▶ Stringent model bye-laws for the functioning/governance of the IPAs and conduct of IPs to set exemplary standards for the profession
- ▶ Detailed process and rules to define the rights and obligations of IRPs and RPs
- ▶ Manner of conduct of meetings of the CoC and approval of the resolution plan
- ▶ Appointment and remuneration of the liquidator, and the manner and process to be followed for liquidation of assets by the liquidator, including provision of adequate information and consultation with relevant stakeholders
- ▶ Details on what constitutes proof of claims made during the CIRP and liquidation process and how they need to be verified

These documents are expected to be finalized by the IBBI in mid-November 2016 after consideration of public comments.

Key challenges to the implementation of the Code

Expecting the Code to be an immediate answer to all the malaises related to insolvency resolution and NPAs in the country may be a little presumptuous. Significant uncertainties and challenges would have to be surmounted before the Code could be a success on the ground.

Mind-set of existing stakeholders: lenders, borrowers and judiciary

- ▶ A complete transformation of the banking system is needed. Specifically, aspects related to the development of early warning mechanisms, astute credit monitoring, proactive commercial decision making with respect to the way forward and elimination of inter-creditor conflicts would need to be overhauled. [A more detailed analysis is presented on page 18]
- ▶ Banks would also need to exercise professional judgment in the selection of appropriate IPs/advisors and not follow a "lowest cost" policy without consideration of technical credentials and experience commensurate with the complexity and magnitude of the situation.
- ▶ Stressed/distressed business owners/managers should acknowledge and focus on the inefficiencies in their current business models in a timely manner and communicate any liquidity issues to financial creditors and other stakeholders well in advance - along with a turnaround plan.
- ▶ Funds availed from lenders (or other sources) by business owners should be utilized for the purpose for which they were granted/intended.
- ▶ Dues should be paid off on time as against using operational creditors as a source of working capital financing by inordinately delaying payments.

- ▶ Government authorities (local, state and central) need to ensure that all commitments made (land allocation, approvals etc.) are completed as per scheduled/reasonable timelines and dues payable are paid on time to the business community.
- ▶ The Code is very clear that insolvency or bankruptcy is a commercial issue, backed by law to enforce transparency and objectivity. It is not another law behind which the inevitable can be delayed. The judiciary should support the implementation of the law as intended.

Legal matters

- ▶ The Code does not provide an opportunity to the borrower to be heard before the commencement of CIRP.
- ▶ There are numerous matters (sale of part of an organization, carve-out of business etc.) that need the approval of shareholders as per the Companies Act, 2013. It is unclear whether such actions contemplated in the resolution plans (or otherwise) can be completed without such approvals.
- ▶ The exclusion of security collateral held by financial services provider from liquidation estate is a welcome statutory recognition of netting and set off arrangements. However, it is more broadly worded than that envisaged under the international legislative instruments or in the context of netting arrangement for financial collateral under the ISDA framework. There may be some creative structuring around this exemption. It will be good to have some of these issues clarified in the rules and regulations.

Other matters

- ▶ There is a view that the current 180-day (plus 90 days) period may not be adequate to nail down a resolution plan, especially in complex/large cases. While this is a consideration, various stakeholders can work constructively together to address many of the matters, including building a feasible resolution plan (pre-packs) even before the commencement of the insolvency resolution process such that the process could be completed efficiently.
- ▶ Development of professionals who have the integrity and skills to perform the onerous tasks of an IP in insolvency and bankruptcy cases is critical. Lenders may have to insist on

such IPs producing a “personal” or “surety” bond to protect the fiduciary nature of the work and ensure that committed individuals become IPs.

- ▶ Development of IUs as an institution is critical for evidencing the proof of claims/default. The lack of a robust IU structure may lead to legal interventions and delays.
- ▶ A key aspect of the Code is that it helps makes the distinction between “malfeasance” and “business failure.” Malfeasance should lead to prevention from participation in the resolution plan. Practical implementation of this aspect would be a challenge.
- ▶ There is currently no cross-border insolvency framework.
- ▶ The current provisioning norms, as prescribed by the RBI, may need to be aligned with the Code. Also, existing schemes of restructuring outlined by the RBI (CDR, 5/25, SDR, S4A etc) would also have to be synchronized with the Code.

Next steps

The government has indicated that the Code could be operational by the end of 2016 or early 2017. The key activities that would need to be completed before notification of the Code are as follows:

- ▶ All rules and regulations made under the Code, shall be laid before each house of the Parliament while it is in session for a total period of 30 days. Period of 30 days may be comprised in one session or in two session or more successive sessions.
- ▶ Appointment of the additional five members of the IBBI
- ▶ Framing regulation for the formation and functioning of IUs
- ▶ Inviting applications and granting transitional certifications to eligible IPs and IPs and scrutinizing such applications and ensuring that only exemplary professionals are certified would need significant expertise and effort from the government.

The Code has started an interesting journey and is a step in the right direction. The success of the Code would, however, be measured upon implementation, which hinges primarily on a tectonic shift in the mindset of its stakeholders.



4

Insolvency regime in other geographies

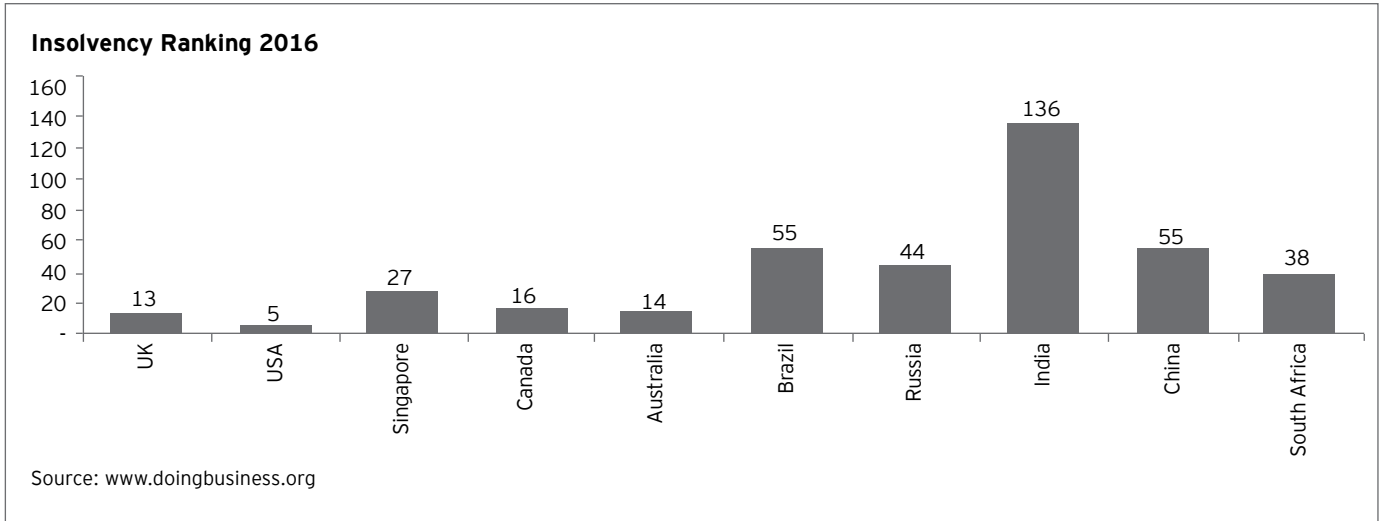
- ▶ How does the Code compare with other geographies?
- ▶ How does the Code measure with the UK?

How does the Code compare with other geographies?

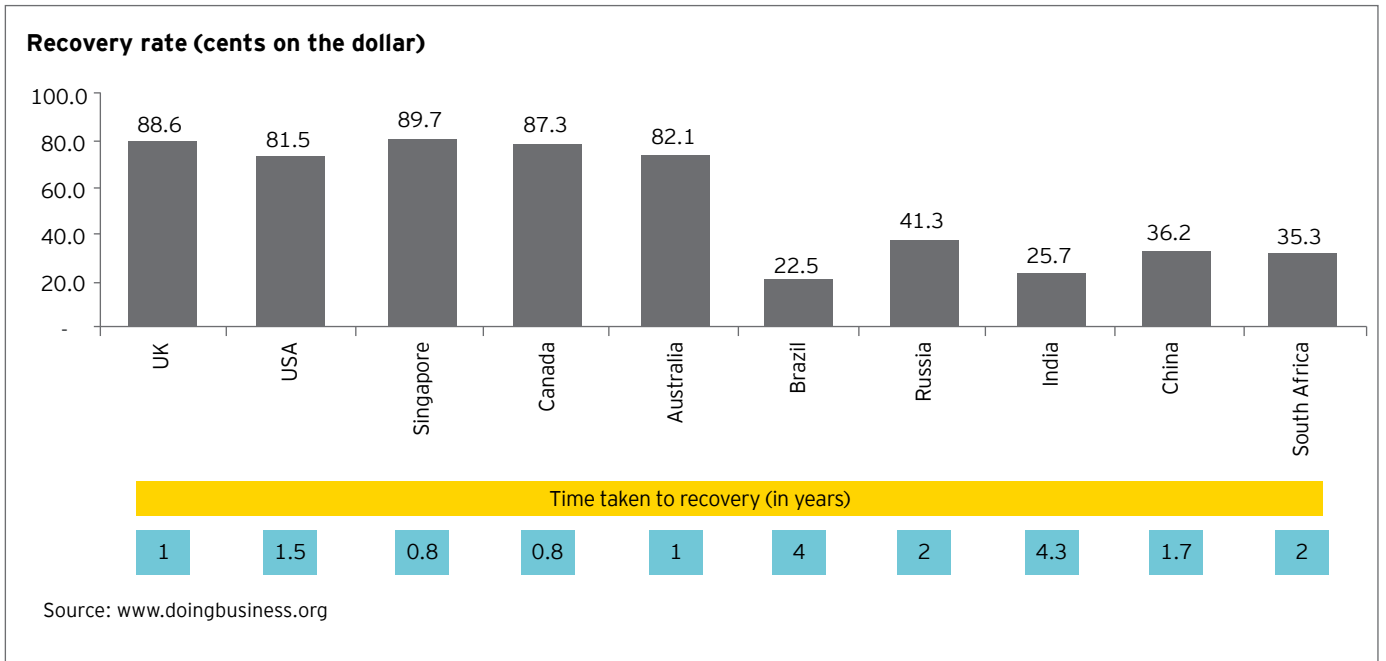
A comparison of key provisions

Sl.No.	Details	India*	UK	Brazil	Canada	Australia	Singapore
1.	What triggers the process?	Default & voluntary	Default, insolvency & voluntary	Default, insolvency & voluntary	Default, insolvency & voluntary	Default, insolvency & voluntary	Default, insolvency & voluntary
2.	Amount of default which triggers the process	Rs 100,000	N/A	~ USD 40,000	USD 1000	N/A	SGD 10,000
3.	Regime - Debtor or Creditor in control	Creditor	Creditor	Debtor	Creditor	Creditor	Creditor
4.	During the Insolvency process who is in charge of the co.?	IP	IP	BoD	BoD	IP	IP
5.	Who can recommend the appointment of an IP?	Creditor, debtor or court	Creditor, debtor or court	Court	Creditor, debtor or court	Creditor, debtor or court	Creditor, debtor or court
6.	Who can be the IP?	Individual or firm	Individual	Individual or firm	Individual or corporate	Individual	Individual
7.	How many regulators (IPA)?	To be decided	Five	N/a	One	Two	Three
8.	Who fixes the remuneration - Insolvency process?	Market forces, approved by creditor	Market forces, approved by creditor	Court	Market forces, approved by creditor	Market forces, approved by creditor	Market forces, approved by creditor
9.	Who fixes the remuneration - Liquidation process?	Creditors (market forces) or court (scale based)	Market forces, approved by creditor	Court	Market forces, approved by creditor	Market forces, approved by creditor	Market forces, approved by creditor
10.	Is IP required to provide surety bond or professional insurance?	No	Yes	No	Yes	Yes	Yes
11.	Does IP get protection under the law?	Yes	Yes	No	Yes	Yes	Yes
12.	Is there a moratorium period?	Yes	Yes	Yes	Yes	Yes	Yes
13.	How long is the moratorium period for the co, under the insolvency process?	180 days (as extended to 270 days)	Entire period till plan is approved	180 days	180 days	Upto 30 days	Entire period till plan is approved
14.	Is it mandatory to form a credit committee?	Yes	No	No	No	No	No
15.	Are there specialized courts to deal with Insolvency?	Yes	No	No	Yes	No	No
16.	Who runs the liquidation process?	IP	IP	IP	IP	IP	IP
17.	Who does the IP report to during liquidation?	Court	Court	Creditor or court	Creditor or court	Creditors	Creditor and court
18.	Period of antecedent transaction	Up to 2 years	Up to 2 years, unlimited in case of fraud	3 years	Up to 5 years	Up to 10 years	Up to 5 years
19.	Is there a licensing / examination process to become an IP?	Yes	Yes	No	Yes	Yes	Yes
20.	Are the licenses renewed?	Once in 3 years	Annually	N/a	Annually	No, but have to satisfy certain conditions	Once in 3 years

*Based on the Code and draft regulations in public domain



As per the Doing business index 2016 released by World Bank, India continues to fare the worst amongst the BRICS nation. And with 136th rank, India is far behind the developed economies such as UK, US, and others



Among several requisites of a effective insolvency regime, recovery is one of the most important parameters. At 25.7 cents per dollar, India is ahead only of Brazil amongst BRICS nation

How does the Code measure with the UK?

A vast majority of the legal systems in the Commonwealth countries are founded on English common law. Hence, it is not a surprise that the Code closely mirrors the UK Insolvency Regime. The Bankruptcy Law Reforms Committee (BLRC) decided to move away from the existing “debtor in possession” regime to a “creditor in control” regime; the UK’s creditor in control regime is one of the most established and recognized globally.

Although the Code is based on the UK structure, the BLRC has identified key aspects of the legislation that may not work in an Indian scenario, and therefore appropriately customized it for India.

Some of the key similarities and differences between the Insolvency Law in the UK and the Code are detailed below:

Key similarities:

- 1. Creditors drive the process; licensed IPs run the process:** If a borrower is in default, a creditor can file an application to the court and start the insolvency process. The creditors are in control in determining the future course of action. A licensed IP will run the process.
- 2. Any creditor or the debtor can initiate the process:** In the event of default, a creditor can initiate the insolvency process. The debtor can also initiate the process by making an application to the court. The process is broadly similar irrespective of whether the application is filled by a creditor or debtor.
- 3. Moratorium provided during the insolvency period:** Upon commencement of the insolvency resolution process, a moratorium will be available to the corporate debtor during which period no suits can be instituted or recovery action can be initiated.
- 4. Clear waterfall of payments outlined during liquidation:** Under both the UK and the India regime, the legislation provides a clear waterfall of payments during liquidation, giving priority of payment to secured and preferential creditors. During liquidation, the liquidator pays the liquidation costs first before making payment to any preferential/secured creditors.
- 5. Multiple IPAs (or equivalent) regulated by a Board:** In the UK, there are multiple self-regulating bodies including ICAEW, ACCA and ICAS. Any professional who intends to become an IP needs to register with such a body and pass an exam (besides putting in minimum hours of practical training). There is a common board, which oversees the functioning of all the self-regulating bodies and brings in consistency in their functioning. In India as well, the draft regulations provide for multiple IPAs to be formed under the IBBI.

Key differences:

- 1. Creditors’ involvement during the insolvency process:** In the UK, the IP is an officer of the court and once the appointment and remuneration are approved by the creditors, the IP is generally not required to take any further approvals from the creditors with respect to the management of operations of the corporate debtor during the insolvency period. However, in under the Code (Section 28), there are multiple actions for which the IP needs prior approval from the creditors. There is a greater involvement of creditors in India during the insolvency process.
- 2. Performance security/bond to be provided by the IP:** In the UK, IPs are required to provide a general and a specific bond based on the value of assets involved under the case. The bond is to cover a situation if any fraudulent act is committed by the IP. The provision for a bond was initially specified in the draft of the Code submitted to the JPC but removed in the final draft that was enacted. Further, while only an individual can be an IP in the UK, as per the draft regulations in India, individuals and partnership firms (with unlimited liability) can take IP appointments.
- 3. Voting rights of creditor classes:** In the UK, all creditors (except secured creditors to the extent of the value of their security), including operational (trade) creditors, have voting power in the creditor committee in the ratio of the amount outstanding – particularly for the approval of a resolution plan. However, in India, only financial creditors (secured or unsecured) can vote in a creditor committee. They need to ensure, though, that a minimum of “liquidation value” is provided to the operational creditors in any resolution plan. In India, 75% of the financial creditors (in value) have to approve the resolution plan proposed during the insolvency process. In the UK, creditors with a simple majority approve the plan.
- 4. Deadline for the completion of the insolvency resolution process:** The Code specifies that if a resolution plan is not approved by the creditors within 180 days (or as extended to 270 days) of the CIRP, the liquidation process would automatically be triggered. In the UK, no such timeline has been specified under the law.
- 5. Remuneration of liquidator; timeline for completion of liquidation:** In the UK, remuneration for the IP in liquidations is generally decided based on discussion between the creditors and the IP, taking into account the time spent, assets realized, complexity of the case etc. If a consensus cannot be reached, the court can fix the remuneration. In India, the liquidation remuneration could be decided by the creditors in certain circumstances while in other cases, it would be decided based on the scale of realization and distribution (the court might consult the creditors or the IP while fixing the remuneration).
In India, as per the draft regulations, the liquidator is required to liquidate the assets within a period of two years. Extension can be granted in exceptional cases. There is no such requirement in the UK for the liquidator.



5

Case studies

- ▶ Insolvency resolution process
- ▶ Liquidation process

Insolvency resolution process

Facts of the case:

ABC Limited (the Company), which commenced operations in 2001, is a 100% holding company for four different companies operating in the healthcare sector. The Company has eight operating hospitals across India. In addition, there are two more hospitals under construction, with more than 50% work completed but on hold due to funding challenges. Four of the eight operating hospitals were acquired in the last three years. All the acquired hospitals are run by independent management with overall reporting to the central management team.

Based on the latest consolidated financial information available for the year ended June 2016, the Company had a top-line of INR7,500 million, with EBITDA of INR1,000 million and net loss of INR1,500 million. The Company had:

- ▶ term loans of INR6,000 million,
- ▶ working capital loan of INR1,200 million,
- ▶ unsecured financial debt of INR1,000 million and
- ▶ operational creditors of INR1,200 million (mainly trade and capex suppliers and employee dues).

A term loan of INR1,200 million is due for repayment in the next 12 months. The majority of the debt is in the holding company; however, some of the debt is also in the operating entities.

Total financial debt is provided by a syndicate of six banks with the lead banker holding 37.5% and the balance divided equally among the other banks, with each holding 12.5%.

The Company has around 3,500 employees and workmen, and the employee cost has significantly increased over the last few years. Apart from the employee cost, rental cost is the other significant expense, with 7 of the 10 properties on a long-term lease.

ABC Limited has been breaching covenants for the last few quarters and has defaulted on the repayment of its quarterly instalment for the last three quarters. However, it has managed to make payments on a delayed basis to avoid NPA classification.

The promoter (holding majority shareholding) has proposed a plan with the following key points to deal with the situation:

- ▶ Disbursal of additional INR500 million to expedite the construction of two hospitals that they believe will be high-cash-generating assets, based on a feasibility study report.
- ▶ Additionally, the term loan repayable in the next 24 months should be deferred and a revised repayment schedule should be agreed. A cash flow statement for the next three years has been submitted by the Company to support the proposal.
 - ▶ Interest rate should be reduced by 50% for the next six quarters and then reset at a higher rate to cover the loss.
 - ▶ Personal guarantee and additional security will be provided on the personal assets of the promoter.
 - ▶ Banks can charge a one-time fee of INR75 million to agree to the proposal.
 - ▶ To improve the operational cash flow from the business, the promoter would also make changes in headcount and procurement cost.

Options available to banks:

ABC Limited was in a difficult financial position and required a clear strategy and open communication between all the stakeholders for revival. As far as the banks are concerned, they had three options:

- a) Do nothing and ask the promoter to infuse capital to revive the Company first
- b) Accept the promoter's proposal on debt restructuring (everything else business as usual)
 - ▶ The bankers could have accepted the proposal of the promoter. If the plan was successfully implemented, it would have resulted in the recovery of debt in the long term by the banks.
 - ▶ However, in case the plan was not successful, it would have deteriorated the value of the asset, possibly facilitated asset-stripping and negligible value would have been realized via delayed liquidation for all external stakeholders including secured creditors, unsecured creditors, employees and suppliers.
- c) Act proactively to rescue and revive the business

To choose an option with the objective of maximization of benefit to all stakeholders, the banks had to evaluate deeper and make an independent assessment of business viability. They needed to answer the following questions:

1. What were the reasons for the current distress in the Company? How much of that could have been changed?

2. What was the cash flow-generation capability of the Company in the short, medium and long term?
3. What was the confidence level in the existing management? Were there any indications of diversion of funds or willful default?
4. What support or restructuring was required to revive the business? How much more money might have been required to revive the Company? What was the possibility of getting additional equity or debt funding from the market?
5. What could have been the strategy from the other classes of lenders, creditors, management etc.?

- (v) There was a benchmarking study done with other hospitals in the same geography and the report identified a few measures to save annual costs in the range of INR200 million to INR300 million. The report also provided details of the potential of consolidating some functions such as finance, procurement and HR into a single unit for all the hospitals.
- (vi) The report indicated the potential of improving the working capital cycle by 10 days.
- (vii) The expected capex to complete the under-construction hospital was approximately INR1,000 million.
- (viii) An estimate of the liquidation valuation (if put into liquidation today) vs. the going concern valuation was provided in the IBR report.

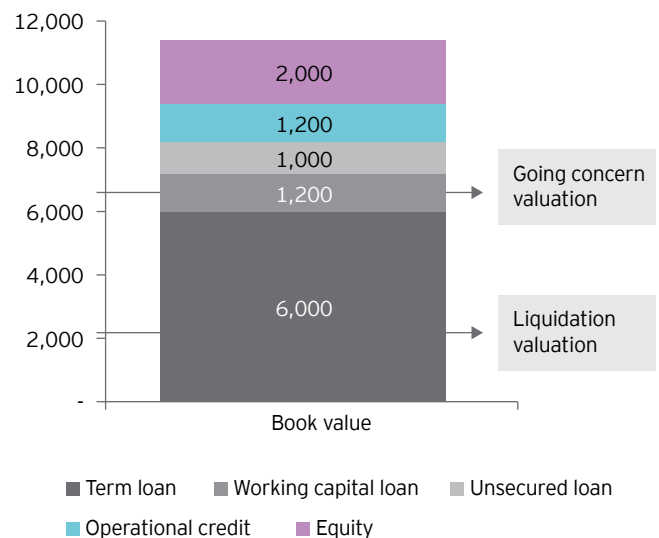
Commissioning of IBR to assess viability

Option A was not an option as it would have only delayed the inevitable with a risk of the assets being stripped of any residual value.

To answer the questions noted above, the banks in their core committee (combining the debt of the entire Company) decided to get an independent business review (IBR) done. They expected the IBR to help in assessing the viability of the business and validating the promoter's assertions. In four weeks, the banks received an IBR report. Some of the key facts included in the report were as follows.

- (i) On an as is basis, EBITDA from business would only be able to service part of the interest in the next 12-18 months and no principal payment would be possible. Principal repayment could only start after 18 months.
- (ii) All the four greenfield hospitals had optimal utilization levels and were cash flow positive; however, margins had been either flat or declining in the last 3 years.
- (iii) From the four operating hospitals acquired by the group, two would be free cash flow positive only in 2019 and the other two in 2022.
- (iv) The report identified a list of non-core assets, which could be liquidated to realize cash of up to INR500 million. Also, there were assets worth INR500 million that were not yet pledged against any loan and could be provided as additional security against a loan.

Please refer to the chart below



What did the banks do?

Based on the IBR report, the bankers concluded that the business was viable and they wanted to support it. Else, they ran the risk of taking the Company into liquidation, which would result in significant loss of value to all class of creditors. Further, a delayed liquidation would result in further deterioration of value.

However, the banks also recognized the need for operational and financial restructuring along with close monitoring and, therefore, all the stakeholders should cooperate in the turnaround strategy to minimize their losses.

Accordingly, the banks decided to appoint an external agency to perform the role of monitoring the business closely (to prevent loss of value) and develop a comprehensive resolution plan.

The resolution plan developed by the external agency suggested the following:

- (i) Bank debt be converted to Equity to the extent of 26% (of Equity) - INR 2,000 million
- (ii) A financial investor to be brought in to fund the completion of one under-construction project (equity and priority debt)
- (iii) A part of the debt (INR 1,000 million) be converted to a long-term instrument carrying a nominal rate of interest with repayment being made over 5 years starting in 2021.
- (iv) Two hospitals to be sold at the earliest and timelines to be stipulated for this to bring down debt
- (v) An operational turnaround plan to be implemented, including consolidating the back office function, consolidating the supply chain, and rationalizing the employee base
- (vi) Key cash flow and profitability covenants agreed on going forward

The resolution plan was discussed with all the key stakeholders - banks, promoters and potential investors. Based on the comments received, the plan was modified and an in-principle agreement was reached.

Code vs outside the Code

Under the current circumstances, the banks decided to invoke the Code to get an approval on the resolution plan. The following benefits could be realized upon invoking the Code.

1. There would be a moratorium period of 180 (or 270) days where no proceedings can be started against the Company - a time that can be utilized to refine the resolution plan and seek requisite approvals.
2. There would be an independent insolvency professional running the process. The IP would be a registered professional with rights and duties defined under the law.
3. The plan approved by the creditors under the Code will also be approved by NCLT. The transparency of the process would have legal sanctity and would not subject the bankers to scrutiny or investigation.
4. The plan approved would be binding on all classes of creditors and no further action can be taken for the next 12 months if the plan is implemented as approved. If a plan outside the Code is agreed upon, any financial or operational creditor could still file for insolvency under the Code.
5. Under Section 14 (2), the supply of essential goods or services shall not be terminated, hence, supporting the going concern of the company till the time a plan is approved.

Conclusion

In summary, the banks could help revive the Company because of the following:

- ▶ The banks acted on a timely basis (rather than postpone the problem) and they based their decision making on an independent business review.
- ▶ They appointed an independent agency to monitor operations (and arrest loss of value) and develop a comprehensive resolution plan.
- ▶ The resolution plan was discussed and modified based on the views of various stakeholders - before triggering the 180-day deadline specified under the Code.
- ▶ The Code was then invoked to benefit from the legal protection available - post which the resolution plan could be approved and implemented.

Liquidation process

Facts of the case:

Refer below a balance sheet for XYZ Limited, based on the balance sheet and additional information provided provide a working for outcome to different class of creditors.

Liability	"Amount (Rs. Million)"	Assets	"Amount (INRMillion)"
Equity share capital	1,600	Land & Building	4,500
Preferential share capital	1,200	Fixtures and fittings	800
		Stock	435
Term loan	1,400	Debtors and prepayments	540
Working capital loan	1,000	Other current assets	425
Unsecured financial creditors	800	Cash	125
Government dues	120	Accumulated losses	1,155
Workmen dues	240		
Employee liability	380		
Operational creditors	1,240		
	7,980		7,980

Additional information:

Secured Creditors:

- Term loan is secured against fixed charge on land & building and fixtures & fittings. Bank A with INR 1,000 million term loan outstanding has first charge on the assets and Bank B with INR 400 million outstanding has second charge on the assets.
- Working capital loan is provided by Bank B and secured against a floating charge on stock, debtors and other current assets of the Company.

Other Liabilities:

- Workmen dues include amount payable for up to last 15 months
- Employee liability include provision for bonus payable of Rs.50 million, which was discretionary based on performance of the company and not yet announced to the employees. Also, INR 25 million is outstanding for employees for more than 12 months

- Last three years of tax assessment pending and total demand raised by the department is INR 1,200 million. This has not been included in the balance sheet. However, liquidator has managed to get an assessment completion certificate and agreed a final liability of Rs.400 million.

Fixed assets and other assets:

- Land & building realised 65% of book value and there would be a cost of INR.100 million in realising the assets.
- Fixtures and fitting would realise 25% of book value, net of any realisation cost. Stock, debtors and other current assets would realise 60% of book value.

Other information:

- There was a pending insurance claim filled by the Company for a quality breach by a supplier, which was not recorded in the books. Liquidator has managed to recover INR 150 million from the insurance company. Lease for the office premises had a lock in period of 10 years, out of which three years have expired. Landlord has submitted a claim of Rs.120 million for the remaining seven years of the lease period.
- Based on amount realised and distributed cost of liquidation is computed to be Rs.175 million.
- Pending insolvency period cost was Rs.75 million mainly including interim funding, remuneration of the IP, unpaid cost for running the company during the period etc.
- The secured creditors have decided to relinquish their security interest to the liquidation estate and receive proceeds from the sale of assets by the liquidator in the manner specified in Section 53.

Response:

Table 1: Total value realized by liquidator

Assets	"Book value (Rs. Million)"	%	"Amount realised (INR Million)"
Land & Building	4,500	65%	2,925
Fixtures and fittings	800	25%	200
Stock	435	60%	261
Debtors and prepayments	540	60%	324
Other current assets	425	60%	255
Cash	125	100%	125
Insurance claim			150
	6,825		4,240

Table 2: Order of priority

Section reference	Order of priority	Note	"Amount (Rs. million)"	"Amount (Rs. million)"
Total value realised during liquidation				
	Realised from secured assets		4,090	
	Less : Cost of realising secured assets	1	-100	
	Collection from insurance claim	2	150	4,140
Distribution of assets as per Section 53 of the IBC				
53 (1) (a)	Insolvency resolution process costs	1	-75	
53 (1) (a)	Liquidation process costs	1	-175	-250
Amount available for workmen and secured creditors				3,890
53 (1) (b) (i)	Workmen's dues for the period of up to twenty-four months	3	-240	
53 (1) (b) (ii)	Debts owed to a secured creditor			
	Term loan Bank A	3	-1,000	
	Term loan Bank B	3	-400	
	working capital loan	3	-1,000	-2,640
Amount available for distribution to employees				1,250
53 (1) (c)	Wages owed to employees	4	-305	-305
Amount available for distribution to financial unsecured creditors				945
53 (1) (d)	Financial debts owed to unsecured creditors		-800	-800
Amount available for distribution to government dues				145
53 (1) (e)	Central government and state government dues			
	Recorded in balance sheet		-120	
	Tax claim settled for open assessment		-400	-520
Amount available for any remaining debt and dues				-375
53 (1) (f)	Any remaining debt and dues			
	Operational creditor		-1,240	
	Employee claim for more than 12 months	4	-25	
	Rent claim for unexpired lease period	5	0	-1,265
Amount available for preference shareholder				-1,640
53 (1) (g)	Preference shareholders		-1,200	-1,200
Amount available for equity shareholder				-2,840
53 (1) (h)	Equity shareholders		-1,600	-1,600
	Net (Shortfall) /excess			-4,440

Note 1:

- ▶ Rs.100 million of cost for realising fixed assets has been deducted from the amount realised. Alternatively, it could also be included in the liquidation cost.
- ▶ In case the value realised is less than the insolvency and liquidation cost amount realised would be distributed between the all the cost pari passu.

Note 2:

- ▶ Claim recovered from insurance company of Rs.150 million has added to total value realised. It could be argued to use this realisation against unsecured creditors, since this is not realised from a secured assets.

Note 3:

- ▶ Workmen dues and secured creditors have pari passu claim on the amount available after liquidation and Insolvency cost.
- ▶ Bank A has a first charge on the secured fixed assets, in case of a situation where amount realised from secured fixed assets was less than the total outstanding of term loan of Rs.1,400 million, Bank A with first charge should be given preference over the Bank B. To the extent Bank B was not paid under sec 53 (1) (b) (ii), they should be paid under section 53 (1) (d).
- ▶ In case of working capital loan, Bank B has charge over the floating assets i.e Stock, debtor and other current assets of the Company. In the current situation, floating assets realised Rs. 965 million. Shortfall of Rs.35 million is set off against the excess realisation from the secured fixed assets. However, it could be argued to treat the shortfall as unsecured financial creditor under section 53 (1) (d).

Note4:

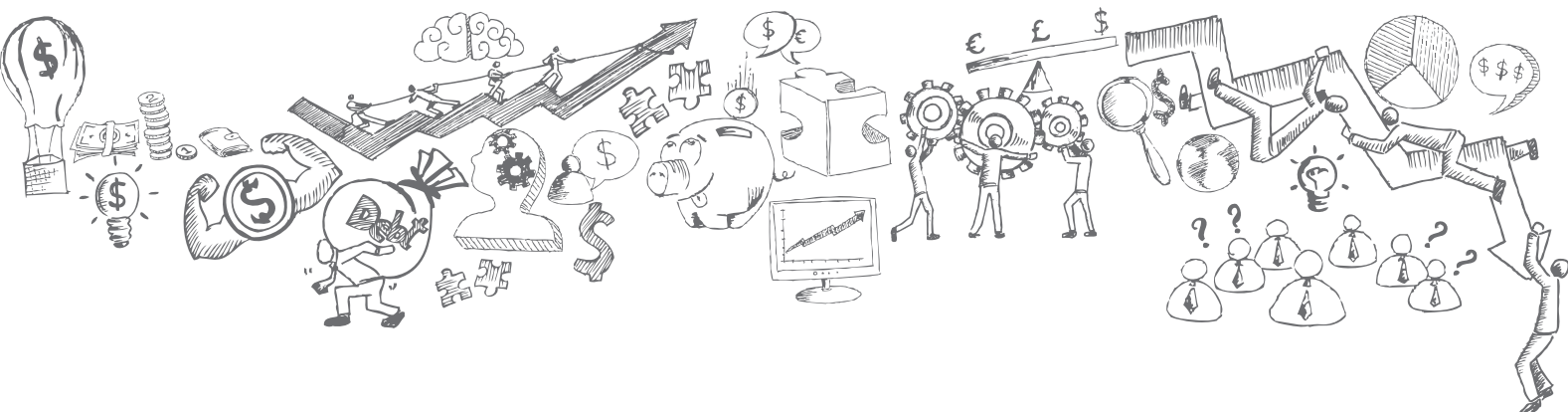
- ▶ Employee liability for more than 12 months has been included under section 53 (1) (f) as other debts.
- ▶ Bonus of Rs.50 million is not included in the employee liability as it is not declared and hence not due to the employees.

Note 5:

- ▶ Rent claim for unexpired lease period has been included under section 53 (1) (f) as other debts at nil value. As based on draft regulation 36, payment of periodic nature can only be claimed till the time order for liquidation is passed under section 33 of the IBC. This may, however be subject to further clarification by appropriate authorities.

Table 3: Outcome to different class of creditors

Currency: Rs. Million	Amount outstanding	Amount realised in liquidation	% realised
Workmen	240	240	100.0
Employees	380	305	80.3
Secured creditor	2,400	2,400	100.0
Unsecured creditors	800	800	100.0
Government dues	520	145	27.9
Any remaining debt and dues	1,265	-	-
Preference shareholder	1,200	-	-
Equity shareholder	1,600	-	-
Total	8,405	3,890	46.3





FAQs

Question - What is the impact of the Code on the existing legislations such as SARFAESI, SICA, and Companies Act?

Response - The Code consolidates and amends the laws relating to reorganisation and insolvency of corporations, partnerships and individuals.

It may be noted that existing judicial proceedings under Companies Act shall be transferred from CLB and High court to NCLT. Also the proceedings under SICA shall abate, with the option for the company to make a reference to NCLT within 180 days from the commencement of the Code.

Further on declaration of moratorium, all actions under Sarfaesi be prohibited till the insolvency resolution process under the Code. Besides, there are numerous matters (sale of part of an organisation, carve-out of business, etc.) that need the approval of shareholders as per the Companies Act, 2013. Whether such actions contemplated in the resolution plans (or otherwise) can be completed without such approvals needs to be evaluated. The draft regulations supporting the Code, however, state that such approvals may not be needed.

Question - Can the Code be triggered in case of non-payment of dues by Government-owned companies?

Response - The Code shall apply to:

- ▶ any company incorporated under the Companies Act, 2013 or
- ▶ any other company governed by any special Act for the time being in force,

- ▶ any Limited Liability Partnership incorporated under the Limited Liability Partnership Act, 2008
- ▶ such other body incorporated under any law for the time being in force, as the Central Government may, by notification, specify in this behalf; and
- ▶ partnership firms and individuals,

There is no specific exclusion of any company owned by the Government and the Code shall apply to such companies.

Question - What has been the response of the RBI to the Code? Specifically, how does this impact bank provisioning guidelines?

Response - The current provisioning norms as defined by the RBI may need to be aligned with the Code. For instance, one of the possibilities could be that the RBI continues with the existing classification norms such that for the first 90 days after default, the account can be treated as an SMA and after 90 days as an NPA. After approval of the resolution plan, the borrower can be classified as standard.

Further, the existing schemes of restructuring outlined by the RBI (CDR, 5/25, SDR, S4A, etc.) would also have to be synchronized with the Code.

RBI could also play a pivotal role by developing a better early warning system for banks based on a robust covenant framework. With better early warning reporting, RBI could preempt the banks to take appropriate action in a timely manner, thereby acting as a virtual information utility.

Question - How does the Code help avoid litigations that may delay revival?

Response - The Code provides a moratorium during the CIRP that protects the borrower from any suits or recovery actions during that period. Besides, a resolution plan approved by the NCLT during CIRP would be binding on all parties.

Question - Should creditors trigger the insolvency process upon every default? Or should they evaluate other options outside the framework?

Response - No situation is the same and a one-size fits all approach may not make sense. An objective evaluation has to be done on a regular basis by the creditors, along with evolving a strong early warning mechanism based on robust covenant framework.

Upon a default, the creditors should evaluate their options based on an Independent Business Review before charting their course of action. Please refer pages to pages 18 to 19 and the section on case studies for a detailed discussion on the same.

Question - Does the Code provide immunity to the financial creditors to take hard measures (including haircuts) without fear of undue vigilance? What are the consequences of lack of consensus or lack of action?

Response - The Code does not, explicitly, provide any immunity to the lenders for their actions. However, inaction or lack of consensus amongst the financial creditors during the CIRP would mean liquidation - mostly an economically inferior outcome as compared to resolution.

The resolution plans could be developed by anyone who intends to and can submit it to the RP. Upon receipt of all the resolution plans, the RP will recommend the appropriate plan to the Committee of Creditors. Upon approval of a resolution plan by the CoC with a voting of 75% majority, it would need to be approved by the NCLT. The plan so approved becomes binding on all creditors including the dissenting creditors.

The transparency of the process of development and approval of the resolution plans and the lack of a more beneficial alternative should address the concerns of the creditors.

Question - What are the rights of foreign creditor vis-à-vis domestic creditors?

Response - The Code does not make a distinction between domestic and foreign creditors. Any creditor, operational or financial, could exercise rights available under the Code in so far as the application for insolvency is made within India and under the Code.

Question - What are the powers to minority creditors, operational creditors, and unsecured creditors? Can they block the resolution or liquidation process?

Response - 75% of the financial creditors (secured and unsecured) would vote on the resolution plan. In the plan approved, Operational creditors should receive at least the value equivalent to what they would get in a liquidation scenario. Operational creditors and shareholders don't have any voting rights on the plan.

However, where there are no financial creditors or the financial creditors are related party, the CoC shall be formed by the operational creditors. Also the Code doesn't restrict any class of creditors or shareholders to propose a resolution plan.

Question - How would personal guarantees of the promoters be enforced?

Response - The Code allows the creditors to invoke the CIRP of both, the corporate debtors and its personal guarantors. This would mean that the Code shall override proceedings to enforce personal guarantees under SARFAESI, Indian Contracts Act etc. with respect to the CIRP. There are no other changes to the rights of the creditors to enforce personal guarantees.

Question - How would the ranking between the first charge secured creditor, second charge secured creditor and workmen compensation dues be decided?

Response - As per the reading of the Code, workmen compensation dues and secured creditors would rank pari passu. Also, as per the Code, you need to relinquish security before participating in the distribution. Both first charge and second charge secured creditors would rank pari passu with respect to the distribution under Section 53(1). Therefore, as a first charge creditor, you are expected to take a commercial call if you want to enforce security under existing means available or relinquish it for distribution under section 53.

However, regulation 45 of the Liquidation process states that the contractual arrangement between recipients with equal ranking under section 53 (1), if disrupting the order of priority, the liquidator can make the payment to one of the recipients nominated by all the recipient parties to the contractual arrangement. The practical application of such distribution will evolve over a period of time.

Question - Consider a situation if there are two secured creditors, one with a fixed charge and another with floating charge, and the amount realised from the fixed charge assets is more than the fixed charge debt and amount realised from floating charge assets is less than the floating charge debt.

Then, would there be a set off between shortfalls of the floating charge debt with the excess of fixed charge assets or floating charge shortfall will be treated as an unsecured claim.

Response - Under Section 53, you relinquish your security to be part of the liquidation distribution. Therefore, the source of realisation should not impact the distribution specified under Section 53 - these would be distinct from each other.

Question - If amount is realised from unsecured assets, would they still be available to secured creditors first (as per order of priority in sec 53) or will they be equally available to all class of creditors (secured or unsecured).

Response - All collections - irrespective of the source of realisation - should go into a common pool of the liquidation estate. The distribution from this liquidation estate should happen as per Section 53 of the Code.

Question - Definition of employee's dues - Will this include any discretionary bonus? In case of an employee car lease foreclosure, who would pay the foreclosure cost?

Response - As per the Code, only unpaid dues for last 12 months can be paid to employees. Besides, only legal and contractual dues should be included as liabilities. If a car lease is a contractual liability of the borrower, the resulting foreclosure cost should be included under unsecured liabilities (and not employee liability).

Question - Supply of essential goods or services - can supplier ask for change in the terms and condition of the trade during CIRP?

Response - In the draft regulations, a list of essential supplies is defined. It is also mentioned that the supplier of essential supplies cannot make payment of past debt a condition for supply during CIRP. However, there is nothing in the regulation stopping the supplier to re-negotiate payment terms with the RP during the CIRP. Besides, if in the context of any business, the RP feels that a particular goods/ service should be included as 'essential', he would have to apply to the NCLT and seek such a declaration.

Question - What will happen to future unexpired warranty given by the Company on the products sold, in case of liquidation? Will that claim be included in unsecured claims?

Response - It would depend upon the contractual arrangement between the customer and the debtor. Any liability which is not due on the insolvency commencement date may not be included in the claims.

Question - Can IP take control of the assets in a subsidiary?

Response - As per Section 18 of the Code, one of the key responsibilities of the IP is to take control and custody of the assets of the borrower. However, IP cannot take control over the assets of a subsidiary of the borrower. With respect to the subsidiary, he can only act in the capacity of a shareholder (i.e. step in to the shoes of the borrower).

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