

[2019] 2 IBJ (Art.) 39

Revival of Corporate Debtors under the Companies Act, 2013



In this article, the authors dwell on the revival of the corporate debtors under the Companies Act, 2013 (Act) in the backdrop of the discussion paper issued by the Insolvency and Bankruptcy Board of India proposing to introduce a new provision in the IBBI (Liquidation Process) Regulations, 2016 for compromise or arrangement of the corporate debtor under section 230 of the Act to revive the corporate debtor as a going concern before the liquidation process commences.

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Introduction

On 27 April 2019, the Insolvency and Bankruptcy Board of India (“IBBI”) issued a discussion paper along with draft regulations (“**Discussion Paper**”) in relation to the corporate liquidation process under the Insolvency and Bankruptcy Code, 2016 (“**Code**”). One of the key proposals in the Discussion Paper is to introduce a new provision in the IBBI (Liquidation Process) Regulations, 2016 (“**Liquidation Regulations**”) for compromise or arrangement of the corporate debtor under the provisions of section 230 of the Companies Act, 2013 (“**2013 Act**”) as an attempt to revive the corporate debtor as a going concern before the liquidation process commences.

Section 230 of the 2013 Act provides that where a compromise or arrangement is proposed with the creditors or members of the company then the National Company Law Tribunal (“**NCLT**”) may, on an application made to it, direct that a meeting of the creditors and/or members, as the case may be, held to consider the proposed compromise or arrangement. The application proposing such

compromise or arrangement under section 230 can be made by (a) the company; (b) the members of the company; (c) the creditors of the company; or (d) the liquidator appointed under the Code.

The scheme of compromise or arrangement (“**Scheme**”) once approved [by majority of persons representing three-fourths in value of the creditors or members (as the case may be)] and sanctioned (by the NCLT) is binding on the company as well as all the creditors and/or members of the company and in case of a company under liquidation, on the liquidator and the contributories of the company.

Revival v. Liquidation

In the matter of *Arcelor Mittal India Pvt. Ltd. v. Satish Kumar Gupta* [2018] 1 IBJ (JP) 563 (SC), the Supreme Court stressed upon resolution of the corporate debtor and observed that “the ‘Corporate Debtor’ consists of several employees and workmen whose daily bread is dependent on the outcome of the CIRP. If there is a resolution applicant who can continue to run the corporate debtor as a going

concern, every effort must be made to try and see that this is made possible".

The fallouts of liquidation of corporate debtor were also discussed by the National Company Law Appellate Tribunal ("NCLAT") in the corporate insolvency resolution process against Binani Cement Ltd. wherein the NCLAT as follows:

"Liquidation brings the life of a corporate to an end. It destroys organisational capital and renders resources idle till reallocation to alternate uses. Further, it is inequitable as it considers the claims of a set of stakeholders only if there is any surplus after satisfying the claims of a prior set of stakeholders fully. The 'I&B Code', therefore, does not allow liquidation of a 'Corporate Debtor' directly. It allows liquidation only on failure of 'Corporate Insolvency Resolution Process'. It rather facilitates and encourages resolution in several ways."

The aspect of ensuring revival of the corporate debtor was also discussed by the Supreme Court in its judgement passed in *Swiss Ribbons*¹ case. The Supreme Court in its order discussed the objective of the Code and stated that the Code is first and foremost a Code for **reorganization and insolvency resolution** of corporate debtors. The Supreme Court further observed that the primary focus of the legislation is to ensure revival and continuation of the corporate debtor by protecting the corporate debtor from its own management and from a corporate death by liquidation and therefore, the liquidation should be availed of as a last resort only if there is no resolution plan or the resolution plans submitted are not up to the mark.

Applicability of section 230 to the Liquidation under the Code

The Scheme under section 230 of the 2013 Act in relation to corporate debtor facing liquidation under the Code was first proposed in the case of Gujarat NRE Coke Limited ("**GNCL**"). Subsequent to the passing of liquidation order of GNCL by the adjudicating authority, the promoter/director of GNCL approached the NCLT with a scheme under section 230 for revival of

GNCL. Pursuant to the promoter's proposal, the NCLT issued necessary directions for convening and holding of separate meetings of creditors and shareholders to consider and approve the scheme of arrangement. However, the NCLAT, in appeal filed by Jindal Steel and Power Ltd. stayed convening of the meetings of stakeholders of GNCL.

While the Supreme Court and the NCLAT stressed upon revival of corporate debtor, section 33 of the Code mandated the adjudicating authority to order liquidation of corporate debtors under if (a) the adjudicating authority did not receive the resolution plan before the expiry of maximum time period of 270 days (including one time of extension of 90 days) or (b) the adjudicating authority had rejected the resolution plan(s) due to non-confirmation of the requirements as set out under section 31 of the Code. There is no provision in the Code which gives power to the adjudicating authority to order for revival under section 230 of the 2013 Act. In view of this, the orders passed by the adjudicating authority in certain cases for liquidation of corporate debtors were challenged before the NCLAT wherein the NCLAT ordered for revival of corporate debtors under section 230.

The NCLAT relied upon the judgements passed by the Supreme Court in *Meghal Homes*² and *Swiss Ribbons (supra)* and directed the liquidator, in its order in *S.C. Sekaran v. Amit Gupta*³ ('S.C. Sekaran' case), that the liquidator should take necessary steps in terms of Section 230 of the 2013 Act before taking steps to sell the assets of the corporate debtor. The NCLAT also directed that only in case a revival is not possible, should the NCLT and the liquidator proceed with the sale of company's assets. The order passed by the NCLAT in *S.C. Sekaran* case (*supra*) presented a ray of hope for the stakeholders of the corporate debtors facing liquidation proceedings under the Code.

While directing the liquidator to proceed for revival of corporate debtor under section 230 in the matter of *Y Shivram Prasad v. S Dhanpal*⁴ ('Y Shivram Prasad' case), the NCLAT held that, as the liquidation of

2. *Meghal Homes Pvt. Ltd. v. Shree Niwas Girni K.K. Samiti.* (2007) 7 SCC 753

3. MANU/NL/0049/2019

4. MANU/NL/0103/2019

1. *Swiss Ribbons Pvt. Ltd. v. Union of India.* [2019] 2 IBJ (JP) 73 (SC)

corporate debtor would be taken up under the provisions of the Code, the arrangement of scheme should be in consonance with the statement and object of the Code only. The NCLAT also held that the scheme must ensure maximisation of the assets of the corporate debtor and balance the stakeholders without any discrimination. Before the approval of an arrangement or scheme, the NCLT should follow the same principle and should allow the liquidator to constitute a committee of creditors to find out whether the arrangement of scheme is viable, feasible and having appropriate financial matrix.

Can the Defaulting Promoters propose the Scheme?

The proposed regulation 12A permits a liquidator to file an application for compromise or arrangement of corporate debtor under section 230 within 7 days of the liquidation order having been passed by the adjudicating authority. Also, members or creditors of the corporate debtor are permitted to file an application under section 230 within 10 days of the order of liquidation. Thus, in terms of the proposed amendments, the members or creditors of the corporate debtor may also propose the Scheme for revival of corporate debtors. In *Y Shivram Prasad* case also, the NCLAT had allowed the members and/or the creditors to approach the company through the liquidator for compromise or arrangement by making proposal of payment to all the creditor(s).

Notably, section 35(1)(f) of the Code prohibits sale of property of the corporate debtor in liquidation to the ineligible resolution applicants under section 29A of the Code. However, it is being proposed that the ineligibility norms under section 29A of the Code may not apply to the Scheme under section 230 of the 2013 Act for revival of corporate debtors.

The question that whether the members of the corporate debtor under liquidation can prefer an application under section 230 of the 2013 Act and whether such petition is maintainable or not came for consideration before the NCLAT in the matter of the GNCL. The appellant contended that the ex-directors or the promoters of the corporate debtor, who have

been declared ineligible under sections 29A or section 35(1)(f) of the Code to file 'resolution plan', were not eligible to file application under section 230 for the revival of the corporate debtor under liquidation.

In view of the observations of the Supreme Court in *Swiss Ribbons* case (*supra*) that "the interest of the corporate debtor have, therefore, being bifurcated and separated from that of this promoters/ those who are in management", the NCLAT passed interim order allowing the liquidator and the promoters of the corporate debtor to suggest the arrangement under section 230 of the 2013 Act.

Another aspect to note is that pursuant to the directions given by the Hon'ble NCLAT in *S.C. Sekaran* case (*supra*), the liquidator of *Hindustan Dorr Oliver Ltd. ("HDOL")* invited expression of interest ("Eoi") from potential sponsors interested in proposing the scheme for the purpose of reviving HDOL. The invitation of Eoi also stipulates a condition that the parties interested in proposing the scheme for revival of HDOL must fulfil the eligibility criteria set out in the notice including that the proposed sponsors must not be ineligible under section 29A of the Code. It is pertinent to note that though the NCLAT had directed the liquidator to take necessary steps under section 230 of the 2013 Act for revival of corporate debtors, the order did not provide any guidance as to the eligibility of the parties proposing the scheme for revival.

Conclusion

While the proposed regulation 12A is welcome step, as it attempts to ensure revival of the corporate debtor in the interest of all the stakeholders, certain clarifications/amendments are still required for effective implementation of the proposal:

- The Supreme Court, in its judgement in *Swiss Ribbons* case (*supra*), said that the defaulters' paradise is lost and the economy's rightful position has been regained. Therefore, in case the ineligibility norms are dispensed with, the proposed regulation 12A would effectively offer another lifeline to the defaulting promoters to make a bid for acquiring control and management of the corporate debtor and as such defeat the spirit of law laid down under section 35(1)(f) read with section 29A.

- There is no clarity if a third party (other than promoters, members or creditors of the corporate debtor), who is willing to acquire the corporate debtor as a going concern, can approach the liquidator and propose a Scheme for acquisition of corporate debtor under section 230 of the 2013 Act.
- The proposed regulations do not clarify if there will be any requirement to apply for and obtain no-objection letters from the stock exchange in respect of the scheme in case the corporate debtor is listed on any recognized stock exchange.
- The NCLAT, in *Y Shivram Prasad case (supra)*, mandated that the committee of creditors (“CoC”) shall review and decide upon the viability and feasibility of the scheme of arrangement. However, the proposed regulation 12A does not have any such provision. Accordingly, the regulations should also clarify how the liquidator will decide upon and ascertain the credibility of the proposal of compromise or arrangement for corporate debtor.
- The members and the operational creditors do not have a right to interfere with the decision of the CoC under the Code. But the Scheme under section 230 of the 2013 Act has to be approved by the members and the creditors of the corporate debtor with prescribed supermajority. Therefore, in case the Scheme is proposed by non-promoter entity, then, the defaulting promoters and their related parties would obstruct the Scheme by not approving the same. This is on account of the fact that section 230 permits the promoters also to participate in the voting process.
- The regulations should also clarify if the waterfall mechanism prescribed under section 53 of the Code would need to be considered while proposing the Scheme under section 230 of the 2013 Act for revival of corporate debtor.



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