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INSOLVENCY AND BANKRUPTCY CODE, 2016 - ROLES, RESPONSIBILITIES AND RISK FOR INSOLVENCY PROFESSIONALS

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Introduction to the Code



Why we needed a new Code?

Problem of too many yet too little

Erstwhile Regime	Criticism
The SARFAESI Act, 2002	Non-inclusive regime Designed for enforcement and not revival
The Recovery Of Debts Due To Banks and Financial Institutions Act, 1993;	Overburdened DRTs
Sick Industrial Companies (Special Provisions) Act, 1985	Prescribed revival of a sick company under the same management often ineffective Moratorium provision used to delay. No time bound process meant that moratorium often continued indefinitely BIFR route used to delay legal action by banks for debt recovery even upon failure of CDR loan restructuring.
Corporate Debt Restructuring under RBI Guidelines	Voluntary regime Too little too late
Strategic Debt Restructuring under RBI Guidelines	Voluntary regime, with effective Bank management (not natural for Banks)
S4A	Sustainability study challenges, valuation challenges



Need for a comprehensive Code



Ecosystem per the Code



Adjudicating Authority

Exclusive jurisdiction to deal with insolvency matters e.g. NCLT/NCLAT, DRT/DRAT

Creditors



Financial



Operational



Corporate



Insolvency and Bankruptcy Board

Ensure transparency and governance by regulating IU/IP appointment and functioning



Information Utilities (IU)

Maintain data on Debtors to overcome information asymmetry amongst Creditors



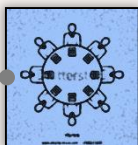
Insolvency Professionals Agency (IPA)

Disciplinary body for Insolvency Professionals



Insolvency Professionals (IP)

IPA-approved licensed professionals to take on role of Resolution Professional (RP)



Committee of Creditors (CoC)

RP appoints CoC to discuss and decide resolution in best interests of all creditors



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Understanding the Code and the new Borrower- Lender relationship



Corporate Insolvency Resolution Process - Trigger

***FINANCIAL CREDITORS** are those creditors who have extended credit for time value of money';
OPERATIONAL CREDITORS are those creditors who have extended credit in exchange for goods and services and other debt payable to the Central or State Government.

Who	Any Financial Creditor (Including ARCs) or Operational Creditor
When	Financial Creditor*: Upon default > INR 1,00,000 (GoI can increase up to INR 1,00,00,000) Operational Creditor*: Upon default > INR 1,00,000 (GoI can increase upto INR 1,00,00,000) + Non-payment by Corporate Debtor for a period of 10 days after issue of Demand Notice.
New Infrastructure	Intent to introduce Information Utility infrastructure to streamline information asymmetry, reduce time taken to determine actual financial health of corporate debtor.

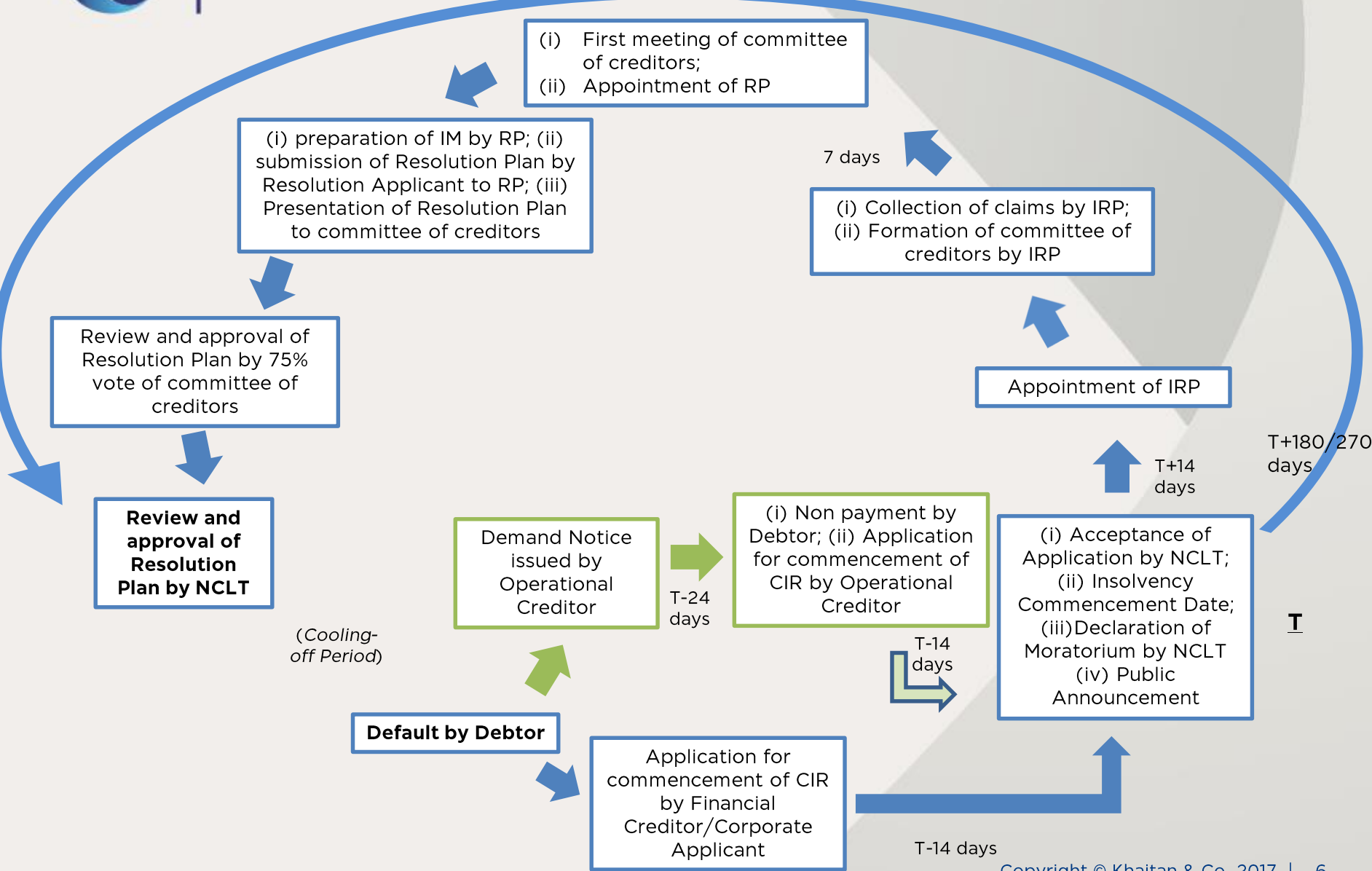
Key Takeaways:

Move away from complicated court driven "balance sheet test Operational Creditors can bring down the house of cards.

Food for thought: *Are defaults other than payment defaults a trigger under the Code?*



Corporate Insolvency Resolution ("CIR"): Process Flow





Understanding Resolution Professionals



Who is an insolvency professional?

- Any person who is:
 - Enrolled with an insolvency professional agency**; **and**
 - Registered with the Insolvency and Bankruptcy Board as an insolvency professional.
- Insolvency Professionals can, however, form Insolvency Professional Entity, which can provide resources to the IP.
- Insolvency Professional Entity can be a partnership firm, limited liability firm or a private limited company. All the partners / directors of the company shall be jointly and severally liable for the acts of the individual IP taking up assignment.

** There are 3 IPAs registered with IBBI as on date i.e.

- Indian Institute of Insolvency Professionals of ICAI;
- ICSI Insolvency Professionals Agency; and
- Insolvency Professional Agency of Institute of Cost Accountants of India.



Transitional Registration

Insolvency and Bankruptcy (Registration of Insolvency Professionals) Regulations, 2016 provide for transitional registration. An individual may be eligible to apply if:

- he has received a Bachelor's Degree from any University in India or abroad; **AND**
- has, for a period not less than **15 years**, been a **CA enrolled as a member of ICAI**, CS enrolled as a member of ICSI, cost accountant enrolled with Institute of Cost Accountants of India, lawyer enrolled with any Bar Council, an actuary enrolled with the Institute of Actuaries of India, working in the field of management of businesses, an officer in the Indian Corporate Law Service, or working in the field of insolvency; **AND**
- has for a period of not less than **3 years in the last 10 years**, been employed with one or more financial service providers and has carried out work relating to debt restructuring, enforcement or recovery, or engaged in work with respect to:
 - debt restructuring,
 - turnaround of corporate persons,
 - corporate restructuring,
 - acquisition or sale of assets, shares or businesses of corporate persons,
 - conduct of liquidation of assets of a corporate person, including the winding up of a company,
 - raising debt finance and/or equity funding for corporate persons for expansion, project finance, refinancing etc., or
 - selling, recovering or monitoring nonperforming assets or stressed assets, whether singly or cumulatively.

The application for transitional registration is required to be made to the Chairperson of the Board with certain documents (such as your degree, passport size photographs etc.) and will have to be submitted in hard copy. (**Schedule 1** of the Registration Regulations).



Employees registering as Professionals disallowed from Insolventcy

The IBBI rejected an application for registration as an IP under regulation 7 of the Insolvency and Bankruptcy Board of India (Insolvency Professionals) Regulations, 2016 (IP Regulations) through its first regulatory order. The applicant had applied for registration as an IP through the Indian Institute of Insolvency Professionals (affiliated with the ICAI) (IIIP). Such application was forwarded by the IIIP to the Board.

Reasons for rejection:

- Clause 23 of the Code of Conduct of the IP Regulations makes it clear that an IP must not 'engage in any employment', i.e a person must not play two roles - profession and employment - simultaneously. The objective behind such a requirement is that an IP must have *undivided loyalty and unflinching attention* towards his professional obligations. The 'time bound resolution' principle envisaged in the Code requires time critical service from the IP.
- Clause 23 mandates a comprehensive prohibition on other employment and is not intended to address issues of independence or conflicts of interest (for which there are comprehensive provisions contained in other regulations under the Code).
- Regulation 7(2) of the IP Regulations requires an IP to abide by the Code of Conduct contained in the IP Regulations at all times.

Clause 23 states: "An insolvency professional must not engage in any employment, except when he has temporarily surrendered his certificate of membership with the insolvency professional agency with which he is registered."



Who can be a resolution professional?: 'Independence' test

If the insolvency professional, and all partners and directors of the insolvency professional entity (IPE) of which he is a partner or a director are independent of the corporate debtor.

Factors to determine independence:

- eligible to be appointed as an independent director for the corporate debtor as per provisions of the Companies Act 2013
- not a related party to the corporate debtor
- in the last 3 financial years, he or she has not been an employee or a proprietor or partner of (A) any firm of auditors, company secretaries of the corporate debtor; or (B) any legal or consulting firm that has or had any transaction with the corporate debtor as its client amounting to 10% or more of the gross turnover of such legal or consulting firm.

The resolution professional who is a director or a partner of an IPE, shall not continue as a resolution professional, if the IPE or any of its partner or director represents any other stakeholders.

This test is also applicable at the time of appointment of 'liquidators' under the Code.

Further, the Code prescribes that there must be no disciplinary proceedings against such person proposed to be appointed as the resolution professional.



Powers of the Interim Resolution Professional/ Resolution Professional

- Management of the affairs of the corporate debtor shall vest
- Powers of the board shall stand suspended and be exercised by IRP
- Officers and managers of the corporate debtor shall report to the IRP and provide access as may be required
- Financial institutions maintaining accounts of the corporate debtor shall act on the instructions of the IRP
- Right to access IU records of the corporate debtor
- Avoidance Powers
- Take control over assets of the Debtor including those that are situated outside India
- Can appoint consultants, lawyers other professionals
- Enter in to or amend contracts
- Raise Super Sr. Finance (incl. secured w/o consent if 2x cover is met) Vs Raise Super Sr Finance but subject to CoC approval

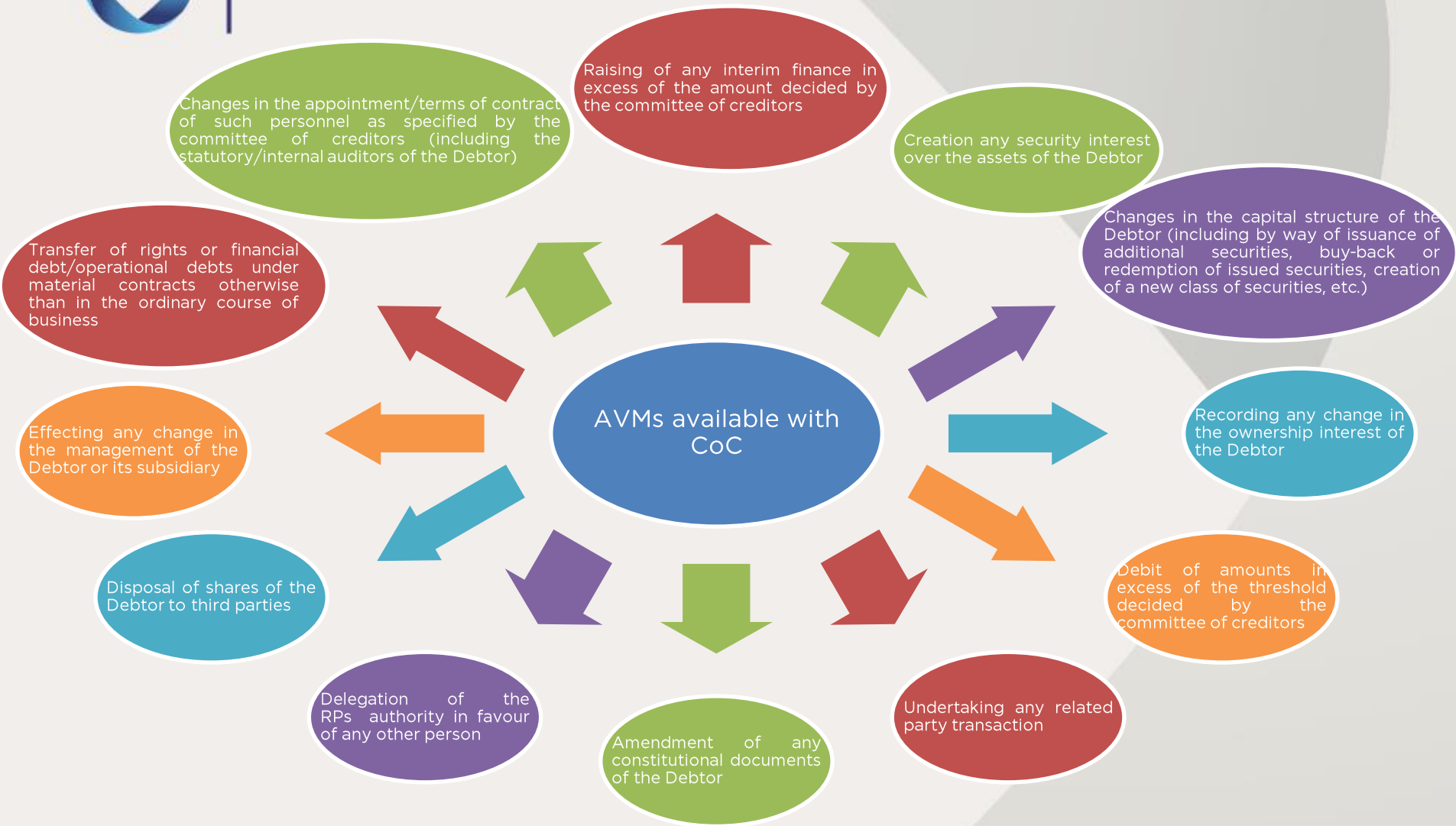


Duties of the Interim Resolution Professional / Resolution Professional

- Limited Board oversight; Manage the entire CIR process
- Collect all claim information and set claim process and timeline
- Prepare IM which will form the basis of the Resolution Plan
- Manage Resolution Plan process (Code allows multiple Resolution Applicants)
- Constitute CoC
- To protect and preserve the value of the property of the corporate debtor and manage the operations as a going concern



Committee of Creditors in charge



Food for thought: Is the CoC/IP also subject to the liabilities that the board of directors would ordinarily be subject to?



Other aspects of being an Insolvency Professional

- Only those who have appeared and cleared the Limited Insolvency Examination or National Insolvency Examination are eligible to work as Insolvency Professionals (IPs). The IBBI is yet to begin conducting the National Insolvency Examination.
- The IP needs to have a broad and overall approach and has to take into consideration the interests of all the stakeholders involved, and cannot limit himself to the interest of financial stakeholders.
- Management of the business of the company including all administrative co-ordination will form an integral part of his role since the board of directors of the company is defunct during the moratorium period.
- The IP may have to negotiate terms of engagement with suppliers, financial partners, employees and workmen.

Such individuals do not have the management bandwidth or wherewithal to run a company, IPs may commence hiring professional sub-agents, including retired industry professionals, who have experience in the relevant sector. To conclude, the profession of insolvency professionals will evolve over the coming years and is expected to be at par with developed jurisdictions such as US and UK.



Remuneration and costs

- An insolvency professional must provide services for remuneration which is charged in a transparent manner, is a **reasonable** reflection of the work necessarily and properly undertaken, and is not inconsistent with the applicable regulations.
- An insolvency professional shall **not accept any fees or charges other than those which are disclosed** to and approved by the persons fixing his remuneration.
- An insolvency professional shall disclose all costs towards the insolvency resolution process costs, liquidation costs, or costs of the bankruptcy process, as applicable, to all relevant stakeholders, and must endeavour to ensure that such costs are not unreasonable. **Thus, the fees of the IRP/ RP appointed for the particular matter shall receive priority in the liquidation waterfall which prioritizes the insolvency resolution process costs and such other costs over all other claims.**



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Liquidation



Initiation of liquidation

Circumstances under which liquidation of a company is initiated:

- If the NCLT does not receive a resolution plan before expiry of the insolvency resolution process period (i.e. 180 days/ 180 + 90 days)
- If the NCLT rejects the resolution plan submitted to it on account of reasons such as contravention of applicable law, non-conformity with requirements specified by the board, if the plan does not provide for:
 - (a) requisite repayment of the debts of operational creditors
 - (b) for meeting the insolvency process costs
 - (c) management of the corporate debtor

The insolvency professional acting as the resolution professional shall, upon commencement of liquidation be appointed as the liquidator for the process, unless replaced by the NCLT.



Roles and responsibilities of Liquidator

- To receive, collect and verify claims of all the creditors
- To take into custody / control and evaluate all the assets, property, effects and actionable claims of the corporate debtor - protect and preserve the assets and properties.
- Form and hold liquidation estate as fiduciary of the benefits of the creditors
- Carry on business for beneficial liquidation as necessary
- Sell movable and immovable properties by auction/ private contract
- Obtain professional assistance
- To institute or defend suit
- Investigate financial affairs of corporate debtor for undervalued/ preferential transactions
- Apply to NCLT for orders and directions as may be required
- Prepare preliminary report, assets memorandum, sale report etc
- Maintain relevant records
- Realise and distribute



The beginning of a new profession: Strict quality check

- Given that running a company is a huge responsibility, which further increases if the company is big in size, IPs replacing promoters need to have **certain minimum experience** to be able to understand the complexities of businesses and run the company.
- **Concerns have been raised** that Insolvency Professionals (IPs) are not equipped to run any company. In one specific case, a debtor said it had lost an order valued Rs 1.30 crore due to negligence of the concerned IP.
- Reports indicate that **IBBI will form a team to investigate** whether service providers, including IPs, take adequate internal-control measures, procedures and safeguards in performing their duty, with a 10-day prior notice.
- In case of negligence, they may face **disciplinary action**.



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Questions



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