

# **Global Professional opportunities under insolvency Regime - Pre-Packaged IRP under the IBC- A boon for Creditors of MSMEs**

By

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The Insolvency and Bankruptcy Code 2016 is comprehensive legislation for all types of entities – for insolvency and bankruptcy including voluntary liquidation and voluntary bankruptcy. It is one of the finest, simplest legislation.

Once we start work in India we can look at whole globe for practice in this area. To become insolvency professional we need 10 years membership as CA but to practice in all other areas including filing applications in NCLT and NCLAT we can do from first

day of our membership. Have a look at this amazing area which person having finance expertise can do wonders and benefit all stakeholders

In insolvency/bankruptcy proceedings, a well designed legal, institutional and regulatory framework that balances right of debtors and creditors is of utmost importance to facilitate the extension of credit and enable economic development. This in turn have developed numerous professional opportunities for those who are well versed with financial aspects, compliance mandates etc.

A thorough list of such professionals opportunities present under IBC is given below:

1. Insolvency professionals in the category of
  - a. Interim Resolution Professional : Appointed by Applicant/NCLT
  - b. Resolution Professional : Appointed by Committee of Creditors
  - c. Liquidator
  - d. Bankruptcy Trustee
2. Advisory to secured creditor
3. Negotiator
4. Assistance to Insolvency professionals by acting as legal counsel or professional advisor
5. Mediator
6. Conciliator
7. Arbitrator
8. Administrator
9. Recovery Officer
10. Practice before NCLT and NCLAT
11. Drafting of documents and application, notices etc
12. Assistance in process of liquidation
13. MSME Advisory
14. Risk analyst- addressing key areas of concern

15. Forensic audit
16. Mergers and amalgamations
17. Real estate transactions & IBC
18. Expert in finding buyer for assets in liquidation
19. Expert in making resolution plan

An ideal legislature in this respect should provide for the restructuring and preservation of distressed yet viable businesses, and at same time provide for the orderly resolution of distressed and non-viable businesses. The law should also ensure the transparency, efficiency and most essentially timeliness of resolution mechanism, as these have a direct impact on the allocation of credit risk and risk management in the financial sector, and consequently also influence access to credit and its cost. A good legal mechanism backed by efficient infrastructural mechanism offers predictability and enhances investor's confidence in credit recovery system. On 28<sup>th</sup> May, 2016 an historical Act was enacted when President of India gave his assent to the Insolvency and Bankruptcy Code, 2016 (the Code), which provided a comprehensive legal and institutional machinery to deal with increasing defaults in repayments of debts, in a way where interests of all the stakeholders are balanced.

The Insolvency and bankruptcy provision prior to the enactment of the code could be find in the Presidency Towns Insolvency Act, 1909, and the Provincial Insolvency Act, 1920. These statutes still continue to apply. Further the Corporate debtor facing insolvency will face two process:

1. Insolvency resolution and
2. Liquidation

In an Attempt of insolvency resolution fails the liquidation will take place. However, the Insolvency under code be triggered on default amount of 1 Lakh and the government is empowered to specify any other limit not more than one crore (s. 4). In view of power under s. 4 from 24<sup>th</sup> march 2020 minimum default amount would be one crore- ministry

of corporate affairs vide notification No. 30/9/2020-Insolvency. The Insolvency resolution starts with admission order by Adjudicating Authority under Ss. 7, 9 or 10 as the case may be.

- Section 7: Financial Creditor that means-Any person to whom a financial debt is owed and includes a person to whom such debt is legally assigned to or transferred
- Section 9: Operational Creditor that means- A person to whom an operational debt is owed and includes any person to whom such debt is legally assigned or transferred
- Section 10: Corporate Debtor that means- A corporate applicant who owes a debt to any person
- Section 54A – Pre Packaged IRP for MSME

The Code envisaged the following:

- *The Code will facilitate the assessment of viability of the enterprise at a very early stage so as to minimize the erosion of the value of business.*
- *The Code will enable symmetry of information between creditors and debtors by ensuring that access to this information is made available to all creditors to the enterprise, either directly through establishment of Information Utilities or through the insolvency professional.*

In insolvency/bankruptcy proceedings, a well designed legal, institutional and regulatory framework that balances the rights of debtors and creditors, is of utmost importance, to facilitate the extension of credit and enable economic development. An ideal legislation in this respect should provide for the restructuring and preservation of distressed yet viable businesses, and at same time provide for, the orderly resolution of distressed and non-viable businesses. The law should also ensure the transparency, efficiency and most essentially, timeliness of the resolution mechanism, as these have a direct impact, on the allocation of credit risk and risk management in the financial sector, and consequently also influence access to credit and its cost. A good legal mechanism backed by efficient infrastructural mechanism, offers predictability and enhances the

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- *The Code will ensure a time-bound process to better preserve economic value of the enterprise.*
- *The Code will ensure a collective process where all stakeholders participate to collectively assess viability.*
- *The Code will respect the rights of all types of creditors*
- *The Code ensures that, the outcome of bankruptcy must be binding*
- *The Code will ensure clarity of priority, and that the rights of all stakeholders are upheld in resolving bankruptcy.*

### **Journey of the Code, after it's Enactment**

The Code, being an economic law has evolved continuously through experimentation. Ever since implementation of the Code, the Insolvency Law Committee has been prompt in implementing changes, to make course correction/s, through amendment/s. The Code has so far witnessed five legislative interventions, four of which was by way of Ordinances, as the Government was keen to continuously improve resolution framework, without waiting for parliamentary sessions. Each of these five amendments has strengthened the processes, keeping in view the emerging market realities and so as to preserve the spirit of the Code. The following major change have been implemented in the Code till date:

- The fact that very first resolution plan approved under the Code, yielded a haircut of 94% for the financial creditor/s (FC), while promoters indirectly retained the control of the company, made it appear that unscrupulous persons have been rewarded, at the expense of creditors, which was not acceptable and was against the spirit of the Code. Hence a prompt course correction was made through insertion of Section 29A by an Ordinance (The Insolvency and Bankruptcy Code (Amendment) Ordinance, 2017) that prohibited persons with specified ineligibilities from submitting resolution plans, in a corporate insolvency resolution process (CIRP), to ensure sustained resolution of stress.
- Soon after, another amendment was made to by the way of the Insolvency and Bankruptcy Code (Amendment Ordinance), 2018, to enable retail consumers in the real estate industry such as homebuyers, to have the right to initiate insolvency against real estate developers and the right to be represented in the committee of creditors (CoC), bringing them at par with banks and other financial creditors, in real estate projects. To encourage a speedy resolution, the Ordinance also relaxed voting threshold, for certain decisions taken by the CoC. Besides, promoters of MSMEs, who are not willful defaulters, were exempted from the rigors of Section 29A.
- Thereafter, the Insolvency and Bankruptcy Code (Amendment) Act, 2019 was enacted, to primarily mandate that the insolvency resolution process of a corporate debtor, shall not extend beyond three hundred and thirty days from the insolvency commencement date, which will include the time taken in legal proceedings, in order to prevent undue delays in the completion of the CIRP.
- Soon after, another amendment by the way of the Insolvency and Bankruptcy Code (Amendment) Ordinance, 2019 to prevent misuse of the Code, by imposing an additional requirement, for certain classes of financial creditors, for filing an application. These classes include real estate allottees and security or deposit holders, represented by a trustee or agent. The application by these creditors should be filed jointly, by at least 100 such creditors or 10% of their total number, whichever is less. The Ordinance also mandated that the supplies of goods and services, considered critical by the resolution professional, could not be discontinued, during the moratorium period.

- In between on November 15, 2019, Ministry of Corporate Affairs by Notification No. S.O. 4126(E) notified the provision under the Code, relating to Personal Guarantors to Corporate Debtors.
- By way of a notification dated 24 March 2020, recognizing the need for protecting smaller businesses, the Government of India, had also raised the minimum threshold, for initiating corporate insolvency resolution processes (CIRP) to Rs. 1 crore from the earlier Rs. 1 lakh. This was followed by 1 year suspension, on initiation of any new insolvency proceedings, for defaults occurring on or after 25<sup>th</sup> March 2020, irrespective of the size of default.
- The most important amendment and talked-after change of the date, came on 4<sup>th</sup> April, 2021 by the way of the Insolvency and Bankruptcy Code (Amendment) Ordinance, 2021, which inter-alia added Part III-A to the Code, introducing a framework for pre-packaged insolvency resolution (Pre-pack) for corporate debtors qualifying as micro, small and medium enterprises (MSMEs). A Corrigendum to the Ordinance was also pronounced on the following day. The Ordinance finally became an Act on 11<sup>th</sup> August, 2021.

### **Understanding The Pre-Pack Insolvency Resolution Process**

As the nomenclature suggests, pre-packs are restructuring plans, which are agreed to, by the debtor and its creditors, prior to the insolvency filing, and then sanctioned by the court, on an expedited basis. It is a type of restructuring in which creditors and debtors collaborate on an informal agreement, before submitting it for approval. MSMEs companies are mostly run by small promoters, making it impossible to re-surrect them, if the administration is removed under the standard CIRP. The Pre-Packs encourages current promoters to participate, with the board maintaining power and the debtor presenting the base resolution package, which will then be put to the bidding process, through the Swiss challenge. As a result, Pre-pack is expected to assist corporate debtors, in reaching an agreement with creditors and addressing the whole liabilities side of the company. It is being viewed as a time-bound and budget friendly, insolvency resolution that will trigger minimal market uncertainty, maximize value, protect jobs, and reduce the workload, on the National Company Law Tribunal (NCLT).

In wake of economic lockdowns in and around the country, the Government of India contemplated, possible rise in corporate and individual insolvencies, as was also listed in reports

of The World Bank and The International Monetary Fund. The hardest hit were expected to be the MSMEs. Formal Corporate Insolvency Resolution Process (CIRP) as prescribed under Insolvency and Bankruptcy Code, 2016 (the Code), requires a Resolution Applicant to rescue a failing company, through a resolution plan. At time when most companies, industries and economies are reeling under stress, the likelihood of finding a Resolution Applicant, to rescue a failing company, is remote. Thus it was felt that if all failing companies, were to undergo insolvency proceeding, most of them may end up with liquidation, for want of saviors to rescue them, leading to a pre-mature death and distress sale of assets, realising abysmally little for creditors, which is against the spirit of the Code. Consequently, the Code made another course correction, to suspend filing of applications, for initiation of CIRP, in respect of defaults arising during lockdown period, for a year commencing on 25th March, 2020. This insulated a company, which did not have a default as on 25th March, 2020, but commits a default during the lockdown period, from being pushed into an insolvency proceeding. However, this suspension took away an effective option for resolution, in respect of debt arising during this period. Therefore, the Government constituted a sub-committee of Insolvency Law Committee (ILC) vide order dated 24.6.2020 to prepare a detailed scheme, for implementing pre-pack and pre-arranged insolvency resolution process. The sub-committee designed a pre-pack framework within the basic structure of the Insolvency and Bankruptcy Code, 2016, and submitted a detailed report in October, 2020. With no absolute certainty of end of this pandemic and revival of economy as whole, there is no denying the fact, that the availability of Resolution Applicant will be a constraint for quite some time. Moreover, CIRP may not yield a desirable outcome. Therefore, sub-committee felt it necessary to provide an effective mechanism, to enable the stakeholders to find a resolution. Enrichment with the experience, from implementation and stabilization of the Insolvency and Bankruptcy Code, 2016, evolution of the ecosystem and growing jurisprudence, had prepared ground to look at new initiatives, to further improve the effectiveness of the Code. There is no denying the fact the out-of-court settlements are speedier and if, with such resolutions, regulators extend the same regulatory exemptions, as available to settlements made under the Code framework, the whole resolution process, becomes over-all immensely effective. Finally, through an ordinance dated April 4, 2021, the government established a Pre-Packaged Insolvency Resolution Process ("Pre-Packs"). The Ordinance amended the Code and added a new Chapter IIIA to the Code.



## **The United Nations Commission on International Trade Law (UNCITRAL); on Pre-Packs**

UNCITRAL uses the term '*expedited re-organization proceedings*' for pre-packs, as these proceedings, follow the procedure of re-organization, but on an expedited basis, combining voluntary re-structuring negotiations, where a plan is negotiated and agreed to by the majority of affected creditors, with re-organization proceedings commenced, under the insolvency law to obtain court confirmation of the plan, in order to bind dissenting creditors. The IMF observes the following two variants of pre-packs:

- pre-packaged plans, where both the negotiation and voting for the plan, take place, prior to commencement of the rehabilitation procedure and court approval is sought immediately upon commencement, and
- pre-negotiated plans, where the plan is negotiated prior to commencement but formal voting takes place, once the proceedings have commenced. In a pre-pack, a troubled company and its creditors, negotiate the terms of an insolvency resolution plan, prior to the commencement of the formal insolvency process, which allows formal process, to be implemented at maximum speed. The most prevalent form of pre-pack process envisages a resolution plan, which is negotiated and finalized, between the creditors and the debtor, before the commencement of statutory proceedings, and is sanctioned under the statute.

### **Relevant Statutes**

By IBC Amendment Act, 2021, the following Sections have been added to the Code:

- In Section 5 of the Code clauses 2A, 23A, 23B, 23C and 23D have been inserted, to prescribe necessary definitions and clauses 5(b), 11, 15, 19, 25 & 27 have been amended.
- Section 11A has been inserted to set priority of disposal of application, in case where application for initiation of insolvency proceeding, have been filled under other sections of the Code, together with application for initiation of Pre-Packs.
- Chapter III-A, comprising of 16 sections 54A to 54P has been inserted, to provide detailed mechanism under the Code
- Section 67A has been inserted, to prescribe certain penalties, for fraudulent management of corporate debtor, during Pre-Pack Process.

- Section 77A has been inserted to prescribe punishment, for offences related to Pre-Packs.
- Besides, sections 4, 61, 65, 77, 208, 239, 240 and 240A have been amended to enable implementation of new Mechanism.

Rules and regulations are arms and wings of any legislation. Therefore, Ministry of Corporate Affairs, by notification no. G.S.R. 256(E) dated April 9, 2021 notified Insolvency and Bankruptcy (pre-packaged insolvency resolution process) Rules, 2021 consisting of 4 Rules and a form for filling of application to the Adjudicating Authority. IBBI too vide Notification No. IBBI/2021-22/GN/REG071, prescribed Insolvency and Bankruptcy Board of India (Pre-Packaged Insolvency Resolution Process) Regulations, 2021. It comprises of 51 Regulations divided into 10 Chapters and a Schedule comprising of 14 forms, numbered P1 to P14.

Also, Ministry of Corporate Affairs (MCA) vide. Notification No. S.O. 1543(E), notified ten lakh rupees, as the minimum amount of default, for the matters relating to the pre-packs.

## **Initiation of Pre-packs**

### ***Eligibility for Pre-pack***

The Central Government issued the Notification being S.O 1543 (E) dated 9 April 2021 specifying Rs 10,00,000 as requirements of minimum default for an MSME corporate debtor, to initiate a pre-pack. The Central Government can by notification alter this minimum default value for starting the pre-pack process, for defaults up-to Rs 1,00,00,000. The ordinance for Pre-pack for MSMEs will help the sector in many ways.

The process of Pre-pack can be initiated by any corporate debtor classified as MSME under Section 7(1) of the MSME Development Act, 2006. It is pertinent to note that the criteria for clarification of an enterprise as an MSME has undergone a change which is applicable w.e.f July 1, 2020 and now the classification criteria are based on investment as well as annual turnover. The revised criteria are as follows:

|   |
|---|
| Revised Classification applicable w.e.f 1st July 2020                             |
| Composite Criteria: Investment in Plant & Machinery/equipment and Annual Turnover |

| Classification  | Micro  | Small  | Medium  |
|---|--|--|---|
| <b>Manufacturing Enterprises and Enterprises rendering Services</b> | Investment in Plant and Machinery or Equipment:<br>Not more than Rs.1 crore and Annual Turnover; not more than Rs. 5 crore | Investment in Plant and Machinery or Equipment:<br>Not more than Rs.10 crore and Annual Turnover; not more than Rs. 50 crore | Investment in Plant and Machinery or Equipment:<br>Not more than Rs.50 crore and Annual Turnover; not more than Rs. 250 crore |

### ***Pre-Condition for Initiation of Pre-Pack***

- a. Corporate Debtor is an MSME mandatorily
- b. Default meets the minimum threshold of Rs.10 lakhs
- c. Such corporate debtor, should not have undergone a pre-pack or CIRP process within three years of the initiation date;
- d. Such corporate debtor, should not be undergoing a CIRP;
- e. Such corporate debtor, against whom there is no order of liquidation under Section 33 of the Code;
- f. Subject to Section 240A of the code, corporate debtor should be eligible, to submit a resolution plan, under Section 29A of this Code.
- g. The unrelated financial creditors, representing not less than 10% of value of the total financial debt of such creditors may propose names of insolvency professionals and those representing not less than 66% in value of the financial debt, have accepted the proposal of such Insolvency Professional, being appointed as Resolution Professional for conducting the Pre-pack of such a corporate debtor.
- h. There is a declaration, made by the majority of the directors or partners of the corporate debtor, stating (as specified) inter alia:
  - i. The corporate debtor, within a period of 90 days, will file for initiating the Pre-Pack;

- ii. The Pre-pack will not be initiated to defraud any person;
- iii. The approved resolution professional's name;
- g. The members of the corporate debtor, are required to pass a special resolution or at least three-fourth of the total number of partners of the corporate debtor, as the case may be, are required to pass a resolution, approving the filing of the Application for Pre-pack
- h. The corporate debtor shall furnish the financial creditors with a:
  - A declaration as specified in Form P6 specified in the Insolvency and Bankruptcy Board of India (Pre-packaged Insolvency Resolution Process) Regulations, 2021 (Regulations).
  - special resolution as specified in Section 54A(2)(g),
  - a base resolution plan as specified under Section 54K,
  - any other documents, as specified in order, to obtain approval from its financial creditors (as per the specified form) for filing an application for initiating Pre-pack.

From the above the role of Corporate Debtor, Financial Creditor and resolution professional can be summarized as follows:

### ***Corporate Debtor's Acts***

- Corporate Debtor (CD) members need to pass special resolution or at least three-fourth of the total Corporate Debtor partners (i.e. in case of LLP), required to pass a resolution, approving Application filing.
- Corporate Debtor will then immediately prepare a “Base Resolution Plan” (BRP) for insolvency resolution of Corporate Debtor., which is required to comply with provisions of Sections 30(1) and 30(2) of the Code.
- Majority directors/partners of Corporate Debtor, should also make a declaration in Form P6, giving the following matter, that:
  - a. Corporate Debtor shall file Application, within a period of maximum 90 days
  - b. Resolution professional, proposed to be appointed & approved
  - c. Declaration that Pre-pack is not being started, with a plan to defraud anyone;
  - d. Nomination has been completed.

The application to Adjudicating Authority for initiation of pre-pack process, is to be made in Form 1 as specified in Insolvency and Bankruptcy (prepackaged insolvency resolution process) Rules, 2021 along with a fee of Rs 15,000. In case, electronic facility is not available for filing such application, i.e. the application and the accompanying documents may be filed in physical form, and wherever the accompanying documents are bulky, the same may be submitted in scanned portable document format, in a data storage device, such as a compact disc or a USB flash drive, acceptable to the Adjudicating Authority. A copy of the application must also be provided to the IBBI, by registered post or speed post or by hand or by electronic means, before filing it with the Adjudicating Authority.

### ***Unrelated Financial Creditor Approvals***

- Pre-pack Scheme requires Corporate Debtor to convene a meeting of its financial creditors, who are not its related parties, by serving a 5 day notice, before the date of the meeting, unless a shorter time is agreed to by financial creditors. Following approvals needed in the said meeting by the Corporate Debtor:
  - The unrelated financial creditors, equal to not less than 66% in value of the financial debt due, should approve filing of the Application.
  - Before such approval, Corporate Debtor needs to share with the unrelated financial creditors: Resolution; Base Resolution Plan & the Declaration;
  - Such Unrelated financial creditors, equal to not less than 10% in value of total financial debt of such creditors, should also propose, name of insolvency professional to be appointed as the resolution professional, for taking up the Pre-pack process.
  - Such Resolution Professional also has to be approved, by unrelated financial creditors, with a weighted voting share of minimum 66% (Nomination Process).

Where Corporate Debtor has no financial debt, such Corporate Debtor is required obtain the above approvals from unrelated operational creditors, in the same form and manner as required to be obtained by Unrelated financial creditors.

### ***Report by Resolution Professional***

After the Nomination Process, the Resolution Professional who has been approved, is required to prepare a report, confirming whether the conditions precedent, as stated below are fulfilled & the Base Resolution Plan is in accordance with provisions of Sections 30(1) & 30(2) of the Code. Before we move ahead it is pertinent to understand these Sections.

Section 30(1) requires the Resolution Applicant to submit an affidavit pursuant, confirming its eligibility under section 29A of the Code to submit resolution plan. Section 30(2) requires Resolution Professional to examine the resolution plan submitted to him to ensure that such resolution plan:

- Has provided for the priority of the payment of insolvency resolution process costs, to the payment of other debts of the corporate debtor;
- Has provided for the payment of debts of the operational creditor, not less than, the higher of:
  - Amount to be paid, to such creditor in the event of liquidation; or
  - Amount to be paid, to such creditor if the amount is to be distributed, as per the order of priority under section 53(1);
- Has provided for the payment of debts of the financial creditor (not voting in favour of the resolution plan), not less than the amount paid to such creditors, in the event of liquidation of the corporate debtor, as per section 53(1).;
- Provides for the management of the affairs of the corporate debtor, after approval of the plan;
- Provides for the implementation and supervision of the resolution plan;
- Does not contravene, any of the provisions of the law, for the time being in force; and
- Confirms to such other requirements, as specified by the board.

A formal application for starting a pre-pack has to be made before Adjudicating Authority i.e. National Company Law Tribunal (NCLT) along-with:

- Declaration;
- Resolution;
- Approval;
- the name and written consent of the proposed RP;
- Report;
- Declaration regarding any avoidance transactions, under Chapter III of the Code or fraudulent or wrongful trading under Chapter VI of the Code; and

- Information relating to books of account of the corporate debtor;
- Audited financial statements of corporate debtor, for last 2 (two) financial years;
- Provisional financial statements, for the current financial year, made up to the date of Declaration;
- Written consent of the insolvency professional, proposed to be appointed as authorized representative of a class of creditors (if applicable).

Application has to be admitted, by the Adjudicating Authority within 14 days, where the same is complete & thus above conditions are satisfied. Such date of admission is considered as pre-packaged insolvency commencement date [ICD] of the corporate debtor.

If the case be so, Adjudicating Authority is required to give notice to the applicant to rectify the defect in the Application within 7 (seven) days from the date of receipt of such notice by applicant, if any.

### ***Moratorium and Appointment of Resolution Professional***

Upon admission of application, a Moratorium is declared by the Adjudicating Authority, under which the restricted actions, under Section 14(1) & 14(3) of the Code are prohibited. It is important to note here that the Pre-pack Framework excludes the applicability of Section 14(2) of the Code which lays down that even during moratorium, the supply of essential goods or services to the corporate debtor shall not be suspended.

With the above, the Adjudicating Authority shall, subject to certain conditions, appoint the resolution professional based on the Nomination Process.

### ***Public Announcement***

The Adjudicating Authority, causes a public announcement to be made, of initiation of the Pre-pack process, by the resolution professional, within 2 days of appointment of Resolution Professional, providing information, like name and basic details of the corporate debtor; the date of commencement of Pre-pack Insolvency Resolution Process; and name, address and e-mail address of the Resolution Professional. The format for such Public Announcement has been specified in Form P9.

Such Public Announcement is also required to be, sent to every creditor of the corporate

debtor; sent to the information utilities; and published on the website, if any, of the corporate debtor and the Insolvency and Bankruptcy Board of India (IBBI).

The pre-pack should be completed within a period of 120 days, and the resolution professional should submit the approved resolution plan (by the CoC) to the Adjudicating Authority. If such time period elapses the resolution professional shall file an application for the termination of pre-pack.

### ***Preparation of List of Claims***

Contrary to the normal CIRP, the CD in a Pre-pack has to prepare a preliminary list of various creditors, along with details of such creditors, their security interest & guarantees, if any, and submit it to the Resolution Professional within a period of 2 (two) days from ICD.

Based on the records of the corporate debtor and any other related & relevant material on record, Resolution Professional must confirm such details received and maintain a list of claims.

Further Resolution Professional is required to inform every creditor regarding its claims, as per list received from the corporate debtor and as confirmed by the Resolution Professional thereafter, and seek objections, if any.

### ***Formation of Committee of Creditors***

The Resolution Professional shall within a period of 7 days of the commencement of the pre-packaged insolvency period, constitute a Committee of Creditors ("CoC") based on the list of claims submitted by the corporate debtor and confirmed by the Resolution Professional. The composition of the CoC during a Pre-pack shall be on the same footing or in a similar way to its composition during a normal CIRP, if the corporate debtor has Unrelated Financial Creditors. The committee's first meeting is to be within seven days of its constitution. Provisions laid down in Section 21 of the Code shall *mutatis mutandis* apply to the pre-packs. Section 21(2) provides that the CoC shall comprise all financial creditors. However, the proviso to Section 21(2) states, inter alia, that a financial creditor shall not have the right of representation, participation or voting in a CoC meeting if it is a related party of the corporate debtor. However, where the



Corporate Debtor has no financial debt or all financial creditors are related, the CoC shall consist of unrelated operational creditors as follows:

- Ten largest operational creditors by value, (if the number of operational creditors is less than ten, the CoC shall include all such operational creditors) ;
- One representative elected by all workmen other than those workmen included in Largest operational creditors; and
- One representative elected by all employees other than those employees included in largest operational creditors.

### ***Information Memorandum***

The Corporate Debtor is required to prepare a preliminary information memorandum containing information relevant for formulating a resolution plan and submit it to the Resolution Professional within two days from ICD.

- Thereafter Resolution Professional has to finalize such information memorandum and submit to members of CoC within fourteen days of ICD after receiving an undertaking from the members of the CoC that such member shall maintain confidentiality of the information and shall not use such information to cause an undue gain or undue loss to itself or any other person.

### ***Management of Corporate Debtor in Pre-pack***

A vital change from the normal CIRP set-up and with an intention to not disrupt regular business operations and not adversely affect the business reputation in any manner, the Pre-pack Framework lays down that management of the affairs of the Corporate Debtor shall continue with its board of directors/partners, i.e. the earlier Management itself, subject to the following conditions:

- The board/partners, of the Corporate Debtor shall make the best & all possible efforts to preserve & protect value of the various properties of the Corporate Debtor and manage it as a going concern;
- All interest groups, like the promoters, shareholders/partners, various employees etc of

the corporate debtor shall continue to exercise their statutory/ contractual rights and discharge their various duties & obligations vis-à-vis the corporate debtor.

Thus while the management of daily business of the Corporate Debtor still remains with the earlier Management, as before, in principle, the Resolution Professional is duty bound to:

- (a) Monitor regularly, such management of the Corporate Debtor by the earlier Management itself
- (b) Promptly Inform the CoC in case such earlier Management fails to carry out, breaches or violates any of its obligations as per the Pre-pack Framework.

***Vesting management of corporate debtor with resolution professional***

Although the Pre-pack Framework intends minimum & negligible business disruptions, as the existing management continues to run the business during the Pre-pack process; (unlike in a CIRP), it still has certain checks and balances, as said below.

If at any stage of the Pre-pack, CoC by minimum 66% of its vote, can resolve to transfer & vest management of the Corporate Debtor with the Resolution Professional. In such case, RP needs to make an application to the adjudicating authority for approving such replacement. Such authority can pass an order, accepting such request & granting such relief, if it is satisfied:

- a. That there has been gross mis-management of the affairs of the Corporate Debtor, which are prejudicial to its interests and/or
- b. All or any affairs of the Corporate Debtor have been conducted in a fraudulent manner, which is prejudicial its interests

It should be noted that while the daily management and business affairs of the Corporate Debtor remains retained with the earlier Management (unless a Replacement takes place), the Ordinance says that provisions of Section 28 of the Code, shall apply equally to a Pre-pack Insolvency Resolution Process. Therefore such earlier Management still needs to take prior approval of CoC before undertaking any action/s laid down, in Section 28 of the Code

Further, the Pre-pack Scheme also lays down that earlier Management cannot undertake transaction/s above a threshold limit, as decided by CoC. Thus the Pre-pack set-up, in a way, sets out a debtor in possession of the business running, with a creditor in control mode of resolution process.

### ***Approval of resolution plan***

The base resolution plan as submitted to the financial creditors, before the initiation of Pre-pack should be submitted to the Resolution Professional, by the corporate debtor, as a base resolution plan, within 2 days of the pre-packaged insolvency commencement date.

The CoC may consider and approve the Base Resolution Plan, if the Base Resolution Plan provides for full discharge of the debts owed to operational creditors. However, the Resolution Professional is required to invite prospective resolution applicants, within 21 days from the date of ICD, to submit a resolution plan for the corporate debtor, to compete with the Base Resolution Plan, in case the CoC is not satisfied with the Base Resolution Plan or if the Base Resolution Plan impairs any claims of operational creditors.

The Resolution Professional, after approval from the CoC, shall determine the criteria required to be satisfied by prospective resolution applicants and and/or their resolution plans, while submitting the resolution plans. These criteria must be set, having regard to the complexity and scale of operations of the business of the corporate debtor and such other conditions, as may be specified by IBBI. The CoC shall also determine the matrix to evaluate the resolution plans submitted by the prospective resolution applicants. The CoC may also consider providing the corporate debtor, an opportunity to revise the Base Resolution Plan, before inviting prospective resolution applicants.

The Resolution Plans must provide the following:

- a) an affidavit that the resolution applicant is eligible to submit a resolution plan under the Code;
- b) a statement giving details, if the resolution applicant or any of its related party/ies has failed to implement or contribute, to the failure of implementation of any resolution plan, approved by the Adjudicating Authority, at any time in the past;
- c) an undertaking that every information and record provided in connection with or in the resolution plan, is true and correct and discovery of false information and record, at any time, will render the resolution applicant ineligible to participate in any resolution process under the Code;
- d) the term of the plan and its implementation schedule;

- e) the management and control of the business of the corporate debtor, during its term;
- f) a statement, as to how it has dealt with the interests of all stakeholders of the corporate debtor; and
- g) adequate means, for supervising its implementation.

The Resolution Plan must also demonstrate that:

- (a) it addresses the cause of default;
- (b) it is feasible and viable;
- (c) it has provisions for its effective implementation;
- (d) it has provisions for approvals required and the timeline, for the same;
- (e) the resolution applicant has the capability, to implement the Resolution Plan;
- (f) the amount payable under the Resolution Plan, to the operational creditors, shall be paid in priority, over financial creditors; and
- (g) the amount payable under the Resolution Plan, to the financial creditors, who have a right to vote and did not vote in favour of the Successful Resolution Plan, shall be paid in priority over financial creditors, who voted in favour of the Successful Resolution Plan.

In the event, where no Resolution Plans are received, which are in accordance with the provisions of the Code and the Pre-pack Regulations, the CoC shall re-consider the Base Resolution Plan for approval. However, if the Compliant Resolution Plans are received, then the CoC shall evaluate such Resolution Plans presented by the Resolution Professional and select a Resolution Plan from amongst them. If this plan is significantly better, than the Base Resolution Plan, then it may be approved by the CoC, with a voting share of 66%.

Here the term “significantly better” in relation to a resolution plan, would mean that the score of the resolution plan, is higher than that of another resolution plan, by a certain number or percentage, as approved by the CoC, and disclosed in the invitation for resolution plans. However, if such Plan is not selected for approval, then the Resolution Professional shall disclose the score allotted to it and the Base Resolution Plan based on the Evaluation Matrix to the concerned bidder and the corporate debtor respectively and invite them to improve the Resolution Plan and the Base Resolution Plan respectively within 48 hours. The Plan, having higher score after improvement/ revision, shall be considered by the CoC for approval, after considering the feasibility and viability of the Plans and the manner of distribution proposed,

taking into account the order of priority amongst the claimants, as per waterfall mechanism set out in Section 53(1) of the Code.

### ***Approval of Resolution Plan***

A Plan once approved by the CoC is submitted to the Adjudicating Authority. The Adjudicating Authority shall approve the Successful Plan provided:

- (a) the Successful Plan, satisfies the conditions stipulated under Section 30(2) of the Code; and
- (b) the Successful Plan, has provisions for effective implementation.

On such approval, the plan becomes binding on the corporate debtor and its employees, members, creditors, government agencies, guarantors and other stakeholders involved in the Plan. The moratorium will cease to exist and the resolution professional shall forward all records relating to the conduct of the pre- pack process and the resolution plan, to the IBBI to be recorded on its database.

Besides, the successful resolution applicant should also obtain the necessary approval required under any law for the time being in force, within a period of one year from the date of approval of the resolution plan, by the Adjudicating Authority or within such period as provided for in such law, whichever is later. However, that where the resolution plan contains a provision for combination, the resolution applicant shall obtain the approval of the Competition Commission of India under that Act, prior to the approval of such resolution plan by the CoC.

### ***Termination of Pre-pack***

A Pre-pack may be terminated upon the occurrence of the following events:

- A Plan is taken up for consideration by the CoC, after revised plans have been submitted by the corporate debtor, as well as prospective resolution applicant, but none of it is approved by the CoC;
- the CoC does not approve a Plan, before the expiry of 90 days from ICD; and
- the CoC decides, by a minimum voting share of 66%, any time between ICD and approval of a Plan, to terminate the Pre-pack.

If the Pre-pack of a corporate debtor, has been terminated on account of first two grounds as mentioned above and the Adjudicating Authority may pass an order, not only terminating the Pre-pack, but also liquidating the said corporate debtor.

### ***Initiation of the CIRP***

At any time during the Pre-pack process but before the approval of a Plan by the CoC, the CoC by exercise of minimum 66% of the voting rights may resolve, to initiate the CIRP against the corporate debtor. In such case, the Adjudicating Authority will pass an order commencing CIRP of the said corporate debtor and such order shall be deemed to be an order of admission under Section 7 of the Code.

### ***Time-Limit for Completion of the Pre-pack***

There are strict timelines for the completion of the formal stage of the Pre-pack under the Code which are as follows:

- a plan is required to be approved by the CoC within a period of 90 days from the ICD, failing which the Pre-pack may be terminated.
- the entire Pre-pack process i.e., the formal process post admission of Pre-pack process, including obtaining necessary orders from the Adjudicating Authority approving the a plan or terminating the Pre-pack,

### ***Appeal against an order of Approval passed by NCLT under section 54L***

An appeal against an order approving a resolution plan under section 31 may be filed on the following grounds, namely: –

- the approved resolution plan is in contravention of the provisions of any law for the time being in force;
- there has been material irregularity in exercise of the powers by the resolution professional during the pre-pack resolution period;
- the debts owed to operational creditors of the corporate debtor have not been provided for in the resolution plan in the manner specified by the IBBI;
- the insolvency resolution process costs have not been provided for repayment in priority to all other debts; or

- the resolution plan does not comply with any other criteria specified by the IBBI.

### ***Punishment for offenses relating to Pre-pack***

According to the Section 54P part VII pertaining to Offences and Penalties under the Code would apply in the case of Pre-packs. However, the punishment under Section 77A of the Code, has been added as an extension, to the already existing section on punishment (Section 77), wherein the punishment is the same for a particular set of offenses corporate debtor and any person who knowingly and wilfully authorizes or permits the furnishing of false material or omission any material fact, knowing it to be material while

- A. providing information in the application **to** initiate pre-packaged insolvency resolution process under Section 54C or,
- B. information provided w.r.t to the list of claims and preliminary information memorandum under Section 54G of the code;

shall be punishable with imprisonment for a *term which shall not be less than three years*, but which *may extend to five years* or with fine which shall *not be less than one lakh rupees*, but which *may extend to one crore rupees*, or with both.

### ***Priorities among different mechanism of the Code***

With insertion of chapter III A, Part II of the Code that deals with Insolvency resolution and Liquidation, for the Corporate Persons has now 8 chapters and application for Insolvency Resolution, can be made under following sections:

- Section 7 Normal CIRP by Financial Creditor
- Section 9 Normal CIRP by Operational Creditor
- Section 10 Normal CIRP by Corporate Applicant
- Section 54C pre-packaged insolvency resolution process by Corporate Applicant
- Section 57 Fast track insolvency resolution process

The newly inserted Section 11A set priority, in disposal of applications under section 54C and under section 7 or section 9 or section 10. According to it,

- where an application filed for pre-pack is pending, the Adjudicating Authority shall pass an order to admit or reject such application, before considering any application filed for normal CIRP, during the pendency of such application for pre-pack, in respect of the same corporate debtor.
- Where an application for pre-pack is filed within fourteen days of filing of any application for normal CIRP, which is pending, in respect of the same corporate debtor, then the Adjudicating Authority shall, first dispose-off the application for pre-pack.
- Where an application for pre-pack is filed after fourteen days of the filing of any application for normal CIRP, in respect of the same corporate debtor, the Adjudicating Authority shall first dispose-off the application for normal CIRP.

However, the above priority rules shall not apply where an application for normal CIRP is filed and pending as on the date of the commencement of the Insolvency and Bankruptcy Code (Amendment) Act, 2021.

### ***Conclusion***

The pre-packaged insolvency resolution process recognizes the importance of hybrid insolvency process, which is simpler, affordable and cost effective. It is a boon for MSMEs and its creditors. This hybrid system will combine creditors' needs on the one side with the need to protect MSMEs' independence on the other. It will also prove instrumental in reducing litigation, which is frequently caused by defaulting promoters seeking to retain ownership of their businesses. The National Company Law Tribunal-Ahmedabad, in matter of ***GCCL Infrastructure & Projects Limited*** delivered first order admitting application filed for initiation of pre-pack insolvency resolution process. This has paved way for many more resolution in coming times. The pre-pack mechanism is effective in arriving at a quick resolution for distressed companies and we might see this mechanism being rolled out to all corporations over time as legal issues are settled through case laws.

### **Annexure: List of Forms for pre-pack**



***Prescribed in the Insolvency and Bankruptcy (Prepackaged Insolvency Resolution Process) Rules, 2021***

FORM-1: APPLICATION BY CORPORATE APPLICANT TO INITIATE PRE-PACKAGED INSOLVENCY RESOLUTION PROCESS UNDER CHAPTER III-A OF THE CODE

***Prescribed in Insolvency and Bankruptcy Board of India (Pre-packaged Insolvency Resolution Process) Regulations, 2021***

FORM P1: WRITTEN CONSENT by Insolvency Professional to Act as Resolution Professional (Under regulation 7(1))

FORM P2: LIST OF CREDITORS by Corporate Applicant (Under regulation 14)

FORM P3: APPROVAL OF TERMS OF APPOINTMENT OF RESOLUTION PROFESSIONAL by Creditors (Under regulation 14(5))

FORM P4: APPROVAL FOR INITIATING PRE-PACKAGED INSOLVENCY RESOLUTION PROCESS by unrelated financial creditors (Under regulation 14(7))

FORM P5: WRITTEN CONSENT TO ACT AS AUTHORISED REPRESENTATIVE (Under regulation 15(iii))

FORM P6: DECLARATION BY DIRECTOR/PARTNERS (Under regulation 16(1))

FORM P7: DECLARATION REGARDING EXISTENCE OF AVOIDANCE TRANSACTION(S) (Under regulation 16(2))

FORM P8: REPORT OF THE INSOLVENCY PROFESSIONAL (Under regulation 17)

FORM P9: PUBLIC ANNOUNCEMENT (Under regulation 19(2))

FORM P10: LIST OF CLAIMS (Under regulation 20)

FORM P11: INVITATION FOR RESOLUTION PLANS (Under regulation 43)

FORM P12: COMPLIANCE CERTIFICATE (Under regulation 49 (1) )

FORM P13: APPLICATION FOR TERMINATION OF PRE-PACKAGED INSOLVENCY RESOLUTION PROCESS (Under regulation 49(4) )

FORM P14: APPLICATION FOR VESTING MANAGEMENT WITH RESOLUTION PROFESSIONAL (Under regulation 51)

Quick links:

[www.insol.org](http://www.insol.org)

see websites of other country insolvency organisations

<https://ibbi.gov.in/>

<https://nclat.nic.in/>

<https://nclt.gov.in/>

<https://msme.gov.in/>

<https://ica.nic.in/>

<https://www.mca.gov.in/>

<https://www.sebi.gov.in/>