

## Insolvency and Bankruptcy Board of India

13<sup>th</sup> April, 2022

### Consultation paper on issues related to reducing delays in the corporate insolvency resolution process

This paper presents in detail four issues which contribute, directly or indirectly to delays in the corporate insolvency resolution process and suggests changes to the Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 (CIRP Regulations).

#### Part 1: Substantiating default in admitting applications by operational creditors

2. This part deals with the issue of inadequate information/documents provided by operational creditors (OCs) to establish the transaction and the default at the time of filing application u/s 9 of the Insolvency and Bankruptcy Code, 2016 (Code).

3. Section 9 of the Code provides a time limit of 14 days for admission or rejection of an application for initiating insolvency proceedings. It is observed that one key reason for delay in admitting the application is that there is a requirement to verify the existence of debt and default. It is often times difficult to ascertain existence of debt and default from the evidence filed along with the application for admission. Besides, promoters of the CD file objections to the application on grounds contesting the existence of the transaction, debt or the default. Thus, significant time is lost in the process of establishing the debt and default.

4. Analysis of data of admitted applications from the filings made before the IBBI by the IPs, shows that no application was admitted in 14 days. Further, time taken for admission of section 9 applications in the last 2 financial years is presented in the following table:

Year	Data available for applications admitted u/s 9	Average time taken for admission from date of filing (days)	No. of applications where admission took < 1 year	No. of applications where admission took 1-2 years	No. of application where admission took more than 2 years
2020-21	153	468	54	84	15
2021-22	207	650	39	86	82

5. Section 9(3) lays down the record and evidence to be furnished by the OC along with his application. Section 9(3)(e) requires submission of other information as may be prescribed. Rule 6 prescribes that application u/s 9 should be filed in Form 5, accompanied with documents and records required therein and as specified in the CIRP Regulations. This provision in the Rule envisages the IBBI to specify documents / records that may be required to be submitted along with Form 5 to supplement.

6. It is pertinent to note that an OC registered under the Goods and Services Tax provisions, is required to furnish details of sales and purchases of goods and services along with GST amount by filing GST returns and such return filing system is automated. GSTR-1 contains detailed information of all the outward goods and services of a business. It includes details of invoices, debit notes, credit notes, and revised invoices for outward goods and services and is required to be filed by the supplier of goods/services every month or quarter. GSTR-3B is a monthly self-declaration to be filed by a registered GST dealer - a simplified return to declare summary GST liabilities for a tax period. This return contains information relating to outward supplies of goods/services, amount of taxes paid etc. Rule 138 of the CGST Rules, 2017 provides for the e-way bill mechanism and in this context, it is important to note that “information is to be furnished prior to the commencement of movement of goods” and “is to be issued whether the movement is in relation to a supply or for reasons other than supply”. Thus, GSTR-1 and GSTR-3B filed by the OC along with e-way bill, wherever applicable can serve as proof to establish that the supply of goods/services to the CD has actually happened and thus, can be used as evidence in establishing default.

7. Such information will also be helpful if the OC can submit these details as additional documents with the claim forms submitted with the interim resolution professional (IRP) or resolution professional (RP). This will reduce time taken by the IRP to verify and decide on admission of the claims.

8. **Proposal:** In view of the above, it is proposed to amend the CIRP Regulations to provide for filing copies of GSTR-1 and GSTR-3B returns filed by the operational creditors along with e-way bill as additional documentary evidence. It is also proposed that the same information may also be submitted as part of the claim documents submitted to the IRP for easier verification and admission of claims. **Draft amendments are placed in Annexure A.**

## **Part 2: Facilitating information availability for the preparation of information memorandum and preparation of avoidance applications**

9. Section 18 of the Code provides that the IRP shall “*collect all information relating to the assets, finances and operations of the corporate debtor for determining the financial position of the corporate debtor*”. Further, clause (2) of section 23 states that the “*The resolution professional shall exercise powers and perform duties as are vested or conferred on the interim resolution professional under this Chapter*”. Thus, the IRP/RP are vested with the duty of collection of all the information regarding financial details of the CD.

10. The IRP/RP in performance of the above stated duty face numerous difficulties in collecting information regarding the financial position of the CD. The information acquired by the IRP/RP form the basis for the information memorandum (IM). The IM is crucial to establish a base line of the CD and is required to be shared with prospective resolution applicants for them to assess the CD before making a resolution plan. Valuation of the CD is also based on the available information regarding assets and liabilities. Timely preparation of the IM and completion of the valuation exercise are crucial to timely completion of the CIRP.

11. Section 19 imposes a liability on the personnel of the CD, its promoters or any other person associated with the CD to provide all assistance and cooperation to the IRP/RP. The Code also provides a relief to the IRP/RP wherein he may choose to file an application under section 19 such that the AA may pass an order to the personnel of the CD to extend all assistance and cooperation to him. Thus, there is an obligation under the Code and a remedial measure to provide information to IRP/RP for conduct of the CIRP. However, in several cases the IRP/RP do not have adequate information to prepare a comprehensive IM leading to further constraints in the conduct of the CIRP. The registered valuers appointed by the RP have also expressed concern that the limited information available constraints the valuation exercise, in some cases giving a limited picture of the CD.

12. The obligation on the CD, its promoters and employees under the Code is not easy to realise in practice. It is necessary to provide for a means for the IRP/RP to seek cooperation and in the event of non-cooperation, to establish the same. It would also be required to establish that the information obtained was partial and inadequate in order to establish non-cooperation.

13. Unavailability of requisite information /documents also constrains the RP from acting upon the questionable transactions by way of which assets may have been diverted or siphoned off. The RP is also constrained for information as the CD and its promoters and sometimes the employees do not cooperate, as they might have benefitted from such transactions.

14. A financial creditor might have undertaken independent valuation exercise for the CD as a whole or for the assets hypothecated or securitised with it before extending a loan. The valuation exercise is also repeated from time to time until recovery is made or during restructuring or while declaring such loans as non-performing assets. In these exercises the creditors come into possession of information, documents related to the different assets of the CD, including plant & machinery, inventories etc.

15. Banks and other financial creditors who have conducted mandatory audits of the CD for their requirements could share the reports or extracts of the relevant portions with the RP. RP may be able to use the report in respect of fraudulent transactions as such and in respect of other transactions, it may help in identifying the patterns of suspicious transactions and potential related parties even though period of audits may not coincide with the look back periods.

16. **Proposal:** In order to strengthen the availability of information with the IRP/RP for the preparation of the IM and the avoidance applications, it is essential that the information available with the CD, its promoters, its employees and the creditors be made available to the IRP/RP in a timely manner. A clear legal obligation is to be placed on all these stakeholders in order to ensure that information sharing happens. The following is proposed:

- (i) The CIRP Regulations be amended to impose an obligation on the CoC with regard to providing of all the relevant information they possess in terms of the assets of the CD from valuation exercises or stock audits, the relevant extracts from the transaction or forensic audits to IRP/RP in a timely manner.

(ii) The CIRP Regulations be amended to enable the IRP/RP to seek relevant information from the promoters of the CD, employees, partners and others and to place an obligation on them to share all the information that is sought by the IRP/RP in a timely manner.

**Draft amendments are placed in Annexure A.**

**Part 3: Dealing with avoidance applications after closure of a CIRP**

17. Most jurisdictions provide several mechanisms to challenge transactions entered into by a CD prior to the commencement of the insolvency proceeding. These mechanisms, generally known as avoiding powers or claw-back actions, allow the retrospective avoidance of certain transactions<sup>1</sup>. Therefore, the existence of avoiding powers may create several benefits i.e., promote a fair and efficient insolvency system – which treats stakeholders equitably, minimises costs inherent to insolvency and maximises stakeholder’s wealth<sup>2</sup>. Further, such provisions address opportunistic, value-destroying behaviour usually faced by debtors in the zone of insolvency, ensuring that creditors as a whole are treated equitably by allowing payments made or property transferred under certain transactions to be returned to the CD or their effect reversed. Thus, the existence of avoidance powers may help maximize the value of the firm, not only ex-post (i.e., once the company is in insolvency) but also ex ante, since it may discourage market participants to enter into transactions with an insolvent debtor. Further, transaction avoidance rules are widely considered to be an important tool for the regulation of related party transactions in insolvency<sup>3</sup>.

18. The Code attempts to preserve commercial morality by incorporating provisions for avoidance of certain transactions, and penalising suspended directors’ misconduct. Accordingly, the RP or the liquidator is obliged under the Code and the Regulations to file applications in respect of avoidance transactions (preferential transactions, undervalued transactions, extortionate transactions, and fraudulent transactions) found by him during the CIRP and liquidation process to the AA seeking appropriate relief.

19. Regulation 35A of the CIRP Regulations requires the RP to form an opinion whether the CD has been subjected to any transaction covered under sections 43, 45, 50 or 66 on or before the 75<sup>th</sup> day of the insolvency commencement date (ICD). Where the RP is of the opinion that the CD has been subjected to any transactions covered under these sections, he shall make a determination, on or before the 115<sup>th</sup> day of the ICD, under intimation to the Board. Further, he shall apply to the AA for appropriate relief on or before the 135<sup>th</sup> day of the ICD.

20. While the RP/liquidator may have filed an application with the AA, it may not always be possible for the AA to consider and dispose of the application during the tenure of the CIRP or the liquidation process. The application may remain pending with the AA for disposal, when the process comes to an end and consequently, the IRP/RP/liquidator is relieved. Section 26 of the

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<sup>1</sup> Jackson, T. H. (1984). Avoiding powers in bankruptcy. *Stanford Law Review*, 725-787.

<sup>2</sup> Mevorach, I. (2011). Transaction Avoidance in Bankruptcy of Corporate. *ECFR*, 235-258.

<sup>3</sup> Zwieten, K. v. (2018). Related Party Transactions in Insolvency. *ECGI Working Paper Series in Law*, 1-21.

Code clarifies that the filing of an avoidance application by the RP shall not affect the proceedings of the CIRP. However, section 36(3)(f) provides that the liquidation estate shall comprise any asset or their value recovered through proceedings for avoidance of transactions. Further, the application may have been disposed of when the process was on, but an appeal against the order disposing the application may be pending when the process comes to an end.

21. According to information available as of 28<sup>th</sup> February, 2022 with the Board, 708 applications in respect of avoidance transactions valued at around Rs. 2.00 lakh crore have been filed with AA. Of these, only a handful of applications have been disposed of by the AA and few appeals have been filed against the orders of the AA disposing these applications. Several such applications are pending even after approval and implementation of resolution plan.

22. Once the resolution plan is approved, the RP demits office and the CoC also has no active role. The avoidance applications however, await adjudication. The issue that arises for consideration is by whom and how the applications would be taken to logical conclusion. Section 30(2) (f) of the Code empowers the Board to specify such other requirements as required in the Resolution Plan. In furtherance of value maximization principle and to bring clarity on the issue it is proposed to clarify the issue through amendment in CIRP Regulations.

23. **Proposal:** Accordingly, it is proposed that the CIRP Regulations be amended to provide that how the avoidance applications and proceedings will be pursued, shall be specifically mentioned as part of resolution plan submitted to AA for approval. **Draft amendment is placed in Annexure A.**

#### **Part 4: Significant difference in valuations during a CIRP and appointment of a third valuer**

24. Regulation 27 (1) of the CIRP Regulations provides that, the RP shall, within seven days of his appointment but not later than forty-seventh day from the insolvency commencement date, appoint two registered valuers to determine the fair value and the liquidation value of the corporate debtor in accordance with regulation 35.

25. Regulation 35 provides that the fair value and liquidation value of the CD shall be determined by two registered valuers and the values be computed in accordance with internationally accepted valuation standards. It also provides that, *“if in the opinion of the resolution professional, the two estimates of a value are significantly different, he may appoint another registered valuer who shall submit an estimate of the value computed in the same manner; and the average of the two closest estimates of a value shall be considered the fair value or the liquidation value, as the case may be.”* The assessment of difference in the valuation has been left to the opinion of the RP leading to scope for discretion.

26. The valuation exercise is an important concern in the insolvency process as it plays an important role in decision making by the CoC. It helps to determine the minimum entitlement to operational creditors and to dissenting financial creditors. Though not a floor price for the assets, it serves as a guidance for assessing the resolution plans.

27. The exercise of valuation is by nature subjective. Given that there are no notified standards in India and registered valuers tend to use different standards, which could lead to difference in approach and methodologies adopted for valuation. Further, the assessment or understanding of valuation reports have to be done discounting for several caveats and assumptions also. Differences also occur with the kind of asset being valued and approach used has to be nuanced.

28. Valuation is also required under other legislations. Section 260 of the Companies Act, 2013, requires the company administrator to prepare a valuation report. Here there is requirement of only 1 (one) valuer to be appointed. Similarly, under SEBI (Issue of capital and disclosure requirements) 2018, which provide that where specified securities are issued on a preferential basis for consideration other than cash, the valuation of the assets in consideration for which the equity shares are issued shall be done by an independent valuer, which shall be submitted to the stock exchanges where equity of share of issuer are listed. The Code also makes a departure for the fast-track insolvency resolution process where only one registered valuer is required to be appointed. International practice also shows that valuation is done by one valuer.

29. The Handbook on Policy, Standards and Procedures for Real Estate Valuation by Banks and HFIs in India issued in 2011 by IBA and NHB states the following:

*1.9 Obligations of the Banks/HFIs*

*Wherever the value of the property is more than Rs.10 crore, two valuers of Category A or B shall be appointed in order to get the valuation done. In case the difference in the valuation arrived at by both the valuers is not more than 15 percent, the average value is considered. In case the difference is more than 15 per cent, then, a third valuer, who shall also be a senior valuer in the A or B category, shall be appointed and the bank/HFI shall take an appropriate considered decision on the value.'*

30. **Proposal:** In order to remove ambiguity, to reduce any potential litigation and to provide a guiding factor in the appointment of the third valuer, it is proposed that the CIRP Regulation be amended to provide a threshold of 25% difference for appointing a third valuer. Different thresholds of difference for each asset class may also be considered, if required. **Draft amendment is placed in Annexure A.**

31. **Economic analysis:** The time boundness of the resolution process is a unique and key feature of the Insolvency and Bankruptcy Code, 2016. The availability of correct information is crucial for admission of applications in a timely manner, in order for the resolution process to be initiated. It also shortens the time available with the promoters of the CD and reduces the risk of siphoning off while the application awaits admission. The objectives of resolution and value maximisation are dependent on early completion of the process. The process timelines are laid out in such a manner that the preparation of the IM and the valuation exercise are completed within a prescribed timeline, so that the process of inviting and considering resolution plans can happen subsequently. Lack of information hindering these activities is an avoidable delay and hence strengthening the regime that enables the IP to complete these key milestones is a necessity. The recovery from avoidance applications improves value maximisation and has a direct bearing on the realisable value of the resolution. The lack of clarity on who will pursue the applications after approval of

the resolution plan leaves a gap where there is no proper follow up of the applications and proceedings. The lack of clarity on the appointment of a third valuer leads to delays as such appointments happen at a later stage of the process, hampering the process until such time such third value becomes available. The key intent is to reduce the delays and hence reduce further value erosion during the process.

**32. Public comments:** The Board accordingly solicits comments on the proposals discussed above and the draft regulations placed in the Annexure. After considering the comments, the Board proposes to make regulations under clauses (aa) and (t) of subsection (1) of section 196 of the Code.

**33. Submission of comments:** Comments may be submitted electronically by **03<sup>rd</sup> May, 2022**. For providing comments, please follow the process as under:

- (i) Visit IBBI website, [www.ibbi.gov.in](http://www.ibbi.gov.in);
- (ii) Select 'Public Comments';
- (iii) Select '**Discussion paper – CIRP April 22**'
- (iv) Provide your Name, and Email ID;
- (v) Select the stakeholder category, namely, - a) Corporate Debtor; b) Personal Guarantor to a Corporate Debtor; c) Proprietorship firms; d) Partnership firms; e) Creditor to a Corporate Debtor; f) Insolvency Professional; g) Insolvency Professional Agency; h) Insolvency Professional Entity; i) Academics; j) Investor; or k) Others.
- (vi) Select the kind of comments you wish to make, namely, a) General Comments; or b) Specific Comments.
- (vii) If you have selected 'General Comments', please select one of the following options:
  - a) Inconsistency, if any, between the provisions within the regulations (intra regulations);
  - b) Inconsistency, if any, between the provisions in different regulations (inter regulations);
  - c) Inconsistency, if any, between the provisions in the regulations with those in the rules;
  - d) Inconsistency, if any, between the provisions in the regulations with those in the Code;
  - e) Inconsistency, if any, between the provisions in the regulations with those in any other law;
  - f) Any difficulty in implementation of any of the provisions in the regulations;
  - g) Any provision that should have been provided in the regulations, but has not been provided; or
  - h) Any provision that has been provided in the regulations but should not have been provided.
- (viii) And then write comments under the selected option.

34. If you have selected 'Specific Comments', please select para number and then sub-para number and write comments under the selected para/sub-para number.

35. You can make comments on more than one para/sub-para, by clicking on more comments and repeating the process outlined above from point 33 (vi) onwards.

36. Click 'Submit' if you have no more comments to make.

GAZETTE OF INDIA

EXTRAORDINARY

PART III, SECTION 4

PUBLISHED BY AUTHORITY

**INSOLVENCY AND BANKRUPTCY BOARD OF INDIA  
NOTIFICATION**

New Delhi, the \_\_\_\_\_, 2022

**Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) (Second Amendment) Regulations, 2022.**

**No. IBBI/2021-22/GN/\_\_\_\_\_.** In exercise of the powers conferred by clause (t) of sub-section (1) of section 196 read with section 240 of the Insolvency and Bankruptcy Code, 2016 (31 of 2016), the Insolvency and Bankruptcy Board of India hereby makes the following regulations further to amend the Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016, namely: -

(1) These regulations may be called the Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) (Second Amendment) Regulations, 2022.

(2) They shall come into force on the date of their publication in the Official Gazette.

**2.** In the Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 (hereinafter referred to as the principal regulations),

i. In the principal regulations, regulation 2B shall be added namely:-

***“2B. Record or evidence of transaction, debt and default by operational creditor.***

*The operational creditor shall furnish copies of GSTR-1 and GSTR-3B filed under the provisions of the relevant Goods and Services Tax Acts read with the relevant Rules along with copy of e-way bill, wherever applicable.*

*Provided that this shall not apply to those goods and services which are not covered under any of the Goods and Services Act and to those within the limits not requiring registration under the above stated Acts.”*

ii. In the principal regulations, regulation 4C shall be added namely:

***“4C. Access to financial information***

*Without prejudice to section 19(2), the interim resolution professional or the resolution professional, as the case may be, shall seek information from the members, promoters, partners, board of directors and joint venture partners of the corporate debtor in a listed*

*format which shall also provide the time window for providing such information and they shall provide such information within such time.”*

- iii. In the principal regulations, under regulation 7, sub-regulation (2)(b), the following shall be added namely:-

*“(v) copies of GSTR-1 and GSTR-3B under the provisions of the relevant Goods and Services Tax Acts read with relevant Rules along with copy of e-way bill, wherever applicable.*

*Provided that this shall not apply to those goods and services which are not covered under any of the Goods and Services Acts and to those within the limits not requiring registration under the above stated Acts.”*

- iv. In the principal regulations, under regulation 35, sub-regulation (4), shall be added namely:-

*“(4) The creditor shall provide to the interim resolution professional or resolution professional, the valuation reports in respect of the assets of the corporate debtor wherever available. IRP/ RP shall, in turn share this information with the concerned registered valuers for the purposes of this regulation, shall include a statement of remarks on the significant difference between the value submitted and the earlier valuation of the assets provided by the creditors.”*

- v. In the principal regulations, under regulation 35, an explanation, shall be added namely:-

*“Explanation: ‘Significantly different’ for the purposes of this regulation shall mean a difference of 25 per cent in value.”*

- vi. In the principal regulations, under regulation 35A, sub-regulation (4), shall be added namely:-

*“(4) For the purposes of sub-regulation (1) to (3), creditors shall provide any information that they have regarding transactions that may fall under sections 43, 45, 50 or 66 of the Code, that may be available from the audits conducted by the creditors to the resolution professional.”*

- vii. In the principal regulations, under regulation 36, sub-regulation (3A), shall be added namely:-

*“(3A) For the purposes of purposes of sub-regulation (1) to (2), creditors shall provide financial statements of the corporate debtor available with them to the resolution professional.”*

- viii. In the principal regulations, under regulation 38, sub-regulation (2)(c), the following shall be added namely:-

*“(d) provides for the manner in which proceedings in respect of avoidance transactions under Chapter III or fraudulent or wrongful trading under Chapter VI of the Code, if any, will be pursued after the approval of the resolution plan.*

*Provided that this clause shall not apply to any resolution plan that has been submitted to the Adjudicating Authority under sub-section (6) of section 30 of the Code on or before the date of commencement of the IBBI (Insolvency Resolution Process for Corporate Persons) (Amendment) Regulations, 2022.”*

Mr. Ravi Mital  
Chairperson  
[ADVT.- \_\_\_\_\_]

Note: The Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 were published vide notification No. IBBI/2016-17/GN/REG004, dated 30<sup>th</sup> November, 2016 in the Gazette of India, Extraordinary, Part III, Section 4, No. 432 on 30<sup>th</sup> November, 2016 and were last amended by the Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) (Second Amendment) Regulations, 2021 published vide notification No. IBBI/2021-22/GN/REG075, dated the 14<sup>th</sup> July, 2021 in the Gazette of India, Extraordinary, Part III, Section 4, No. 284 on 14<sup>th</sup> July, 2021.

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