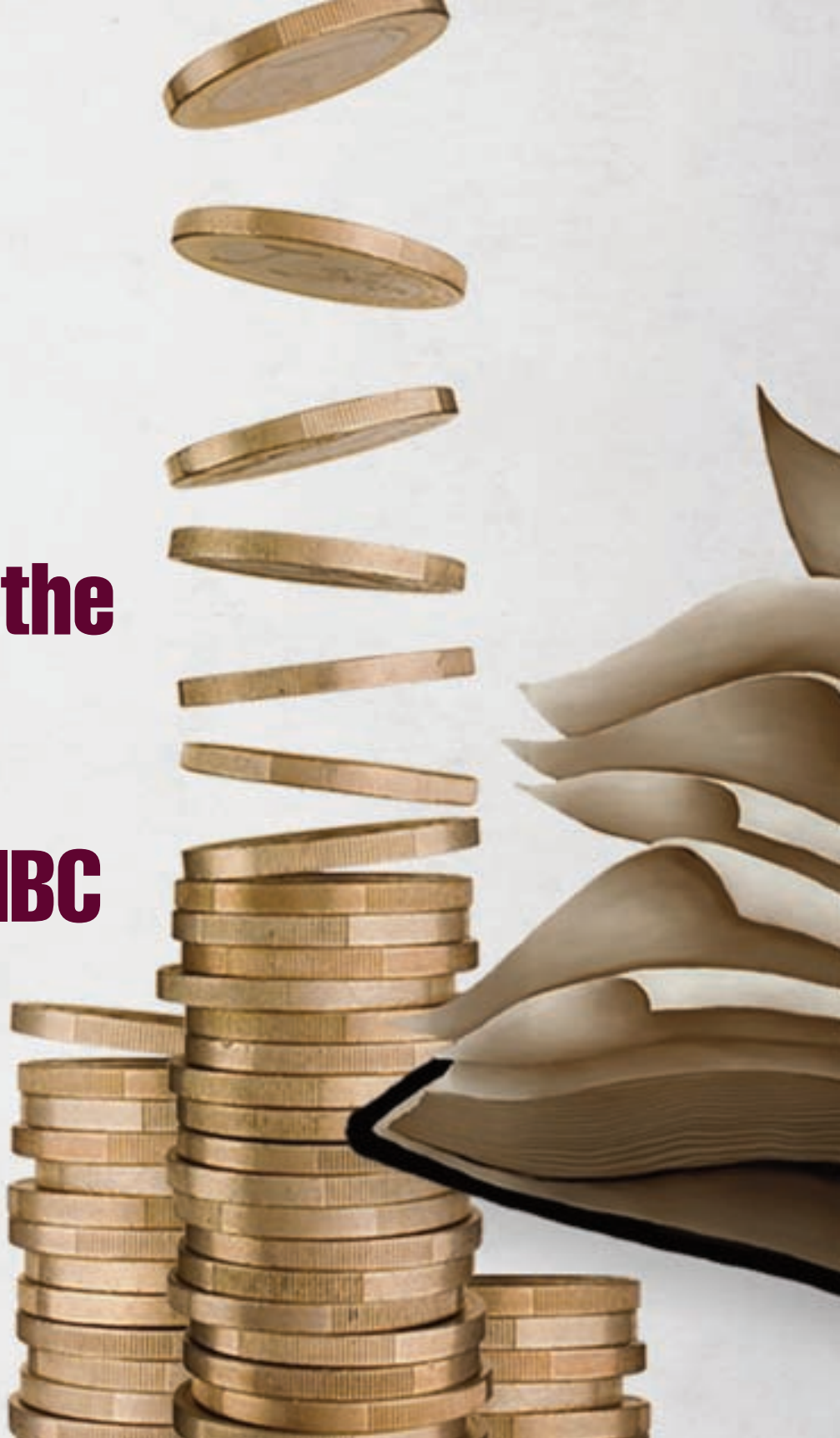


Creating Inroads in the Liquidation Process under the IBC



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The Background

The recently introduced legal, regulatory and policy changes that have been introduced in the Indian BFSI sector have not only geared up the pace at which the sector is operating but has also created a change in the overall dynamics. On 31st December 2016, gross Non Performing Assets (NPA) in the Indian Banking Sector stood at approximately 9.3 % of total advances¹. This has adversely affected the economy at large leading to blockage in huge amounts of capital, which could be deployed for other productive purposes, thereby derailing the spirit of entrepreneurship in the country. In order to combat with this situation, the RBI has been taking several steps and initiatives in the past few years such as Joint Lender Forum, Strategic Debt Restructuring and Scheme for Sustainable Structuring of Stressed Assets (S4A) to name a few that have aimed to tackle the quantum of bad loans. With the introduction of these initiatives, the Insolvency, and Bankruptcy Code 2016 (IBC) enforces a comprehensive regime that offers a viable alternative for resolution of various issues and strikes an optimal balance between debtors' concerns and interests of stakeholders.

The Liquidation Process

On 15th December 2016, the Central Government notified the rules by which companies can go through liquidation under the Insolvency and Bankruptcy Code 2016. These Regulations provide details of procedures to be reckoned to start with the issue of liquidation order under Section 33 of the Code till dissolution order under Section 54 (i.e. Chapter III of Part II of IBC). The regulations governing liquidation offer a comprehensive strategy to implement the process of liquidation. The rules require the liquidator to prepare and submit a preliminary report, asset memorandum, sale report, progress report and final report prior to initiating the liquidation process with the National Company Law Tribunal (NCLT).

The New Role of a Liquidator

The liquidator is the Insolvency Professional who attempts to evaluate and realize the assets of the company to ease the process of liquidation. Although the power/functions of the liquidator appear similar to the functions of the liquidator under Companies Act 1956, there is an element of dynamism included backed by independence in the

execution of responsibilities. Even though the new regulations have eased the regulatory compliances, there are a few challenges that are yet to be tackled and addressed to, when it comes to a seamless execution of the said

processes. The fee payable to liquidator shall form a part of the liquidation cost. This incentive to the liquidator, to liquidate the asset in an efficient/ time-bound manner, maximizes the return to the stakeholders. Although these incentives aim at obtaining a quick and efficient resolution, there are liability provisions as well for liquidators (for contravening the provisions of the code). Liability provisions for the insolvency professionals are discussed in further details below.

Liability Provisions of Liquidation

The IBC has strict liability provisions for the insolvency professionals, including the liquidator. If a liquidator contravenes the provisions of the IBC, the Adjudicating Authority may punish him with imprisonment or impose a fine or both. The Insolvency and Bankruptcy Board of India ("Board") also has the power to impose penalty and/or suspend/cancel the registration of the liquidator as insolvency professional, after completion of the disciplinary proceedings, which could be initiated either on a direction by the Adjudicating Authority or upon receipt of a complaint by any aggrieved person or by the Board itself. The relevant provisions are explained below:

1. By the Adjudicating Authority:

- a. Under Section 70(2), any insolvency professional who deliberately contravenes the provisions of the corporate insolvency resolution process (Part II of IBC), shall be punishable with imprisonment for a term which may extend to six months, or with minimum fine of one lakh rupees, which may extend to five lakh rupees or with both;
- b. If the Adjudicating Authority is satisfied on an application made under Section 47(1) of IBC by any creditor about any undervalued transaction, which the liquidator has not reported to the Adjudicating Authority, despite having sufficient information or opportunity, it may direct the Board under Section 47(2) to initiate disciplinary proceedings against such liquidator.

2. By the Board:

The Board may:

a. Upon direction of the Adjudicating Authority under Section 47(2);

b. Upon receipt of a complaint under Section 217(1) from any person aggrieved by the functioning of an insolvency professional;

c. Under Section 218(1), if the Board has reasonable ground to believe that an insolvency professional has contravened any provisions of the IBC or rules or regulations made or directions issued by the Board; direct any person or persons to act as investigating agency to conduct the inspection or investigation of the insolvency professional or insolvency professional agency or information utility. On completion of inspection or investigation, the Board under Section 219 may issue show cause notice to the insolvency professional or insolvency professional agency or information utility and under Section 220 (1) may appoint a disciplinary

committee to consider the reports of the investigating authority. (The Rule 11(1) to (7) of the Insolvency and Bankruptcy Board of India (Insolvency Professionals) Regulations, 2016, framed under powers conferred by Section 196, 207, 208 read with Section 240 of the IBC, contain the procedure and timelines for issuance and disposal of show cause notice).

Under Section 220(2), if the disciplinary committee is satisfied that sufficient cause exists upon examination of the report of the investigating authority, it may impose a penalty as specified in sub-section (3) or suspend or cancel the registration of the insolvency professional or insolvency professional agency or information utility. Under sub-section (3), upon contravention of any provisions of IBC or rules or regulations made thereunder, the disciplinary committee may impose penalty which is three times the amount of the loss caused, or likely to have been caused, to persons concerned or three times the amount of unlawful gain made on

account of any contravention, whichever is higher and in case the loss or unlawful gain is not quantifiable, the total amount of penalty imposed shall not exceed more than one crore rupees.

Conclusion

It is evident that the role of liquidator is going to be both critical as well as rewarding. He has to strike an optimal balance with respect to the interest of all the stakeholders in an unbiased way. Overall, the IBC is a right move in solving the problem of NPAs. It is expected that implementation of the code and liquidation provisions can potentially unlock capital to the tune of Rs 25,000 Crores, blocked in form of NPA over next few years². This will encourage entrepreneurship by releasing the blocked capital, strengthen the bond market and strengthen creditor's right. It will fulfill the Government's vision to bring Indian regulations in line with the best international practices.