

Introduction of Pre-Packaged Insolvency Resolution Process under the Insolvency and Bankruptcy Code, 2016

I. INTRODUCTION

The Upper House of Parliament in India, being the Rajya Sabha passed the Insolvency and Bankruptcy Code (Amendment) Bill, 2021 (“**Amendment**”) on 3rd August 2021 which introduces a Pre-Packaged Insolvency Resolution Process (“**PIRP**”) within the scheme of the Insolvency and Bankruptcy Code, 2016 (“**Code**”). The Amendment had already cleared the Lower House of Parliament, the Lok Sabha on 28th July 2021.

The Amendment replaces the Ordinance passed by the President of India on 4th April 2021. At the time, the Ordinance was promulgated with a view to combat the impact of the COVID-19 pandemic on the Indian economy and protect micro, small and medium sized businesses from the onslaught of applications for commencement of corporate insolvency resolution process (“**CIRP**”) under the Code. This was a step taken in addition to the temporary suspension of the CIRP mechanisms under the Code (as per Section 7, 9 and 10 of the Code) vide the Ordinance dated 24th March 2020 for a period of 6 (*six*) months which was further extended on 25th December 2020 for a period of 3 (*three*) months.

Pre-packaged insolvency is a financial plan initiated by the Corporate Debtor (hereinafter referred to as “**CD**”) where the restructuring is pre-posed and agreed in advance with creditors and other stakeholders for a CD. The Amendment inter alia has introduced Chapter III-A which contains sections 54A to 54P to facilitate PIRP for corporate persons defined as micro, small and medium enterprises (“**MSME**”) under sub-section Section 7(1) of the Micro, Small and Medium Enterprise Development Act, 2006 (“**MSMED Act**”). The Government has introduced the Amendment to ensure that PIRP serves as a cost effective and value maximising outcome which preserves jobs and ensures continuity of business and business ownership.

In this news alert we attempt to decode the salient features of the Pre-Packaged Insolvency Resolution Process (PIRP).

II. SALIENT FEATURES

A. Key Definitions

1. Base Resolution Plan

It is defined as a resolution plan provided by the CD under clause (c) of sub-section (4) of Section 54A (section for initiation of PIRP).

2. Pre-Packaged Insolvency Commencement Date

This means the date of admission of an application for initiating the PIRP by the Adjudicating Authority under clause (a) of sub-section (4) of Section 54C.

3. Pre-packaged Insolvency Resolution Process Costs

This has been defined as (i) the amount of any interim finance and the costs incurred in raising such finance; (ii) the fees payable to any person acting as a resolution professional and any expenses incurred by him for conducting the pre-packaged insolvency resolution process during the pre-packaged insolvency resolution process period, subject to sub-section (6) of Section 54F; (iii) any costs incurred by the resolution professional in running the business of the CD as a going concern pursuant to an order under sub-section (2) of Section 54J; (iv) any costs incurred at the expense of the Government to facilitate the pre-packaged insolvency resolution process; and (v) any other costs as may be specified;

B. Qualification

As per Section 4 of the Amendment, the minimum threshold for initiation of PIRP is a debt not exceeding Rs. 1,00,00,000/- (*Rupees One Crore only*).

Furthermore, in order to make an application for PIRP, the CD ought to fulfil the requirements laid down in Section 54A of the Code. These criteria inter alia include no prior CIRP or liquidation should be admitted against the CD; Financial Creditors (not being related party of the CD) not having less than 66% of the financial debt of the CD have accepted the proposal of an Insolvency Professional to be appointed as the Resolution Professional for PIRP and a specific declaration from the directors/partners of the CD declaring the CD's intention to initiate PIRP. The Resolution Professional has to file a report confirming that the CD has fulfilled the requirements under Section 54A of the Code.

C. Simultaneous disposal of Applications

The Amendment introduces Section 11A of the Code which provides that if an application for PIRP under Section 54C of the Code is pending against any CD, the same ought to be considered prior to the admission / rejection of CIRP applications

under Sections 7, 9 or 10 of the Code filed against the same CD. Further, if an application for PIRP is filed within 14 (*fourteen*) days of applications pending under Sections 7, 9 or 10 of the Code, the Application for PIRP is to be admitted or disposed of prior to the pending applications. In the event the application for PIRP is filed after 14 days of applications filed for CIRP under Sections 7, 9 or 10, the application for CIRP must be disposed of first.

However, this Section is not applicable to CIRP applications filed and pending on the date of commencement of the Amendment i.e. 4th April 2021.

Pertinently, under Section 54O of the Code, the Committee of Creditors (“CoC”) with not less than 66% of the vote can at any time after the initiation of PIRP but before the approval of a Resolution Plan opt for CIRP to be initiated if the Corporate Debtor qualifies for the same. The Resolution Professional ought to intimate the Adjudicating Authority of the decision of the CoC. It is then incumbent on the Adjudicating Authority to pass the order within 30 (*thirty*) days of such intimation given by Resolution Professional for termination of PIRP and initiation of CIRP, appointment of Resolution Profession under PIRP as Interim Resolution Professional for CIRP and declaration of pre-packaged insolvency resolution process costs which shall become part of the CIRP costs. Any order passed by the Adjudicating Authority has the same effect as an order passed under Section 7 of the Code and CIRP shall commence from the date of such order.

D. Process for initiation of PIRP

The CD can file an application for initiating the PIRP in the prescribed format only if the CD has met the requirements under Section 54A of the Code.

The Adjudicating Authority must either accept or reject the application by passing an order within a period of 14 (*fourteen*) days. The PIRP shall commence from the date of acceptance of the application.

On the PIRP commencement date, the Adjudicating Authority shall, in conjunction with the order of admission under Section 54C: (a) declare a moratorium for the purposes referred to in sub-section (1) read with sub-section (3) of Section 14, which shall apply mutatis mutandis to the proceedings under this Chapter; (b) appoint a Resolution Professional as named in the application.

The PIRP should be completed within a period of 120 (*one hundred twenty*) days, and the Resolution Professional must submit the resolution plan approved by the CoC, to the Adjudicating Authority within a period of 90 (*ninety*) days from the commencement of PIRP. If such time period elapses the Resolution Professional shall

file an application before the Adjudicating Authority for the termination of PIRP. Upon the filing of such an application the Adjudicating Authority may pass an order terminating the PIRP or extending the time period for completion of PIRP.

E. Management of the affairs of the Corporate Debtor

As per Section 54H of the Amendment, the management of the CD during the PIRP vests in the board of directors or partners of the CD as the case maybe. However, the powers vested in the Directors/Partners are subject to the provisions of Sections 54H (b) and 54H(c). Pertinently, Section 54J empowers the CoC to vest the management of the CD with the Resolution Professional subject to confirmation by the Adjudicating Authority. The Adjudicating Authority may allow such application preferred by the Resolution Professional if it is found that the affairs of the CD are being conducted in a fraudulent manner or there has been gross mismanagement of the affairs of the CD.

F. Approval of Resolution Plan

The base resolution plan as submitted to the financial creditors before the initiation of PIRP shall be submitted to the Resolution Professional by the CD as a base resolution plan within 2 (*two*) days of the PIRP commencement date. The CD is given an opportunity by the CoC to revise the base resolution plan. The base resolution plan as submitted ought to comply with the provisions of Section 30 of the Code. If the plan is approved then it is submitted to the Adjudicating Authority; if not, the Resolution Professional shall file an application for termination of PIRP. The approval of the base resolution plan shall require a majority vote of at least 66% of the CoC. Thereafter, if the Adjudicating Authority is satisfied that the resolution proposal as approved by the CoC meets the requirements of Section 30(2) of the Code, it must approve the plan within 30 (*thirty*) days of receiving it. The order of approval will have effect according to the provisions provided in sections 31(1), (3) and (4) of the Code. Alternatively, the Adjudicating Authority can also reject the resolution plan if it is satisfied that the resolution plan does not conform to the requirements of Section 30(2) of the Code pursuant to which, an order as per Section 54N may be passed.

The decision of the Adjudicating Authority can be appealed under Section 61(3) of the Code.

G. Fraudulent Management of Corporate Debtor and Punishment

The Amendment introduces Section 67A which provides that on and after the PIRP commencement date, if an officer of the CD manages its affairs with the intent to defraud creditors or for any fraudulent purpose, then on the application of the

Resolution Professional, the Adjudicating Authority can pass an order imposing upon such officer a penalty of not less than Rs. 100,000/- which may extend to Rs. 100,00,000/-. Pertinently, the provisions relating to avoidable transactions as provided under sections 43 to 51 of the Code and applicable to CIRPs shall apply to PIRPs as well.

In addition, the provision for punishment is made under Section 77A of the Code, which is an extension given to the already existing section on punishment i.e. Section 77. Section 77A provides that if the CD and any person who knowingly and wilfully authorises or permits the furnishing of false material or omission of any material fact knowing it to be material while providing information in the application under Section 54C or with respect to the list of claims under Section 54G of the Code, such they shall be punishable with imprisonment for a term which shall not be less than 3 (*three*) years, but which may extend to 5 (*five*) years or with fine which shall not be less than Rs. 100,000/- but which may extend to Rs. 100,00,000/- or with both.

III. RATIONALE BEHIND THE LAW

With CIRP suspended for a period of 1 (*one*) year i.e. 25th March 2020 - 24th March 2021, the MSME sector was severely affected. As per the Statement of Objects and Reasons, the Amendment has been introduced to address the specific requirements of the MSME sector by providing an efficient and alternative framework under the Code for a quicker, cost-effective insolvency resolution process that is least disruptive to the business, ensuring, among other objectives, the preservation of jobs.

IV. CONCLUSION

With the introduction of pre-packaged insolvency, the Indian government has aligned itself with nations such as the United Kingdom, the United States of America, Canada and Singapore.

The introduction of a PIRP mechanism is definitely a welcome move for the MSME sector. A perusal of the Amendment shows that the provisions of PIRP have been prioritised over CIRP mechanisms possibly because they seek to balance the needs of creditors whilst protecting insolvent MSMEs inter alia from the economic ripple effect caused by COVID-19. Whilst the Amendments seek to empower the board of director with the management of the CD during PIRP, they also strike a balance through Sections 67A and 77A of the Code which prevent the perpetration of fraud during PIRP by an officer of the CD.

Whilst the efficacy of PIRPs remain to be seen, much of its success will depend on the whether or not the Government introduces complimentary measures to ensure that

the Adjudicating Authorities are equipped to handle and effectively dispose of PIRP Applications in the face of the severe backlog of CIRP Applications already choking the system.

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