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P27



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P66



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P61



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P55



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P40

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P24



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P37

let's arbitrate



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P64



India's Extradition Story

A Glimpse of the Bygones!

P08

expert speak



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P19

expert speak



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P70

expert speak



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P32

Erstwhile Directors Under IBC - Right of Participation and Supply of Resolution Plans: A Desultory Exercise

■ Varsha Banerjee & Kunal Godhwani



he Bankruptcy Law Committee in its report¹ underlined that the creditors have had low power when faced with default and

promoters stay in control of the company even after default, whereas, when a default takes place, control is supposed to transfer to the creditors and equity owners shall have no say in the company. Considering the above, the Insolvency and Bankruptcy Code, 2016 (Code) provided a shift of control from the defaulting debtor's management to its creditors and a debtor-in-possession regime to a creditor-in-control regime.

The Code envisages that, once a Petition against the Corporate Debtor is admitted, the resolution professional is required to collate claims and form a Committee of Creditors. The Committee of Creditors as constituted above, in their meeting(s) then assess the viability and resolution, if any, of the Corporate Debtor in its commercial wisdom, failing which the Corporate Debtor is to be liquidated. However, during the insolvency resolution process, the Resolution Professional is required to issue notice of each meeting to

the members of the suspended board of directors of the Corporate Debtors in terms of Section 24(3) of the Code who have no right to vote in such meetings.

The information memorandum and resolution plan(s) are one of the most vital and critical documents in the resolution process of Corporate Debtor which are shared with members of the Committee of Creditors and the Resolution Applicants, only after receiving an undertaking from such parties to the effect that they will maintain confidentiality as regards the information.

In light of the above provision of the Code, the rights of the erstwhile Board were read in a conservative manner providing for a limited participation in the insolvency process. However, the scope and ambit of the rights as available to the erstwhile Board under Section 24 of the Code, has been recently interpreted by the Hon'ble Supreme Court in the Corporate Insolvency Resolution Process of Ruchi Soya Industries Ltd.. In the said matter, the resolution plan(s) as received by the Committee of Creditors were not shared with the suspended board of directors and the objections towards the same as raised by the



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erstwhile management and/or suspended board before the Adjudicating Authority and the Appellate Tribunal were also rejected. The rejection of the objection by the Adjudicating Authority and the Appellate Tribunal was premised on the fact that the Committee of Creditors is the sole authority to decide on the viability, feasibility and financial matrix of a resolution plan and thus resolution plan(s) are not required to be shared with the erstwhile board of the Corporate Debtor. The decision of the Adjudicating Authority and the Appellate Tribunal ultimately reached the Hon'ble Supreme

Court and the Hon'ble Supreme Court² held that though the erstwhile Board of Directors are not members of the Committee of Creditors, yet, they have a right to participate in each and every meeting of the committee of creditors, and such right of participation inherently warrants sharing of the resolution plan(s) with them beforehand, for an effective participation in order to enable them to discuss along with members of the committee of creditors all resolution plans that are presented at such meetings. The decisions of the Hon'ble Supreme Court is based on the fact that

Section 31(1) of the Code which provides that the members of the erstwhile Board of Directors, who are often guarantors, are vitally interested in a resolution plan which binds the erstwhile board and the guarantors. A resolution plan may scale down the debt of the principal debtor, resulting in scaling down the debt of the guarantor as well, or it may not. The resolution plan may also scale down certain debts and not others, leaving guarantors of the latter kind of debts exposed for the entire amount of the debt and hence, their effective participation is warranted.

CONCLUSION

The above decision of the Hon'ble Supreme Court seeks to provide right of meaningful participation to the erstwhile Board of Directors who are often the guarantors and accordingly, vitally interested in the resolution plans which impacts and interferes with the rights of guarantors who indeed should have a right to object to the Resolution Plans. However, granting right to the erstwhile board of directors to raise their objections during the Corporate Insolvency Resolution Process in certain instances may create impediment in resolution of the Corporate Debtor which is a time bound process and in absence of due conclusion in time may result in liquidation of the Corporate Debtor hampering the rights of all stakeholders. The right of providing resolution plan and other documents to the erstwhile suspended board should not become a tool for the erstwhile suspended board to undermine the process of the Code which seeks to eliminate persons who, on account of their misconduct, have contributed to the defaults and are otherwise undesirable for the company.

The mere supply of the resolution plans for effective participation of the erstwhile board of directors per se will not serve the interest of the erstwhile board in as much as in absence of any right to vote in such meetings, the mere supply of documents shall result in a desultory exercise.

The rights of erstwhile Board particularly as the guarantors are, even otherwise protected, since the same are required to be in consonance with the provisions of the Indian Contract Act failing which the resolution plan shall be in contravention to the provisions of the Indian Contract Act and accordingly, cannot pass a muster under Section 30(2)(e) of the Code.

The presence of erstwhile board of directors will facilitate or help the resolution professional or the Committee of Creditors to appreciate any given resolution plan is case/matter specific and the same could have been left to the wisdom and at the discretion of Committee of Creditors whereby, necessary resolution to such effect could have been passed at the meeting of the Committee of Creditors. The law as laid down by the Hon'ble Supreme Court for the purpose of safeguarding the interest of the erstwhile board by granting them meaningful participation in light of ultimate discretion of the Committee of Creditors as regards approval and/rejection of a resolution plan, including the treatment of personal guarantees, will thus not automatically enrich the armour of the erstwhile Board in every insolvency proceedings. The decision and the mandate of the Committee of Creditors is the basic touchstone on which resolution under the Code is premised.¹²



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¹The report of the Bankruptcy Law Reforms Committee Volume I: Rationale and Design Dt. Nov. 2015 available at https://ibbi.gov.in/uploads/resources/BLRCReportVol1_04112015.pdf

²Judgment dated 31.01.2019 passed by Hon'ble Supreme Court in Civil Appeal No. 8430 of 2018.