Liquidation Under Insolvency And Bankruptcy Code, 2016- Compulsory?

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Is Liquidation Compulsory Under IBC, 2016?

The insolvency resolution process in India has in the past elaborated the simultaneous operation of several statutory instruments. This includes the Sick Industrial Companies Act, 1985, the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest, 2002, the Recovery of Debt Due to Banks and Financial Institution Act, 1993 and the Companies Act, 2013.

The involuntary liquidation provisions in the Insolvency and Bankruptcy Code, 2016 ("IBC") came into effect on 15th December 2016. Along with this, the Insolvency and Bankruptcy Board of India (Liquidation process) Regulations 2016 ("Regulations") were published and came into effect. These Regulations seek to improve the Liquidation process with a view to spending less time and costs in the execution and maximising creditor recoveries. The Regulations set out the procedural aspects of the new liquidation processes including appointment, remuneration, powers and functions of the liquidator; details on how creditors can make claims and information about the realisation and distribution process.

Every distressed company has to go through a hierarchy of processes which include a compulsory insolvency resolution process prior to liquidation and the final dissolution only after the competition of such liquidation process. Thus every company dissolved pursuant to the IBC has to mandatorily undergo the preceding Corporate Insolvency Regulation Process ("CIRP") and liquidation process.

Now the question for consideration is whether a company has to compulsorily undergo a liquidation process?

In order to answer the question, we can refer to the following provisions.

Section 54 of IBC- Application for Dissolution- where the assets of the Corporate Debtor have been completely liquidated, the liquidator shall make an application to the Adjudicating Authority for the dissolution of such Corporate Debtor[1].

Regulation 14 of the IBBI (Liquidation Process) Regulations, 2016- Early Dissolution- if it appears to the Liquidator that:

1. the realizable properties of the Corporate debtor are insufficient to cover the cost of the liquidation process; and
2. the affairs of the corporate debtor do not require any further investigation;

He may apply to the Adjudicating Authority for early dissolution[2].

Rule 11- NCLT Rules, 2016- Inherent Powers of NCLT- Nothing in these rules shall be deemed to limit or otherwise affect the inherent powers of the Tribunal to make such orders as may be necessary for meeting the ends of justice or to prevent abuse of the process of the tribunal[3].

Analysis

A conjoint reading of the aforementioned provisions suggests that an application of dissolution shall be made where the assets of the corporate debtor are completely sold. Hence, it may be naturally implied that where the Corporate Debtor has no assets at the very commencement of the liquidation, the liquidation period may not be required.

The following question has been answered in a number of judgements passed by the National Company Law Tribunal ("NCLT"):

In *Synew Steel Pvt Ltd CP (IB)N.96/BB/2020* ,[4] initially the application was filed under Section 10 of the IBC read with Rule 7 of I & B (AAA) Rules, 2016, inter alia seeking to initiate CIRP in respect of the M/S Synew Steel Pvt Ltd on the ground that it has committed default of an amount of Rs. 1, 18,56,964/- which includes claims from both Financial Creditors and Operational Creditors. The Adjudicating Authority admitted the case and CIRP was initiated in respect of the Corporate Applicant.

It was pointed out by the Insolvency Resolution Professional (IRP) that he is unable to constitute the Committee of Creditors (COC) because there were no assets (movable or immovable) with the Corporate Debtor except a cash balance of Rs. 729/-. The entire share capital of the Corporate Debtor was eroded. Because of no business being conducted by the Corporate Debtor in the last 3 years, there has been no revenue.

The NCLT referred to the following provisions before going into the merits of the case

1. Section 54 of IBC
2. Rule 14 of IBBI (Liquidation Process) Regulations, 2016
3. Rule 11 of NCLT Rules, 2016

The Tribunal held that *"there would be no useful purpose served, by placing the Corporate Debtor under a Liquidation Process, under the extant or provisions of Code. Since the Assets of Company were realized, the liquidation process under the provisions or Code is deemed to have been completed under Chapter III of Part II of Code and thus it would be just and proper for the Adjudicating Authority to dissolve the company as proposed by the Resolution professional and the Applicant Company i.e. Synew Steel Private Limited is ordered to be dissolved with immediate effect".*

In another case of *Central Bank of India vs. Dev Blessing Traders Private Limited CP (IB) 1384/(MB)2017[5]* wherein the NCLT (Mumbai Bench) admitted the Petition under Section 7 of the IBC and after the application was admitted Moratorium was imposed as per Section 14 of IBC during the CIRP period. The Resolution Professional has reported that as per the balance sheet of the Corporate Debtor company there was no asset for liquidation so as to justify the outstanding debt. The Liquidator stated that "*there has been no assets realizable or saleable, it will only increase the cost of liquidation, can opt for "Dissolution*".

The Tribunal held that "not only it is just and equitable but because of the fact that no asset is available for the purpose of Liquidation as reported by the Resolution Professional, this a fit case of Corporate Debtor to be

prescribed under section 54 of the Insolvency Code".
Before closing the matter and the proceedings, the Bench is of the conscientious opinion that an explanation is to be sought from the Central Bank of India who has granted a substantial loan to its Corporate Debtor, prima facie, without ascertaining the position of the assets of the company. The bank authority is required to tell the terms and conditions under which the loan was granted to the Debtor Company.
In another case of *Arvind Gawada vs. Zeel Global Projects Pvt Ltd. C.P. (IB) 248/2017* the NCLT (Mumbai Bench) admitted the petition under Section 9 of the IBC. The Resolution Professional has reported that as per the balance sheet of the Corporate Debtor Company there was no asset for liquidation so as to satisfy the outstanding debt and thereafter filed an application under Section 54 of IBC read with Regulation 14 of IBBI (Liquidation Process) Regulations, 2016.
The Liquidator while preparing the preliminary report in compliance with Regulation 33 i.e. based upon and detailing the capital structure of the corporate debtor and the estimates of its assets and liabilities as on the liquidation commencement date came to the conclusion that there being no assets realizable or saleable, it will only increase the cost of liquidation. The NCLT held that *"it is just and equitable but because of the fact that no asset is available for the purpose of Liquidation as reported by Learned Resolution Professional, thus is a fit case of a Corporate Debtor to be dissolved as prescribed under section 54 of the Insolvency Code, ordered accordingly, stood 'Dissolved' from the date of this order"[6].*
Early dissolution can help reduce the pendency of the cases if the said application filed by the Resolution Professional is genuine. The genuineness of the application can be ascertained by going into the relevant documents of the company.
As per the data available for the year 2020, less than 6% of the total number of cases filed under IBC have found resolution till the end of March 2020, the latest data from the Insolvency and Bankruptcy Board of India ("IBBI") shows. A total of 3774 cases or CIRPs have been filed since the IBC came into force. Out of these, about 43% have closed by way of resolution, liquidation or other means, total of 1604 cases. The remaining 57% or 2710 cases are still ongoing, many of which have exceeded the 330 day maximum time limit set under the IBC.(SOURCE: IBBI)
Conclusion
After considering the aforementioned cases and provisions we can conclude that in situations where it is clear that the assets are going to be inadequate to cover the costs of the liquidation process, the affairs of the Corporate Debtor do not require any examination, whenever after the preparation of the Preliminary Report. The liquidator can apply to the tribunal for early dissolution. But the onus to prove the legitimacy of such cases lies on the Resolution Professional so that no debtor can take advantage of the early dissolution process as provided under IBC. Also, the Adjudicating Authority in such cases shall go into the merits of the case and then pass an appropriate order.
All the above mentioned cases and the provisions are in consonance with the objective of IBC. The early dissolution process can save a great deal of time and decrease the pending cases. However, the proper due-diligence is a *prima facie* requirement while deciding cases pertaining to early dissolution.

- [1] https://ibbi.gov.in//uploads/legalframwork/2020-09-23-232605-8ldhg-e942e8ee824aa2c4ba4767b93aad0e5d.pdf
- [2]https://ibbi.gov.in//uploads/legalframwork/96336966a318bbeff79f7dc0c115f08e.pdf
- [3] https://nclt.gov.in/sites/default/files/All-PDF/Rules_NCLT_latest.pdf
- [4] https://nclt.gov.in/sites/default/files/December/final-orders-pdf/cp%20ib%2096%20of%202020%20%285%29.pdf
- [5] https://nclt.gov.in/sites/default/files/Interim-order-pdf/Dev%20Blessing%20Traders%20Private%20Limited%20CP%201284-2017%20NCLT%20ON%2011.02.2019%20FINAL-DISSOLUTION.pdf
- [6] https://www.legitquest.com/case/arvind-gawada-v-zeel-global-projects-private-limited/17328E

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