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Leveraging Accentuating Role of Resolution Professional in Insolvency Scenario

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ABSTRACT

Company law is an organizational law. Organizational change via. Restructuring has an impact on constituents of the value chain, whether it is shareholders, creditors, suppliers, employees and consumers. The obvious questions which come to fore, are how are the rights of the stakeholders going to be affected? What processes and compliances are carried out for 'Restructuring'? One of the compliances in this context is due diligence. Assessment of liability, credit worthiness, IP, MK capitalization, long term agreement with suppliers are some the facets which becomes quintessential to analysis in this regard. Thus, the process of restructuring, involves inter alia, firstly, Due diligence; secondly, protecting the rights or interest of buyer and seller acquirer and acquiree via web of contracts like share sell agreement, warranty and confidentiality, as all of these have to be done sector specific; thirdly, large number of regulators for compliances including impact of restructuring on organization which are getting mergered or which is being merged. The instant research paper is trying to vividly and comprehensively address the pertinent questions and problems in the domain of "Insolvency" and "Restructuring" from the lens of extant laws of the land and judicial precedents, helping to delve into the vital facets of Resolution Professional growing role in the "Insolvency proceedings and beyond" in the realm of company law.

Keywords: *Synergy; Restructuring; Insolvency; Due Diligence; Japanese Keiretsu Model.*

I. INTRODUCTION

The Growth and expansion along with diversification via. takeover and merger process has been widely held to be the ultimate objective of the corporate or business restructuring. A vital aspect in this endeavour is "Synergy", for the quintessential purpose to remain competitive in market segment, industry and territorial coverage in which business caters to. The causes of restructuring have been manifolded, namely, market competition, growth, synergy, insolvency (looking from stress and opportunities perspective), redefine market segment, creation of allied conglomerate among others. The Company law deals with single corporate entity, not with

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group companies. “Compliance” and “Disclosure” are important facets which forms the core of obligations from the perspective of corporate entities in line with the law of the land. Compliance with market regulator, to ensure equitable and fair playing ground to market entities and stakeholder is a vital aspect in this context.

Review of Literature and Judicial Precedents

Reliance has been placed on varied judicial precedents in judicial system of India and other countries. Comparative Analysis of law and statutes implementation in foreign countries and utility of Common Law and Statutory provisions in form of enactment have been relied upon for analysis. Proper citation and relevance of a case with the topic in question has been referred for explicating the averments and supplicating the arguments and comments posited to exemplify the topic of the paper. In comparative analysis with foreign countries, references have been on extant rules/statutes/laws of the countries. The judicial precedents have been the guiding light in this topical discussion as it helped to understanding the evolving facets of Legal framework of the Corporate ecosystem setup and the company law which forms the basis for “Insolvency proceedings” where the objective is to “revive the company from the doldrums of insolvency situation”.

Problem Statement

There are varied processes by which companies do “Restructuring”, it includes *inter alia*, Merger, Amalgamation, Demerger spinoff, Takeover as well as Alliances and Strategic Partnership. British laws supported shareholders primacy. They started experiments with organizations and instruments. Trade and commerce, spices, clothes and crafts were the focus. Industrial revolution encouraged finance and growth among the shareholders. Some quintessential changes which shaped the commerce of the times. Credit structure came into picture. Structure of debt started innovating. Though banking institutions were Companies under Companies Act 2013, but regulations are stringent under RBI and Banking regulation Act. Free Transferability under S.44 of the Companies Act 2013[2] of negotiable instruments were some of the facets which underwent changes with the passage of the time.

A vital aspect of the study is: **Is it possible to spell out the ‘evolving’ role of “Resolution**

[2] S.44 of the Companies Act 2013 states that, “Prospectus or statement in lieu of prospectus to be filed by private company on ceasing to be private company.(1) If a company, being a private company, alters its article in such a manner that they no longer include the provisions which, under clause (iii) of sub- section (1) of section 3, are required to be included in the articles of a company in order to constitute it a private company, the company-(a) shall, as on the date of the alteration, cease to be a private company; and (b) shall, within a period of 2 thirty] days after the said date, file with the Registrar either a prospectus or a statement in lieu of prospectus, as specified in sub-section (2) …”

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Professional" in today's context of Insolvency Proceedings?

Insolvency and Bankruptcy Code Framework

Insolvency and Bankruptcy Code, 2016 is a framework for tackling scenarios where company is in a stress condition. The company is unable to pay debt. Typically, the Capital, debt ratio for manufacturing industry specific companies is in the ratio of 1:2, whereby the debt of company is higher than the capital. But people still invest as industry is futuristic and has the potential to grow. Gestation period in business process may be more. The future potential of cash flow in the promising projects undertaken by the company may be realised after a significant long period of time[3] and sometimes, it becomes a necessity as the competitive forces work in your favour only if you take the "first mover advantage"[4].

II. Dynamic nature of industry

Typically, in a software industry, the Research and Development is a huge area which warrants investment, effort and time. There was significant possibilities of failure, however, investment decision which are long-term oriented without any short term focus could lead to improper strategic decision making. Looking from the prism of 'disruptive technologies' in software domain, investment of technology becomes a determining factor about the potential success which may be in offing for the company. Improper strategic decision with lack of focus, vision, mission and objective would build on to the stress of the company, where its sustenance would itself come in question. Disruptive Technologies in any domain, including for example in Software Industry, are continually shaping the business landscape[5] of Intellectual Property Management. The advent of plenitude of technology such as, Cloud Computing in a distributed network platform, vide Internet of Things (IoT), Artificial Intelligence, Internet of Things, Fuzzy Logic/Decision Trees/Neural Network/Intelligent Systems, Decision Support Systems, Management Information System and Knowledge based System are changing with the passage of time. The strategy should not only be providing credence to jurisprudential understanding, as discussed at length in the present paper, but also strategy should subsume in its ambit multitude of factors pertaining to economic, finance, law and technological advancement. Managing Uncertainty and Risk is key to success in the business ecosystem. Intellectual Property (IP) Management, as an effective tool is a holistic concept which involves planning,

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[3] Hamel G. (1990), Competition for competence and interpartner learning within international strategic alliances, Strategic management journal 12 (S1), pg 83-103

[4] Prahalad, C.K. and Hamel, G. (1990) The Core Competence of the Corporation. Harvard Business Review, pg 79-91

[5] G Hamel, YL Doz, CK Prahalad (1989), Collaborate with your Competitors and Win, Harvard business review 67 (1), pg 133-139

coordination and in inclusive assessment from varied angle including IP Valuation and IP Audit is inherent and imperative requirement for IP Management, Technology change should be dovetailed based on demand pull and technology push economic scenarios, Financial Cash flow assessment and Decision support system holds key to proper decision making along with proper assessment of Marketability of a Product or Process[6] and to reap the benefits, as it provides "First Mover Advantage"[7], as has to be strongly propounded by famed business strategists Gary Hamel[8] and Sumonto Ghosal.

Capital-Debt Ratio

Capital Debt ratio is not market driven but because of regulatory interface, for example absorption of technology could influence others to make compatible products in direct competition, thereby encouraging companies to do Research and Development (R&D). It helps to bring fund, say in the instant case only debt is allowed by Government, so that tech would stay afloat once debt is repatriated back. Debt equity ratio vary based on sector and market specific scenarios. Compliances as mandated by law has to be adhere to. The incubation of value-added technology in varied sectors, for example in vehicle manufacturing sector, considering environmental pollution as one of the criteria influencing the industry, a comparison between electric vehicle and Internal combustion engines running on diesel and petrol and an investment in such specific technology could yield long term result or may be not. Change in technology, regulation and behavioural pattern is changing the industry landscape, which is also influencing factor for the stress build up in an organisation's long-term perspective. Marketability of shares forms a vital point in the analysis of the fair share exchange ratio for the method of valuation as held in ***Miheer H. Mafatlal v. Mafatlal Industries Ltd***.[9] In a scheme of amalgamation, 'appointment date' and 'effective date' have an important role to play. In case of merger of a wholly owned subsidiary with the parent holding company, the parent company need not file petition for sanction to tribunal as held in ***Mahaamba Investments v. IDI Limited***[10]. It is vital to ensure that compliances should be meet with, as seen in the case of ***Marshall Sons and Co. (India) Ltd. vs. ITO***[11], it was held that it is mandatory for every scheme of merger to provide the date of merger as 'appointment date'

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[6] G Hamel, YL Doz, CK Prahalad (1989), Collaborate with your Competitors and Win, Harvard business review 67 (1), pg 133-139

[7] Prahalad, C.K. and Hamel, G. (1990) The Core Competence of the Corporation. Harvard Business Review, pg 79-91

[8] Hamel G. (1990), Competition for competence and inter-partner learning within international strategic alliances, Strategic management journal 12 (S1), pg 83-103

[9] Miheer H. Mafatlal v. Mafatlal Industries Ltd. (1996) 87 Com Cases 792 (SC)

[10] Mahaamba Investments v. IDI Limited (2001) 105 Comp. Cases 16 (Bom)

[11] Marshall Sons and Co. (India) Ltd. vs. ITO (1996) 223 ITR 809 (SC)

while filing application of the same with Tribunal.

Porter Five Force Analysis

The five forces in a marketplace have to be viewed from the prism of firstly, the core aspect of competition rivalry; secondly, the bargaining power of the supplier in the value chain of business ecosystem; thirdly, the 'buyer bargaining power' has to be factored in; fourthly, barriers to entry in the marketplace via. Threat of substitution; and finally the fifth aspect, threat of new entry of players have to be necessarily analysis, reviewed and reassessed in a detailed manner so that the demand and supply side in any management endeavor is comprehensively studied, before venturing into any kind of strategic decision making process.

Creditor's Role in Insolvency

Creditors are worried leading to Insolvency as they trigger the process. Insolvency process is triggered by creditor and is basically tailored to protect their interest. All stakeholders including the common people, stakeholders, creditors 'secured' or 'unsecured' have a contesting interest, which set the ground for 'equitable balancing exercise' between stakeholders, whereby they are to be treated equitably in this process. Insolvency code brings equity and balance. In some countries primacy to creditors or laborers or workers or government acquires credence. The various models which are at vogue in various parts of the globe include *firstly*, the Government model of Insolvency in Scandinavian countries and work in continental countries too where the primacy is to look at the interest of the trade union and labour market; *secondly*, Market model of Insolvency, which is influenced by market factors among others; *thirdly*, Creditor model of insolvency, where the financial and operational creditors are having the primacy to trigger the insolvency proceedings; *fourthly*, the Stakeholder model of Insolvency looks holistically to the stakeholders in the value chain of the business ecosystem. Balance is tilted based upon the choice of the insolvency model adopted. Code of Insolvency is also influenced by social political and economic condition of country. The "Japanese Keiretsu model" had a profound effect on the Indian set up[12]. In India, Board for Industrial and Financial Reconstruction (BIFR) used to decide which companies to revive. In India, creditors are institution driven via. bank as that time where they were captive with 51% equity stake held by government and family companies. Market model is not good in general as no promoter would not like to lose control of organisation. In India, primarily the companies were either family-owned concerns or Government run before the inception of Liberalization, Privatization

[12] "Japanese Keiretsu model" had a profound effect on the Indian set up as it influenced the board with Government policy also given primacy in such model.

and Globalisation in early 1990's.

III. Harmonious attempt of tackling insolvency

Attempts to bring insolvency law to help reorganize of insolvency process has been in vogue for a significant long period of time, however the focus has been changing with the passage of time. Earlier in 1970s, to revive and protect the industries, mostly manufacturing industry was priority.as they were indigenous industries and was based on the industry labour model of generating employment to the huge labour base. Less competition from few industries in some sectors from internal industries and parallel import, with restrictions to import from other countries, large number of licensing as approval were required, changed the scenario as the Industries Development and Regulations Act 1951 came to fore. Central Government had the power to decide the sector where license is being provided ushering in the License Raj regime. Other considerations for protecting the labour sector and the jobs for the engaging employed youth was another factor which weighed in for the lager interest of the economic well-being of the populace. Government acquisition of sick industries in 1970s to 1980s to acquire sick industries, especially the Public Sector Units (PSUs) has a tremendous influence on the decisions of the companies at that time. It is commonly believed that Government could run these companies. Another factor which had a bearing, was the better control to financial institutions which was with the objective to bring professionalism to industrial process. There was a growing clamour that India following the Nehru-Mohalanobis model was looking to erstwhile Soviet Union for the socialist model of development of the economy. Some opine Government wanted to bring Japanese model, that is the ***'keiretsu system'.*** As the control of government via these governed owned or heavy staked financial institutions would be efficient in tackling the situation for multiple perspective including firstly, how to determine sick industry; secondly, who would be capable to determine sickness and; thirdly, concept of revival where public financial institutions would engage in the well-being of the company, so in that accord they became important stakeholder in the value chain of the development of the business ecosystem.

Now, the vital question which came up was how to determine sickness. In this context, the erosion of capital, if company sustains loss for three consecutive years had its impact on capital. Creditors or Board of directors would determine erosion of capital refer back to Board for Industrial and Financial Reconstruction (BIFR), where the BIFR would determine sickness. If the BIFR decides that the answer to sickness of the company is in affirmative, then it would develop plan for revival. However, talk to bring public financial institutions to play a role in

revival of company became an important factor. It took too much time to understand the sickness reason or evolve plan to revive. The failure is long delay as remaining assets depreciated or destroyed, which undermined the very purpose of 'revival plan'. Failure to expedite the resolution lead to long litigation of the nature of civil dispute in Courts, adding to the ordeal. The second reason, promoter led board got opportunity to siphon off the fund and refer to BIFR leading to a chaotic situation and the ground for promoters to highly misused the fund as till BIFR decided the fate of the case, till that time of BIFR's decision, the promoters were safeguarded. However, it created a bad signal for the budding entrepreneurial culture in the country. There were addition issues of lack of expertise and foresight about industry, which did not augur well for the industry. Still, BIFR sustained for close to 30 years from 1985 to 2016. It did not yield much result. However, not all was lost in vain as it left with lot of learnings. Justice Iradi committee recommendation for setting up the Company Law Tribunal (CLT) and also paved the way to look into the role of officer liquidator. Prof. ML Mitra committee setup by RBI to recommend for Cross border insolvency laws into India also formed the backdrop in which the quintessential role of resolution professional was strengthened. Insolvency law is perceived to reorganize the company and enterprise by recapitalization and reorganization.

However, the backdrop had its second stage with the induction of Sick Industrial Companies Act of 1985 (SICA), though it too was not so successful and left with lot of learning. The third stage the Government made external attempted to "secure the financial institutions ", rather than recapitalization or reorganization. This policy put huge burden on financial organisations. As people, secured loan either before or after reorganization and they did not pay back the loan. So, most of the financial organizations including the Scheduled banks under S.7 of Banking Regulation Act, 1949 or Non-Banking Financial Companies (NBFC) got stressed up Non-Performing Assets (NPA). So, banks were also stressed up. How to make health of banks better was the primary focus and emphasis in the third stage.

In the third stage, the recovery of debts due to bank and financial institutions under the Recovery of Debts And Bankruptcy Act, 1993 created a tribunal and Appellate tribunal setup. The idea was to take away from civil court to fast-track court for speedy redressal of the issues[13]. Seen in the backdrop was the banking reform committee, Narasimhan committee report which had a profound influence in the future of such cases. It is pertinent to note that civil cases of industrial loans went to these tribunal. Another attempt to "securitize the loan",

[13] Recovery of Debts And Bankruptcy Act, 1993

people started telling bank not capable to recover loan, a special purpose vehicle (SPV) as Asset Restructuring company (ARC) brought the act of securitization and reconstruction of financial assets and enforcement of Security interest Act 2002, commonly called the SARFAESI Act[14]. Bank would define when loan is NPA as per the guidelines provided by RBI[15] u/d the aforesaid Act[16], then NPA would be sold to qualified institutional buyers (QIB) by cash or security that is pay through (cash) or pass through via. security[17]. The wider objective was to maintain liquidity of bank. This was a failure as this liquidity did not happen as absence of debt market or rather an immature debt market in India at that time. It is pertinent to note that in a famed case of ***Saraswati Industrial Syndicate Ltd. v. CIT***[18], it was held that when two companies amalgamate, then the transferor company loses its identity. For amalgamation, pursuant to Tribunal's order sanctioning the scheme, the transferor company stands dissolved without having to go through the process of winding up or liquidation.

LIC[19], UTI[20] and SBI[21] giving loans to industry at the same time also buying bad loan, QIB[22] allowed to access debt market they are allowed to raise debenture or other securities to fund via IPO[23] or FPO[24]. but in India no such concept as in US, had taken shape and hence, it did not take off. It is vital to note that the role of ARC[25] was to get NPA[26] from bank and give security to QIB who in turn gave it back to banks as it tried to go for Recovery via. negotiation, litigation, muscle power through appointment of recovery agents did not augur well with the financial and economic setup of that times. After RBI came up with informal solution of involving bank as " lender consortium" was solution which got mixed response from the experts of those time. The questions were how and on what grounds the scheme was being framed without going into tribunal to reframe loan structure was the moot point, nonetheless the guideline of negotiation between stakeholders and primarily the creditor growing role in the decision making was shaping up at that time. Another approach was how quickly to liquidate so that it has be re-deployed. The first phase is of restructuring the company via. reorganization, while the second phase is to secure via induction of fresh blood in financial

[14] Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002
[15] Reserve Bank of India
[16] Ibid.
[17] Ibid.
[18] Saraswati Industrial Syndicate Ltd. v. CIT (1991) 70 Com Cases 184 (SC)
[19] Life Insurance Corporation of India formed by an Act of Parliament in 1st of September, 1956.
[20] Unit Trust of India established by an Act of Parliament in 1963
[21] State Bank of India established by State Bank of India Act, 1955
[22] Qualified Institutional Buyers accessing the debt market through instruments.
[23] Initial Public Offer
[24] Follow on Public Offer
[25] Asset Restructuring Company
[26] Non-Performing Assets of the bank and financial institutions

institutions. The scenario comes into play if it is not possible to come out with a solution. Three facets which have a bearing include, firstly, Central Government control in market; secondly, Market condition and thirdly, Ownership structure. Objective of Insolvency is either to liquidate or to revive the company.

IV. POWER OF REGULATING PROFESSIONAL AND WINDING UP

Process is diverse in Companies Act, 2013 under Insolvency and Bankruptcy Code (IBC), 2016, as two types of Creditors are identified that is, Operational creditors and Financial creditors. The objective of IBC is to rationalise conflicting interest of creditors. It is famously called that the Conflict between the Commons, who have secured interest over companies' assets and the Anti-commons. The fixed charges include the charges which has been created by contract. Remedy is simply recovery of assets by liquidating of charges, that is freeze assets and sell that by court order to recover debt. Secured creditor have an upper hand that is why law during the British times called them as 'Commons'. There can be "unsecured creditor" also. As they do not have charges over company, anti-commons as they are commonly referred to; they too have a say on the portion of the assets they are being liquidated. It is vital to note that they can be 'financial creditors' also. Assets are limited, as there is no mitigation in this context, so there are long term litigation to decide the fate of the assets. With time, asset value is devalued. So, it is quintessential to note that the creditors are not homogeneous group as such.

V. GROWING ROLE OF RESOLUTION PROFESSIONAL

Resolution Professional allowed to participate in insolvency and liquidation process, need to have qualifications. It can be firm or individual. If it is a firm, then it is qualified resolution professional; however, in case of the individuals, he has to be qualified to be as an Advocate, Chartered Accountant, Company Secretary, Financial experts as they have to take examination and post which taking passing the examination, they qualify to be fit for 'resolution professional'. Resolution Professional qualifications examinations are conducted by Insolvency and Bankruptcy Board of India (IBBI). IBBI also prescribes regulations regarding their conducts. They have specific responsibilities and duties during the insolvency proceedings. Drawing a comparative law analysis, in the realm of company law, Compliances becomes the vital pillar in this endeavour as Company Law is all about set of compliances and disclosures, as seen in the case of ***Re. Haycraft Gold Reduction and Mining Co.***[27], where it was held that, "*subject to provisions of extant law, only on the authority of resolution of the*

[27] Re. Haycraft Gold Reduction and Mining Co. (1897) 2 Ch. 230 (Australian Judgment)

Board of Directors and if the managing director, manager, secretary or other officer calls for a meeting without due diligence and without any authority, then it would not be effectual unless the Board ratifies the meeting before it is being held…" In Indian context, as held in ***Johny Ghandy v Catholic Syrian Bank Ltd***.[28] (1995) 84 Com Cases 520, that, "*the directors have the power to postpone the date of the meeting…*"

VI. STAGES IN INSOLVENCY PROCEEDINGS

There are three stages in Insolvency proceedings during which the status of Insolvency Resolution Professional status changes. In the first stage, they are known as 'provisional resolution professionals'; while in the second stage they become 'resolution professional' and in the third stage, if the proposed resolution do not go through, they become 'liquidator' of company. Their duties include *inter alia*, *firstly*, arrange meeting of the Committee of Creditors (COC); *secondly*, take control of company operations and assets and hold it in trust called as the "Insolvency Trust"; *thirdly*, they are privileged to go for Executory contract on behalf of the company going through insolvency proceedings. Thus, the Resolution Professional has the power to reject executory contract, that is contract entered by management of company just before commencing of insolvency process; and *fourthly*, running companies as ongoing concern until handed over to new buyer or new management. Resolution professional steps into shoes of company's management by running the company as an ongoing concern.

VII. CONCLUSION

An analogy could be drawn, just as it is important to take control of a wrecked ship from high sea to dock for repair and then relaunch the 'refurbished' ship again to high sea. As per S.25 of Companies Act 2013, the duties of resolution professional, to preserve and protect the asset of corporate debtor and to continue the business is a vital aspect in its journey to revive the company during the insolvency proceedings. And take custodian control of corporate debtors including business record as a quintessential role of a resolution professional. They can also appoint accountants and legal professionals. For the protection of Minority Rights, Section 241(2) application came up in ***Union of India v. Satyam Computers Ltd***.[29], with the application of Section 408 of Companies Act 1956 when the Central Government may by itself apply to the tribunal so as to ensure that it is neither prejudicial to public interest, the company nor prejudicial or oppressive to the members. When read with provisions of IBBI, the steps that the resolution professional undertake include, *firstly,* conducting the meeting of Committee of

[28] Johny Ghandy v Catholic Syrian Bank Ltd. (1995) 84 Com Cases 520
[29] Union of India v. Satyam Computers Ltd. (2009) 148 Comp. Cases 252

Creditors (COC); *secondly,* preparation of information memorandum as per S.29[30]- enables the bidder company to bid for the company; *thirdly*, bid for debtor company by process of law controlling share would be transferred from promoter or whoever is having control of company. Bid tells how company would be refinanced, recapitalized and as to how control of management would be transferred and *modus operandi* of payment of the debts to creditors; *fourthly*, there would be submission of Resolution plan as per S.30; *fifthly*, approval of Resolution plan in line with S.31. It is important to note that adjudication process was based on the report of the resolution professional the tribunal, National Company Law Tribunal (NCLT) takes into consideration the equitable matters as they come into picture. It is important to note that the decision of the tribunal is binding on the stakeholders including the creditors, as such legally the tribunal gives the stamp that insolvency process is complete and a fresh *de novo* management would look after the company as the it is revived from the state of insolvency, the very objective of the insolvency processing what was aspired for. All in all, as in the aforesaid analogy, the certificate from the tribunal which is being sent to Registrar of Companies is an authoritative stamp that the ship is okay to go to high sea in its new 'refurbished' avatar.

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[30] Sec. 29 of the Companies Act, 2013