REPORT
OF THE
INSOLVENCY LAW COMMITTEE
ON
PRE-PACKAGED
INSOLVENCY RESOLUTION
PROCESS

JULY, 2021

Ministry of Corporate Affairs
Government of India

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REPORT OF THE INSOLVENCY LAW COMMITTEE ON PRE-PACKAGED INSOLVENCY RESOLUTION PROCESS

New Delhi, the 16th July, 2021

To,

The Honourable Union Minister of Finance and Corporate Affairs

Madam,

We have the privilege and honour to present this fourth part of the report of the Insolvency Law Committee, set up on 16th November, 2017 (reconstituted on 6th March, 2019 as Standing Committee) to make recommendations to the Government for Pre-Packaged Insolvency Resolution Process framework.

2. The Committee had the benefit of the comments received from public and participation by various institutes, industry chambers and experts in various disciplines. An attempt has been made to provide a comprehensive framework in order to provide a speedier, cost effective, semi-formal and less disruptive mechanism for insolvency resolution of MSME corporate debtors in distress.

3. We thank you for giving us this opportunity to put together our views to design a vital framework for insolvency resolution of stressed MSME corporate debtors which is need of the hour due to disruption caused by COVID-19 pandemic worldwide, including India.

4. We believe pre-packaged insolvency resolution framework will ensure positive signal to debt market, employment preservation, ease of doing business and preservation of enterprise capital.

Your Sincerely,

(Rajesh Verma)
Chairman

(Dr. M. S. Sahoo) Member	(Pankaj Jain) Member Rep. DFS	(T.K.Vishwanathan) Member	(U. K Sinha) Member
(Saurav Sinha) Member Rep.	(Ch. S.S. Mallikarjuna Rao) Member Rep.	(Uday Kotak) Member	(Bahram Vakil) Member
(Shardul Shroff) Member	(President ICAI) Member	(President ICSI) Member	(President ICoAI) Member

Gyaneshwar Kumar Singh, Member Secretary

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PREFACE

In the five years since its enactment, the Insolvency and Bankruptcy Code, 2016 (IBC/ the Code) has brought about a significant shift in credit and recovery behaviour. As compared to the previous insolvency and reorganisation frameworks, the IBC has aided in higher credit realisations and quicker recovery of businesses. Notably, it has aided economic growth by freeing up capital in failed businesses and has changed the way the Indian society perceives business failures. While the enactment of the Code has itself had significant economic and social impact, prompt amendments to the law to alleviate difficulties in implementation have kept it relevant and sensitive to the needs of the market. The enactment of the Code and its swift implementation played an indisputable role in improving India's performance in the World Bank's Ease of Doing Business ranking from 130 in 2017 to 63 in 2020. India has also received the acknowledgment of being amongst the 10 economies that have improved the most on the ease of doing business scale after implementing regulatory reforms.

The Code being an economic legislation has continuously evolved through the empirical learnings from its implementation and developments made thereof. For this purpose, the Insolvency Law Committee has been constituted by the Ministry of Corporate Affairs, which has provided three sets of recommendations towards the continuous strengthening of the provisions of the Code. The latest session of the Committee took place in the midst of Covid-19 pandemic. The impact of the pandemic and ensuing lockdowns on the global economy has been severe, and India is no exception to the same. In order to combat the impact of the Covid-19 pandemic, several stimulus measures have been taken by the Central Government with the aim of providing relief to affected companies and promoting recovery from the financial stress. In order to mitigate the immediate threat of stressed corporate entities from being pushed into insolvency proceedings, the minimum amount of default for initiating CIRP was increased from one lakh rupees to one crore rupees. Further, the filing of applications for initiating insolvency proceedings for any default occurring during the period from 25.03.2020 to 24.03.2021 was suspended.

In addition to the aforesaid measures, the Central Government undertook various relief and credit support measures for MSMEs and indicated the notification of a special insolvency resolution framework for corporate MSMEs under the Code. MSMEs play a significant role in the Indian economy by providing employment and contributing to the gross domestic product. Like other sectors of the economy, MSMEs were severely affected by the pandemic. Even before the current crisis, due to the unique nature of corporate MSMEs, the Committee had recommended special measures for treatment of corporate MSMEs undergoing CIRP. Their simpler business structures, limited access to finance and resulting sensitivity to socio-

economic instability make them more vulnerable to economic shocks and failures, which may be difficult to resolve under the regular insolvency process. Accordingly, the Committee considered that the time was ripe for providing an efficient alternative insolvency resolution framework for addressing the concerns of corporate MSMEs.

Owing to the specific attributes of MSMEs, there has been global recognition of the value of a hybrid insolvency process that is simpler, low-cost and time-efficient. In October 2020, a sub-committee of this Committee, proposed a detailed scheme of a pre-packaged insolvency resolution process. The Committee studied the recommendations of the sub-committee and found it suitable to recommend the Government to design a pre-pack process as a viable alternative framework for insolvency resolution of corporate MSMEs building on the sub-committee's suggestions, but with several modifications as outlined in this report. It offers a simple, less rigid, cost-effective, and accessible insolvency process that is least disruptive to the continuity of the business of the corporate MSMEs and promotes preservation of employment. Accordingly, this Report provides recommendations of the Committee on the legal design of a pre-pack process for corporate MSMEs for inclusion in the Code.

The recommendations of the Committee seek to provide a pre-pack process for corporate MSMEs which is voluntary in nature. The business and viability of corporate MSMEs is best understood by their promoters and original management. Given this, the pre-pack process adopts a hybrid model of debtor-in-possession with creditor-in-control features. Such debtor participation will incentivise timely detection and resolution of stress and cause minimum disruption to business operations. In order to address issues related to debtor's moral hazard and for balancing creditor-debtor interests, the legal design for pre-pack process retains the core elements of the CIRP and provides certain additional safeguards. The salient features of the process are as follows:

(i) *Eligibility and pre-initiation requirements* – The pre-pack process will be available only for corporate MSMEs who have committed a default of at least one lakh rupees. The Central Government may notify a higher default threshold up to one crore rupees. To maintain the sanctity of the process, errant corporate debtors that are ineligible as per Section 29A of the Code are not permitted to initiate the process.

(ii) *Pre-initiation requirements* – The pre-initiation stage will be a combination of formal and informal mechanisms to ensure a consensus-based initiation. A resolution professional should be proposed by unrelated financial creditors of the corporate debtor to oversee due compliance with the pre-initiation requirements. At the pre-initiation stage, the corporate debtor is required to prepare and share a base resolution plan with its unrelated financial creditors. Thereafter, the unrelated financial creditors will approve the filing of an

application for initiation of the process. The corporate debtor will also obtain appropriate internal approvals for initiation.

(iii) *Initiation of the pre-pack process* – After completion of the pre-initiation requirements, the corporate debtor will file an application for initiation along-with appropriate documents before the Adjudicating Authority (AA). The AA will either admit or reject the application within a period of fourteen days. When the application is admitted, the AA will (i) order a moratorium, (ii) appoint a resolution professional, and (iii) cause a public announcement. The pre-pack process should be completed within a total of 120 days from the date of the order of admission, which is divided into two parts - (i) 90 days for the conduct of pre-pack process, and (ii) 30 days for adjudication before the AA.

(iv) *Conduct of the pre-pack process* – The pre-pack process should provide for a simplified and faster claims verification process without compromising the sanctity of the claims collation process. The original management of the corporate debtor will continue to manage its operations, and the entire process will be conducted by the resolution professional with appropriate oversight of the committee of creditors (CoC). The CoC will also maintain supervision over the management of the corporate debtor by retaining the power to take key decisions related to running its business during the process.

(v) *Consideration and Approval of Resolution Plans* – The corporate debtor will submit a base resolution plan, which will compete with the resolution plans received from the market. In case the base resolution plan is sought to be approved through a non-competitive process, it should provide for full payment of the claims of the operational creditors. Further, where the base resolution plan is being approved and does not provide for full payment of claims of the creditors, the CoC may require promoters to dilute their equity interests or otherwise, provide reasons for the same. The resolution plan approved by the CoC, shall be submitted to the AA for its approval. Once approved by the AA, the resolution plan should be binding on all the stakeholders and receive similar treatment to a plan approved under the CIRP.

(vi) *Closure of the pre-pack process* – The pre-pack process will close in four possible scenarios - (i) approval of resolution plan by the CoC and the AA; (ii) simpliciter termination of the pre-pack process by the AA either on completion of time period or on request of the CoC; (iii) initiation of CIRP by the AA on request of the CoC; and (iv) initiation of liquidation proceedings by the AA in exceptional circumstances.

In recognition of the unique importance of corporate MSMEs to the Indian economy and taking into account the end of the suspension of the provisions related to CIRP on 24th March 2021, the Central Government took quick steps to implement the recommendations of this Committee through the Insolvency and Bankruptcy Code (Amendment) Ordinance, 2021. It must be emphasized that the pre-pack process represents an effective addition to the insolvency resolution framework under the Code. While the IBC in itself has served as a

significant and game-changing economic and legislative reform, it is hoped that the pre-pack process furthers another phase of much-needed structural reform, especially for small businesses and leads to the development of a robust market-driven resolution mechanism for corporate MSMEs.

I am confident that this Report will aid in understanding of the pre-pack process. Its implementation would need to be closely monitored so as to ensure that it functions as a robust and effective framework for resolving the financial distress of corporate MSMEs.

Rajesh Verma
Secretary, Ministry of Corporate Affairs &
Chairman, Insolvency Law Committee
New Delhi, July 16, 2021

ACKNOWLEDGMENTS

The Insolvency Law Committee takes this opportunity to submit the fourth part of its Report for recommending a framework for Pre-Packaged Insolvency Resolution Process which provide the stressed MSME corporate debtors with an alternative route for resolving insolvency. The Committee would like to thank the industry chambers, professional institutes, law firms, academicians and other experts who made valuable suggestions for review of the Code.

The Committee expresses its gratitude to the members of Insolvency Law Committee, for their valuable contribution in the review process, and for their participation, deliberations particularly including with respect to drafting of the said framework.

The Committee acknowledges the research support provided by the team from Vidhi Centre for Legal Policy comprising of Mr. Debankshu Mukherjee, Ms. Aishwarya Satija, Ms. Manmayi Sharma, Mr. Oitihjya Sen and Mr. Akash Jauhari

The Committee is grateful to Ministry of Corporate Affairs for providing logistical support and would like to make a special mention of the dedicated efforts put in by the team of officers of the Insolvency Division at the MCA comprising Mr. Rakesh Tyagi, Director, Mr. Satyajit Roul, Joint Director, Mr. Saurabh Gautam, Deputy Director, Ms. Sunidhi Misra, Assistant Director, Mr. Sourav Sardar, Assistant Manager, and Ms. Parul Chautani, Research Associate for collating suggestions, facilitating discussions and providing administrative and technical support for the functioning of the Committee.

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LIST OF DEFINED TERMS

BLRC	Bankruptcy Law Reforms Committee
BLRC Report	Report of the Bankruptcy Law Reforms Committee, Volume I (2015)
CA, 1956	Companies Act, 1956
CA, 2013	Companies Act, 2013
CIRP	Corporate Insolvency Resolution Process
CoC	Committee of Creditors
Code/ IBC	Insolvency and Bankruptcy Code, 2016
Committee	The Insolvency Law Committee
IBBI	Insolvency and Bankruptcy Board of India
IMF	International Monetary Fund
Rs.	Rupees
MCA	Ministry of Corporate Affairs
MSMEs	Micro, Small & Medium Enterprises
NCLAT	National Company Law Appellate Tribunal
NCLT	National Company Law Tribunal
OECD	The Organisation for Economic Co-operation and Development
RBI	Reserve Bank of India
Report	Report of the Committee
Sub-committee	The Sub-Committee of the Insolvency Law Committee constituted to propose a detailed scheme for implementing a pre-pack and pre-arranged insolvency process
Sub-committee Report	Report of the Sub-Committee of the Insolvency Law Committee (October 2020)
SICA	Sick Industrial Companies (Special Provisions) Act, 1985
UK	United Kingdom
UNCITRAL	United Nations Commission on International Trade Law
UNCITRAL Legislative Guide	United Nations Commission on International Trade Law, Legislative Guide on Insolvency Law Part II (2004)
US	The United States of America

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CHAPTER 1 - BACKGROUND

I. Introduction

1.1. The enactment of the Code in May 2016, overhauled and consolidated the fragmented and inefficient insolvency resolution framework in India. Part II of the Code introduced what has now been described by the Hon'ble Supreme Court, as a paradigm shift in the corporate insolvency regime,[1] by establishing a time-bound, creditor-in-control framework aimed at maximizing the value of assets and balancing the interests of all stakeholders concerned.

1.2. The enactment of the Code also paved the way for a series of unceasing efforts by this Committee, that was constituted by the MCA on 16 November 2017, to periodically evaluate the insolvency framework and the functioning of the Code.[2] Since its constitution, the Committee has, in numerous meetings, and through three prior reports, taken stock of the functioning of the Code, and highlighted issues and recommendations addressing the efficacy and implementation of the corporate insolvency, liquidation and individual insolvency processes under the Code.[3]

1.3. Thus, the Indian insolvency ecosystem has evolved significantly over the five years of the implementation of the Code. The Code in itself has been amended in quick response to emerging issues and in line with changing market realities to further the primary objectives of the Code, i.e., time-bound insolvency resolution, promotion of entrepreneurship and availability of credit and to balance the interests of all stakeholders.

1.4. The growing maturity of the insolvency ecosystem has significantly improved the corporate insolvency landscape and redefined the debtor-creditors relationship. The increasing stability and robustness of the corporate insolvency framework has also given the market the required confidence and appetite to undertake stress resolution mechanisms that do not require recourse to the formal process of the Code. For instance, there is a growing trend towards early resolution of stress as

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[1] *See Innoventive Industries v ICICI Bank*, (2018) 1 SCC 407

[2] Order of the Ministry of Corporate Affairs, (November 16, 2017) <http://www.mca.gov.in/Ministry/pdf/constitutionOrder_17112017.pdf> accessed 6 June 2021

[3] Reports of the Insolvency Law Committee dated March 2018, October 2018 and February 2020

there is a rise in the number of settlements, in the shadow of the Code.[4] In fact, predicting such evolution of the insolvency eco-system, the BLRC Report had indicated that pre-packaged rescue or sales could eventually be allowed "*as part of NCLT supervised scheme of arrangement and operationalised through rules at an appropriate stage after wider consultation with the stakeholders*".[5]

1.5. However, with the advent of the Covid-19 pandemic, India, like many other countries, had to suspend the operation of the Code for a period of one year,[6] so as to prevent a wave of forced insolvencies and liquidations of corporate firms reeling under the stress of the pandemic. This circumstance also had the effect of catalysing the need for hybrid and alternative frameworks for quick insolvency resolution and exit.

1.6. Taking stock of the situation, the MCA constituted a Sub-committee of this Committee to propose a detailed scheme for implementing a hybrid insolvency mechanism, in the form of a pre-packaged insolvency resolution process under the Code.[7] A Sub-committee was thus constituted on 24th June, 2020, which, after detailed discussions, conceptualized the design for a pre-packaged insolvency resolution framework, in its report submitted on October, 2020.

1.7. The report of the Sub-committee was put out for public comments, and thereafter, in line with earlier practice, the Committee consolidated all such views and recommendations from several stakeholders; deliberated upon the framework suggested by the Sub-committee and considered international best practices. The Committee had also to heed the urgent domestic requirements expected from an alternative insolvency resolution framework. Owing to the suspension of the Code, and raising of the default threshold for the CIRP, many pandemic-affected MSMEs did not have access to the Code during its suspension and needed access to quick

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[4] Rajya Sabha, Synopsis of Debate, Response of the Union Minister of Finance and Corporate Affairs (September 19, 2020) p. 182 <http://164.100.47.5/newsynopsis1/Englishsessionno/252/Synopsis%20_E_%20dated%2019.09.pdf> accessed 11 June, 2021

[5] Ministry of Finance, *Interim Report of the Bankruptcy Law Reforms Committee* (2015) p. 25 and 79 <https://ibbi.gov.in/uploads/resources/BLRCReportVol1_04112015.pdf> accessed 1 June 2021

[6] By virtue of Section 10A of the Insolvency and Bankruptcy Code, 2016, as amended by the Insolvency and Bankruptcy Code (Second Amendment) Act, 2020

[7] Office order of the Ministry of Corporate Affairs dated 24 June 2020, requiring 'Constitution of sub-committee of Insolvency Law Committee to propose a detailed scheme for implementing prepack and prearranged insolvency resolution process'

and affordable resolution or exit mechanisms. In response to this situation, the Central Government had announced plans to notify a special insolvency framework for MSMEs under Section 240A of the Code.[8]

1.8. In deliberating the recommendations of the Sub-committee, the public responses to it, and the urgent domestic requirements for stress resolution of MSMEs, the Committee recognized that the pre-packaged insolvency resolution process, being an alternative, semi-formal, quick and cost-effective mode of corporate insolvency resolution, could well address the needs of pandemic affected corporate MSMEs, which being the backbone of our economy, are arguably one of the most important stakeholders.

1.9. Thus, building on the recommendations of the Sub-committee, the Committee has recommended the design and implementation of an alternative and effective pre-packaged insolvency resolution framework for MSMEs in this Report. It recommends a framework that seeks to supplement the basic and most successful elements of the existing corporate insolvency framework, in a way that is tailor-made to provide for quick and cost-effective insolvency resolution of MSMEs. Considering the urgency to provide an alternative insolvency resolution framework for pandemic-affected MSMEs and lifting of the suspension of provisions related to the CIRP on 25th March, the President promulgated the Insolvency and Bankruptcy Code (Amendment) Ordinance, 2021 on 4th April 2021. This Ordinance implements the recommendations of the Committee which have been encapsulated in this Report.

II. Working Process of the Committee

1.10. The Committee had its first meeting on 14th May 2020. It had further meetings on 28th January 2021, 3rd February 2021, 4th February 2021, and 6th February 2021.

1.11. The MCA, on 8th January 2021 had invited comments from the public on the pre-packaged framework recommended by the Sub-committee through an online facility available on the websites of the MCA and the IBBI, up till 22nd January 2021, which was the last date for submission of comments. The MCA also consulted with other regulators and ministries, i.e., the IBBI, the Department of Financial Services,

[8] Government of India, 'Speech of Nirmala Sitharaman Minister of Finance' (February 1, 2021) <https://www.indiabudget.gov.in/doc/Budget_Speech.pdf> accessed 1 June 2021

the Department of Economic Affairs, and also the Ministry of Micro, Small and Medium Enterprises.

1.12. The MCA engaged the Vidhi Centre for Legal Policy to assist the Committee by providing research on the relevant legal principles and international jurisprudence, and to assist the Committee in drafting this Report.

III. Structure of the Report

1.13. The Report is divided into 7 chapters -

a. The present Chapter, i.e., Chapter 1, provides a brief introduction, context to the contents and recommendations of this Report. It also details the working process of this Committee, and in the instant paras, details the structure of this Report.

b. Chapter 2 details the need for a pre-pack process for MSMEs, by outlining the contemporary understanding and international practices in implementing pre-pack processes and also details the design principles adopted by the Committee in furthering its recommendations.

c. Chapter 3 details the Committee's recommendations on the eligibility requirements for corporate debtors to opt for the pre-pack process. It also details the pre-initiation requirements that need to be fulfilled – such as obtaining approvals from specific stakeholders – before the corporate debtor can file an application for initiating the pre-pack process.

d. Chapter 4 details the recommendations of the Committee in relation to the initiation of the pre-pack process as well as the effects of such initiation, such as declaration of moratorium and time-limit for the pre-pack process.

e. Chapter 5 deals with recommendations of the Committee regarding conduct of the pre-pack process. It details the role and involvement of management of the corporate debtor, the CoC as well as the resolution professional.

f. Chapter 6 deals with the recommendations of the Committee regarding consideration and approval of resolution plans under the pre-pack process. It also details recommendations of the Committee in proposing

a new methodology for invitation, selection and consideration of resolution plans, akin to the Swiss challenge method.

g. Chapter 7 deals with the recommendations of the Committee regarding the closure of the pre-pack process. It provides for different scenarios in which a pre-pack process may come to an end and consequences thereof.

CHAPTER 2 – NEED FOR PRE-PACKAGED INSOLVENCY RESOLUTION PROCESS FOR MSMES

I. Background

2.1. The COVID-19 pandemic and consequent lockdowns have been a shock to the economy – leading to increasing unemployment, lowering demand, and recurring disruptions in multiple sectors.[9] Although some sectors are now on the path to recovery, the effect on smaller businesses has been disproportionate.[10] The RBI Financial Stability Report released in January 2021 notes that *"The continuing adverse impact on MSMEs due to lack of cash flows, low demand, lack of man power and lack of capital could lead to prolonged stress in the sector and large-scale permanent closure of units with associated implications for employment."*[11] This is especially concerning in the Indian context where MSMEs are considered to be the *backbone* of the country's economy.

2.2. The Government has taken various measures to ease the distress faced by MSMEs.[12] However, it is often more difficult for MSMEs to combat macroeconomic shocks than it is for larger enterprises. While larger businesses tend to be robust in a variety of legal and regulatory climates, MSMEs' ability to survive and thrive is vastly sensitive to the quality of their environment.[13] For example, the OECD has observed that MSMEs are particularly vulnerable to macroeconomic and financial shocks,

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[9] *See* Krishnarajapet V. Ramaswamy, 'Impact of COVID-19: Micro, Small and Medium Enterprises in India, Pandemic Shock of COVID-19 and Policy Response: A Bird's Eye View' (Korea Institute for International Economic Policy, 2020) <http://www.igidr.ac.in/wp-content/uploads/2021/02/opinionPaper.pdf> accessed 1 June 2021

[10] ibid

[11] Reserve Bank of India, 'Financial Stability Report' (January 2021) p. 83 <https://www.rbi.org.in/Scripts/PublicationReportDetails.aspx?UrlPage=&ID=1162> accessed 1 June 2021

[12] For instance, widening the scope of the definition of 'MSME' wherein the investment limit has been revised upwards, an additional criterion of turnover has been introduced, and the distinction between manufacturing and service sector enterprises has been eliminated. *See* Reserve Bank of India, 'Covid-19 and its Spatial Dimensions in India' <https://rbidocs.rbi.org.in/rdocs/Publications/PDFs/03CH_271020206C458AE369944258A62779FF5A2F5362.PDF> accessed 1 June 2021

[13] Ronald B. Davis and others, *Micro, Small, and Medium Enterprise Insolvency: A Modular Approach* (1st edn, Oxford University Press 2018) p. 1

noting that MSME insolvencies in Denmark, Italy, Spain, and Ireland exceeded 25 percent in 2007-2008.[14] Moreover, the nature of MSMEs makes them more susceptible to fail or shut down in times of financial distress. For example, they often lack collateral and have undiversified suppliers and consumers, leading to lower access to finance and more dependence on counterparties for survival.[15]

2.3. Therefore, access to an effective insolvency law is crucial for MSMEs to survive financial crises. Considering this, the Minister of Finance and Corporate Affairs had announced that a special insolvency framework for MSMEs would be notified utilizing Section 240A of the IBC.[16] **The Committee noted the adverse impact that the pandemic has had on MSMEs and agreed that it would be beneficial to explore an insolvency mechanism which caters to the needs of MSMEs.**

2.4. Considering that the thrust of the enforcement under the Code has been on resolving corporate insolvency and the jurisprudence in this regard has substantially settled, it was felt that an effective alternative for corporate MSMEs may now be carved out. Therefore, the Committee has focused on finding an alternative to the CIRP to resolve the insolvency of corporate MSMEs. In order to apprise itself of the global best practices on the insolvency procedures suited to MSMEs, the Committee analysed contemporary thought and jurisprudence that has evolved globally in this regard.

i. *Contemporary understanding of MSME insolvency*

2.5. Globally, insolvency procedures are often found to be "*complex, lengthy, and rigid procedures*" making them ill-suited for addressing the needs of insolvent MSMEs.[17] This is partly due to the fact that MSMEs typically have limited access to credit and lack necessary sophistication to withstand prolonged statutory processes.[18] Further, MSMEs typically lack adequate resources to fund complex insolvency proceedings

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[14] ibid

[15] ibid

[16] Government of India, 'Speech of Nirmala Sitharaman Minister of Finance' (February 1, 2021) <https://www.indiabudget.gov.in/doc/Budget_Speech.pdf> accessed 1 June 2021

[17] Wolfgang Bergthaler, Kenneth Kang, Yan Liu, and Dermot Monaghan, 'Tackling Small and Medium Sized Enterprise Problem Loans in Europe' IMF Staff Discussion Note (2015) p. 10 <https://www.imf.org/external/pubs/ft/sdn/2015/sdn1504.pdf> accessed 28 May 2021

[18] World Bank, *Report on the Treatment of MSME Insolvency* (2017) p. 1 <https://openknowledge.worldbank.org/bitstream/handle/10986/26709/114823-WP-PUBLIC-weds-510-MSME-Insolvency-report-low-res.pdf?sequence=1&isAllowed=y> accessed 28 May 2021

or appoint necessary professionals and experts to conduct such proceedings.[19] They also face difficulties in obtaining additional funding during a proceeding required for their continued trading and thereby reducing the prospects of a successful rescue.[20] This often results in creditors of MSMEs being reluctant to participate in insolvency proceedings, as the cost of participation often fails to outweigh the perceived recovery expected out of such proceedings.[21] Instead, creditors are often incentivised to initiate recovery proceedings or invoke guarantees rather than participating in workouts.[22]

2.6. Recently, and especially owing to the wave of MSME insolvencies associated with the economic shock of the Covid-19 outbreak, efforts are being seen at the international level to provide a specific and well-tailored insolvency resolution framework for distressed MSMEs.[23] Recent reports and publications from the World Bank,[24] the UNCITRAL[25] and the IMF[26] have highlighted that formal proceedings for business insolvency, that are often costly, complex, lengthy and procedurally

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[19] World Bank, *Report on the Treatment of MSME Insolvency* (2017) p. 5-6 <https://openknowledge.worldbank.org/bitstream/handle/10986/26709/114823-WP-PUBLIC-weds-510-MSME-Insolvency-report-low-res.pdf?sequence=1&isAllowed=y> accessed 28 May 2021

[20] ibid, p. 24

[21] ibid, p. 12

[22] Wolfgang Bergthaler, Kenneth Kang, Yan Liu, and Dermot Monaghan, 'Tackling Small and Medium Sized Enterprise Problem Loans in Europe' IMF Staff Discussion Note (2015) p. 10 <https://www.imf.org/external/pubs/ft/sdn/2015/sdn1504.pdf> accessed 28 May 2021

[23] IMF Staff Discussion Note, 'Insolvency Prospects Among Small and Medium Enterprises in Advanced Economies: Assessment and Policy Options', (April 2021) para 30, p. 20 <https://www.imf.org/en/Publications/Staff-Discussion-Notes/Issues/2021/03/25/Insolvency-Prospects-Among-Small-and-Medium-Sized-Enterprises-in-Advanced-Economies-50138>, accessed 9 June 2021. *Also see* Jean Pesme, 'New Principles for Insolvency: Supporting Small Business' Key Role in the Covid-19 Recovery' (World Bank Blogs, April 23, 2021) <https://blogs.worldbank.org/psd/new-principles-insolvency-supporting-small-businesses-key-role-covid-19-recovery> accessed 9 June 2021

[24] World Bank, *Principles for Effective Insolvency and Creditor Debtor Regimes*, (2021) <https://openknowledge.worldbank.org/handle/10986/35506> accessed 9 June 2021

[25] United Nations Commission on International Trade Law Working Group V, *Draft Text on a Simplified Insolvency Regime*, (58th Session, 3-7 May, 2021) <https://uncitral.un.org/en/working_groups/5/insolvency_law> accessed 9 June 2021

[26] *See* IMF Staff Discussion Note, 'Insolvency Prospects Among Small and Medium Enterprises in Advanced Economies: Assessment and Policy Options', (April 2021) <https://www.imf.org/en/Publications/Staff-Discussion-Notes/Issues/2021/03/25/Insolvency-Prospects-Among-Small-and-Medium-Sized-Enterprises-in-Advanced-Economies-50138>, accessed 9 June 2021

rigid, may be unsuitable for MSMEs. At a national level, countries such as Singapore and Australia have implemented reforms to their insolvency laws, in order to provide simplified, faster and low-cost processes for eligible MSMEs.[27]

2.7. While suggesting reforms to simplify and design accessible and cost-effective insolvency resolution frameworks for MSMEs, contemporary international best practices promote the need for a comprehensive set of debt restructuring tools such as out-of-court or hybrid restructuring mechanisms, simplified reorganisation procedures, lesser court intervention and emphasis on informal negotiation and pre-packaged reorganisation.[28] The recommendations and contemporary practise on MSME insolvency can be broadly summarised as below:

a. Need for a simpler, low-cost and timely process: The trend towards recognition of alternative processes for insolvency resolution of MSMEs is primarily based on the realisation that the complexity and cost of ordinary corporate insolvency procedures are prohibitive for MSMEs and work better for larger firms.[29] The World Bank, in its 2017 report had noted that "complex insolvency systems deter MSMEs from resorting to formal procedures to tackle financial distress."[30] The World Bank report had also highlighted that MSMEs lack the funds and resources to cover the costs of formal insolvency processes. The World Bank recommendations for shorter time periods and reduced formalities have been echoed in the UNCITRAL Working Group's Draft Text on a Simplified Insolvency Regime.[31]

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[27] Australia's Simplified Debt Restructuring Process, introduced in the Corporations Amendment (Corporate Insolvency Reforms) Act 2020 and Singapore's Simplified Insolvency Programme introduced in the Insolvency, Restructuring and Dissolution (Amendment) Act 2020

[28] IMF Staff Discussion Note, 'Insolvency Prospects Among Small and Medium Enterprises in Advanced Economies: Assessment and Policy Options', (April 2021) p. 25 <https://www.imf.org/en/Publications/Staff-Discussion-Notes/Issues/2021/03/25/Insolvency-Prospects-Among-Small-and-Medium-Sized-Enterprises-in-Advanced-Economies-50138>, accessed 9 June 2021

[29] ibid, p. 7

[30] World Bank, *Report on the Treatment of MSME Insolvency* (2017) p. 12. <https://openknowledge.worldbank.org/bitstream/handle/10986/26709/114823-WP-PUBLIC-weds-510-MSME-Insolvency-report-low-res.pdf?sequence=1&isAllowed=y> accessed 9 June 2021

[31] United Nations Commission on International Trade Law Working Group V, *Draft Text on a Simplified Insolvency Regime*, (58th Session, 3-7 May, 2021) <https://uncitral.un.org/en/working_groups/5/insolvency_law> accessed 9 June 2021

b. Provision of a hybrid, informal mechanism: The IMF Staff Discussion Note highlights the value of hybrid restructuring processes for MSMEs, as they facilitate out-of-court-restructuring and lessen the judicial intervention to only critical points – such as to prevent creditor action against the debtor, and to confirm the agreement negotiated between the debtor and the creditors.[32] Pertinently, the IMF Staff Discussion Note advocates the pre-packaged reorganisation plan as a simple and effective hybrid restructuring technique for MSMEs, as it "requires only minor legal changes and results in huge time reductions and minimal use of the resources of the courts."[33]

c. Effective measures to facilitate debtor and creditor participation: The World Bank, in its 2017 report had highlighted that the lack of information of the debtor's viability potentially undermined creditors' trust, as a result of which they preferred to enforce their claims outside of the insolvency system.[34] The UNCITRAL Working Group's Draft Text on a Simplified Insolvency Regime states that such MSME insolvency regimes should provide for effective measures to facilitate creditor participation and should advocate for a more debtor-in-possession approach in order to involve and incentivise the debtor towards insolvency resolution.[35]

2.8. Thus, special insolvency procedures for MSMEs, such as simplified or pre-packaged proceedings could ensure that there is an accessible, timely and value-maximising insolvency resolution framework for MSMEs. The importance of such frameworks

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[32] IMF Staff Discussion Note, 'Insolvency Prospects Among Small and Medium Enterprises in Advanced Economies: Assessment and Policy Options', (April 2021) p. 25 <https://www.imf.org/en/Publications/Staff-Discussion-Notes/Issues/2021/03/25/Insolvency-Prospects-Among-Small-and-Medium-Sized-Enterprises-in-Advanced-Economies-50138>, accessed 9 June 2021

[33] ibid

[34] World Bank, *Report on the Treatment of MSME Insolvency* (2017) p. 12 <https://openknowledge.worldbank.org/bitstream/handle/10986/26709/114823-WP-PUBLIC-weds-510-MSME-Insolvency-report-low-res.pdf?sequence=1&isAllowed=y> accessed 28 May 2021

[35] *See* United Nations Commission on International Trade Law Working Group V, *Draft Text on a Simplified Insolvency Regime*, (58th Session, 3-7 May, 2021) <https://uncitral.un.org/en/working_groups/5/insolvency_law> accessed 9 June 2021

tailored for MSMEs is being recognised globally, given MSMEs are crucial to the supply chain and economic and social welfare of society.[36]

2.9. The Committee took note of the above and felt that it may be beneficial to understand the contours of pre-packaged insolvency processes across different jurisdictions, as the same has been recommended to be a beneficial tool for MSME insolvency. A brief overview of the prominent understanding of pre-packs is provided below.

ii. *Pre-packaged insolvency processes*

2.10. 'Pre-packaged' insolvency processes are generally hybrid processes that combine the advantages of informal workouts—which are often economical, swift processes without involving complex procedural requirements—with certain features of formal insolvency processes. [37] Pre-packaged bankruptcy proceedings first emerged in the US, to avoid the relative costs and complicated negotiation processes involved in an ordinary bankruptcy proceeding filed under Chapter 11 of the US Bankruptcy Code.[38] A pre-packaged bankruptcy process allows for an out-of-court negotiation of a debt-restructuring or reorganisation plan, which is subsequently confirmed by the bankruptcy court "*without invoking the procedures of a full-blown bankruptcy case*".[39] In addition to pre-packaged bankruptcies, debtors in the US can also opt for a 'pre-arranged route' wherein the debtor negotiates with its creditors to reach an agreement regarding the plan of reorganisation at the pre-commencement stage, while, the actual solicitation of votes takes place upon formal commencement of bankruptcy proceedings.[40]

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[36] Organisation for Economic Cooperation and Development, *Economic Policy Reforms: Going for growth*, (2018), Ch. 3, p. 97 <https://www.oecd.org/economy/growth/policies-for-productivity-the-design-of-insolvency-regimes-across-countries-2018-going-for-growth.pdf> accessed 10 June 2021

[37] Bo Xie, *Comparative Insolvency Law: The Pre-pack Approach in Corporate Rescue* (Edward Elgar Publishing, 2016) p. 28

[38] Bo Xie, *Comparative Insolvency Law: The Pre-pack Approach in Corporate Rescue* (Edward Elgar Publishing, 2016) p. 28

[39] Marc S Kirschner and Dan A Kusnetz and Laurence Y Solarsh and Craig S Gatarz, 'Prepackaged Bankruptcy Plans: The Deleveraging Tool of the '90s in the Wake of OID and Tax Concerns' (1991) 21 Seton Hall L Rev 643 p. 661

[40] Bo Xie, *Comparative Insolvency Law: The Pre-pack Approach in Corporate Rescue* (Edward Elgar Publishing, 2016) p. 189

2.11. In contrast, in an ordinary Chapter 11 bankruptcy proceeding, a debtor files a bankruptcy petition before initiating negotiations with its creditors. Subsequently, the debtor typically negotiates with statutory committees, including a committee of unsecured creditors, to finalise the terms of the reorganisation plan and seek their votes.[41] In practice, Chapter 11 bankruptcy cases often take substantial time, involve significant costs and can be ineffective and burdensome.[42] A survey that captured the median duration of ordinary Chapter 11, pre-packaged and pre-arranged cases indicates that pre-packaged Chapter 11 proceedings are less time-consuming than ordinary Chapter 11 proceedings.[43] For this reason, pre-packs are widely used by debtors for resolving insolvency: according to the case study, of the 304 Chapter 11 cases resolved during the period between 2003 and 2016, 22% were found to be pre-packaged cases.[44]

2.12. Like in the US, pre-packs are fairly common in the UK as well, representing nearly 30% of all administrations.[45] However, unlike the US Bankruptcy Code, the Insolvency Act, 1986 of the UK does not envisage or expressly enable pre-packs. Instead, 'pre-packaged administrations' have emerged as "*a feature of the way the current market has developed*".[46] Pre-packs in the UK refer to an arrangement wherein the sale of all or part of the business or assets of the debtor is negotiated with major creditors prior to the formal appointment of the insolvency practitioner as an

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[41] *See* Marc S Kirschner and Dan A Kusnetz and Laurence Y Solarsh and Craig S Gatarz, 'Prepackaged Bankruptcy Plans: The Deleveraging Tool of the '90s in the Wake of OID and Tax Concerns' (1991) 21 Seton Hall L Rev 643 p. 661

[42] *See* American Bankruptcy Institute, *ABI Commission to Study the Reform of Chapter 11* (2014) p. 12 <https://abiworld.app.box.com/s/vvircv5xv83aavl4dp4h> accessed 28 May 2021; Michelle J. White, 'Does Chapter 11 Save Economically Inefficient Firms?, (1994) 72(3) Washington University Law Review 1319 <https://core.ac.uk/download/pdf/233171509.pdf> accessed 28 May 2021

[43] Norman N. Kinel, 'The Ever-Shrinking Chapter 11 Case' (Restructuring Global View, 20 August 2018) <https://www.restructuring-globalview.com/2018/08/the-ever-shrinking-chapter-11-case/> accessed 28 May 2021 "The median duration of the cases examined by Fitch for traditional chapter 11, pre-arranged (or pre-negotiated) and prepackaged cases were eleven, four and two months respectively."

[44] ibid

[45] *See* The Insolvency Service, *Corporate Report Pre-Pack Sales in Administration Report* (2020), <https://www.gov.uk/government/publications/pre-pack-sales-in-administration/pre-pack-sales-in-administration-report> accessed 28 May 2021

[46] Ben Larkin et al, *Restructuring Through US Chapter 11 and UK Prepack Administration*, in Christopher Mallon and Shai Y. Waisman (eds), *Law and Practice of Restructuring in in the UK and US* (1st edn, Oxford University Press 2011), p. 231

administrator, and the sale is executed soon after their appointment.[47] In contrast, in a regular administration, the administrator takes over the management of the debtor and initiates negotiations regarding the outcome of the administration, *after* being formally appointed as an administrator.[48] As the Insolvency Act, 1986 allows for an out-of-court appointment of the administrator—the debtor or any creditor classified as a 'qualified floating charge holder' is allowed to appoint an administrator without requiring a court order. Subject to recent regulatory reform that increases the scope for creditor involvement in certain pre-pack sales,[49] courts typically allowed administrators to "*dispose of the business and assets of a company in advance of a creditors' meeting and without the need for direction from the court*".[50]

2.13. The prevalence of pre-packs in other jurisdictions can be explained by the relative advantages associated with pre-packs in comparison with ordinary insolvency proceedings. Primarily, as a significant part of the process is arranged and finalised *ex ante*, the formal proceeding often takes significantly less time to conclude than ordinary insolvency proceedings. Further, owing to its swift nature, costs involved in engaging professionals and conducting lengthy negotiations are also minimised in pre-packs.[51] Moreover, they have the potential of imposing minimal disruptions or interruptions in the operations of the business of the debtor,[52] thereby allowing

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[47] Insolvency Practitioners' Association, *Statement of Insolvency Practice 16*, para 1 <https://insolvency-practitioners.org.uk/uploads/documents/f30389ce35ed923c06b2879fecdb616a.pdf> accessed 28 May 2021; Rodrigo Olivares-Caminal, *Debt Restructuring*, (1st edn, Oxford University Press 2011) p. 146

[48] *See* Lorraine Conway and Ali Shalchi, *Pre-pack administrations* (House of Commons Library, Briefing Paper No. 5035)) para 1.2 <https://researchbriefings.files.parliament.uk/documents/SN05035/SN05035.pdf> accessed 28 May 2021

[49] *See* the Administration (Restrictions on Disposal etc. to Connected Persons) Regulations 2021, <https://www.legislation.gov.uk/ukdsi/2021/9780348220421?view=plain> accessed 5 June 2021. *Also see* Para 2.15 of this Report

[50] Rodrigo Olivares-Caminal, *Debt Restructuring*, (1st edn, Oxford University Press 2011) p. 150

[51] Vanessa Finch, *Corporate Insolvency Law Perspectives and Principles* (2nd edn, Cambridge University Press 2009) p. 454, 455

[52] Lorraine Conway and Ali Shalchi, *Pre-pack administrations* (House of Commons Library, Briefing Paper No. 5035) p. 9 <https://researchbriefings.files.parliament.uk/documents/SN05035/SN05035.pdf> accessed 28 May 2021

for greater preservation of jobs and better recovery by operational creditors.[53] Pre-packs also help in reducing the indirect costs associated with lengthy and public insolvency proceedings: by reducing the period of the formal insolvency proceeding, pre-packs help in minimising the adverse impact of public acknowledgement of insolvency.[54]

2.14. While pre-packs offer certain benefits over ordinary insolvency proceedings, there are certain criticisms levelled against the manner in which pre-packs are conducted. For example, till very recently in the UK, the administrator enjoyed wide discretion to execute a pre-pack sale without requiring prior approval from the creditors of the debtor. As the administrator is typically appointed by the debtor itself, it can result in a potential conflict of interest between that of the management—who play a crucial role in the appointment of the administrator—and that of the creditors of the debtor—on whose behalf the administrator is statutorily required to act.[55] Pre-packaged administrations are also often criticised for the lack of transparency and the non-involvement of unsecured creditors in the decision-making process.[56] Additionally, pre-packs in the UK have been subject to severe criticisms owing to the prevalence of connected-party sales: more than 50% of all the pre-packs conducted in 2018 and 2019 were classified as 'connected-party sales'.[57] Primarily, connected-party sales are seen as enabling businesses to continue trading "*shorn of many of its debts to the benefit of its existing owners*", thereby allowing the perpetuation of unviable businesses at the cost of creditors' interest. [58]

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[53] Teresa Graham, *Graham Review into Pre-pack Administration: Report to The Rt Hon Vince Cable MP* (2014) paras 7.9-7.12 <http://data.parliament.uk/DepositedPapers/Files/DEP2014-0860/Graham_review_into_pre-pack_administration_-_June_2014.pdf> accessed 28 May 2021; Vanessa Finch, *Corporate Insolvency Law Perspectives and Principles* (2nd edn, Cambridge University Press 2009) p. 455-457

[54] Vanessa Finch, *Corporate Insolvency Law Perspectives and Principles* (2nd edn, Cambridge University Press 2009) p. 457-458

[55] Vanessa Finch, *Corporate Insolvency Law Perspectives and Principles* (2nd edn, Cambridge University Press 2009) p. 459-461

[56] Sandra Frisby, 'Insolvency Law and Insolvency Practice: Principles and Pragmatism Diverge?, Current Legal Problems', Volume 64 (2011) pp. 349–397, 379

[57] *See* The Insolvency Service, *Corporate Report Pre-Pack Sales in Administration Report* (2020), <https://www.gov.uk/government/publications/pre-pack-sales-in-administration/pre-pack-sales-in-administration-report> accessed 28 May 2021

[58] Teresa Graham, *Graham Review into Pre-pack Administration: Report to The Rt Hon Vince Cable MP* (2014) para 7.46 <http://data.parliament.uk/DepositedPapers/Files/DEP2014-0860/Graham_review_into_pre-pack_administration_-_June_2014.pdf> accessed 28 May 2021

2.15. The Committee noted that while some of the above criticisms are applicable to pre-packs in general, most of them are relevant to the specific nature of pre-pack sales prevalent in the UK. For example, in the US, the concern regarding lack of participation of creditors is not applicable, as every impaired class of creditors are provided an opportunity to vote upon a reorganisation plan, including pre-packaged and pre-arranged plans, under Chapter 11.[59] Further, necessary safeguards are often introduced to prevent potential abuse of the process, such as the mandatory requirement for an *ex-ante* scrutiny by an independent expert for connected-party sales, or the need for approval of the company' creditors, which was recently introduced in the UK.[60]

iii. *Suitability of a pre-packaged insolvency resolution process for MSMEs*

2.16. On reviewing the above, the Committee felt that pre-packaged insolvency proceedings can offer a viable alternative framework for resolving the insolvency of corporate MSMEs in a simplified, cost-effective and expeditious manner. It noted that there is no single blueprint for designing a pre-pack process and various jurisdictions have come up with their own version of hybrid processes. Similarly, it felt that it may be beneficial to design a pre-packaged insolvency process for corporate MSMEs that is suitable in the Indian context.

2.17. It noted that the Sub-committee has already recommended a comprehensive framework and design for pre-packaged insolvency. While suggesting the design of the proposed framework, the Sub-committee noted that a mechanism like the pre-pack process may be a pressing need for corporate MSMEs as a full-fledged CIRP may be too burdensome to resolve their debts. Despite this, it recommended that since a special insolvency framework is to be notified for corporate MSMEs under

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[59] Title 11 of the United States Code, Section 1126. It is worth highlighting that Sub-chapter V of Chapter 11, introduced under the Small Business Reorganisation Act, 2019, relaxes some of the plan confirmation requirements of ordinary Chapter 11 proceedings, to provide a less-rigid and tailor-made process for 'small business debtors' that come within the ambit of Sub-chapter V. *See* A Guide to the Small Business Reorganization Act of 2019 (Revised and updated May 2020), <http://abi-org.s3.amazonaws.com/SBRA/Guide_to_SBRA_Revision_5-13.pdf> accessed 14 June 2021

[60] *See* The Administration (Restrictions on Disposal etc. to Connected Persons) Regulations 2021, <https://www.legislation.gov.uk/ukdsi/2021/9780348220421?view=plain> accessed 5 June 2021. The Administration (Restrictions on Disposal etc. to Connected Persons) Regulations 2021 prohibit an administrator from making a substantial disposal of all or a substantial part of the company's business and assets to connected persons, unless she either obtains creditor approval of the proposed disposal, or the connected persons can obtain a written 'qualifying report' by an 'evaluator' and can submit the same for the administrator's consideration.

Section 240A, the pre-pack process may be available for all corporate debtors under the Code (and not just MSMEs).

2.18. Although Section 240A of the Code allows modifications and exceptions to be made to the CIRP when applicable to MSMEs, it may not facilitate the introduction of a comprehensive pre-packaged insolvency process that is an *alternative* to the formal CIRP. The Committee thought that instead of modifying the existing insolvency mechanisms available under the Code, it will be beneficial if corporate MSMEs have access to a new hybrid process. This will allow MSMEs to choose if they want to opt for such a process voluntarily, and promote collective resolution of MSMEs facing financial distress. Thus, the Committee noted that an alternative route for insolvency resolution of corporate MSMEs may be contemplated as a separate chapter under the Code.

2.19. After analysing the recommendations of the Sub-committee for the design of the pre-pack process, it concluded that the features of the proposed pre-pack process are aligned with the global best practices on insolvency frameworks for MSMEs. It also felt that the proposed pre-pack process may, in fact, be better suited for corporate MSME than it would be for larger corporates. *Firstly*, the proposed pre-pack process allows a corporate debtor to approach the Adjudicating Authority with a base resolution plan that it has negotiated with its unrelated financial creditors before initiation of formal proceedings (see para 6.12.). Negotiating such plans may be easier for MSMEs, who would usually have fewer creditors and simpler debt structures, compared to large corporates. Further, MSMEs would often have fewer interested resolution applicants than larger corporates. Consequently, resolving stress faced by MSMEs may be more feasible through a pre-pack process than a full-fledged CIRP.

2.20. *Secondly*, since part of the proposed pre-pack process takes place before formal proceedings are initiated (see part II of Chapter 3), the pre-pack process would be less costly and time-consuming than CIRP proceedings. The pre-pack process will, thus, be more suitable for MSMEs as they would often be unable to afford high insolvency process costs.[61] *Thirdly*, the proposed pre-pack process does not displace the management of the corporate debtor and is designed to be a debtor-in-possession process (see paras 5.11. to 5.16.). This may be especially useful for MSMEs as it may allow avoiding loss of goodwill and facilitate the MSMEs to

[61] *See* Ronald B. Davis and others, *Micro, Small, and Medium Enterprise Insolvency: A Modular Approach* (1st edn, Oxford University Press 2018)

negotiate continuation of contracts with suppliers even after formal insolvency proceedings are triggered. Considering that the management of an MSME would have significant knowledge about its business, its continuation may be less disruptive and more value maximizing.[62]

2.21. *Finally,* ensuring transparency and accountability in a debtor-in-possession insolvency process may be difficult in case of large corporates. Maintaining oversight of the management's activities would be cumbersome where the business of the corporate debtor is large and diversified. The Committee discussed that the IBC was enacted in the backdrop of failure of debtor-in-possession rescue procedures under SICA.[63] The BLRC Report took note of this and suggested that the CIRP should require takeover of management by the resolution professional, noting that "*The law must appoint a resolution professional as the manager of the resolution period, so that the creditors can negotiate the assessment of viability with the confidence that the debtors will not take any action to erode the value of the enterprise*."[64] Therefore, the Committee felt that it would be prudent to exercise caution while providing for a debtor-in-possession approach under the IBC, and concluded that such an approach may be more suited to MSMEs than to large corporations. Additionally, it noted that while designing such a process for MSMEs, regard must be had to building sufficient safeguards to avoid any possible misuse of the process.

2.22. **Based on the above, the Committee was of the opinion that the pre-pack process should only be available to corporate debtors that are MSMEs.** It felt that the pre-pack process would undoubtedly go a long way in alleviating the distress that MSMEs are facing due to the pandemic. Likewise, it will provide such MSMEs access to a flexible, quick and cost-effective process, allowing them to be more stable and innovative in the long term. Thus, **it decided to review the recommendations of the proposed pre-pack process made by the Sub-committee and accordingly, recommend the design of a suitable framework for pre-packaged insolvency resolution of corporate MSMEs.** The discussions contained in this Report detail the deliberations and recommendations of the Committee in this regard. One of the

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[62] *See* International Monetary Fund, *Orderly and Effective Insolvency Procedures* (1999) <https://www.imf.org/external/pubs/ft/orderly/> accessed 1 June 2021

[63] *See* Ministry of Finance, *Interim Report of the Bankruptcy Law Reforms Committee* (2015) <https://www.ibbi.gov.in/uploads/resources/57420f272e1515f0c9c137f1a6423d78.pdf> accessed 1 June 2021

[64] Ministry of Finance, *The Report of the Bankruptcy Law Reforms Committee Volume I: Rationale and Design* (2015) para 3.4.2 <https://ibbi.gov.in/BLRCReportVol1_04112015.pdf> accessed 1 June 2021

members stated the importance of pre-pack process for non-MSME corporate debtors. On this, the Committee agreed that in due course of time, it may be considered if the pre-pack process should be made available for non-MSME corporate debtors based on the experience gained in its implementation.

II. Design Principles of the Pre-Pack Process

2.23. The Committee wanted to abide by certain key considerations that would serve as guiding principles in finalising the design of the pre-pack process. The Sub-committee had, on its part, relied on three main principles in proposing a pre-pack process. These are: (i) the basic structure of the Code should be retained; (ii) there should be no compromise of rights of any party; and (iii) the framework should have adequate checks and balances to prevent any abuse. Additionally, the Sub-committee had also identified three basic features of the Code for retention in the proposed pre-pack process, i.e., inclusion of creditor-in-control features, imposition of moratorium during resolution and emulation of the binding nature of an approved resolution plan.

2.24. Keeping these principles identified by the Sub-committee in mind, the Committee sought to add and abide by the following design features for a pre-pack process for corporate MSMEs -

a. Alternate and Voluntary mechanism with Core elements of the CIRP: The Committee wanted to ensure that the pre-pack process for MSMEs is designed as a shorter and cost-effective alternative for the insolvency resolution of corporate MSMEs, that supplements the existing corporate insolvency framework under the Code. The Committee agreed that the pre-pack process should be utilised on the basis of voluntary and consensus-based needs and efforts of MSMEs and their stakeholders (i.e., their members and creditors). These elements would ensure the development of an accessible insolvency framework that incentivises early insolvency resolution of MSMEs. Further, in line with the Sub-committee, the Committee emphasized that the core features of the CIRP under the Code should be suitably retained in the pre-pack process, so as to promote further development of fair creditor-debtor relationships.

b. Time-bound and Speedy Resolution process: In line with the recommendation of the Sub-committee as well as contemporary practice as detailed above, the Committee emphasized that the pre-pack process

should provide a shorter timeline than the formal CIRP, for timely and cost-effective resolution of MSMEs. In line with the hybrid, informal attributes of a pre-pack process, the Committee also agreed that where possible, the rigidities and formalities associated with the more formal CIRP should be avoided.

c. Balancing creditor-debtor incentives: Acknowledging the progress of the Indian insolvency ecosystem towards fairer creditor-debtor relationships, the Committee wanted to ensure a balancing of incentives for both creditors and debtors at the pre-initiation stages of the pre-pack process, as well as the post-admission stages involving the more formal conduct of the process. Towards this end, the Committee recognised the need to uphold the creditor-in-control features of the CIRP, along with a debtor-in-possession approach that recognises the benefits of retaining a management that is likely to be well-positioned to protect the business and interests of the MSME.

d. Suitable Safeguards to address debtors' Moral Hazard: The Committee was cognisant that the availability of a debtor-friendly pre-pack process might be a moral hazard especially in case of MSMEs where there are gaps in information availability. Thus, it agreed that suitable checks and balances should be provided on the debtor's right to remain in possession, and to protect the interests of the creditors. Thus, it was agreed that like in a CIRP, the resolution professional should supervise and conduct the pre-pack process and ensure availability of appropriate information in relation to the MSME corporate debtor. It was also decided that the CoC and the resolution professional should be given special powers to seek orders from the Adjudicating Authority to check against any misconduct by the debtor's owners and managers. For additional deterrence, appropriate civil and criminal remedies were also recommended to ensure that the debtor does not misuse the pre-pack process at any stage.

e. Need for a detailed legal framework: The Committee agreed that given the unique design of the pre-pack process being recommended by it, it would be important to clearly delineate the roles and responsibilities of the key players (namely the debtor, creditors, the resolution professional and the resolution applicants) for ensuring legal certainty. Towards this

end, the Committee emphasized that the statutory backbone of the pre-pack process should be sufficiently detailed to provide necessary guidance for its smooth implementation.

CHAPTER 3 – ELIGIBILITY AND PRE-INITIATION REQUIREMENTS

I. Eligibility

3.1. The primary aspect deliberated by the Committee, while designing the pre-packaged insolvency resolution process ('pre-pack process') under the Code, was the kind of corporate debtors that should be eligible to opt for such a process. The deliberations of the Committee on various aspects of eligibility criteria are discussed below.

i. *MSME corporate debtor and default*

3.2. As discussed above, the Committee decided that the pre-pack process should be available only to corporate debtors that are MSMEs as an alternative to the CIRP under the Code (see para 2.4.). **In this regard, the Committee noted that the Code should provide that the pre-pack process is available for corporate debtors classified as 'MSMEs' as per Section 7(1) of the MSME Development Act, 2006.** This reference to the definition of an MSME has been used under the Explanation to Section 240A of the Code, and the Committee discussed that jurisprudence developed on the interpretation of the reference to the definition of MSMEs as under Section 240A may be applicable to the pre-pack process as well.[65]

3.3. Further, the Committee considered if default should be a requisite criterion for eligibility to apply to the pre-pack process. In this regard, the Sub-committee had recommended that a default by the corporate debtor should be required in the present framework.[66] It had suggested that the pre-pack process may be implemented in phases and in the first phase, it may commence in respect of corporate debtors with "*defaults from Rs.1 lakh to Rs.1 crore and COVID-19 defaults for which CIRP is not available today.*"[67]

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[65] *See Amit Gupta v Yogesh Gupta*, Company Appeal (AT) (Insolvency) No. 903 of 2019, NCLAT. Decision date – 20 December 2019.; *Ashish Mohan Gupta v The Liquidator of M/S Hind Motors*, Company Appeal (AT) (Insolvency) No. 875 of 2019, NCLAT. Decision date - 13 April 2021

[66] Ministry of Corporate Affairs, *Report of Sub-Committee of the Insolvency Law Committee on Pre-Packaged Insolvency Resolution Process* (2020) <https://www.ibbi.gov.in/uploads/resources/24c7fc03cdffff69960ce374416fa646.pdf> accessed 1 June 2021, para 3.27

[67] ibid, para 3.17

3.4. The Committee agreed with the recommendation of the Sub-committee that the corporate debtor should have committed a default to be eligible for the pre-pack process. It discussed that since the pre-pack process is a mechanism to resolve 'insolvency', it should require the corporate debtor to establish that it is facing financial distress. Notably, introduction of the default test in the Code for determination of insolvency was deliberated by the BLRC Report extensively, and it was noted that such test may promote early detection and resolution of insolvency.[68] Considering that the jurisprudence on proving default has now settled under the CIRP, the Committee noted that there may be no merit in introducing a new standard for proving distress. **Thus, it agreed that the MSME corporate debtor should have committed a default to be eligible to initiate a pre-pack process.**

3.5. The Committee deliberated on the appropriate default threshold in the present context. It noted that since the pre-pack process is to apply to MSMEs, the default threshold should not be too high. **Thus, it recommended that the Code should provide that the pre-pack process would apply to cases where the corporate debtor has committed a default of at least Rs. 1 lakh. Further, the Central Government should have the flexibility to notify a higher amount as the minimum default threshold, which may not be higher than Rs. 1 crore. Such default threshold in the pre-pack process will be distinct from the default threshold notified for CIRP.** The Committee also noted that there wasn't a need for a maximum default threshold as suggested by the Sub-committee as such a cap might exclude certain corporate MSMEs from the process.

3.6. Additionally, **the Committee agreed with the Sub-committee's recommendation that the pre-pack process should also be available in respect of COVID-19 defaults** (i.e., defaults protected from CIRP under Section 10A) as one of the aims of the pre-pack process is to alleviate stress for pandemic-affected MSME corporate debtors.

ii. *Eligibility as per Section 29A*

3.7. Section 29A lays down the requirements that a person has to fulfil to be a resolution applicant during the CIRP. This means that in order to submit a resolution plan in a CIRP, a person would have to be eligible as per the provisions of Section 29A.

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[68] *See* Ministry of Finance, *Interim Report of the Bankruptcy Law Reforms Committee* (2015) <https://www.ibbi.gov.in/uploads/resources/57420f272e1515f0c9c137f1a6423d78.pdf> accessed 1 June 2021

Where the corporate debtor undergoing CIRP is an MSME, Section 240A provides that the resolution applicant is exempted from certain requirements of Section 29A (clauses (c) and (h)).[69]

3.8. Notably, Section 29A was not included in the original text of the IBC at the time of its enactment, and was inserted in the Code by way of an amendment soon after the operationalisation of CIRP.[70] Through this provision, persons, who by their misconduct contributed to the defaults of the corporate debtor or are otherwise undesirable, are prevented from gaining or regaining control of the corporate debtor.[71] It is intended to protect creditors of the company by preventing unscrupulous persons from rewarding themselves at the expense of creditors and undermining the processes laid down in the Code.[72]

3.9. The Committee noted that Section 29A was inserted to fill a gap in the Code, and it has formed the foundation for determining if an interested party is fit to be a resolution applicant and gain control of the corporate debtor. Since its introduction, Section 29A has been the subject of several rounds of litigation and has been interpreted by many courts. The constitutionality of Section 29A (in general) has also been upheld by the Supreme Court[73], and jurisprudence on the interpretation of this provision is now settling. **Therefore, the Committee noted that the provisions of Section 29A should also apply for determining eligibility of a person to be a resolution applicant in the pre-pack process.**

3.10. Additionally, unlike the CIRP, the pre-pack process requires the corporate debtor to submit a base resolution plan for consideration of the CoC (see para 6.12.). Such a base resolution plan is to be prepared by the corporate debtor and shared with its unrelated financial creditors prior to initiation (see para 3.43.). The Committee considered if the corporate debtor should be required to be eligible as a resolution applicant as per Section 29A. It noted that the base resolution plan is essentially a 'resolution plan' that is prepared and negotiated by the corporate debtor before opening of formal proceedings. Given this, the eligibility criteria for a corporate

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[69] Insolvency and Bankruptcy Code, 2016, Section 240A(1)

[70] *See* Insolvency and Bankruptcy (Amendment) Ordinance, 2017 and Insolvency and Bankruptcy Code (Amendment) Act, 2018

[71] Insolvency and Bankruptcy Code (Amendment) Bill, 2018, Statement of Objects and Reasons

[72] Ministry of Corporate Affairs, *Report of the Insolvency Law Committee* (2018) para 14.1 <https://ibbi.gov.in/uploads/resources/ILRReport2603_03042018.pdf> accessed 1 June 2021

[73] *Swiss Ribbons Pvt. Ltd. v Union of India* (2019) 4 SCC 17

debtor to submit a base resolution plan should be the same as the eligibility criteria for a third party submitting a resolution plan. The Committee, thus, felt that the corporate debtor should also be eligible as per Section 29A under the pre-pack process.

3.11. Notably, development of the base resolution plan is a crucial part of the pre-pack process. After the formal process begins, the CoC may approve the base resolution plan as the resolution plan for the corporate debtor or make it subject to market-based competition to arrive at a resolution plan for the corporate debtor. In this way, the base resolution plan submitted by the corporate debtor becomes the basis on which the CoC decides the manner of resolving the corporate debtor's insolvency. Therefore, it is crucial to determine whether the corporate debtor is eligible to submit a resolution plan at the very beginning of the pre-pack process. **The Committee recommended that the Code should provide that the corporate debtor should be eligible to be a resolution applicant in accordance with Section 29A in order to be eligible to apply for the pre-pack process.**

3.12. Further, the Committee noted that the exemption from clauses (c) and (h) of Section 29A provided to resolution applicants of MSME corporate debtors undergoing CIRP, should equally apply to the pre-pack process as well. Although the Sub-committee had divergent views on whether the relaxation of Section 29A(c) should be extended to the pre-pack process, the Committee felt that such relaxations should be consistently applied across different insolvency processes. **In this regard, the Committee decided that the exemptions available to MSMEs under Section 240A(1) should be applicable in the pre-pack process as well, and suitable amendments may be made to Section 240A(1) for this purpose.**

iii. *Overlap with CIRP*

3.13. The Committee noted that the pre-pack process is an alternative to the CIRP, and therefore, the corporate debtor may choose to go for either process at a given point of time. **Thus, the Committee agreed that the Code should provide that a corporate debtor in respect of whom a CIRP has been admitted, would not be eligible to apply for the pre-pack process.**

3.14. Further, there may be scenarios where an application for CIRP and pre-pack are pending together. The Committee deliberated on whether the Code should lay down the order in which the Adjudicating Authority may consider such applications. It noted that ordinarily, the Adjudicating Authority would dispose of

the application that has been filed first.[74] However, since the corporate debtor will need to make preparations before being able to file an application to initiate the pre-pack process, CIRP applications may often be filed (and remain pending) before a pre-pack application is filed. If the Adjudicating Authority then considers the CIRP application first, it would lead to very few instances of a corporate debtor being able to avail the pre-pack process.

3.15. Moreover, although the Code envisages that a CIRP application should be disposed of within 14 days of its filing, such disposal takes much longer in practice. Where a CIRP application has been filed and is pending for a long period, the corporate debtor may not have certainty on the feasibility of negotiating a base resolution plan in the absence of rules on prioritising simultaneous CIRP and pre-pack applications. Even if a base resolution plan has been negotiated by the corporate debtor in such a scenario, delay in disposal of CIRP application may lead to value erosion and make the negotiated plan moot. Further, different NCLTs may adopt different practices on the manner of disposal of simultaneous applications – leading to inconsistent practices. For instance, some NCLTs may give preference to pre-pack process applications since there is prior negotiation between parties, whereas others may entertain applications on the basis of the date of filing.

3.16. Thus, **the Committee noted that the mechanism for determining the priority for disposing pre-pack and CIRP applications that are simultaneously pending should be laid down in the Code. In this regard, the Committee decided that the following principles may be reflected in the Code –**

a. **Where an application for initiating a pre-pack process is filed first, the Adjudicating Authority should first decide whether to admit or reject such application, before considering any CIRP application that is filed subsequently.** This approach provides an objective manner of dealing with simultaneous applications as it considers the application that has been filed first before any subsequent applications.

b. **Where an application for initiating CIRP is filed and subsequently a pre-pack application is filed within 14 days of the former, the Adjudicating Authority should first dispose of the application for**

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[74] *See Incredible Unique Buildcon Limited v Clutch Auto Limited,* Company Petition No. (IB)-15(PB)/2017, NCLT. Decision date – 10 March 2017;2017 SCC OnLine NCLT 94

initiating the pre-pack process.[75] Although under this approach the application that has been filed subsequently is to be disposed first, such a provision may be necessary to allow effective access to pre-packs in practice. The filing of a pre-pack application requires more preparation while CIRP applications can often be filed (and are indeed filed) immediately on default. Further, certain creditors may rush to file a CIRP application if they discover that the corporate debtor is attempting to negotiate a base resolution plan with its creditors. This may make accessibility to pre-packs limited, hindering quicker and cost-effective resolution of the stress faced by MSME corporate debtors. Therefore, the Committee thought that it would be suitable to allow corporate debtors a small window, after the filing of a CIRP application, to file a pre-pack application that would be considered first. In practice, this will only help debtors that are at an advanced stage of preparation for filing the pre-pack application.

c. **Where an application for initiating CIRP is filed and subsequently a pre-pack application is filed after 14 days of former, the Adjudicating Authority should first dispose of the application for initiating CIRP.** As with (a), this approach provides an objective manner of dealing with simultaneous applications as it considers the application that has been filed first before any subsequent applications.

d. In order for this mechanism outlined in paragraph b and c. to work as intended, the Committee noted that it was critical that the 14-day time-limit be strictly adhered to (see para 4.9.). **The filing systems of the NCLTs will need to monitor this closely to prevent abuse of the process.**

iv. *Cooling off period*

3.17. The Committee also noted that it is crucial to bar a corporate debtor from availing the pre-pack process if it has recently undergone another pre-pack process or CIRP. This would be necessary to avoid repeat insolvency filings and deter misuse. **It**

[75] A copy of an application for initiation of a corporate insolvency resolution process filed by a financial or an operational creditor is sent to the registered office of the corporate debtor before it is filed with the Adjudicating Authority. Therefore, the corporate debtor will have adequate notice of the filing of such an application. *See* Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016, Rule 4(3) and 6(2)

agreed that, as recommended by the Sub-committee, a corporate debtor should not be eligible to apply for a pre-pack process if it has undergone the same in the last three years. This may include any conclusion of the previous pre-pack process – approval of a plan, termination, conversion to CIRP or liquidation. Similarly, **a corporate debtor should not be eligible to apply for a pre-pack process if it has completed a CIRP in the last three years.**

3.18. **The Committee also agreed that, as provided in Section 11(d) in respect of CIRP, the Code should also provide that a corporate debtor cannot apply for a pre-pack process if a liquidation order has been passed against it. In other words, the pre-pack process cannot be used for disturbing the finality of a liquidation order.**

II. Pre-initiation Requirements

3.19. Pre-packs are hybrid mechanisms, with part of the process taking place informally and the other part in formal proceedings.[76] This means that a lot of preparation for the pre-pack takes place before approaching courts or tribunals, thus distinguishing it from formal rescue procedures like the CIRP. The Committee discussed the pre-initiation requirements that should be provided for the pre-pack process to work efficiently.

3.20. After reviewing practices in various jurisdictions and detailed deliberations, the Committee agreed that the initiation of the pre-pack process should be by an application made by the corporate debtor. Although the CIRP allows creditors to trigger the process, in a pre-pack, the debtor and creditors should have come to a consensus about the manner of resolution before formal proceedings are initiated. Therefore, there may be merit in only allowing the corporate debtor to file an application to initiate a pre-pack process. However, the Committee adopted a cautionary approach and noted that due consent from financial creditors of the corporate debtor should be obtained before initiation of the process to limit abuse.

3.21. Further, since the pre-pack process will have a significant impact on the future prospects of the corporate debtor, it is important to ensure that both the management and members of the corporate debtor have approved the filing of the application for initiation. Additionally, the Committee noted that although the pre-

[76] Bo Xie, *Comparative Insolvency Law: The Pre-pack Approach in Corporate Rescue* (Edward Elgar Publishing, 2016) p. 28

commencement process takes place informally, providing some degree of supervision over the activities of the corporate debtor would be prudent.

3.22. Based on the above, the Committee decided that the pre-initiation requirements for the pre-pack process may be of three kinds. First, a resolution professional should be appointed to oversee due compliance with the pre-initiation requirements. Second, the corporate debtor should be required to obtain approvals from its management and members for initiation of the pre-pack process. And third, the corporate debtor must obtain requisite approval from its unrelated financial creditors for the initiation of the pre-pack process. In practice, such approval is likely to be granted on the basis of the negotiations between parties in respect of the terms of the base resolution plan proposed by the corporate debtor. The discussions of the Committee in respect of each of these aspects is reflected below.

i. *Appointment and role of the resolution professional*

3.23. As noted above, the Committee discussed that the corporate debtor would have to satisfy various requirements at the pre-initiation stage to be eligible to apply for the pre-pack process. The Sub-committee did not envisage supervision over the activities of the management of the corporate debtor at the pre-initiation stage. Nevertheless, the Committee noted that maintaining transparency, creating accountability and keeping some degree of oversight over the corporate debtor will be important to avoid any misuse of the pre-pack process. It thus discussed that including an objective third party to oversee the activities at the pre-initiation stage may aid in building trust among stakeholders and curbing any misuse of the process. It was felt that the appropriate person to play this role may be an independent insolvency professional.

3.24. Insolvency professionals are regulated by the IBBI and are subject to various regulations to monitor their conduct. The IBBI also exercises disciplinary powers over such professionals. Given this, insolvency professionals are expected to act independently and can be effectively monitored and regulated. The Committee also took a note of the practice of pre-packs in the UK, where the insolvency practitioner has extensive powers. For instance, an insolvency practitioner (administrator) is appointed from the beginning and she oversees the pre-pack process. Since the pre-pack process in the UK is targeted towards the sale of the distressed business, courts in the UK have tended to uphold the discretion of the insolvency practitioner in executing such pre-packaged sales, without having to take any statutory approval

from creditors.[77] However, to ensure proper conduct of the process, the role and actions of the insolvency practitioners acting in a pre-pack process in the UK are regulated by guidance given in the form of the 'Statement of Insolvency Practice 16' (SIP-16) issued by the Insolvency Practitioners Association.[78] Further, given the concerns around pre-pack sales to connected parties in the UK, recent regulatory reforms have also been introduced prohibiting the administrator from making a substantial disposal of the company's business and assets to connected persons, unless she either obtains creditor approval of the proposed disposal, or the connected persons obtain a written 'qualifying report' by a third-party evaluator and submit the same for the administrator's consideration.[79]

3.25. The Committee noted that such extensive powers, as are provided to insolvency practitioners in the UK, may not be suitable in the Indian context. However, insolvency professionals have the capacity to act as independent third parties with requisite knowledge and expertise in insolvency proceedings in India as well. They can also be regulated effectively, as they have a two-layered regulatory system - with IBBI and insolvency professional agencies overseeing their conduct. **Considering this, the Committee decided that it may be appropriate for an insolvency professional to be appointed as a resolution professional at the pre-initiation stage.**

a. Role of resolution professional at pre-initiation stage

3.26. The Committee discussed that during the pre-initiation stage, the resolution professional should act independently and in the best interests of the creditors of the corporate debtor. It noted that during this period, the primary role of the resolution professional would be to maintain detailed records of the events at the pre-initiation stage and regularly report developments to the IBBI. Although the IBBI does not have any specific supervisory role over the corporate debtor during the pre-pack process, submission of regular reports will help in creating a record of

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[77] *See for example Re Transbus International ltd*, [2004] 2 All ER 911*; Re T&D Industries plc* [2000] BCC 956; *See also* A. Kastrinou and S. Vullings, 'No Evil is Without Good: A Comparative Analysis of Pre-pack Sales in the UK and the Netherlands', (2018) 27(3) International Insolvency Review, p. 320, 321

[78] *See* Insolvency Practitioners' Association, 'Statement of Insolvency Practice 16' <https://insolvency-practitioners.org.uk/uploads/documents/f30389ce35ed923c06b2879fecdb616a.pdf> accessed 26 May 2021

[79] *See* The Administration (Restrictions on Disposal etc. to Connected Persons) Regulations 2021, <https://www.legislation.gov.uk/ukdsi/2021/9780348220421?view=plain> accessed 5 June, 2021

the chain of actions taken at the pre-initiation stage and inculcate a culture of compliance. Additionally, the resolution professional should also prepare a report for the Adjudicating Authority in which she details if the corporate debtor is eligible to apply for a pre-pack process and if it has duly met the pre-initiation requirements. Such a report should be submitted to the Adjudicating Authority at the time of filing an application for initiating the pre-pack process.

3.27. Apart from the above-mentioned oversight functions, the Committee discussed that the resolution professional may also help the corporate debtor and its creditors in facilitating decision-making in relation to matters that require such decisions. The resolution professional can also help in bridging any information asymmetry between parties by guiding them on the manner and nature of information to be shared in line with the requirements of the Code. She may also advise parties on other professionals they should consider hiring to facilitate smooth negotiations and voting. For instance, she may guide them on the appropriate kind of valuer they should appoint or ascertain if authorised representatives need to be appointed for certain classes of creditors.

3.28. While the resolution professional should have some flexibility in performing such facilitative functions, the Committee noted that resolution professionals should exercise caution and not act as advisers to the directors or management of the corporate debtor. It discussed that the resolution professional should take care to avoid any conflicts of interest in her role and should explain the boundaries of her role to the corporate debtor from the beginning. If the resolution professional were to provide advice to the corporate debtor on the manner of structuring and negotiating its plan, it may lead to distrust from creditors and confirmation bias from the resolution professional. This may defeat the independent role that the resolution professional is envisaged to perform.

3.29. It was brought to the Committee's notice that some MSMEs may lack the sophistication to draft and negotiate plans with its creditors and may require hands-on guidance or advice at every step. The Committee however felt that conflicts of interest would be unavoidable if a more intrusive role were to be performed by the resolution professional. Thus, it noted that if required the corporate debtor may seek advice of other professionals on its own in this regard, but the proposed resolution professional cannot be permitted to be more closely involved.

b. Manner and terms of appointment of the resolution professional

3.30. As noted above, the resolution professional will oversee the actions taken by the corporate debtor and will prepare a report certifying its compliance at the pre-initiation stage. Therefore, it may not be suitable for the corporate debtor to appoint the resolution professional itself. The Committee discussed that in order to facilitate balanced outcomes, it may be suitable for her name to be proposed and confirmed by the financial creditors. If such an appointment is made by those creditors, it may in fact help build trust of the creditors in the process. Further, since it is the unrelated financial creditors who are to form the CoC and vote on a plan (see para 5.31.) under this process (as is the case in CIRP), it may be suitable for such proposal and confirmation to come from such creditors only.

3.31. Considering the above, **the Committee agreed that a specified fraction of the unrelated financial creditors of the corporate debtor should propose the name of the insolvency professional to be considered for appointment as a resolution professional. The specific threshold of financial creditors required to make such a proposal may be specified in the regulations. However, this threshold should not be too high, in order to avoid making the process cumbersome. The name of such insolvency professional and the terms of her appointment would then be required to be approved by sixty-six percent in value of the unrelated financial creditors of the corporate debtor**. The terms of appointment at this stage may include the fee payable to the resolution professional for performing her pre-initiation duties, fee payable to professionals like authorised representatives (if any) at the pre-initiation stage, etc. The Committee discussed that the resolution professional should start performing her pre-initiation duties and functions once approval of unrelated financial creditors for her appointment has been obtained.

3.32. Further**, a resolution professional must provide her consent and must certify that she is eligible for such appointment**. The Committee discussed that the eligibility criteria herein may be similar to that in CIRP, and may provide that the proposed resolution professional should not have any disciplinary proceedings pending against her, should not be a related party of the corporate debtor, should be eligible to be appointed as an independent director for the corporate debtor, etc.

3.33. Additionally, **the Committee discussed that the Code should clarify that the fee payable to the resolution professional (as approved by unrelated financial creditors) should form part of the pre-pack process costs.** However, such inclusion of pre-initiation costs within the process costs would only be relevant if the application for initiating the process is admitted, since without such admission a formal process would not have begun. **Thus, where such an application is not**

admitted or not filed, any pre-initiation fee may be borne by the corporate debtor and be negotiated by the relevant parties informally. Considering this, the Committee felt that the treatment of pre-initiation fee of the resolution professional and authorised representative (if any), in cases where a pre-pack process is not formally initiated, may not be required to be provided in the Code.

ii. *Internal approvals of corporate debtor*

3.34. As noted above, the pre-pack process will have a significant impact on the business and operations of the corporate debtor. Although the process allows the corporate debtor to propose a plan to resolve its debts, such resolution may be subject to a competitive market-driven process that can lead to a permanent change in ownership and control. Thus, there is a possibility of the original management not retaining control of the corporate debtor after completion of the process. Further, the design of the pre-pack process allows the CoC to apply to the Adjudicating Authority to get the management displaced on certain grounds (see para 5.30.) or get the process converted into a CIRP (see part II of Chapter 7). This means that despite its debtor-in-possession approach, the pre-pack process may eventually lead to significant changes which may be beyond the control of the corporate debtor and its original management.

3.35. Given the gravity of the outcomes, the Committee noted that the corporate debtor should be required to avail certain internal approvals before initiating the pre-pack process. It agreed with the recommendation of the Sub-committee that one such approval may be granted by the board of directors or partners of the corporate debtor. Since the top management will take the lead in preparing the plan, negotiating with creditors at the pre-filing stage and also be best positioned to understand the day-to-day business of the corporate debtor, it would be best placed to decide if the pre-pack process should be initiated or not and make appropriate disclosures to the relevant creditors for commencing the process.

3.36. Consequently, **the Committee noted that the majority of board of directors or partners of the corporate debtor should provide a declaration stating – (a) the time within which the corporate debtor will file an application for the pre-pack process, (b) that such application is not being filed to defraud any person, and (c) the name of the insolvency professional proposed and approved to be appointed as the resolution professional by unrelated financial creditors. In order to ensure that there is no misuse of the pre-pack process, the Committee felt that the time-**

period for the purposes of the declaration referred to in point (a) should not exceed 90 days.

3.37. Additionally, the Committee noted that the members of the corporate debtor should also have approved the initiation of the pre-pack process as its primary stakeholders before the advent of insolvency. Currently under the Code, shareholders are required to pass a special resolution if a corporate debtor is applying for initiating a CIRP[80] or is undertaking voluntary liquidation[81]. Notably, the mandate of availing a special resolution prior to filing an application for initiating CIRP by the corporate debtor was not provided in the Code initially. This Committee, in its first report released in March 2018, recommended that such a requirement of a special resolution was crucial and recommended amendment to Section 10 in this regard.[82]

3.38. In order to arrive at the above recommendation, it had discussed that the requirement of a special resolution for initiating insolvency proceedings was provided in various erstwhile insolvency laws. For instance, under the CA, 2013 (and CA, 1956 before that), various provisions which were operational prior to enactment of the Code required actions like approval of amalgamation by the company (other than the sick company in a scheme for revival and rehabilitation),[83] winding up of the company,[84] approval of arrangement by liquidator,[85] etc. to be approved by a special resolution. Further, even under the Limited Liability Partnership (Winding-Up and Dissolution) Rules, 2012, a resolution passed by at least three-fourths of the total number of partners is required for initiating voluntary winding up[86], providing declaration of solvency[87], approving transfer of assets

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[80] Insolvency and Bankruptcy Code, 2016, Section 10

[81] ibid, Section 59

[82] Ministry of Corporate Affairs, *Report of the Insolvency Law Committee* (2018) para 4.6 <https://www.mca.gov.in/Ministry/pdf/ReportInsolvencyLawCommittee_12042019.pdf> accessed 1 June 2021

[83] Companies Act, 2013, Section 262(2)

[84] ibid, Section 271(1)(a)

[85] ibid, Section 319

[86] Limited Liability Partnership (Winding-Up and Dissolution) Rules, 2012, Rule 5

[87] ibid, Rule 7

during winding up[88], and allowing arrangement with creditors during winding up[89].

3.39. Based **on the above, the Committee agreed that the corporate debtor should be required to avail a special resolution from its members or a resolution by three-fourth of its partners for availing their consent for the initiation of the pre-pack process.** In this regard, it was brought to the Committee's notice that the Sub-committee had recommended an ordinary resolution of members or a vote of a simple majority of the partners of the corporate debtor instead. However, the Committee felt that it may be more appropriate to not deviate from the practice followed under various erstwhile insolvency laws as well as the current practice under the Code. Thus, it concluded that a special resolution of the members or resolution of three-fourth of partners may be more suitable.

iii. *Approval of unrelated financial creditors and sharing base resolution plan*

3.40. The Sub-committee had recommended that initiation of the pre-pack process should be by an application of the corporate debtor. However, it noted that "*Before making an application for initiation of pre-pack, the proposal should have buy-in of a certain threshold of its stakeholders to have reasonable assurance of resolution.*"[90] Therefore, it suggested that prior to making such an application, the corporate debtor should be required to avail an approval from a majority of its unrelated financial creditors for the initiation of the pre-pack process.

3.41. The **Committee agreed that the corporate debtor should require an approval from its unrelated financial creditors for the initiation of the pre-pack process**. It noted that since the process is voluntary, consensus among both the debtor and creditors is important. Decisions required to be taken at the pre-initiation stage of the pre-pack process are of the nature that require the same kind of sophistication as is required for approval of a resolution plan under the CIRP. Although the Code recognises various kinds of creditors, only unrelated financial creditors have the power to vote in the CoC in the CIRP. The Committee noted that this status of

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[88] ibid, Rule 20

[89] ibid, Rule 22

[90] Ministry of Corporate Affairs, *Report of Sub-Committee of the Insolvency Law Committee on Pre-Packaged Insolvency Resolution Process* (2020) para 3.21 <https://www.ibbi.gov.in/uploads/resources/24c7fc03cdffff69960ce374416fa646.pdf> accessed 1 June 2021

unrelated financial creditors is a core feature of the CIRP and the role of such creditors within the CoC has been upheld[91] by the Supreme Court. In line with the current approach of the Code, unrelated financial creditors of the corporate debtor may be best suited to grant approval at the pre-initiation stage of the pre-pack process as well.

3.42. Such approval of creditors at the pre-initiation stage is required to show that there is a broad consensus between the debtor and the financial creditors on the manner in which the corporate debtor proposes to resolve its debts. In other words, approval of unrelated financial creditors prior to initiation of the pre-pack process is indicative that a sufficient number of such creditors support the base resolution plan proposed by the corporate debtor (without compromising their right to choose a better plan in subsequent stages of the process). Considering this, the Committee noted that it may be appropriate that the threshold for pre-initiation approval be the same as that required for final approval of a plan. It noted that this may also help in more pre-packaged base plans eventually getting approved by the CoC in later stages of the proceedings. **Therefore, it recommended that sixty-six percent in value of the unrelated financial creditors of the corporate debtor should be required to approve the initiation of the pre-pack process.**

3.43. Moreover, the Committee discussed that to ensure that the unrelated financial creditors have access to relevant information required to provide such approval, the Code should mandate that the corporate debtor share copies of the base resolution plan, the declaration of majority of board of directors or partners (see para 3.36.), and the members' or partners' resolution (see para 3.39.) with its unrelated financial creditors prior to obtaining their approval. Additional information required to be shared in this regard may be detailed in the subordinate legislation.

[91] ibid, para 3.44

CHAPTER 4 – INITIATION OF PRE-PACK PROCESS

I. Filing and Admission of an Application

4.1. As noted above, an application for initiating the pre-pack process may be filed by a corporate debtor if it meets the eligibility criteria and has completed the pre-initiation requirements. Such an application should be filed with the Adjudicating Authority within the time stipulated in the declaration issued by the board of directors or partners of the corporate debtor (see para 3.36.). On receiving such application, the Adjudicating Authority shall decide whether to admit or reject the application and pass an order to this effect. The discussions of the Committee in respect of filing of the application by the corporate debtor, the admission or rejection of the application by the Adjudicating Authority, and the effect of the order of admission have been outlined below.

i. *Filing of application by corporate debtor*

4.2. The Committee discussed that a corporate applicant[92] shall file an application with the Adjudicating Authority, on behalf of the corporate debtor, in line with the application form provided in the subordinate legislation, along with the requisite fee and documents prescribed therein. It was discussed that the application should be submitted along with three kinds of documents, - (a) documents supporting the eligibility of the corporate debtor for the pre-pack process; (b) documents evidencing that the corporate debtor has completed the pre-initiation requirements; and (c) miscellaneous documents regarding the financial position of the corporate debtor.

4.3. *First*, in relation to supporting the corporate debtor's eligibility, the application form should require the corporate debtor to provide documents evidencing that the corporate debtor is an MSME and that the requisite default has occurred. Along with this, the corporate debtor should also provide an affidavit stating that it is eligible to be a resolution applicant as per Section 29A of the Code.

4.4. *Second*, in relation to demonstrating compliance with the pre-initiation requirements, it should submit copies of the declaration of the majority of directors or partners and the requisite resolution of members or partners. The corporate applicant should also be required to submit the form in which unrelated financial

[92] Insolvency and Bankruptcy Code, 2016, Section 5(5)

creditors have provided the approval for appointment of the resolution professional and the approval for initiation of the pre-pack process. In addition to this, it should also provide all relevant details of the relevant financial creditors along with the debts owed to them.

4.5. It was noted that a form recording consent of the resolution professional to be so appointed, along with a declaration regarding her eligibility for the same, should be provided with the application. Additionally, a report prepared by the resolution professional should also be submitted. This report should confirm if the corporate debtor meets the eligibility criteria, if it has satisfied the pre-commencement requirements and if the base resolution plan prepared by the corporate debtor conforms to the stipulated requirements.

4.6. *Third*, the Committee discussed that the application form may require submission of various documents that provide information about the financial position of the corporate debtor. For instance, as is required in the application form under Section 10 of the Code, the application form may require submission of a statement of affairs of the corporate debtor, its audited financial statements, relevant books of accounts, etc.

4.7. It was also felt that it may be difficult to thoroughly investigate if the corporate debtor has undertaken any actions that may fall within the scope of provisions related to avoidance of antecedent transactions (Sections 43-51) or fraudulent or wrongful trading (Sections 66 and 67). Considering that the time available during the formal conduct of the pre-pack process is very limited, there may be situations where such actions are left unidentified. Although the resolution professional may attempt to investigate and file such actions during the pre-pack process, the Committee noted that it may be useful to obtain a declaration regarding existence of any such transactions at the time of admission to deter such transactions in the lead up to the process and ensure transparency. Thus, it agreed that along with the application, the corporate applicant should submit a declaration stating if the corporate debtor in question has been the subject of any transaction within the meaning of Sections 43-51 or Sections 66-67.

ii. *Admission or rejection of application by Adjudicating Authority*

4.8. Once an application for initiating the pre-pack process is filed by the corporate debtor, the Adjudicating Authority shall pass an order either admitting or rejecting the application. The Committee discussed that the Adjudicating Authority should

analyse if the application is complete and if the corporate applicant has submitted the requisite documents along with the application. Based on the contents of such application, the Adjudicating Authority may assess if the corporate debtor is eligible for the pre-pack process and if it has complied with the pre-initiation requirements. The Committee discussed that, at this stage, the Adjudicating Authority should take caution to not get into any lengthy or comprehensive assessment of the solvency of the debtor or the appropriateness of the base resolution plan. Instead, the focus of the assessment at this stage should be to analyse if sufficient documentation has been provided for establishing that the application is complete. Further, to satisfy itself regarding the eligibility of the corporate debtor, the Adjudicating Authority may rely on the report of the resolution professional (see para 3.26.) since she oversees the pre-initiation stage as an independently regulated professional.

4.9. Although the efficiency of all kinds of insolvency proceedings hinges on the time taken to complete them, in a pre-pack process time is especially of essence at the admission stage. The pre-pack process is designed on the basis that the corporate debtor and its unrelated financial creditors have reached a broad consensus on the manner of resolving its insolvency. Such consensus will be based on certain agreed terms that would be reflected in the base resolution plan. The Committee discussed that, in practice, such a plan will be negotiated on various factors like value of the corporate debtor's assets, the value and nature of its debts, and the proposed manner of repayment and restructuring of debts. Since such factors will be time-sensitive, a delay in admission of the pre-pack application may lead to frustration of the terms agreed to by the parties. This may defeat the purpose of initiating a pre-pack process. Consequently, **the Committee suggested that NCLTs should attempt to prevent delays in admission or rejection of applications as far as possible.**

4.10. It also noted that the Code provides a time-period of fourteen days for admission or rejection of applications for triggering the CIRP[93] and the insolvency resolution process[94] under Part III of the Code. **The Committee felt that this may be emulated in the pre-pack process as well and agreed that the Code may provide a time limit of fourteen days for the admission or rejection of a pre-pack application, from the date of its filing.**

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[93] Insolvency and Bankruptcy Code, 2016, Sections 7(4), 9(5), and 10(4)

[94] ibid, Section 100(1)

iii. *Effect of order of admission*

4.11. When an order admitting an application for initiation of the pre-pack process is passed by the Adjudicating Authority, the pre-pack process formally commences. The Committee discussed that an order of admission in the pre-pack process may have similar effects to that of an admission order in CIRP. Thus, it agreed that the Adjudicating Authority should declare a moratorium, appoint a resolution professional, and cause a public announcement, to be made by the resolution professional, along with passing the order of admission. The discussion of the Committee in this regard is outlined below.

a. Declaration of moratorium

4.12. A moratorium is a stay on legal proceedings and transfer or disposal of assets of a debtor who is undergoing insolvency proceedings. It provides a calm period to the stakeholders to focus on insolvency proceedings and attempt to reach consensus on a rescue plan. It is for this reason that the moratorium under Section 14(1) has been provided in the CIRP under the Code. While contemplating the design of the CIRP, the BLRC Report noted –

> *"The motivation behind the moratorium is that it is value maximising for the entity to continue operations even as viability is being assessed during the IRP. There should be no additional stress on the business after the public announcement of the IRP. The order for the moratorium during the IRP imposes a stay not just on debt recovery actions, but also any claims or expected claims from old lawsuits, or on new lawsuits, for any manner of recovery from the entity."*[95]

4.13. The Committee discussed that the same rationale applies to the pre-pack process as well. It noted that a mandatory moratorium, as is provided under Section 14(1), is a core feature of the Code and provides a much-required calm period for smooth completion of the CIRP. Considering this, **the Committee agreed that a moratorium should be ordered by the Adjudicating Authority along with the order of admission. The scope of this moratorium should be similar to the moratorium under Section 14(1) of the Code, and the moratorium should remain in force until the pre-pack process comes to an end.**

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[95] Ministry of Finance, *The Report of the Bankruptcy Law Reforms Committee Volume I: Rationale and Design* (2015) para 5.3.1 <https://ibbi.gov.in/BLRCReportVol1_04112015.pdf> accessed 1 June 2021

4.14. It was noted that along with the moratorium, Section 14 also deals with ensuring continuation of essential and critical supplies during the moratorium period. Section 14(2) provides that the supply of essential services to the corporate debtor cannot be terminated, suspended or interrupted during the moratorium period. Such services include electricity, water supply, telecommunication services, and information technology services.[96] The purpose of this provision is to ensure that the corporate debtor has continued access to basic supplies that are necessary for "*ensuring orderly completion of the proceedings*".[97] Section 14(2A) provides for the continuation of critical supplies, i.e., goods or services that may be critical to protect and preserve the value of the corporate debtor and manage its operations as a going concern, subject to certain exceptions. The identification of supplies that may be critical are made by the interim resolution professional or the resolution professional, who then applies to the Adjudicating Authority to order their continual supply. This provision was inserted in the Code by way of an amendment to allow continuation of supplies that may not be essential to all businesses but are critical for running the corporate debtor as a going concern.[98] The Committee deliberated on whether provisions akin to Section 14(2) and (2A) are required in the pre-pack process.

4.15. While recommending that a moratorium similar to Section 14(1) should be provided in the pre-pack process, the Sub-committee Report suggested that "*The moratorium should not, however, cover essential and critical services as the promoters will continue to run the operations and the RP would neither decide critical services nor control the operations*."[99] The Committee agreed with this recommendation of the Sub-committee. It noted that in the pre-pack process, the management of the corporate debtor is not displaced and the business continues as usual. Thus, the management

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[96] Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016, Regulation 32

[97] Insolvency and Bankruptcy Code Bill, 2015, Notes on Clauses, p. 118

[98] Ministry of Corporate Affairs, *Report of the Insolvency Law Committee* (2020) para 8.13 - 8.19 <https://ibbi.gov.in/uploads/resources/c6cb71c9f69f66858830630da08e45b4.pdf> accessed 1 June 2021

[99] Ministry of Corporate Affairs, *Report of Sub-Committee of the Insolvency Law Committee on Pre-Packaged Insolvency Resolution Process* (2020) para 3.57 <https://www.ibbi.gov.in/uploads/resources/24c7fc03cdffff69960ce374416fa646.pdf> accessed 1 June 2021

and promoters of corporate debtors undergoing CIRP may be better placed to negotiate with their suppliers for continuation of the required supplies and services.

4.16. Further, unlike the CIRP, the resolution professional does not take over the management of the corporate debtor during the pre-pack process. Thus, the resolution professional may not be in a position to identify the supplies that are critical to the business of the corporate debtor in a pre-pack process. Identification of such critical supplies by the corporate debtor itself may be riddled with problems and be prone to misuse. Moreover, the pre-pack process is a timely and quick process. Due to such limited time, the pre-pack process may be perceived as less risky and may keep the goodwill of the business intact. Given this, it may be suitable to allow the corporate debtor to continue its business as it had prior to the initiation of the pre-pack process (subject to limitations discussed in para 5.16.). **The Committee, therefore, agreed that statutory provisions regarding the continuation of essential and critical supplies may not be required in the pre-pack process.**

b. Appointment of the resolution professional

4.17. As discussed above, a resolution professional is proposed and approved by unrelated financial creditors for the corporate debtor for overseeing the pre-initiation stage. The details of such resolution professional will be included in the application, along with her consent for formal appointment and a declaration regarding her eligibility.

4.18. The **Committee discussed that, as in CIRP, the Adjudicating Authority shall consider if the proposed resolution professional is eligible to be so appointed. If so, it shall pass an order confirming the appointment of the resolution professional along with the order of admission. Where the proposed resolution professional does not satisfy the eligibility requirements, the Adjudicating Authority shall appoint a resolution professional recommended by the IBBI.** The Committee discussed that this emulates the process for appointment of an interim resolution professional in CIRP, which is suitable for the pre-pack process as well.

4.19. Similarly, it discussed that the process for replacement of the resolution professional may also be similar to CIRP, and provisions of Section 27 may be made applicable to the pre-pack process.

c. Causing a public announcement

4.20. Once insolvency proceedings are initiated, it is important to announce the opening of such proceedings so that all stakeholders are aware about it. For instance, a public announcement is made under Section 15 of the Code forthwith after the admission of a CIRP application and appointment of the resolution professional. **The Committee noted that a similar public announcement should be made by the resolution professional once she is appointed. It agreed that the Adjudicating Authority should direct the making of such an announcement along with the order of admission of the pre-pack process.**

4.21. A call for claims is also made along with the public announcement in a CIRP. However, since the claims collation process in the pre-pack process is distinct from the CIRP (see part I of Chapter 5), the public announcement should be limited to the declaration that a pre-pack process has been initiated and should not include an invitation for claims.

II. Time Limit for Conduct of the Pre-Pack Process

4.22. In designing the pre-pack process, a key objective sought to be met is the timely resolution of stress for MSMEs. The Sub-committee had noted that MSMEs "*may not have stamina to survive prolonged insolvency proceedings spanning 180/270/330 days, as envisaged in the Code or withstand the extended timelines, that often prevail in practice.*"[100] Thus, from the very beginning of this reform process, there was broad agreement that the total time period of 330 days envisaged by the formal CIRP,[101] which can often be plagued by delays,[102] would be too lengthy.

4.23. The Sub-committee was cognisant that a value maximising solution under the pre-pack process would need to be governed by strict, yet implementable timelines. Towards this end, the Sub-committee recommended a shorter time-period of 120 days for completion of the pre-pack process. The Committee noted the recommendations of the Sub-committee favourably.

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[100] Ministry of Corporate Affairs, *Report of Sub-Committee of the Insolvency Law Committee on Pre-Packaged Insolvency Resolution Process* (2020) para 3.16 <https://www.ibbi.gov.in/uploads/resources/24c7fc03cdffff69960ce374416fa646.pdf> accessed 1 June 2021

[101] *See* Insolvency and Bankruptcy Code, 2016, Section 12

[102] Insolvency and Bankruptcy Board of India, *Insolvency and Bankruptcy News* (The Quarterly Newsletter of the Insolvency and Bankruptcy Board of India, Vol. 13, 2019) p. 18 <https://ibbi.gov.in/uploads/publication/62a9cc46d6a96690e4c8a3c9ee3ab862.pdf> accessed 1 June 2021

4.24. It was brought to the Committee's notice that insolvency frameworks that cater towards insolvency resolution of small businesses focus on reduction of costs and time needed for completion of the process. Globally, many frameworks have done this by shortening timelines, or eliminating certain formalities from the "standard" insolvency law.[103] For instance, the reorganization process for small businesses[104] as provided under Chapter 11 of the U.S. Bankruptcy Code are treated differently than a traditional Chapter 11 case primarily due to accelerated deadlines and the speed with which the plan is confirmed.[105] Moreover, the UNCITRAL Working Group's Draft Text on a Simplified Insolvency Regime. in its recent session in July, 2021, validates this approach by advocating for "*short time periods for all procedural steps in simplified insolvency proceedings, narrow grounds for their extension and the maximum number, if any, of permitted extensions.*"[106]

4.25. Considering the above, **the Committee agreed with recommendations of the Sub-committee and decided that the pre-pack process should be completed within a total of 120 days from the date of admission.** Further, the Committee noted that, in the interests of efficiency and maximisation of value, the time limit in the pre-pack process should be construed to be mandatory. It discussed that to enable such mandatory interpretation, suitable repercussions may be provided for breach of

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[103] *See* World Bank, *Report on the Treatment of MSME Insolvency* (2017) p. 12 <https://openknowledge.worldbank.org/bitstream/handle/10986/26709/114823-WP-PUBLIC-weds-510-MSME-Insolvency-report-low-res.pdf?sequence=1&isAllowed=y> accessed 28 May 2021

[104] These refer to two different special categories of Chapter 11: The first referred to as a 'small business case' created by the Bankruptcy Abuse Prevention and Consumer Protection Act and the second referred to as 'subchapter V' cases, under the Small Business Reorganisation Act, 2019

[105] *See* United States Courts, Chapter 11 Bankruptcy Basics, 'The Small Business Case and Small Business Debtors', <https://www.uscourts.gov/services-forms/bankruptcy/bankruptcy-basics/chapter-11-bankruptcy-basics> accessed 1 June 2021. *Also see* World Bank, *Saving Entrepreneurs Saving Enterprises: Proposals on the Treatment of MSME Insolvency* (2018) <https://openknowledge.worldbank.org/handle/10986/30474> accessed 1 June 2021. Specifically, for 'small business cases' under Chapter 11, the debtor is under a strict 180-day deadline, extendable up to 300-days to propose a plan, which has to be approved within 45 days of filing. In contrast, in ordinary Chapter 11 proceedings, while the debtor's exclusive period for filing a plan is only 120 days, it can be and is usually extended up to 18 months and there is no deadline for plan confirmation.

[106] United Nations Commission on International Trade Law Working Group V, *Draft text on a Simplified Insolvency Regime*, (54th session, 28 June – 16 July, 2021) para 12, p. 19 <https://uncitral.un.org/sites/uncitral.un.org/files/1052_clean_for_submission.pdf> accessed 1 June 2021

time limit.[107] Accordingly, the **Committee decided that the CoC should be required to approve or reject a resolution plan by the 90th day from the date of admission. Where no resolution plan is approved by the CoC until the 90th day, the resolution professional should be required to file an application with the Adjudicating Authority for termination of the pre-pack process.** The Committee felt that this would go a long way in promoting strict enforcement of the time limit for completion of the pre-pack process.

4.26. Where a resolution plan is submitted within the 90-day period or an application for termination is filed, **the Adjudicating Authority should pass suitable orders within a period of 30 days.**

[107] *See for example New India Assurance Company Limited v Hilli Multipurpose Cold Storage Private Limited* (2020) 5 SCC 757; *M/s SCG Contracts India Pvt. Ltd. v M/s KS Chamankar Infrastructure Pvt. Ltd.,* Civil Appeal No. 1638/2019, Supreme Court. Decision Date - 12 February 2019

CHAPTER 5: CONDUCT OF THE PRE-PACK PROCESS

I. Claims Collation Procedure

5.1. The Sub-committee recommended that in place of the claims collection process as envisaged under the CIRP, during the pre-pack process, the corporate debtor should provide a list of outstanding claims and the resolution professional should confirm this with the creditors. **The Committee agreed with the rationale of the Sub-committee to provide a simplified and faster claims verification process. However, it observed that the design of the pre-pack process should not compromise the sanctity of the claims collation process.**

5.2. The creditors wishing to be included for the purpose of voting and participation in the insolvency resolution of a corporate debtor are required to submit claims to the resolution professional. The Committee observed that similar to CIRP, the pre-pack process is a one-stop solution for all types of creditors to resolve their claims. Once the resolution plan is approved by the CoC and the Adjudicating Authority, the claims which are not part of the plan, would stand extinguished and the proceedings related to them stand terminated.[108] A creditor whose claim is not admitted will not be entitled to receive any dividend and will lose all possibility of recovering its debt owed by the corporate debtor. **Accordingly, the Committee recommended that the framework for the claims collation process should ensure that claims of all the creditors are considered and confirmed appropriately to ensure finality.** In this respect, the Committee discussed the different stages of the claims collation process in the manner discussed below.

i. *Stage I - Submission of list of claims by the corporate debtor*

5.3. The Sub-committee had recommended that at the commencement of the pre-pack process, a list of claims should be submitted by the corporate debtor. The Committee agreed with this suggestion. It observed that the legal framework should have sufficient safeguarding measures to avoid any wrongdoing on the part of the promoters or management of the corporate debtor to suppress any valid claims. The Committee was of the view that the promoters or management ought to exercise

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[108] *See Ghanashyam Mishra v Edelweiss Asset Reconstruction,* Civil Appeal No. 8129 of 2019, Supreme Court. Decision date – April 13, 2021; 2021 SCC OnLine SC 313

highest caution and standard of care while submitting the list of claims to the resolution professional.

5.4. They should ensure that claims of all the creditors are recorded correctly in the list of claims, supported by relevant documents evidencing the same. They should neither omit nor reduce a claim nor include or inflate a claim, other than what is legitimately owed to the creditor. **The Committee recommended that in case they are responsible for such nonfeasance, the law should provide adequate legal recourse for the creditors sustaining loss or damage as a consequence thereof. They should be responsible to pay compensation to the concerned creditors for the loss or damage sustained by them. Additionally, the Committee observed that there should be adequate punishment for such actions too.** This is necessary to deter the promoters and management of the corporate debtor from providing any false or misleading information in the list of claims.

ii. *Stage II - Confirmation of the list of claims by resolution professional*

5.5. Once the list of claims is submitted to the resolution professional, she will be required to confirm that the claims mentioned therein are rightfully owed by the corporate debtor. The resolution professional will independently confirm the claims owed to each creditor from the documents supporting the list of claims and the financial information received from the corporate debtor. Considering the consequences of an incorrect list of claims, 'confirmation' in this context implies that a high standard of care and skill is expected from the resolution professional for this exercise.

iii. *Stage III – Informing creditors about the confirmed claims*

5.6. After confirming the claims owed to the creditors of the corporate debtor, the resolution professional shall inform each creditor regarding their confirmed claims. The creditors will then have the option to raise objections to the claims confirmed by the resolution professional. Where any objection is raised by a creditor, she will be required to substantiate the same with supporting documents. These objections will be considered by the resolution professional, and where appropriate, the resolution professional should be empowered to modify the claims accordingly.

iv. *Stage IV – Maintaining an updated list of claims*

5.7. Post-receipt of the list of claims received from the corporate debtor, at each stage the resolution professional will update the list of claims. Thereafter, the resolution

professional shall be required to maintain an updated list of claims during the course of the pre-pack process and keep updating the same whenever she receives additional relevant information in relation to any claim owed by the corporate debtor. Further, the Committee felt that the above-mentioned stages of the claims collation process along with the safeguards will ensure that legitimate claims of all the creditors are part of the updated list of claims maintained by the resolution professional.

5.8. Post-admission, the pre-pack process is a public process, and the resolution professional is required to make a public announcement of its initiation. It is assumed that the stakeholders of the corporate debtor will have adequate information regarding the initiation of the pre-pack process. A creditor not forming part of the updated list of claims, may approach the resolution professional for submission of its claims. Considering the adverse effect of non-inclusion of a legitimate claim, the Committee felt that the resolution professional may consider the claim of such a creditor for inclusion in the list of claims. She may admit the claim of such a creditor, if it is genuine, and update the list accordingly.

II. Finalisation of the Information Memorandum

5.9. The Sub-committee had recommended that immediately after the commencement of the pre-pack process, a preliminary information memorandum should be provided by the corporate debtor.[109] The Committee agreed with the recommendation of the Sub-committee. It is supported by the rationale that the information memorandum is required to be prepared at the earliest, and being privy to the financial information of the corporate debtor, its management is best suited to provide a preliminary version of the information memorandum. On receipt of the preliminary information memorandum, the resolution professional will confirm its contents and prepare the information memorandum to be shared with the resolution applicants. **Similar to the approach adopted in case of list of claims, the Committee recommended that the law should provide adequate safeguards to ensure that reliable and authentic information is provided by the management and promoters of the corporate debtor. In case of any non-feasance, appropriate penal consequences should be provided.**

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[109] Ministry of Corporate Affairs, *Report of Sub-Committee of the Insolvency Law Committee on Pre-Packaged Insolvency Resolution Process* (2020) para 3.51 <https://www.ibbi.gov.in/uploads/resources/24c7fc03cdffff69960ce374416fa646.pdf> accessed 1 June 2021

III. Role of the Management of the Corporate Debtor

5.10. The Committee noted that an active role of the management of the corporate debtor during the conduct of the pre-pack process is a shift from the approach adopted under the CIRP. The Committee deliberated upon the need for continuing the existing management of the corporate debtor, the functions and duties performed by the management of the corporate debtor and safeguarding measures needed to avoid any abuse of process on the part of the original management and promoters.

i. *Need for continuing the existing management of the corporate debtor*

5.11. During the CIRP, the interim resolution professional/resolution professional performs two distinct sets of functions: She conducts the entire CIRP and manages the operations of the corporate debtor during CIRP.[110] The management of the affairs of the corporate debtor are vested in the interim resolution professional/resolution professional and the powers of the board of directors or partners of the corporate debtor are suspended.[111] This provides an assurance to the creditors that the assets of the entity will be protected.[112] The Committee noted that the Sub-committee had recommended a debtor-in-possession model for the pre-pack process wherein the existing management continues to be in possession of the corporate debtor. It suggested a hybrid approach of debtor-in-possession with creditors-in-control for the pre-pack process, with clear demarcation of the responsibilities among the corporate debtor, resolution professional, and the creditors.[113]

5.12. The Committee noted that the requirement of displacement of management of the corporate debtor was inserted keeping in mind the experience under the SICA of a

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[110] Insolvency and Bankruptcy Code, Sections 17, 18, 23 and 25

[111] Insolvency and Bankruptcy Code, Section 17 (1) (a) and (b)

[112] Ministry of Finance, *The Report of the Bankruptcy Law Reforms Committee Volume I: Rationale and Design* (2015) para 5.3.1 <https://ibbi.gov.in/BLRCReportVol1_04112015.pdf> accessed 1 June 2021

[113] Ministry of Corporate Affairs, *Report of Sub-Committee of the Insolvency Law Committee on Pre-Packaged Insolvency Resolution Process* (2020) para 3.37 <https://www.ibbi.gov.in/uploads/resources/24c7fc03cdffff69960ce374416fa646.pdf> accessed 1 June 2021

debtor-in-possession regime.[114] The Notes on Clauses to the Bill of the Insolvency and Bankruptcy Code, 2015 provided the following rationale for this approach –

> *A debtor-in-possession regime allows the existing management to remain in possession of the entity during the resolution process. Past experience suggests that a debtor-in- possession regime gives incentives to the management to propose and implement risky rescue measures, as the costs of failure (leading to liquidation) would largely be borne by creditors. Further, given the informational advantage that existing managers (who are typically under control of controlling promoters) have over other stakeholders,* ***giving them control over the corporate debtor during the corporate insolvency resolution process may result in them proposing risky measures or worse, siphoning off assets or resorting to delaying tactics to extract concessions from creditors.***[115]

5.13. The Committee discussed that the implementation of the IBC has established a robust institutional framework for insolvency and bankruptcy in India. Today the insolvency regime in India is benefited by a specialised group of insolvency professionals regulated by IBBI. Unlike the earlier regime, the creditors acting through the CoC have assumed a dominant role in resolving insolvency of the debtors. **In the light of this institutional backing, the Committee observed that the adoption of the hybrid model as suggested by the Sub-committee may work as long as suitable safeguards are included to limit abuse and prevent value destruction of the type that was prevalent under SICA.**

5.14. The Committee studied the approach adopted by other common law jurisdictions on the requirement to continue the management of the corporate debtor during the insolvency resolution process of MSMEs. Catalysed by the Covid-19 pandemic, countries are evolving their insolvency laws to provide frameworks that are more suited to small businesses. The UK introduced a new permanent "restructuring plan" procedure, wherein, under its moratorium provisions, the day to day running of the business of the debtor company remains with the directors (but under the

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[114] Ministry of Finance, *Interim Report of the Bankruptcy Law Reforms Committee* (2015) para 4.1, p. 40 <https://www.ibbi.gov.in/uploads/resources/57420f272e1515f0c9c137f1a6423d78.pdf> accessed 1 June 2021

[115] Insolvency and Bankruptcy Code, Bill, 2015, Notes on Clauses to clause 17

supervision of an insolvency practitioner).[116] Australia also introduced the 'Simplified Debt Restructuring Process' allowing small businesses to seek simplified debt relief and liquidation.[117] While the general insolvency procedure provides for placing control of the company with the creditors by appointing an independent external administrator,[118] the 'Simplified Debt Restructuring Process' allows directors to retain control over their company while working with a restructuring practitioner to devise a plan to reorganise the company's debts with creditor approval.[119]

5.15. Also, the Committee noted that the contemporary approach suggests benefits in continuing the management of the corporate debtor during insolvency procedures in case of MSMEs. The continuing presence of the debtor's pre-distress decision-makers may be critical to the MSME's viability, because of private information, existing relationships with counterparties, and/or the necessity of combining the costs of decision-making and residual risk-bearing.[120] The UNCITRAL Working Group's Draft Text on a Simplified Insolvency Regime for MSMEs has recently echoed this approach and has recommended that the debtor should remain in control of its assets and the day-to-day operation of its business with appropriate supervision and assistance of the competent authority.[121] This will encourage and incentivise early access of MSMEs to simplified insolvency proceedings and reduce concerns over stigmatization.[122] Such an approach will be cost effective, for instance,

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[116] *See* The Corporate Governance and Insolvency Act, 2020, amending and inserting 'Part A1' dealing with 'Moratorium', in the Insolvency Act, 1986 (June, 2020)

[117] *See* Corporations Amendment (Corporate Insolvency Reforms) Act 2020, Schedule 1

[118] Australian Government, Simplified Debt Restructuring: A Fact Sheet for Small Businesses, p. 2 <https://treasury.gov.au/sites/default/files/2020-12/simplified-debt-restructuring-fact-sheet_0.pdf> accessed 29 May, 2021

[119] ibid

[120] Ronald B. Davis and others, *Micro, Small, and Medium Enterprise Insolvency: A Modular Approach* (1st edn, Oxford University Press 2018), p. 62

[121] United Nations Commission on International Trade Law Working Group V, *Draft Text on a Simplified Insolvency Regime*, (58th Session, 3-7 May, 2021) p. 19 <https://uncitral.un.org/en/working_groups/5/insolvency_law> accessed 9 June 2021

[122] ibid, p. 25

the insolvency practitioners will not be required to run the business, the fees charged by them will be reduced.[123]

5.16. Accordingly, the Committee agreed with the recommendations of the Sub-committee to adopt a hybrid model of debtor-in-possession with creditor-in-control approach as long as it is complemented by appropriate safeguards to prevent abuse. The Committee noted that active debtor participation is one of the key features of the proposed pre-pack framework. Such an approach will ensure that the MSMEs are not disincentivised from seeking timely commencement of insolvency proceedings due to the risk of being displaced from the helm.[124] The fear of displacement in an alternative insolvency procedure like CIRP will incentivise the management or promoters to attempt to initiate a pre-pack process at an early stage of insolvency and to make positive efforts for achieving a successful resolution of insolvency. **Therefore, the Committee recommended that during the pre-pack process, the affairs of the corporate debtor shall be managed by its board of directors or partners, subject to control of the CoC and certain safeguarding measures as discussed below.**

ii. *Functions and duties of the management of the corporate debtor*

5.17. Since continuance of the existing management of the corporate debtor during an insolvency procedure is a radical change (compared to the displacement-oriented CIRP), the Committee noted that it is important to conceptualize how this change will work in practice. The Committee discussed that the management of the corporate debtor will manage its affairs or operate its business under the control and supervision of the CoC and the resolution professional; they shall be required to protect and preserve the value of the property of the corporate debtor and manage its operations as a going concern; cooperation and information sharing with

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[123]Aurolio Gurrea-Martinez, 'Implementing an Insolvency Framework for Micro and Small Firms' (Oxford Business Law Blog, 4 February, 2021) p. 18 <https://www.law.ox.ac.uk/business-law-blog/blog/2021/02/implementing-efficient-insolvency-framework-micro-and-small-firms> accessed 1 June 2021

[124] United Nations Commission on International Trade Law Working Group V, *Draft Text on a Simplified Insolvency Regime*, (58th Session, 3-7 May, 2021) p. 39 <https://uncitral.un.org/en/working_groups/5/insolvency_law> accessed 9 June 2021; *See also* Ronald B. Davis and others, *Micro, Small, and Medium Enterprise Insolvency: A Modular Approach* (1st edn, Oxford University Press 2018), p. 61,62; *Also see* Aurolio Gurrea-Martinez, 'Implementing an Insolvency Framework for Micro and Small Firms', (Oxford Business Law Blog, 4 February, 2021) p. 18. <https://www.law.ox.ac.uk/business-law-blog/blog/2021/02/implementing-efficient-insolvency-framework-micro-and-small-firms> accessed 1 June 2021

the resolution professional and the CoC; and the Central Government and the IBBI should have powers to stipulate their standards of conduct during the pre-pack process.

a. Control of CoC over the management of the corporate debtor

5.18. The Committee discussed the nature of functions and duties performed by the corporate debtor during the pre-pack process. As discussed above, the board of directors and partners of the corporate debtor are responsible for managing its affairs. The Committee observed that similar to the CIRP regime, in the hybrid structure proposed by the Sub-committee, creditors should play a dominant role in taking key decisions in relation to the corporate debtor during the pre-pack process. In this regard, the Committee noted that Section 28 lists out certain actions in respect of the corporate debtor that may be taken with prior approval of the CoC. These actions relate to special situations wherein the rights of creditors are adversely affected or change is required to the capital structure, ownership or management of the corporate debtor.[125] **Accordingly, the Committee recommended that the management of the corporate debtor shall not be permitted to take any of the actions listed under sub-section (1) of Section 28 of the Code, without prior approval of the CoC.**

b. Duty to protect and preserve the value of the property of the corporate debtor and manage its operations as a going concern

5.19. During the CIRP, the interim resolution professional has to make every endeavour to protect and preserve the value of the property of the corporate debtor and manage its operations as a going concern.[126] This helps preserve the value of the corporate debtor and facilitates rescue of the corporate debtor.[127] The Committee discussed that a similar mandate should be provided during the pre-pack process to ensure value preservation during the process. **Since the board of directors or the partners of the corporate debtor are responsible for operating its business, the Committee recommended that they shall endeavour to protect and preserve the**

[125] Insolvency and Bankruptcy Code, Bill, 2015, Notes on Clauses to clause 20

[126] Insolvency and Bankruptcy Code, 2016, Section 20

[127] *See* Insolvency and Bankruptcy Code, 2016, Section 20; *Also see* Wadhwa Law Chamber's, *Guide to Insolvency and Bankruptcy Code*, (2nd edn, Wadhwa Brothers 2021) p. 933

value of the property of the corporate debtor and manage its operations as a going concern.

5.20. Additionally, the Committee noted that the corporate debtor often needs access to external finance in order for continued trading during the course of insolvency proceedings.[128] As suggested by the Sub-committee, **the Committee recommended that the access to interim finance should be available to the corporate debtor subject to the approval of CoC and it shall be included in the costs of the pre-pack process.**

c. Cooperation and information sharing with the insolvency professional and the CoC

5.21. During the pre-pack process, the management is responsible for managing the affairs of the corporate debtor and operating its business. This may result in information asymmetry between the management, the resolution professional and the CoC. **The Committee recommended that the legal framework should seek to achieve symmetry of information and require the management to share the relevant financial information with the resolution professional or the CoC as and when required.** Further, they shall be required to cooperate with the resolution professional and in case of non-cooperation the resolution professional may seek assistance from the Adjudicating Authority as provided under sub-sections (1) and (2) of Section 19 of the Code.

d. Powers of the IBBI and Central Government to impose standards of conduct for the management of the corporate debtor

5.22. The Committee felt that from the onset of insolvency and commencement of the pre-pack process, the management of the corporate debtor operating its business is required to act in a fiduciary capacity. They shall exercise their control over the affairs of the corporate debtor, subject to the general supervision of the CoC and will be required to apply their business judgment to foster the continuation of its operations and preserve (and if possible, enhance) its financial status. However, the Committee noted that under no circumstances the affairs of the corporate debtor should be managed in a manner that undermines the interests of the creditors or other stakeholders in derogation to the objectives of the Code.

[128] Insolvency and Bankruptcy Code Bill, 2015, Notes on Clauses to clause 20

5.23. Since the concept of debtor-in-possession is a new introduction to the scheme of the Code, the Committee felt that there will be a need to take flexible measures to set new standards of conduct for the management and owners of the corporate debtor to uphold the object and purpose of the Code, and to avoid any abuse of process. **Accordingly, the Committee recommended that the Central Government and the IBBI should be equipped with appropriate powers to stipulate standards of conduct for the management, promoters, members, personnel or partners of the corporate debtor.** Such powers will also be useful to resolve potential conflicts with statutory and contractual rights and obligations of the management and the members or partners of the corporate debtor during the process.

iii. *Safeguards*

5.24. The existing management of the corporate debtor is required to perform the aforesaid functions and duties from the commencement of the pre-pack process and till the closure of the pre-pack process. The Committee noted that during the course of the pre-pack process, the existing management or the promoters of the corporate debtor may attempt to manage the affairs of the corporate debtor in a manner which is detrimental to the interests of the creditors and other stakeholders, and in derogation of the provisions of the Code. For instance, where the CoC approves a competing resolution plan, the management or the promoters of the corporate debtor may try to misappropriate or siphon off the funds and assets of the corporate debtor in the immediate aftermath of such approval. **Therefore, the Committee recommended that the proposed legal framework for the pre-pack process should have sufficient safeguards to avoid abuse of the process. The Committee felt that appropriate penalties and punishments should be envisaged in the law to address, check and deter any misuse of the process by the management and promoters of the corporate debtor.**

iv. *Vesting the management of the corporate debtor with the resolution professional*

5.25. As discussed above, the pre-pack process is designed to be a debtor-in-possession process with creditor-in-control features. While sufficient checks to prevent possible misuse by corporate debtors have been built into the design of the process, the Committee felt that there may be scenarios where the management of the corporate debtor would need to be displaced. The Committee first reviewed international practices in this regard.

5.26. The UNCITRAL Legislative Guide discusses that in cases where the debtor continues to manage the operations of the debtor in reorganisation proceedings, the "*ongoing role may depend in large part upon the debtor acting in good faith during the reorganization proceedings; where it does not, its continuing role may be of questionable value.*"[129] A similar approach is advocated for by the UN Working Group's Draft Text on a Simplified Insolvency Regime, which provides for 'limited or total displacement of the debtor-in-possession' such that the competent authority should be authorised to decide on such displacement on a case-by-case basis where the micro or small enterprise debtor is responsible for poor management.[130] The Draft Text reasons that –

> "*This [text] recommends that the competent authority should be authorized to decide on displacement and terms of displacement on a case-by-case basis but circumstances justifying limited or total displacement and persons who may displace the debtor-in-possession should be specified in the law itself to avoid abuses, including unfair and discriminatory treatment of the debtor.*"[131]

5.27. Due to this, some jurisdictions allow courts to transfer the management of the debtor to an insolvency practitioner or trustee on misconduct by the debtor during insolvency proceedings. For instance, Chapter 11 of the US Bankruptcy Code, which follows a debtor-in-possession approach, allows bankruptcy courts to appoint a trustee to displace the management of the debtor at any time prior to plan confirmation.[132] Such an order may be passed by a bankruptcy court if it believes that the debtor has committed fraud, dishonest, incompetence or gross mismanagement during the insolvency proceedings or if it believes that it would be in the best interests of "*creditors, any equity security holders, and other interests of the*

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[129] *See* United Nations Commission on International Trade Law, *Legislative Guide on Insolvency Law*, (2005) Part two <https://uncitral.un.org/en/texts/insolvency/legislativeguides/insolvency_law> accessed 1 June 2021

[130] *See* United Nations Commission on International Trade Law Working Group V, *Draft Text on a Simplified Insolvency Regime*, (58th Session, 3-7 May, 2021) <https://uncitral.un.org/en/working_groups/5/insolvency_law> accessed 9 June 2021

[131] ibid

[132] Title 11 of the United States Code, Section 1104

estate."[133] Notably, although courts have been granted such powers, they are only exercised in exceptional circumstances.

5.28. The Committee took note of the above and attempted to envisage circumstances where the management of a corporate debtor undergoing the pre-pack process would need to be taken over by the resolution professional. It discussed that in cases where the corporate debtor engages in fraudulent activities or mismanages its affairs during the pre-pack process, it will not be desirable to allow it to continue in management. For instance, if the management of the corporate debtor attempts to siphon off its assets during the pre-pack process or does not run it as a going concern deliberately.

5.29. Although sufficient supervisory powers have been given to the CoC and the resolution professional, power to displace the management of the corporate debtor may be an important deterrent to ensure that the management does not engage in any wrongful conduct. For instance, in a scenario where the existing management of the corporate debtor knows that its resolution plan is not going to be approved, it may start mismanaging its affairs to deter any third-party resolution applicant from taking over its business. Although the CoC has the option to apply to the Adjudicating Authority to convert the pre-pack process into a CIRP, this remedy may not be value maximising if significant progress has already been made in the pre-pack process. In such circumstances, replacing the management of the corporate debtor while still continuing the pre-pack process will be an effective solution.

5.30. Considering the above, **the Committee agreed that the Code should enable the Adjudicating Authority to pass an order vesting the management of the corporate debtor with the resolution professional.** The Committee noted the following in respect of exercise of such power by the Adjudicating Authority –

> *First,* since the CoC drives the pre-pack process, it may be best suited to decide if there is a need to make an application to the Adjudicating Authority to pass an order vesting the management of the corporate debtor with the resolution professional. Therefore, the Committee discussed that **where the CoC approves the filing of such an application by a vote of sixty-six percent of its voting share, the resolution professional must apply to the Adjudicating Authority for the same**. It was noted, however, that allowing requests for vesting orders after the

[133] Title 11 of the United States Code, Section 1104(a)

approval of a resolution plan by the CoC may delay the consideration of the plan by the Adjudicating Authority and make the process cumbersome. Thus, the CoC should only be permitted to pass a vote regarding vesting from the date of its constitution until a resolution plan has been approved by it.

Thereafter, **the Adjudicating Authority shall pass an order of vesting only if it is of the opinion that the affairs of the corporate debtor have been conducted in a fraudulent manner or there has been gross mismanagement of its affairs**. However, such fraud or mismanagement should have taken place during the pre-pack process, and parties cannot claim vesting orders for acts committed by the corporate debtor prior to initiation of the pre-pack process. The Committee was conscious that the reason for passing a vesting order is not to penalise criminal actions, but to rectify the effects of such actions on the sanctity of the pre-pack process. Therefore, assessment of wrongful conduct by the management of the corporate debtor should be limited to its actions during the process. It was also noted that the Adjudicating Authority should only pass vesting orders in exceptional circumstances, and only where at least one of the grounds of fraud or gross mismanagement have been met. Caution should be exercised to not pass vesting orders for minor lapses that do not affect the sanctity of the pre-pack process.

Once a vesting order is passed by the Adjudicating Authority, the resolution professional will exercise powers relating to managing the affairs of the corporate debtor, like she does in the CIRP. Therefore, **suitable provisions relating to powers of the resolution professional for management of the affairs of the corporate power under CIRP should be extended to the pre-pack process if a vesting order is passed**.

IV. Role of CoC

5.31. The Committee discussed that the role of the CoC in relation to the conduct of the insolvency process is firmly established under the provisions of Chapter II of Part II of the Code. **The Committee recommended that a creditor-in-control regime similar to the CIRP should be extended to the pre-pack process and the role of the CoC as envisaged and detailed under Chapter II of Part II, ought to be retained in the pre-pack process. In line with this, it was agreed that the CoC should be composed of unrelated financial creditors of the corporate debtor.** It

should exercise decision making powers at various stages of the pre-pack process, such as, by voting to replace the resolution professional, vesting the management of the corporate debtor with the resolution professional, approving a resolution plan, and terminating the process or initiating a CIRP.

i. *Constitution of the CoC*

5.32. The Committee noted that time-efficiency is a key feature of the pre-pack process. The CoC will perform a primary role in respect of the conduct of the pre-pack process. In order to ensure timely completion of the process, the CoC is required to be constituted at the earliest. The Sub-committee had recommended that the CoC should be constituted based on the list of claims provided by the corporate debtor and confirmed by the resolution professional.

5.33. As discussed in para 5.5., the Committee noted that at stage II of the claims collation process, the resolution professional confirms the list of claims received from the corporate debtor. The safeguarding measures at stage I and an independent confirmation by the resolution professional at stage II will ensure that the list of claims maintained at the end of stage II contains authenticated and reliable information. Therefore, **the Committee recommended that the resolution professional shall form the CoC on the basis of the list of claims as confirmed by her at stage II. In case there is any update in the list of claims at subsequent stages, accordingly, the resolution professional shall alter the composition of the CoC and such alteration shall not invalidate any past decisions made by the CoC.**

ii. *Voting threshold and basis of voting by CoC*

5.34. **The Committee recommended that the voting threshold for taking decisions by the CoC should be consistent with the CIRP.** For instance, all major decisions should be approved by sixty-six percent of the voting share in the CoC, and all other decisions should be taken by a majority of fifty one percent of its voting share. Further, the Sub-committee recommended that the CoC should take its decisions on a present-and-voting basis. It suggested that the votes of absentee creditors should be excluded from the total votes while calculating if such thresholds have been met. The Committee considered the merits of deviating from the voting thresholds as provided in the CIRP.

5.35. It was brought to the Committee's notice that the present and voting threshold was suggested for the pre-pack process in order to avoid any bottlenecks in the voting

process, and to ensure that the lack of creditor participation does not obstruct the decision-making. However, the Committee felt that the present and voting requirement may instead distort the decision of the CoC, as voting should be based on the overall exposure, and not simply on the basis of the creditors present at the time of voting. **Thus, it was agreed that the voting criteria should be on a voting share basis and not on a present and voting basis in the pre-pack process. Consequently, the threshold as well as the criteria for voting by the CoC in the pre-pack process should be the same as that provided in CIRP.**

iii. *Authorised Representatives for certain classes of creditors*

5.36. The Committee discussed whether for certain classes of creditors, such as bondholders, etc., the requirement for appointment of authorised representatives should be retained. Such an authorised representative is appointed to represent such classes of creditors and vote on their behalf in the meetings of the CoC. The Sub-committee had recommended that the requirement for appointing such authorised representatives may be dispensed with as it adds an additional layer in the decision-making process and may lead to delays.

5.37. The Committee considered the above recommendation of the Sub-committee, but disagreed with it. It was felt that where creditors are dispersed or varied, with divergent interests, there may be a need for an authorised representative for bringing forward the collective view of such classes of creditors. In fact, the appointment of authorised representatives would actually help avoid bottlenecks in a shorter, time-bound process. The Committee also noted that in some MSMEs, especially those falling within the category of medium-sized enterprises, there may be large CoCs if the corporate debtor has creditors like bond and deposit holders. It may not be possible to have fruitful negotiations in such large meetings and the inability to appoint an authorised representative may decrease the efficiency of negotiations. This view is in consonance with the reasoning as per which authorised representatives were first brought into the Code for representation of the views of classes of financial creditors above a certain number or threshold.[134]

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[134] Ministry of Corporate Affairs, *Report of the Insolvency Law Committee* (2018) para 10.8 <https://ibbi.gov.in/uploads/resources/ILRReport2603_03042018.pdf> accessed 1 June 2021

5.38. **Therefore, the Committee recommended that the mechanism for representation of certain classes of creditors through authorised representatives should be provided for in the pre-pack process, as it is provided under the CIRP.**

V. Role of Resolution Professional

5.39. An insolvency professional, who may be appointed as an interim resolution professional or resolution professional, plays a critical role in the CIRP. She conducts the CIRP from the date of its admission until it comes to an end. The BLRC Report envisaged this role of the resolution professional and noted that –

> "*This entire insolvency and bankruptcy process is managed by a regulated and licensed professional namely the Insolvency Professional or an IP, appointed by the adjudicator. In an insolvency and bankruptcy resolution process driven by the law there are judicial decisions being taken by the adjudicator. But there are also checks and accounting as well as conduct of due process that are carried out by the IPs. Insolvency professionals form a crucial pillar upon which rests the effective, timely functioning as well as credibility of the entire edifice of the insolvency and bankruptcy resolution process.*"[135] (emphasis supplied)

5.40. The resolution professional in CIRP is tasked with various responsibilities, including managing the operations of the corporate debtor; reducing information asymmetry between the corporate debtor and its financial creditors; managing the process of inviting resolution plans; confirming eligibility of resolution plans for approval; etc. The resolution professional also acts as an interface between the corporate debtor, the CoC and the Adjudicating Authority involved in the CIRP. She, therefore, facilitates the smooth conduct of the CIRP for all key stakeholders involved in the process.

5.41. The role of the resolution professional in a CIRP is a core feature of the process. The Committee discussed that although the management of the corporate debtor in a pre-pack process is not displaced, other functions that are performed by the resolution professional in a CIRP should be emulated in the pre-pack as well. Further, the design of the process should ensure that the resolution professional is able to smoothly conduct the process, while being able to access all relevant

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[135] Ministry of Finance, *The Report of the Bankruptcy Law Reforms Committee Volume I: Rationale and Design* (2015) para 4.4 <https://ibbi.gov.in/uploads/resources/BLRCReportVol1_04112015.pdf> accessed 1 June 2021

information as well as maintaining supervision over the activities of the management of the corporate debtor.[136] This is consistent with the approach of the Sub-committee in this regard.

5.42. The recommendations of the Committee relating to the powers and duties of the resolution professional, along with the fee payable to her for her services in the pre-pack process, are provided below.

i. *Powers of the resolution professional*

5.43. The Committee considered the contours of the role and involvement of the resolution professional upon admission of the application for initiation of the pre-pack process. It discussed that maintaining information symmetry between parties is especially relevant in the pre-pack process. Since the debtor's management continues to operate throughout the pre-pack process, it is essential that adequate disclosures are made by the corporate debtor. Therefore, **the Committee noted that the resolution professional should have the power to access books of accounts, records and information available with the corporate debtor. Further, the resolution professional should also have powers to access books, records and information related to the corporate debtor from other sources, similar to the powers provided in Section 17(2)(c) and (d) of the Code**.

5.44. Further, if creditors feel like there is inadequate supervision over the debtor, they may lose trust in debtor-led solutions and be quick to request displacement of the debtor's management, which may eventually lead to an increase in the costs of the proceedings.[137] Given this, **it was agreed that the resolution professional should have the power to attend all meetings of the members, board of directors, any committees of directors or partners of the corporate debtor.** This will promote transparency in the process and allow the CoC to keep a check on the activities of the management of the corporate debtor through the resolution professional.

5.45. In addition to this, the Committee discussed that an important function of the resolution professional in a CIRP is to investigate and file applications for the

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[136] A similar approach has also been suggested by the International Monetary Fund, in its report on *Orderly and Effective Insolvency Procedures* (1999), <https://www.imf.org/external/pubs/ft/orderly/> accessed 1 June 2021

[137] *See* Ronald B. Davis and others, *Micro, Small, and Medium Enterprise Insolvency: A Modular Approach* (1st edn, Oxford University Press 2018)

avoidance of any antecedent transactions[138] or fraudulent or wrongful trading[139]. It was highlighted that not only are these provisions linked to preservation of commercial morality, they are also aimed at swelling the asset pool available for distribution to creditors.[140] The underlying policy of these provisions is to prevent unjust enrichment of one party at the expense of other creditors.[141]

5.46. **The Committee agreed that the resolution professional should have similar powers to investigate and file applications for avoidance of antecedent transactions and fraudulent or wrongful trading**. Although the time available to carry out thorough investigations will be limited in the pre-pack process, it is necessary to have sufficient checks on any undesirable transactions entered into by the corporate debtor in the twilight period leading up to the pre-pack process. Given this**, the Committee agreed that the relevant provisions governing avoidance of antecedent transactions (Sections 43-51) and fraudulent and wrongful trading (Sections 66 and 67) during CIRP, should be made applicable to the pre-pack process as well. Similarly, allied provisions (like Section 26) should also be extended to the pre-pack process.**

ii. *Duties of the resolution professional*

5.47. Principally, it was discussed that the resolution professional should have the duty to act independently, avoid conflicts of interest and exercise her powers in a manner that is in the best interests of stakeholders of the corporate debtor. To this end, she should maintain complete compliance with the regulations issued by the IBBI for the conduct of insolvency professionals, including the code of conduct detailed in such regulations.[142]

5.48. **The Committee noted that the resolution professional should undertake procedural tasks to enable smooth conduct of the pre-pack process**, like she does in a CIRP. For instance, the resolution professional should confirm the list of claims provided by the corporate debtor and inform creditors about their claims; constitute

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[138] Insolvency and Bankruptcy Code, 2016, Sections 43-51

[139] ibid, Sections 66 and 67

[140] Kristin Van Zwieten, Goode on Principles of Corporate Insolvency Law (5th edn, Sweet and Maxwell 2018) p. 616

[141] ibid

[142] *See* Insolvency and Bankruptcy Board of India (Insolvency Professional) Regulations, 2016

the CoC and convene and attend its meetings; prepare the information memorandum; etc.

5.49. Additionally, as noted above, the resolution professional also acts in a supervisory capacity in the pre-pack process. Consequently, **she should have the duty to monitor the activities of the corporate debtor** utilising her powers discussed above. **The resolution professional should inform the CoC immediately if she suspects or has come across any evidence indicating that the board of directors or partners of the corporate debtor have breached their obligations provided under the Code.**

iii. *Fee and expenses of the resolution professional*

5.50. In the case of MSME insolvency, which is likely to have limited value of assets, passivity of some stakeholders and lack of market participation, the need for the insolvency process to expressly include mechanisms for pre-determination of fee and expenses of the insolvency professional that is conducting the process becomes that much more important.[143] Clarifying the manner of determining the fee and expenses that may be incurred by such insolvency professionals may promote their independence and aid in maintaining a clear delineation of responsibility.

5.51. Primarily, **the Committee agreed that any fee paid to and expenses incurred by the resolution professional should be included in the pre-pack process costs and be paid in priority to other debts. This is in line with the treatment of such fees and expenses under the CIRP.**[144] Further, to ensure that there is clarity in determination of such fee and expenses, the Committee agreed that the subordinate legislation should clarify the manner in which such fee and expenses will be borne.

5.52. However, it is important to ensure that the CoC is ultimately approving any fee and expenses that are eventually included in the costs of the pre-pack process. Given this, **the Committee decided that the Code should provide the CoC with an explicit right to impose limits or conditions on the fee and expenses of the resolution professional. Further, any fee and expenses owed to the resolution**

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[143] Ronald B. Davis and others, *Micro, Small, and Medium Enterprise Insolvency: A Modular Approach* (1st edn, Oxford University Press 2018), p. 84. This pre-determination should not be a lump sum, but rather the regulation of criteria that would allow the judge/agency to determine the fee. The criteria ought to be linked with the complexity of the case, the value of assets, and should provide for the increase of the fee based on successful events (approval of a plan, sale as a going concern, etc.). In many jurisdictions, a minimum fixed amount for the insolvency practitioners is also set by regulation/law.

[144] Insolvency and Bankruptcy Code, 2016, Sections 5(13) and 30(2)(a)

professional for her services at the pre-initiation stage, will require to be ratified by the CoC.

VI. Costs of the Pre-pack Process

5.53. Process costs of insolvency proceedings are often given priority in repayment over other debts. Under the CIRP, for instance, the resolution plan is required to provide priority to repayment of process costs over other payments. Similarly, Section 53 provides priority to repayment of liquidation and CIRP costs over other payments while distributing proceeds in liquidation. **The Committee discussed that a resolution plan in a pre-pack process should also provide priority to repayment of the pre-pack process costs over all other payments. Further, whenever the pre-pack process continues into a CIRP (see para 7.26.) or leads to liquidation (see para 7.35.), pre-pack process costs should be given similar priority within the repayments in such CIRP or liquidation process.**

5.54. Further, as discussed in paras 5.20. and 5.51., the amount of interim finance and the costs incurred in raising it as well as the fee and expenses of the resolution professional will form part of the pre-pack process costs. Since the management of the corporate debtor is not displaced in the pre-pack process, the costs of running the business of the corporate debtor need not be part of the pre-pack process costs. However, if a vesting order is passed, the costs incurred by the resolution professional in running the business of the corporate debtor would form part of the pre-pack process costs. Finally, where the government has undertaken any expense to facilitate the pre-pack process, it shall also form part of the pre-pack process costs.

CHAPTER 6: CONSIDERATION AND APPROVAL OF RESOLUTION PLANS

6.1. The Committee noted the recommendations made by the Sub-committee in relation to the consideration and approval of resolution plans. The Sub-committee had recommended that the pre-pack process should start with a base resolution plan.[145] This can either be submitted by the corporate debtor or arranged by the CoC.[146] Further, it recommended that the pre-pack process should offer two optional approaches, one without Swiss challenge but with no impairment to operational creditors, and another with Swiss challenge with the rights of operational creditors and dissenting financial creditors subject to minimum payment requirements provided under Section 30(2).[147] The Sub-committee conceptualised the Swiss challenge method as the process of competition between the base resolution plan and the resolution plans received from the open market. The Committee agreed with the basic framework suggested by the Sub-committee for consideration and approval of the resolution plan by the CoC. In this light, the Committee made the following recommendations.

I. General Principles

i. *Continuance of core features of CIRP*

6.2. The Committee discussed that during the course of the last five years of its implementation, several concepts under the Code have been well-received by courts and tribunals in India. This has resulted in the evolution of a specialized insolvency jurisprudence in the country. **The Committee suggested that while considering a framework for consideration and approval of resolution plans during the pre-pack process, due regard should be given to the insolvency jurisprudence evolved till date. Specifically, caution must be exercised in altering the core features of the Code that have been upheld by the Supreme Court in several cases.**

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[145] Ministry of Corporate Affairs, *Report of Sub-Committee of the Insolvency Law Committee on Pre-Packaged Insolvency Resolution Process* (2020) paras 3.71-3.74 <https://www.ibbi.gov.in/uploads/resources/24c7fc03cdffff69960ce374416fa646.pdf> accessed 1 June 2021

[146] ibid, para 3.72

[147] ibid, para 3.73

6.3. As discussed in detail below, the Committee analysed the recommendations of the Sub-Committee which require alteration to the manner of consideration and approval of a resolution plan, as envisaged for CIRP under Chapter II of Part II of the Code.[148] This procedure will be peculiar to the pre-pack process and a new development in relation to the existing insolvency frameworks under the Code. **Therefore, the Committee recommended that the basic framework for the manner of consideration and approval of resolution plans should be hardwired under the Code. It should adequately balance the interests of the original management, the creditors and the third-party resolution applicants participating in the pre-pack process. In furtherance of the same, the IBBI should have powers to regulate the process of consideration and approval of the resolution plan during a pre-pack process.**

6.4. Further, in case of the CIRP, Section 30 of the Code encapsulates the manner in which the resolution plan may be submitted by a resolution applicant. It also provides for examination of the plan by the resolution professional and its approval by the CoC. The Committee noted that the pre-pack process provides an alternate method for consideration and approval of the resolution plan, and the provisions of the pre-pack process will differ from the requirements of Section 30. However, the Committee observed that certain basic features of Section 30 should be extended to the pre-pack process, in the following manner –

a. *Concepts of Resolution Applicant and Resolution Plans* - **The Committee recommended that the concept of resolution applicant and resolution plan under the pre-pack process should be largely similar to how they are used in a CIRP.** Since the corporate debtor submits a resolution plan (base resolution plan), it will also be considered to be a resolution applicant. It may submit a resolution plan individually or jointly with another person[149] and the assessment of eligibility criteria under Section 29A should be done accordingly. Further, the Committee observed that unless otherwise provided, the base resolution plan will essentially be a resolution plan submitted by the corporate debtor soon after

[148] ibid, paras 3.61 to 3.74

[149] Insolvency and Bankruptcy Code, 2016, Section 5(25) – As per this Section, the resolution applicant means a person who individually or jointly with any other person submits a resolution plan.

commencement of the process.[150] It may include provisions for the restructuring of the corporate debtor, including by way of merger, amalgamation and demerger.[151]

b. *Eligibility affidavit for Section 29A* - As discussed in Chapter 3, Section 29A is made applicable to the pre-pack process and persons filing resolution plans (including the corporate debtor) are required to comply with the same. **Accordingly, the Committee recommended that sub-section (1) of Section 30 should be made applicable to the pre-pack process and a resolution applicant will be required to provide an affidavit that it is eligible under Section 29A.**

c. *Mandatory contents of resolution plan* – Section 30(2) provides for the mandatory contents of the resolution plan including the manner of payment to operational creditors and dissenting financial creditors. **The Committee was of the view that any resolution plan, including the base resolution plan, submitted during the pre-pack process shall be required to abide by the requirements of Section 30(2).** For instance, the resolution plan shall provide for the payment of costs incurred during the pre-pack process in priority to the payment of other debts of the corporate debtor. Further, the Committee noted that the IBBI has powers to specify additional requirements for resolution plans under CIRP.[152] **In furtherance of the objectives of the Code and in order to ensure a successful resolution during the pre-pack process, the IBBI may provide additional or different requirements for the base resolution plan. Where such requirements are specified, the base resolution plan shall conform to the same.**

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[150] Insolvency and Bankruptcy Code, 2016, Section 5(26) – As per this Section, a resolution plan means a plan proposed by resolution applicant for insolvency resolution of the corporate debtor as a going concern in accordance with the provisions of Part II of the Code.

[151] Insolvency and Bankruptcy Code, 2016, *Explanation* to Section 5(26)

[152] Insolvency and Bankruptcy Code, 2016, Section 30(2)(f)

ii. *Preserving the commercial wisdom of the CoC*

6.5. Under Chapter II of Part II of the Code, all decisions on matters of consideration and approval of resolution plans are taken by the CoC.[153] The appropriate solution for resolution of an entity is voted on by the CoC and there are no constraints on the proposals that the resolution professional can present to the CoC in this regard.[154] The Committee noted that this supremacy of the commercial wisdom of the CoC during the CIRP has been reaffirmed time and again by the Supreme Court.[155] It is a settled position of law that the Adjudicating Authority cannot interfere on merits with the commercial decision of the CoC in relation to the consideration and approval of resolution plans.[156] Limited judicial intervention is permitted to confirm that the CoC has complied with the requirements of the Code and applicable regulations issued by the IBBI.[157]

6.6. The Committee noted that a subset of the commercial wisdom of the CoC as recognised by the courts and tribunals relates to the procedure followed during the resolution process. Under Section 30(3), the resolution professional is required to present all eligible resolution plans to the CoC. The Code is largely silent on the manner of consideration and approval of the resolution plans. The IBBI has specified certain regulations for regulating the conduct of the CoC during the resolution process, especially while considering and evaluating resolution plans.[158] Some of them are self-regulating specifications for the CoC, and courts and tribunals at several instances have denied judicial intervention as they fall within the commercial wisdom of the CoC.[159]

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[153] *See* Ministry of Finance, *The Report of the Bankruptcy Law Reforms Committee Volume I: Rationale and Design* (2015) Chapter 5, under the heading 'Business decisions by a creditor committee' <https://ibbi.gov.in/BLRCReportVol1_04112015.pdf> accessed 1 June 2021

[154] ibid, Chapter 5 under the heading 'No prescription on solutions to resolve the insolvency'.

[155] *Kalpraj Dharamshi v Kotak Investment Advisors Ltd.* 2021 SCC OnLine SC 204; *Committee of Creditors of Essar Steel India Limited through Authorised Signatory* 2019 SCC OnLine SC 1478; *K. Shashidhar v Indian Overseas Bank* (2019) 12 SCC 150; *Maharashtra Seamless Limited v Padmanabhan Venkatesh* (2020) 11 SCC 467; *Karad Urban Cooperative Bank Ltd. v Swapnil Bhingardevay* (2020) 9 SCC 729

[156] *Maharashtra Seamless Limited v Padmanabhan Venkatesh* (2020) 11 SCC 467, para 21

[157] ibid

[158] Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016, Regulation 39(3)(3A)(3B)

[159] *See for example,* in *IMR Metallurgical Resources v Ferro Alloys Corporation Ltd.* Company Appeal (AT) (Insolvency) No. 272 of 2020, NCLAT. Decision date - 8 June 2020, paras 12-13. The appellant challenged the evaluation matrix applied by the CoC. The NCLAT observed that it falls within the commercial wisdom of the CoC and it is a settled position of law that approval or rejection of a

6.7. **The Committee observed that the manner of consideration and approval of the resolution plans as proposed below is the core feature of the pre-pack process. It seeks to provide a direction to the CoC for exercising their commercial wisdom to ensure that the pre-pack process is time-efficient, competitive, transparent and value maximising. The CoC will be required to follow the procedure laid down under the Code and the regulations framed therein. However, the decisions taken by the CoC while applying the procedure for consideration and approval of the resolution plan should fall within its commercial wisdom and should not be subjected to judicial intervention.** In other words, the CoC will have complete authority over the evaluation and selection of resolution plans at different stages of the pre-pack process, but no flexibility to derogate from the procedural requirements spelled out in the Code and applicable regulations.

iii. *Role of the corporate debtor*

6.8. As discussed above, during the CIRP, the management of the corporate debtor vests with the interim resolution professional or the resolution professional.[160] The powers of the board of directors or partners of the corporate debtor are suspended and exercised by the interim resolution professional.[161] The corporate debtor as a going concern is separated from its erstwhile management. The eligible promoters/management, independent of the corporate debtor, submits resolution plans along-with the third-party resolution applicants. The corporate debtor *per se* does not participate in its reorganisation or insolvency resolution. This exercise is performed by the creditors along with the resolution applicants (which may include promoters of the corporate debtor), which is one of the core features of the creditor-in-possession model of CIRP.

6.9. On the other hand, the pre-pack process provides for a debtor-in-possession regime with a creditor-in-control model. In the course of the pre-pack process, the management of the affairs of the corporate debtor continues to vest in the board of directors or partners. **The Committee observed that the corporate debtor (or its management) should assume two distinct roles during the pre-pack process: (1) it**

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resolution plan depends upon commercial wisdom of the CoC, which involves evaluation of the resolution plan based on its feasibility. Such commercial wisdom is non-justiciable. *Also see Rai Bahadur Shree Ram v Mr. Bhuvan Madan, Resolution Professional of Ferro Alloys Corporation Ltd.* Company Appeal (AT) (Insolvency) No. 207-208 of 2020, NCLAT. Decision date - 12 March 2020, para 3

[160] Insolvency and Bankruptcy Code, 2016, Section 17(1)

[161] Insolvency and Bankruptcy Code, Section 17(2) of the Code

should have the duty to protect and preserve the value of the property of the corporate debtor and manage its operations as a going concern; and (2) it should have the right to submit a base resolution plan. The first role is discussed in detail in Chapter 5. In the second role, the corporate debtor, acting through the board of directors or partners, shall exercise its independent business judgment while negotiating the base resolution plan with its financial creditors and compete with third-party resolution applicants. Where the resolution plan of a third-party resolution applicant is approved during the pre-pack process, the corporate debtor will undergo reorganisation or insolvency resolution as per the terms of such resolution plan, which may include change in management of the corporate debtor.

II. Submission of Base Resolution Plan by the Corporate Debtor

6.10. As discussed above the pre-pack process can only be initiated by the corporate debtor. The corporate debtor is required to prepare a base resolution plan before filing an application for initiating the pre-pack process. The Committee noted the recommendations of the Sub-committee regarding the process of consideration and approval of the resolution plan during the pre-pack process. The Sub-committee had suggested that the corporate debtor should have the option to initiate the pre-pack process, whether or not, it intends to submit a base resolution plan. It envisaged that in case the base resolution plan is not submitted by the corporate debtors, it will be sourced by the CoC.[162] The Committee felt that for the pre-pack process to be successful, willingness of the original management to participate in the resolution process is of paramount importance.

6.11. The pre-pack process provides an opportunity to the corporate debtor for resolving its financial stress, while competing with the market to regain its control, thereby ensuring value maximisation. Unlike the CIRP, during the pre-pack process the management continues to manage the affairs of the corporate debtor. The management may initiate the pre-pack process and not submit a resolution plan, where it intends to exit the corporate debtor and transfer its control to a third-party resolution applicant. In such a scenario, it will not be incentivised to preserve the value of the corporate debtor's assets and run it as a going concern during the process. This may result in value destruction or siphoning of assets, undermining the primary objectives of the Code. The Committee noted that the sourcing of a base

[162] Ministry of Corporate Affairs, *Report of Sub-Committee of the Insolvency Law Committee on Pre-Packaged Insolvency Resolution Process* (2020) para 3.72 <https://www.ibbi.gov.in/uploads/resources/24c7fc03cdffff69960ce374416fa646.pdf> accessed 1 June 2021

resolution plan by the CoC from a third party after commencement of the formal process may be time-consuming and thus not suitable for inclusion in a time-bound process.

6.12. In the light of the above, **the Committee recommended that a base resolution plan may be submitted only by the corporate debtor. It should be mandatory for the** corporate debtor **to prepare a base resolution plan prior to filing of an application for initiation of the pre-pack process.** As recommended above, the base resolution plan shall be shared with the financial creditors before seeking their approval to file an application for initiating the pre-pack process. The proposed resolution professional shall in its report confirm whether the base resolution plan conforms to the mandatory requirements. **The Committee recommended that after this, the base plan shall be submitted to the resolution professional on commencement of the pre-pack process.**

III. Revision of the Base Resolution Plan

6.13. The Committee felt that once the CoC is constituted it may provide an opportunity to the corporate debtor to revise the base resolution plan. After the CoC is constituted, it should have an option to negotiate the terms of the base resolution plan with the corporate debtor before considering it for approval or inviting prospective resolution applicants to compete. Therefore, **the Committee recommended that a specific provision should be included, clarifying that the CoC has the power to provide an opportunity to the corporate debtor to revise the base resolution plan.**

6.14. Under the proposed framework, the resolution plan submitted by the corporate debtor provides a baseline document for inviting prospective resolution applicants. It's a reference point which may influence the evaluation of the prospective resolution plans received to compete with the base resolution plan. Such an opportunity will ensure that the CoC has an option to settle an expected base value for the purposes of Swiss challenge method and guarantee an expected minimum (in terms of the outcomes). **The Committee was of the view that the opportunity to review the base resolution plan should only be provided before invitation of resolution plans from the open market. Once invitation for submission of resolution plans is made by the resolution professional, the corporate debtor should not be permitted to revise the base resolution plan (unless required for the purposes of the competition within a limited time-window as discussed below).**

IV. Direct Approval of the Base Resolution Plan

6.15. The Sub-committee recommended that where the base resolution plan does not impair the rights of the operational creditors, the CoC should have the option to approve the resolution plan without seeking invitation of resolution plans from the open market.[163] The Committee agreed with the recommendations of the Sub-committee and it was of the view that scope of the term "impairment" should be expressly clarified in the Code.

6.16. It noted that the Code enables market participation for resolution of insolvency which is an essential feature of the CIRP. This ensures value maximization of the corporate debtor for all the stakeholders including the operational creditors. Once all the eligible resolution plans are presented to the CoC, it can take an informed decision for resolution of insolvency in a given case. Exclusion of this process deprives the CoC of the prospect of receiving a better price from the market, and also hampers the interests of the operational creditors.

6.17. The Committee discussed that, generally, unlike financial creditors, the operational creditors do not get the opportunity to participate or vote in the process of approval of resolution plans. As noted above, the approval of a resolution plan without market participation may deprive the operational creditors an opportunity to get a higher price. **Therefore, the Committee observed that where the CoC decides to approve the base resolution plan without invitation of resolution plans from the open market, the interests of the operational creditors should be adequately protected. The Committee recommended that the term 'non-impairment' of rights of operational creditors should mean that the resolution plan should provide for full payment of the claims of operational creditors of the corporate debtor.** Additionally, as discussed at para 6.4., the base resolution plan is required to comply with the mandatory requirements provided for resolution plans under Sections 30(2) and 30(4) of the Code.

V. Invitation and Evaluation of Resolution Plans

6.18. The Sub-committee recommended the Swiss challenge method, with adequate incentives and disincentives to ensure value maximisation. The Committee

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[163] *See* Ministry of Corporate Affairs, *Report of Sub-Committee of the Insolvency Law Committee on Pre-Packaged Insolvency Resolution Process* (2020) <https://www.ibbi.gov.in/uploads/resources/24c7fc03cdffff69960ce374416fa646.pdf> accessed 1 June 2021

discussed that the management of the corporate debtor should have the opportunity to negotiate with the financial creditors of the corporate debtor and present a base resolution plan at the inception of the pre-pack process. This proposal should be weighed by the creditors against the resolution plans submitted by third party resolution applicants from the open market. This will ensure proper price discovery for the corporate debtor's business and assets, resulting in value maximisation. Market participation will also assist the creditors to determine viability of the corporate debtor accurately.[164] **Given this, the Committee recommended that the proposed legal framework should enable invitation of resolution plans from the market in appropriate cases.**

6.19. The Committee felt that invitation for resolution plans should take place after submission of base resolution plan and where such base resolution plan is not approved by the CoC in the manner stated above. It discussed that the threshold for invitation of resolution plan should be similar to the CIRP. For instance, laying down requirements for submission of resolution plans by the resolution professional with the approval of the CoC and specification of other conditions by IBBI.

6.20. The Committee felt that the pre-pack process should ensure information symmetry between the corporate debtor providing the base resolution plan and the third-party resolution applicants submitting the resolution plans. Availability of relevant information about the corporate debtor for formulating resolution plans through the information memorandum will help in solving this problem of information asymmetry at the very first level. **Additionally, the Committee recommended that the resolution professional should share the criteria for evaluating resolution plans with prospective resolution applicants.** Such criteria shall be provided with the approval of the CoC and subject to any conditions as specified by the IBBI. This will encourage the CoC to express the parameters it will apply for evaluating resolution plans and ensure transparency and certainty in the evaluation process.

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[164] Aurolio Gurrea-Martinez, 'Implementing an Insolvency Framework for Micro and Small Firms', (Oxford Business Law Blog, 4 February, 2021) p. 21. <https://www.law.ox.ac.uk/business-law-blog/blog/2021/02/implementing-efficient-insolvency-framework-micro-and-small-firms> accessed 1 June 2021 "The adoption of a system of auctions will avoid some of the costs and problems associated with defining and distinguishing between viable and non-viable firms. Namely, instead of leaving this decision to judges and insolvency practitioners, a system of auctions will indirectly leave this decision to the market. **After all, whether a company is viable or not often depends on subjective perceptions as well as the vision and ability of the individuals behind a business. Therefore, the market will be in a better position to conduct this viability test."**

However, the Committee cautioned that these evaluation standards should be seen as a tool for comparison of the resolution plans. The selection and approval of the resolution plans shall be at the discretion of the CoC.

6.21. Further, the Committee observed that once the resolution plans are submitted to the resolution professional, she shall present the same to the CoC. The nature of duty performed by the resolution professional in this regard will be similar to the CIRP.[165] **The Committee recommended that the task of evaluation of the eligible resolution plans shall be performed by the CoC on the basis of evaluation standards shared at the stage of invitation of resolution plans. Further, if third-party resolution applicants are invited to submit plans, it is only when no resolution plan is received by the resolution professional, that the CoC may consider the base resolution plan for approval due to lack of a competing resolution plan.**

6.22. Also, the Committee discussed that during the pre-pack process, as provided under the CIRP, the CoC is required to consider the feasibility and viability of the base resolution plan or the resolution plan. As seen in practise, the CoC is required to *inter alia* determine whether the plan is commercially viable; whether the resolution applicant or the corporate debtor will be able to execute the provisions of the plan; and if executed, whether it will resolve the insolvency of the corporate debtor thereby making it a viable entity. The Committee noted that such factors require a critical strategic evaluation, which is best left to the commercial wisdom of the CoC. It is these factors which will also govern the laying down of evaluation criteria and their application. **Therefore, the Committee recommended that the CoC shall apply the evaluation criteria to the eligible resolution plans, which shall form part of the commercial wisdom of the CoC and being non-justiciable such actions should not be interfered by the courts or tribunals.**

VI. Competition between the Base Resolution Plan and Selected Resolution Plan

6.23. The Committee studied the design of the Swiss challenge method recommended by the Sub-committee. It noted that the rights and interests of the corporate debtor and the resolution applicants participating in the Swiss challenge method should be adequately balanced to ensure value maximization and transparency of the process. The Committee observed that based on the evaluation of the resolution plans, the CoC shall select a resolution plan that will compete with the base resolution plan

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[165] *ArcelorMittal India Pvt. Ltd. v Satish Kumar Gupta* (2019) 2 SCC 1, p. 460-462

submitted by the corporate debtor. **The Committee recommended that the CoC shall apply the evaluation criteria that has been shared with the resolution applicants in the process of selecting a resolution plan. The resolution applicants (including the corporate debtor) will have no vested right that their resolution plans will be selected by the CoC[166] and the application of the evaluation criteria shall be at the absolute discretion of the CoC.**

6.24. The Committee discussed that the competition between the base resolution plan and the selected resolution plan should take place only when there is scope for the corporate debtor to revise its base resolution plan to offer a higher consideration as compared to the selected resolution plan. **The Committee recommended that a higher threshold can be provided in the evaluation criteria, and resolution plans that meet such criteria would be considered "significantly better" than the base resolution plan.** These higher thresholds will be subject to any conditions specified by the IBBI. They will be shared at the stage of invitation of resolution plans along with the evaluation criteria. **The Committee recommended that where the selected resolution plan meets these criteria and is significantly better than the base resolution plan, the CoC will have the option to directly approve such resolution plan without providing any opportunity to the corporate debtor to compete with the selected resolution plan.** This will disincentivize the corporate debtor from offering a base resolution plan with lower consideration (when a higher value was genuinely possible) and ensure quicker resolutions.

6.25. Further, the Committee observed that where the selected resolution plan is not significantly better than the base resolution plan, it will compete with the base resolution plan to offer the best consideration for the corporate debtor. **The Committee recommended that the manner of competition shall be specified through regulations by the IBBI. The successful resolution plan shall be considered for approval by the CoC.** Further, the Committee noted that the process of invitation, evaluation and selection of the resolution plan and competition between the base resolution plan and the selected resolution plan is a time-consuming process. Repetition of this process will be a time-consuming exercise and disturb the timeline of the pre-pack process. The Committee observed that where the CoC is not able to procure an appropriate resolution plan it may utilise the

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[166] This is similar to the CIRP under Chapter II of Part II of the Code. The Supreme Court in *Swiss Ribbons (P) Ltd. v Union of India* (2019) 4 SCC 17 and *Arcelormittal India Pvt. Ltd. v Satish Kumar Gupta* (2019) 2 SCC 1 has held that the resolution applicant has no vested right that its resolution plan will be considered.

option of CIRP or decide to liquidate the corporate debtor. **Therefore, the Committee recommended that if the CoC does not approve the successful resolution plan, the RP should approach the NCLT to terminate the pre-pack process.**

VII. Approval of the Resolution plan

6.26. As discussed above, the CoC may approve a resolution plan for submitting to the Adjudicating Authority at four stages during the process of consideration of resolution plans - (1) the base resolution plan when it does not impair the rights of the operational creditors, (2) the selected resolution plan when it is significantly better than the base resolution plan, (3) the successful resolution plan from the competition between the base resolution plan and selected resolution plan, (4) the base resolution plan when the resolution professional does not receive any resolution plan after invitation. **The Committee recommended that the prerequisite for approval of the resolution plan by the CoC should be the same as required during the CIRP.** The resolution plan will be approved by the CoC by a vote of not less than sixty-six percent of voting share. It shall approve the resolution plan after considering its feasibility and viability, the manner of distribution proposed, taking into account the order of priority amongst creditors as laid down in sub-section (1) of Section 53, including the priority and value of the security interests of a secured creditor and such other requirements as may be specified.

6.27. The Committee noted that a peculiar feature of the pre-pack process is that the corporate debtor, acting through its management, participates in the insolvency resolution process. If the base resolution plan is approved, then the management or the promoters regain the control of the corporate debtor and their equity interests are likely to be protected. The Committee discussed that in practise once the resolution plan is approved by the Adjudicating Authority, all claims which are not a part of the resolution plan are extinguished.[167] In most cases the creditors are not able to recover their claims in full and are required to take haircuts. The Committee discussed that the waterfall mechanism under Section 53 gives priority to the creditors over the equity interest holders. Even though certain statutory protection is provided to the operational creditors and dissenting financial creditors, the Committee felt that it will not be fair and equitable for the CoC to approve a

[167] *Ghanashyam Mishra v Edelweiss Asset Reconstruction Company Ltd.* Civil Appeal No. 8129 of 2019, Supreme Court. Decision date – 13 April 2021; 2021 SCC OnLine SC 313

resolution plan which provides haircut to the claims of the creditors and restores interests of the equity interest holders of the corporate debtor (especially when the decisions of the management or the promoters resulted in the insolvency of the corporate debtor). **The Committee was of the view that the CoC may require the promoters to dilute their equity interests in the corporate debtor in appropriate cases.**

6.28. **Further, the Committee recommended that where the resolution plan does not provide for the dilution of equity interests and control of the promoters while impairing claims owed by the corporate debtor, the CoC should record reasons for this commercial decision.** The Committee felt that the requirement to give reasons may promote fairness and transparency. The Committee envisaged that this would operate as a self-disciplining mechanism and assist the CoC to reach an informed decision.

6.29. Once the resolution plan is approved by the CoC, it shall be submitted to the Adjudicating Authority for its approval. **The Committee observed that the extent of judicial review exercised by the Adjudicating Authority should be similar to that exercised for plan approval under CIRP.** The Adjudicating Authority will be required to confirm that the resolution plan abides by the procedural requirements stipulated under the Code. Where the resolution plan is rejected by the Adjudicating Authority, it shall terminate the pre-pack process.

6.30. The Committee also discussed whether regulatory benefits extended to a resolution plan approved under the CIRP should also be extended to resolution plans approved during a pre-pack process. As discussed above, the pre-pack process should have adequate procedural safeguards so as to ensure that the basic features of CIRP are retained. **Given this, the Committee recommended that the regulatory benefits available to a resolution plan during a CIRP should be extended to resolution plans approved during the pre-pack process as well. The approved resolution plan should be binding on all stakeholders, and subject to the requirements of Section 32A, the successful resolution applicant during a pre-pack process should start on a clean slate. Also, where the approved resolution plan is contravened, the persons prejudicially affected by the contravention may apply to the Adjudicating Authority for liquidation of the corporate debtor.**

CHAPTER 7: CLOSURE OF PRE-PACK PROCESS

7.1. The Committee discussed the recommendations made by the Sub-committee in relation to closure of the pre-pack process. The Sub-committee suggested that the pre-pack process may be concluded in five possible scenarios - (i) approval of the resolution plan; (ii) closure of the process when no resolution plan is received or approved; (iii) expiry of the timeline; (iv) termination by the CoC; and (v) liquidation by the CoC.

7.2. The Committee noted that during CIRP, if unviable resolution plans are received or financial health of the corporate debtor is weak, the CoC only has the option to liquidate the corporate debtor, or on completion of time-period, the corporate debtor mandatorily undergoes a liquidation process.[168] The Committee was of the view that the pre-pack process differs from the CIRP. In the course of the pre-pack process, the management of the corporate debtor remains in possession and the first set of negotiations for resolving financial stress occurs prior to its commencement. It is a quicker and time-bound process to provide an opportunity to the corporate debtor for resolving its insolvency. On the other hand, during the CIRP the resolution professional is responsible for managing the affairs of the corporate debtor and the erstwhile management or promoters participate along-with the market by submitting a resolution plan. Therefore, the CIRP maximises the value of assets through a full public process, and the pre-pack maximises value by providing a shorter, cost-effective process having elements of public process to maximise value further.[169]

7.3. The Committee concluded that the pre-pack process is an efficient alternative insolvency resolution framework. It is essentially a step before the CIRP when the financial creditors still have faith in the management of the corporate debtor for resolution of insolvency. Therefore, **the pre-pack process should be a special insolvency procedure in addition to the CIRP which provides an alternate option to the MSME to resolve its insolvency.** It should not be understood as an insolvency procedure intended to replace the CIRP. As per the scheme of the Code, the liquidation process can only be initiated for entities which have undergone the

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[168] Insolvency and Bankruptcy Code, 2016, Section 33

[169] Ministry of Corporate Affairs, *Report of Sub-Committee of the Insolvency Law Committee on Pre-Packaged Insolvency Resolution Process* (2020) para 2.25 <https://www.ibbi.gov.in/uploads/resources/24c7fc03cdffff69960ce374416fa646.pdf> accessed 1 June 2021

CIRP. The CIRP offers a flexible procedure for consideration of resolution plans and a larger timeline for the CoC and the market to resolve the insolvency of the corporate debtor. It will be incongruous and against the scheme of the Code to liquidate the corporate debtor without providing it the opportunity to undergo the CIRP.

7.4. Given this, it was noted that the IBC is a legislation aimed at resolution of insolvencies and liquidation is a matter of last resort.[170] **Accordingly, the Committee concluded that the pre-pack process should be a 'liquidation remote insolvency procedure'.** Also, the management of the corporate debtor or the financial creditors opting for the pre-pack process should not have the fear of dissolution of the corporate debtor in case the attempt at insolvency resolution is not successful. There should be an easy exit for the CoC, if at any point they decide to terminate the pre-pack process, and the law should provide an alternative option to initiate a CIRP where the economic realities of the corporate debtor suggest the possibility of resolving the corporate debtor's insolvency. However, as discussed in detail below, the Committee was of the view that where the management of the corporate debtor is responsible for any misconduct during the pre-pack process, the CoC should either opt for CIRP or liquidation.

7.5. Therefore, **the Committee recommended that the pre-pack process will close in four possible scenarios - (i) approval of resolution plan; (ii) simpliciter termination of the pre-pack process at different stages; (iii) termination of pre-pack process and initiation of CIRP; and (iv) liquidation in exceptional circumstances.**

I. Termination of Pre-pack Process

7.6. The pre-pack process is initiated with the approval of sixty-six percent of the unrelated financial creditors of the corporate debtor. The Committee observed that it is important that the CoC should have confidence over the pre-pack process for resolving the insolvency of the corporate debtor. The Committee felt that at any stage during the pre-pack process, if the CoC decides to discontinue the process it should have the option of terminating the pre-pack process. The Committee discussed that the CoC may decide to terminate the pre-pack process for multiple

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[170] *Arun Kumar Jagatramka v Jindal Steel and Power Ltd.*, Civil Appeal No. 9664 of 2019, Supreme Court. Decision date – 15 March 2021; 2021 SCC OnLine SC 220, para 43. *Kridhan Infrastructure Pvt. Ltd. v Venkatesan Sankaranarayan* Civil Appeal No. 3299/2020, Supreme Court. Decision date - 9 October 2020, para 9

reasons including distrust over the conduct of the corporate debtor or lack of viable resolution plans. This ensures the supremacy of the CoC during the pre-pack process, rather than forcing the CoC to wait for the completion of the time-period.

7.7. **Therefore, the Committee recommended that the CoC by a voting share of sixty-six percent may agree to terminate the pre-pack process at any stage after the commencement of the pre-pack process but before a resolution plan is approved by the CoC.** Where the CoC fulfils the procedural prerequisites, the termination of the per-pack process shall be purely it's commercial decision which should not be questioned by any stakeholders before the Adjudicating Authority.

7.8. Further, as discussed in the aforesaid chapters, the pre-pack process shall terminate in the three situations - *first*, on expiry of the ninety days' time-period where the resolution professional does not submit a resolution plan to the Adjudicating Authority (see para 4.25.); *second*, the successful resolution plan during the consideration and approval process is not approved by the CoC (see para 6.25.); *third*, the resolution plan approved by the CoC is rejected by the Adjudicating Authority (see para 6.29.). **The Committee recommended that in the first and second situations, the resolution professional shall be obligated to inform the Adjudicating Authority for termination of the pre-pack process. Accordingly, the Adjudicating Authority shall pass an order for termination of the pre-pack process.**

i. *Consequences of termination of pre-pack process*

7.9. Under Part II of the Code, where an insolvency proceeding is initiated against a corporate debtor, unless such proceeding is withdrawn under Section 12A of the Code, the CIRP will either result in approval of a resolution plan or a liquidation order. Once insolvency of the corporate debtor is identified by the Adjudicating Authority, it will either be resolved through a resolution plan, or the corporate debtor will be dissolved. Part II of the Code provides continuity between the CIRP and the liquidation process. The Code does not deal with a scenario wherein the CIRP ends with no conclusion. **On the other hand, in case of termination, the pre-pack process will terminate without any outcome. Therefore, the Committee felt that the law should explicitly provide certain guidelines for the effect of such termination.**

7.10. The Committee observed that once the Adjudicating Authority passes an order for termination, the corporate debtor ceases to be in the pre-pack process. It noted that

the initiation of the pre-pack process will have three types of effects - (i) imposition of moratorium; (ii) cost incurred during the pre-pack process; (iii) continuance of proceedings for antecedent transactions. The Committee discussed that in order to avoid extended litigation over the consequences of termination of the pre-pack process, the Code should stipulate the manner of dealing with these effects -

a. Effect of moratorium

7.11. The Committee noted that during the course of the moratorium period, the creditors will not be permitted to initiate or continue legal action in respect of their claims against the corporate debtor (see para 4.13.). In situations where the pre-pack process is not successful and results in termination, creditors may be at loss due to the expiry or shortening of their limitation period. The Committee noted that Section 60(6) of the Code ensures the exclusion of moratorium period from calculation of limitation period in respect of claim of the creditors once the moratorium is lifted.[171] This provision starts with a non-obstante provision and overrides anything contained in the Limitation Act, 1963 or any other law for the time being in force.

7.12. **The Committee recommended that Section 60(6) should also be made applicable in respect of the moratorium declared during the pre-pack process.** Where the pre-pack process is terminated the moratorium period shall be excluded in computation of the limitation period specified for any suit or application against the corporate debtor. The Committee discussed that Section 60(6) is a neutral provision applying to the order of moratorium made under Part II. Since the provisions of the pre-pack process will be within Part II of the Code, specific amendments will not be required to this provision, once Section 60(6) is made applicable to the pre-pack process.

b. Manner of payment of cost incurred during the pre-pack process

7.13. The pre-pack process will involve certain kinds of costs, especially the fees payable to the resolution professional (see paras 5.53. and 5.54.). The Committee noted that at the pre-initiation stage, the corporate debtor negotiates with the financial creditors to seek approval for initiating the pre-pack process. Thereafter, it is the

[171] Insolvency and Bankruptcy Code, 2016, Section 60(6) of the Code. "Notwithstanding anything contained in the Limitation Act, 1963 or in any other law for the time being in force, in computing the period of limitation specified for any suit or application by or against a corporate debtor for which an order of moratorium has been made under this Part, the period during which such moratorium is in place shall be excluded."

corporate debtor who files the application for initiation of the pre-pack process. The Committee discussed that the pre-pack process is initiated and driven by the corporate debtor, and hence, the corporate debtor, while considering the option of pre-pack should assume the risks associated with termination of the process. **Therefore, the Committee recommended that in case of termination of the process, the corporate debtor should bear the costs incurred during the pre-pack process.**

c. Continuance of proceedings for antecedent transactions

7.14. Post-commencement of the pre-pack process, the provisions related to avoidance of antecedent transactions[172] and fraudulent or wrongful transactions[173] are also invoked. The Committee discussed that in certain cases, the pre-pack process may be terminated after filing of applications by the resolution professional under these provisions and during their pendency before the Adjudicating Authority. Generally, provisions related to avoidance of antecedent transactions protect the general body of creditors against a diminution of the assets available to them by a transaction which confers unfair or improper advantage on the other party.[174] The Committee considered the rationale of the BLRC Report, in relation to the possibility of recoveries from vulnerable transactions –

> *"The Committee discussed the possibility of identifying and recovering from vulnerable transactions.* ***These are transactions that fall within the category of wrongful or fraudulent trading by the entity, or unauthorised use of capital by the management.*** *There are two concepts that are recognised in other jurisdictions under this category of transactions: of fraudulent transfers, and fraudulently preferring a certain creditor or class of creditors****. If such transactions are established, then they will be reversed. ...*** *"*[175]

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[172] Insolvency and Bankruptcy Code, 2016, Sections 43 to 51

[173] Insolvency and Bankruptcy Code, 2016, Sections 66 to 67

[174] Kristin van Zweiten, *Goode on Principles of Corporate Insolvency Law*, (5th edn, Sweet and Maxwell 2018) para 13.03

[175] Ministry of Finance, *The Report of the Bankruptcy Law Reforms Committee Volume I: Rationale and Design* (2015) para 5.5.7 <https://ibbi.gov.in/BLRCReportVol1_04112015.pdf> accessed 1 June 2021

7.15. The Committee discussed that the provisions related to antecedent transactions and fraudulent or wrongful transactions come into effect once the corporate debtor is declared insolvent by the Adjudicating Authority. Similar to the CIRP, the pre-pack process adopts the default test (or solvency test) for establishing insolvency of the corporate debtor (see para 3.4.). The Adjudicating Authority shall admit an application for initiation of a pre-pack process only upon the existence of default. The Committee was of the view that the termination of the pre-pack process does not have the effect of vitiating the entire process from its inception and rendering the order of admission or the findings of the existence of default a nullity. Despite termination, the corporate debtor continues to be insolvent and recoveries from the avoidance of these transactions may help in the revival of the corporate debtor.

7.16. Therefore, the Committee found merit in continuing the proceedings under the provisions related to the antecedent transactions and fraudulent or wrongful transactions. As observed by the BLRC Report, these transactions are fraudulent in nature and it will be against the interest of the creditors to end the proceedings despite their existence. Further, Section 26 of the Code provides that the filing of an avoidance application by the resolution professional shall not affect the proceedings of the CIRP. This provision makes proceedings for the avoidance applications independent of the CIRP proceedings thereby ensuring that the continuance of one set of proceedings does not affect to timelines of the other. The Committee noted that since this provision is made applicable to the pre-pack process a similar approach will be extended to the pre-pack process (see para 5.46.).

7.17. Accordingly, **the Committee recommended that once the pre-pack process is terminated, the proceedings in relation to the avoidance of antecedent transactions and fraudulent or wrongful transactions may continue.** The Committee felt that due to diverse possibilities it will be difficult to prescribe a general norm for the manner of continuation of such proceedings. Therefore, **the Committee recommended that the Adjudicating Authority should decide upon the manner of continuation of these proceedings on a case-to-case basis and the stakeholders will be required to act accordingly.**

II. Conversion to the CIRP

7.18. The pre-pack process for a MSME can be initiated only where there is an existence of default and the insolvency of the corporate debtor is detected (see para 3.4.). If the pre-pack process is unsuccessful, the corporate debtor is still at default and continues to be insolvent. A CIRP can be initiated by filing a fresh application which

will involve an independent adjudication by the Adjudicating Authority. Due to the absence of a moratorium, creditors will institute or continue individual actions against the corporate debtor. This may result in further delay and diminution of value, which will be against the objective of the Code. Accordingly, **the Committee recommended that the CoC should have the option to directly initiate a CIRP during the pre-pack process for entities eligible under Chapter II of Part II of the Code.**

7.19. **The Committee felt that the CoC should have the option to initiate a CIRP at any stage during the pre-pack process.** Allowing such an option may be useful in cases where a full-fledged public process can help to get better resolution plans for the corporate debtor. With the initiation of the pre-pack process the CoC will have suitable information on the financial health of the corporate debtor. The CoC may make a commercial decision to initiate the CIRP either at the inception of the pre-pack process or during its continuance depending upon the peculiar facts of each case.

7.20. **Hence, the Committee recommended that post-commencement of the pre-pack process and before approving a resolution plan, the CoC may decide to initiate a CIRP.** Also, since initiation of a CIRP would imply termination of the pre-pack process, **the Committee recommended that the voting threshold for the CoC should be similar to the requirement for termination i.e., sixty-six percent.** Once the CoC decides to initiate CIRP the resolution professional will be required to file an application before the Adjudicating Authority. Where the Adjudicating Authority is satisfied that (i) the decision to initiate CIRP is taken by the CoC with requisite majority before approving a resolution plan; and (ii) the corporate debtor is eligible for a CIRP under Chapter II of Part II, it shall terminate the pre-pack process and initiate a CIRP. **The Committee discussed that the Adjudicating Authority will not be required to adjudicate upon the commercial decision of the CoC to initiate a CIRP and an appeal against the order of the Adjudicating Authority may be made only on the grounds of material irregularity or fraud.**

i. *Consequences of initiation of CIRP*

7.21. The Committee discussed that when the pre-pack process is terminated and CIRP is initiated, the law should provide for the status of (i) stage at which the CIRP is initiated; (ii) cost incurred during the pre-pack process; (iii) continuance of proceedings for antecedent transactions and manner of calculating relevant time.

a. Stage at which the CIRP is initiated

7.22. The pre-pack process and the CIRP are independent insolvency resolution frameworks each having their specific benefits and suitable for distinct insolvency resolution strategies. The Committee suggested that an integrous approach should be adopted in order to reap the benefits of these insolvency procedures. **The CIRP should commence from the initial stage i.e., declaration of moratorium, appointment of interim resolution professional and the public announcement stage.**

7.23. An application to initiate CIRP can be filed either by the creditors of the corporate debtor (financial creditors or operational creditors) or the corporate debtor itself.[176] Two or more financial creditors of the corporate debtor can file a joint application for initiation of CIRP.[177] As mentioned above, the decision for initiating CIRP will be jointly taken by at least sixty-six percent voting share of the CoC, thereafter, the resolution professional intimates the CoC's decision to the Adjudicating Authority. Since the CoC comprises the financial creditors, the Committee suggested that an order passed by the Adjudicating Authority on the basis of the CoC's decision to initiate a CIRP has the closest resemblance to the order of admission passed by the Adjudicating Authority on the application filed by the financial creditors.

7.24. **Accordingly, the Committee recommended that an order passed by the Adjudicating Authority for initiating a CIRP on the basis of the CoC's decision shall be deemed to be an order of admission of an application filed under Section 7 of the Code and shall have the same effect.** Once the Adjudicating Authority passes an order for initiating CIRP, the pre-pack process shall be terminated and the Adjudicating Authority shall issue orders stipulated in Section 13 i.e., declaration of moratorium under Section 14, causing public announcement, and appointment of an interim resolution professional. Thereafter, the procedure for CIRP shall be in accordance with the provisions of Chapter II of Part II of the Code.

b. Cost incurred during the pre-pack process

7.25. As recommended in para 7.13., in case of termination of the pre-pack process, the corporate debtor is required to pay costs incurred during the pre-pack process. However, where the CoC decides to initiate the CIRP, the management of the corporate debtor is vested with the interim resolution professional/resolution professional and a moratorium is declared. The Committee noted that in such

[176] Insolvency and Bankruptcy Code, 2016, Sections 7, 9 and 10

[177] Insolvency and Bankruptcy Code, 2016, Section 7(1)

circumstances, the creditors (including the insolvency professional) will be unable to recover their costs directly from the corporate debtor. Such creditors will only have the option to file their claims during the CIRP.

7.26. Further, the Committee discussed that the CoC may, for different commercial reasons, choose to initiate a CIRP or simply terminate the pre-pack process. Generally, the CoC will opt to initiate a CIRP where there is scope to revive the corporate debtor by resolving its insolvency or to maximise its value by seeking a better resolution plan. Where the CoC decides to directly initiate the CIRP, a continuity is maintained between the two insolvency processes. They form part of a cohesive attempt to resolve the insolvency of the corporate debtor and maximize its value. **Therefore, the Committee discussed that costs incurred during the pre-pack process should receive a treatment similar to the CIRP costs while making a transition to the liquidation process. It recommended that where the CoC decides to initiate CIRP, the costs incurred during the pre-pack process shall form part of the CIRP costs which shall be paid in priority during the CIRP.**

c. Continuance of proceedings for antecedent transactions and manner of calculating relevant time

7.27. The provisions relating to avoidance of antecedent transactions[178] and fraudulent or wrongful transactions[179] as applied during the CIRP are extended to the pre-pack process (see para 5.46.). **As the rigor of these proceedings are the same for the two processes, therefore, the Committee observed that the proceedings initiated during the pre-pack process under these provisions should be continued during the CIRP.** The interim resolution professional or resolution professional appointed during the CIRP shall pursue these proceedings before the Adjudicating Authority in accordance with these provisions.

7.28. During the CIRP, provisions relating the avoidance of antecedent transactions[180] apply retroactively from the insolvency commencement date[181] for the stipulated period of time or look-back period. If the time-period stipulated under these

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[178] Insolvency and Bankruptcy Code, 2016, Sections 43 to 51

[179] Insolvency and Bankruptcy Code, 2016, Sections 66 and 67

[180] Insolvency and Bankruptcy Code, 2016, Sections 43 to 51

[181] Insolvency and Bankruptcy Code, 2016, Section 5(12) - "*Insolvency commencement date*" means the date of admission of an application for initiating a corporate insolvency resolution process by the Adjudicating Authority under Sections 7, 9 or Section 10, as the case may be.

provisions is calculated from insolvency commencement date it will also include the time-period spent during the pre-pack process. The Committee deliberated upon the appropriate date for calculating the look-back period when the CIRP is preceded by another insolvency procedure. Especially when the management of the corporate debtor continues to vest in its board of directors or partners (see para 5.16.).

7.29. The Committee noted that one of the conditions to be satisfied before an antecedent transaction can be upset under insolvency law is that the transaction must have been entered into within a specified time before the onset of insolvency, the time varying according to the circumstances.[182] The insolvency (default) of the corporate debtor was detected at the admission stage of the pre-pack process and continuity is maintained between the pre-pack process and CIRP. Given this, **the Committee felt that the look-back period for the antecedent transactions shall be calculated from the date on which the Adjudicating Authority admitted the application for initiation of the pre-pack process.** Otherwise, the look-back period before the onset of insolvency will be shortened, being detrimental to the interests of the general body of creditors.

7.30. The provisions related to the antecedent transactions only cover the transactions taken place prior to the commencement of an insolvency procedure. The Committee noted that during the pre-pack process, the management of the corporate debtor continues to be vested in the board of directors or the partners. While managing the affairs of the corporate debtor they may enter into transactions which are in the nature of antecedent transactions. Such transactions may be identified by the interim resolution professional or resolution professional once the management of the corporate debtor is vested with them during the CIRP. The Committee was cognizant that the possibilities of occurrence of such transactions during the pre-pack process will be comparatively less due to the effect of moratorium and oversight by the resolution professional and the CoC. **However, in the interests of the creditors and to ensure that the law is well equipped to avoid any abuse of process of law, the Committee was of the view that the provisions related to the antecedent transactions should also apply to the susceptible transactions taken place during the pre-pack period.**

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[182] *See* Kristin van Zwieten, *Goode on Principles of Corporate Insolvency Law*, (5th edn Sweet and Maxwell 2018) para 13.04

7.31. Additionally, the Committee discussed that during the pre-pack process, the corporate debtor may undertake certain transactions which are in the nature of antecedent transactions pursuant to the provisions of the Code. For instance, provisions of Section 28 of the Code are made applicable to the pre-pack process (see para 5.18.). The corporate debtor with the prior approval of the CoC may take certain actions such as undertaking any related party transaction or creating any security interest over the assets of the corporate debtor. It was highlighted that an attempt may be made to avoid such transactions if the provisions relating to the antecedent transactions are made applicable to the transactions taking place during the pre-pack process. The Committee felt that a purposive approach is required to be adopted in order to reconcile this issue. A legal sanctity is attached to the transactions taking place pursuant to the provisions of the Code. These are carved out as exceptions to the moratorium requirement serving special purposes under the Code. **Therefore, the Committee was of the view that where transactions undertaken by the corporate debtor were legally permissible during the pre-pack process, an attempt to interpret provisions relating to the antecedent transactions to upset such legally permissible transactions will be incongruous and flawed.**

III. Initiation of Liquidation Proceedings

7.32. As discussed in Chapter 5, management of the corporate debtor shall vest with the resolution professional if the Adjudicating Authority is of the opinion that during the pre-pack process, the affairs of the corporate debtor have been conducted in a fraudulent manner or there has been gross mismanagement of the affairs of the corporate debtor. The Committee discussed that where the management of the corporate debtor is vested with the resolution professional, due to the findings of misconduct on part of the board of directors or partners (see para 5.30.), it will not be appropriate to simply terminate the pre-pack process or approve a resolution plan and vest the management back to them.

7.33. **The Committee felt that if the management is vested with the resolution professional and the pre-pack process is unsuccessful, the pre-pack process should not simply be terminated and that there should be a mechanism to convert pre-pack process directly into liquidation process.** The Committee noted that such an approach will be congruous to the CA, 2013 wherein fraudulent misconduct is one of the circumstances in which the company may be wound up by the tribunal.[183]

[183] Companies Act, 2013, Section 271(c)

Section 271 (c) of the CA, 2013 is a new provision which was not available under the CA, 1956. The Central Government now has the power to petition for the winding up of a company if *inter alia* its affairs are being conducted in a fraudulent manner, notwithstanding the apparent solvency of the company.[184]

7.34. Further, the Committee was cognizant of the risks associated with the debtor-in-possession model adopted under the earlier insolvency regimes in the country. Several concerns suggested that the companies abused provisions of the SICA to siphon away the value from the company's assets during the proceedings.[185] The Committee observed that the risks of liquidation will also act as a deterrent and ensure that the pre-pack process is not abused by the corporate debtor.

7.35. **Therefore, the Committee recommended that where the management of the company is vested with the resolution professional and the pre-pack process is sought to be terminated either due to the provisions of the Code or pursuant to the decisions of CoC, the Adjudicating Authority shall, along-with the termination order pass a liquidation order as per Section 33(1)(b).** The liquidation process stipulated under Chapter III of Part II shall commence in respect of the corporate debtor and the Adjudicating Authority shall appoint the liquidator in accordance with the provisions of this Chapter. Also, **the Committee observed that the transition from the pre-pack process to the liquidation process should be similar to the transition from the CIRP to liquidation process.** For instance, the cost incurred during the pre-pack process shall form part of the liquidation costs.

7.36. The Committee also noted that there may be a situation where the management is vested with the resolution professional, and the resolution plan approved by the CoC seeks to reinstate the original management and promoters of the corporate debtor. This scenario will undermine the pre-pack process, as the original management and promoters responsible for misconduct during the pre-pack process would be benefited at the cost of creditors. Additionally, once a resolution plan is approved by the Adjudicating Authority, its successful implementation is of utmost importance to ensure revival of the corporate debtor. The Committee observed that if such a resolution plan is approved, its implementation, viability and feasibility will be doubtful. Therefore, **the Committee recommended that**

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[184] A Ramaiya, *Guide to the Companies Act*, (19th edn 2021 Vo. 3) p. 4817

[185] Ministry of Finance, *Interim Report of the Bankruptcy Law Reforms Committee* (2015) p. 41 <https://www.ibbi.gov.in/uploads/resources/57420f272e1515f0c9c137f1a6423d78.pdf> accessed 1 June 2021

where the management is vested with the resolution professional, the Adjudicating Authority should not approve a resolution plan which does not change the management or control of the corporate debtor. If such a resolution plan is submitted for approval of the Adjudicating Authority, it shall reject such resolution plan and initiate liquidation process in the manner discussed above.

ANNEXURE I: CONSTITUTION OF THE COMMITTEE

No. 30/3/2019-Insolvency Section
Government of India
Ministry of Corporate Affairs

5th Floor, A wing
Shastri Bhawan, New Delhi
Dated: 06.03.2019

ORDER

Subject: - Re-Constitution of Insolvency Law Committee as Standing Committee for review of implementation of Insolvency & Bankruptcy Code, 2016

The provisions relating to insolvency resolution for corporate persons (Part II of the Insolvency and Bankruptcy Code, 2016), regulation of insolvency professionals, agencies, information utilities and establishment of the Insolvency and Bankruptcy Board of India (the Board) (Part IV of the Code) and Miscellaneous provisions (Part V of the Code) have been brought into force, in phases. Part III of the Code, which deals with insolvency resolution and bankruptcy for individuals and partnership firms is yet to be commenced. Two amendments in the code has been done so far based on the stakeholder's consultation and Insolvency Law Committee (ILC) recommendations. Further ILC has submitted its report on Cross-Border Insolvency.

2. The provisions of the Code are evolving as a result of various judicial pronouncements and amendments made in the Code. Keeping in view the dynamic nature of the issues involved in the implementation of the Code pertaining to the corporate insolvency resolution process, the corporate liquidation process and to address new issues viz cross border insolvency, individual insolvency, group insolvency, avoidance action, Boards investigation powers & regulatory functions etc, it was considered prudent to have an advisory body for guidance & stakeholders consultations on the issues of implementation of code on continuous basis.

3.. Accordingly, in supersession of the Order No 35/14/2017 dated 16.11.2017, the Government hereby re-constitutes the Insolvency Law Committee as Standing Committee for review of implementation of Insolvency & Bankruptcy Code, 2016 consisting of following members:-

1.	Secretary, Ministry of Corporate Affairs	Chairperson
2.	Chairperson, IBBI	Member
3.	Additional Secretary (Banking), Department of Financial Services	Member
4.	Sh. T.K. Vishwanathan, Former Secretary General, Lok Sabha and Chairman BLRC	Member
5.	Sh. U.K Sinha, Ex SEBI Chairman	Member
6.	Nominee of RBI not below the rank of Executive Director	Member
7.	Sh. Sunil Mehta, MD & CEO Punjab National Bank	Member

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8.	Sh. Uday Kotak, President Designate, CII and MD&CEO Kotak Mahindra Bank	Member
9.	Sh. Shardul Shroff, Executive Chairman, Shardul Amarchand Mangaldas & Co.	Member
10.	Sh. Bahram Vakil, Partner, AZB & Partners	Member
11.	President, Institute of Chartered Accountants of India (Vice-President in his/her absence)	Member
12.	President, Institute of Cost Accountants of India (Vice-President in his/her absence)	Member
13.	President, Institute of Company Secretaries of India (Vice-President in his/her absence)	Member
14.	Joint Secretary (Insolvency), Ministry of Corporate Affairs	Member Secretary

3. The Committee will analyze the functioning & implementation of the Code identifying issues impacting the efficiency and effectiveness of the corporate insolvency resolution and liquidation framework prescribed under the Code and make suitable recommendations to address such issues. The Committee will also study the insolvency resolution and bankruptcy framework for individuals and partnership firms and make recommendations for its successful implementation. The Committee may also make any other relevant recommendation as it may deem necessary.

4. The Chairperson of the Standing Committee may also invite or co-opt practitioners, experts (subject specific) who have knowledge or experience of insolvency framework, law and economics and representatives from other regulators or Ministries. The Committee may also consult other stakeholders as part of its deliberations.

5. The non-official members of the Committee shall be eligible for travelling, conveyance and other allowances as per extant government instructions, to be decided by Chairperson of the Committee. Secretarial/technical support to the Committee will be arranged by Ministry of Corporate Affairs or Insolvency and Bankruptcy Board of India.

6. The Committee shall submit its recommendation to Ministry from time to time as directed by Chairperson of the Committee.

7. This issues with the approval of Competent Authority.

(Rakesh Tyagi)
Director

To
All members
Copy to:- PS to CAM
PS to MoS, CA
PPS to Secretary, MCA
Governor, RBI with the request to nominate a member
Secretary, DFS
PS to AS, CA

ANNEXURE II: SUMMARY OF RECOMMENDATIONS

The Committee has recommended that a pre-packaged insolvency resolution process should be made available for MSME corporate debtors. It has suggested the inclusion of a Chapter in the Code that lays down suitable provisions for the pre-pack process. In this regard, a summary of the key recommendations for amendments required in the Code is provided below.

S. No.	Topic/Provision	Summary of Recommendations
Eligibility and Pre-Initiation Requirements		
1.	Eligibility	*i. MSME corporate debtor and default* Corporate debtors that are MSMEs, as per Section 7(1) of the MSME Development Act, 2006, shall be eligible for the pre-pack process ***(Para 3.2.)***. Such a corporate debtor should have committed a default of at least Rs. 1 lakh to apply for the pre-pack process. In this regard, the Central Government may notify a higher default threshold up to Rs. 1 crore ***(Para 3.5.)***. The pre-pack process should also be available in respect of COVID-19 defaults i.e., defaults exempted from the CIRP as per Section 10A of the Code ***(Para 3.6.)***. *ii. Eligibility as per Section 29A* The provisions of Section 29A should apply for determining the eligibility of a person to be a resolution applicant in the pre-pack process ***(Para 3.9.)***. In line with this, the corporate debtor should be a resolution applicant in accordance with Section 29A to be eligible to apply for the pre-pack process ***(Para 3.11.)***.

		The exemptions available to MSMEs under Section 240A(1) should be applicable in the pre-pack process as well ***(Para 3.12.)***. *iii. Overlap with CIRP* A corporate debtor that is undergoing a CIRP should not be eligible to apply for a pre-pack process. Further, if applications for initiating a pre-pack process and a CIRP in respect of the same corporate debtor are simultaneously pending, they should be disposed of in the following manner ***(Para 3.16.)***: - a. Where an application for initiating a pre-pack process is filed first and subsequently a CIRP application is filed, the Adjudicating Authority should first dispose of the application for initiating the pre-pack process. b. Where an application for initiating a CIRP is filed and subsequently a pre-pack application is filed within 14 days of the former, the Adjudicating Authority should first dispose of the application for initiating the pre-pack process. c. Where an application for initiating a CIRP is filed and subsequently a pre-pack application is filed after 14 days, the Adjudicating Authority should first dispose of the application for initiating CIRP. *iv. Cooling off period* A corporate debtor should not be eligible to apply for a pre-pack process if – a. it has undergone the same in the last three years ***(Para 3.17.)***;

		b. it has completed a CIRP in the last three years ***(Para 3.17.)***; or c. a liquidation order has been passed against it ***(Para 3.18.)***.
2.	Pre-initiation requirements	*i. Appointment and role of the resolution professional* A resolution professional should be appointed to oversee due compliance of the corporate debtor with the pre-initiation requirements ***(Para 3.25.)***. Such appointment shall take place in the following manner- a. A specified fraction of the unrelated financial creditors of the corporate debtor should propose the name of the insolvency professional to be considered for appointment as a resolution professional. The threshold of financial creditors required to make such a proposal may be specified in the regulations ***(Para 3.31.)***. b. The name of such insolvency professional and the terms of her appointment would then be required to be approved by sixty-six percent in value of the unrelated financial creditors of the corporate debtor ***(Para 3.31.)***. c. A resolution professional must provide her consent and must certify that she is eligible for such appointment ***(Para 3.32.)***. After the approval under *b.*, the resolution professional should start undertaking her oversight functions at the pre-initiation stage. This will include functions such as - filing regular reports with the IBBI; preparing a report for the Adjudicating Authority detailing if the corporate debtor is eligible to apply for a pre-pack process and if it

		has duly met the pre-initiation requirements; etc ***(Paras 3.26. - 3.29.)***. The fee payable to the resolution professional for services at the pre-initiation stage (as approved by unrelated financial creditors) should form part of the pre-pack process costs. However, where an application for initiation of pre-pack process is not admitted or not filed, any pre-initiation fee may be borne by the corporate debtor and be negotiated by the relevant parties informally ***(Para 3.33.)***. *ii. Internal approvals of corporate debtor* The majority of directors or partners of the corporate debtor should provide a declaration stating ***(Para 3.36.)***: – a. the time within which the corporate debtor will file an application for the pre-pack process (which shall not be more than 90 days from the date of the declaration); b. that such application is not being filed to defraud any person; and c. the name of the insolvency professional proposed and approved to be appointed as the resolution professional by unrelated financial creditors. The corporate debtor should be required to avail a special resolution from its members or a resolution by three-fourth of its partners for availing their consent for the initiation of the pre-pack process ***(Para 3.39.)***. *iii. Approval of unrelated financial creditors and sharing base resolution plan* The corporate debtor should require an approval of at least sixty-six percent in value from its unrelated financial

		creditors for the initiation of the pre-pack process ***(Para 3.42.)***.
Initiation of the Pre-Pack Process		
3.	Filing and admission of an application	*i. Filing of application by corporate debtor* The application for initiation of pre-pack process should be submitted along with three kinds of documents ***(Para 4.2.)***: - a. documents supporting the eligibility of the corporate debtor for the pre-pack process; b. documents evidencing that the corporate debtor has completed the pre-initiation requirements; and c. miscellaneous documents regarding the financial position of the corporate debtor. *ii. Admission or rejection of application by Adjudicating Authority* A period of fourteen days should be provided for the admission or rejection of applications for initiation of the pre-pack process, and NCLTs should attempt to prevent delays in disposal of such applications as far as possible ***(Para 4.10.)***. *iii. Effect of order of admission* A moratorium should be ordered by the Adjudicating Authority along with the order of admission. The scope of this moratorium should be similar to the moratorium under Section 14(1) of the Code, and the moratorium should remain in force until the pre-pack process comes to an end ***(Para 4.13.)***. However, statutory provisions regarding the continuation of essential and critical

		supplies may not be required in the pre-pack process ***(Para 4.16.)***. The Adjudicating Authority shall also appoint a resolution professional along with the order of admission. In this regard, it shall consider if the proposed resolution professional is eligible to be so appointed. Where the proposed resolution professional does not satisfy the eligibility requirements, it shall appoint a resolution professional recommended by the IBBI ***(Para 4.18.)***. Along with the above, the Adjudicating Authority shall cause the appointed resolution professional to make a public announcement of the initiation of the pre-pack process ***(Para 4.20.)***.
4.	Time limit for conduct of the pre-pack process	The pre-pack process should be completed within a total of 120 days from the date of admission. In this period, the CoC should be required to approve or reject a resolution plan by the 90th day from the date of admission. Otherwise, the resolution professional should be required to file an application with the Adjudicating Authority for termination of the pre-pack process ***(Para 4.25.)***. Thereafter, the Adjudicating Authority should pass suitable orders within a period of 30 days ***(Para 4.26.)***.
Conduct of the Pre-Pack Process		
5.	Claims collation procedure	The Pre-pack process should provide for a simplified and faster claims verification process and the sanctity of the claims collation process should not be compromised. ***(Para 5.1.)*** The framework for the claims collation process should ensure that claims of all the creditors are considered and confirmed appropriately to ensure finality ***(Para 5.2.)***.

		A list of claims should be submitted by the corporate debtor which will be independently confirmed by the resolution professional ***(Paras 5.3. and 5.5.)***. The law should provide adequate legal recourse for the creditors sustaining loss or damage as a consequence of any material omission or inclusion of any claims by the management of the corporate debtor ***(Para 5.4.).***
6.	Finalisation of the information memorandum	A preliminary version of the information memorandum should be provided by the management and promoters of the corporate debtor. Adequate safeguards should be provided to ensure that reliable and authentic information is provided by the management and promoters of the corporate debtor ***(Para 5.9.)***. On receipt of the preliminary information memorandum, the resolution professional will confirm its contents and prepare the information memorandum to be shared with the resolution applicants ***(Para 5.9.)***. In case of any non-feasance, appropriate penal consequences should be provided ***(Para 5.9.)***.
7.	Role of the management of the corporate debtor	*i. Continuing the existing management of the corporate debtor* The pre-pack process should provide for a hybrid model i.e., debtor-in-possession and creditor-in-control. The affairs of the corporate debtor shall be managed by its board of directors or partners, subject to the supervision of the resolution professional and the CoC. Further, suitable safeguards should be provided to prevent any abuse or value destruction ***(Paras 5.13. and 5.16.)***. *ii. Functions and duties of the management of the corporate debtor* The management of the corporate debtor shall not be permitted to take any of the actions listed under Section

		28(1) of the Code, without prior approval of the CoC ***(Para 5.18.)***. Since the board of directors or the partners of the corporate debtor are responsible for operating its business, they shall have the duty to endeavour to protect and preserve the value of the property of the corporate debtor and manage its operations as a going concern ***(Para 5.19.)***. Access to interim finance should be available to the corporate debtor, subject to approval of the CoC and it should be included in the costs of the pre-pack process ***(Para 5.20.)***. The legal framework should seek to achieve symmetry of information and require the management to share relevant financial information with the resolution professional or the CoC as and when required ***(Para 5.21.)***. The Central Government and the IBBI should be equipped with appropriate powers to stipulate standards of conduct for the management, promoters, members, personnel or partners of the corporate debtor ***(Para 5.23.)***. *iii. Safeguards* The proposed legal framework for the pre-pack process should have sufficient safeguards to avoid abuse of the process. Appropriate penalties and punishments should be envisaged in the law to address, check and deter any misuse of the process by the management and promoters of the corporate debtor ***(Para 5.24.)***. *iv. Vesting the management of the corporate debtor with the resolution professional* Where the CoC approves the filing of an application for vesting the management of the corporate debtor with the resolution professional by a vote of sixty-six percent of its voting share, the resolution professional must apply to the

		Adjudicating Authority for the same. The Adjudicating Authority shall pass an order of vesting only if it is of the opinion that the affairs of the corporate debtor have been conducted in a fraudulent manner or there has been gross mismanagement of its affairs ***(Para 5.30.)***. Suitable provisions relating to powers of the resolution professional for management of the affairs of the corporate power under CIRP should be extended to the pre-pack process if a vesting order is passed ***(Para 5.30.)***.
8.	Role of the CoC	*i. Constitution of the CoC* A creditor-in-control regime like the CIRP should be extended to the pre-pack process and the role of the CoC, as envisaged and detailed under Chapter II of Part II, should be retained in the pre-pack process. In line with this, the CoC should be composed of unrelated financial creditors of the corporate debtor ***(Para 5.31.)***. The resolution professional shall form the CoC on the basis of the list of claims confirmed by her. In case there is any update in the list of claims at subsequent stages, the resolution professional shall accordingly alter the composition of the CoC and such alteration shall not invalidate any past decisions made by the CoC ***(Para 5.33.)***. *ii. Voting threshold and basis of voting by CoC* The voting threshold for taking decisions by the CoC in the pre-pack process should be consistent with the CIRP ***(Para 5.34.)***. Further, the voting criteria should be on a voting share basis and not on a present and voting basis in the pre-pack process ***(Para 5.35.)***. *iii. Authorised Representatives for certain classes of creditors* The mechanism for representation of certain classes of creditors through authorised representatives should be

		provided for in the pre-pack process, as it is provided under the CIRP ***(Para 5.38.)***.
9.	Role of the resolution professional	*i. Powers of the resolution professional* The resolution professional should have suitable powers to access the books of accounts, records and information of the corporate debtor ***(Para 5.43.)***. She should also have the power to attend all meetings of the members, board of directors, any committees of directors or partners of the corporate debtor ***(Para 5.44.)***. The resolution professional should also have the power to investigate and the duty to file (if required) applications for avoidance of antecedent transactions and fraudulent or wrongful trading. The relevant provisions governing avoidance of antecedent transactions (Sections 43-51) and fraudulent and wrongful trading (Sections 66 and 67) should be made applicable to the pre-pack process as well. Similarly, allied provisions (like Section 26) should also be extended to the pre-pack process ***(Para 5.46.)***. *ii. Duties of the resolution professional* The resolution professional should undertake procedural tasks to enable smooth conduct of the pre-pack process ***(Para 5.48.)***. She should also have supervisory functions, e.g., she should have the duty to monitor the activities of the corporate debtor. The resolution professional should inform the CoC immediately if she suspects or has come across any evidence indicating that the board of directors or partners of the corporate debtor have breached their obligations provided under the Code ***(Para 5.49.)***. *iii. Fees and expenses of the resolution professional*

		Any fee paid to and expenses incurred by the resolution professional should be included in the pre-pack process costs and be paid in priority to other debts ***(Para 5.51.)***. The CoC shall have a right to impose limits or conditions on the fee and expenses of the resolution professional. Any fee and expenses owed to the resolution professional for her services at the pre-initiation stage, will require to be ratified by the CoC ***(Para 5.52.)***.
10.	Costs of the pre-pack process	A resolution plan in a pre-pack process should provide priority to repayment of the pre-pack process costs over all other payments ***(Para 5.53.).***
Consideration and Approval of Resolution Plans		
11.	General principles	The framework for consideration and approval of the resolution plan during the pre-pack process should provide for – (i) continuance of core features of CIRP; (ii) preservation of the commercial wisdom of the CoC, (iii) balancing the interests of the original management, the creditors and the third-party resolution applicants participating in the pre-pack process ***(Paras 6.2.- 6.7.)***.
12.	Submission of base resolution plan by the corporate debtor	It should be mandatory for the corporate debtor to prepare a base resolution plan prior to filing of an application for initiation of the pre-pack process and submit the same to the resolution professional post initiation of the process ***(Para 6.12.)***. The base plan shall be submitted to the resolution professional on commencement of the pre-pack process ***(Para 6.12.)***.

13.	Revision of the base resolution plan	The CoC should have the power to provide an opportunity to the corporate debtor to revise the base resolution plan ***(Para 6.13.)***. This opportunity should be provided before invitation of resolution plans ***(Para 6.14.)***.
14.	Direct approval of the base resolution plan	The CoC may decide to approve the base resolution plan without invitation of resolution plans, if rights of the operational creditors are not impaired. The rights of the operational creditors shall not be impaired where the resolution plan provides for full payment of the claims of operational creditors of the corporate debtor ***(Para 6.17.)***.
15.	Invitation and evaluation of resolution plans	The proposed legal framework should provide for the invitation of the resolution plan, similar to CIRP, to compete with the base resolution plan ***(Para 6.18.)***. The resolution professional should share the criteria for evaluating resolution plans with prospective resolution applicants ***(Para 6.20.)***. The task of evaluation of the eligible resolution plans shall be performed by the CoC based on evaluation standards shared at the stage of invitation of resolution plans ***(Para 6.21.)***.
16.	Competition between the base resolution plan and selected resolution plan	The CoC shall apply the evaluation criteria that has been shared with the resolution applicants to select a resolution plan ***(Para 6.23.)***. A higher threshold can be provided in the evaluation criteria, and resolution plans that meet such criteria would be considered "significantly better" than the base resolution plan. Where the selected resolution plan meets these criteria and is significantly better than the base resolution plan, the CoC will have the option to directly approve such resolution plan without providing any

		opportunity to the corporate debtor to compete with the selected resolution plan ***(Para 6.24.)***. The manner of competition shall be specified through regulations by the IBBI and the successful resolution plan shall be considered for approval by the CoC ***(Para 6.25.)***. If the CoC does not approve the successful resolution plan, the resolution professional should approach the NCLT to terminate the pre-pack process ***(Para 6.25.)***.
17.	Approval of the Resolution Plan	The prerequisites for approval of the resolution plan by the CoC should be the same as required during the CIRP ***(Para 6.26.)***. The CoC may require the promoters to dilute their equity interests in the corporate debtor in appropriate cases ***(Para 6.27.)***. Where the resolution plan does not provide for the dilution of equity interests and control of the promoters while impairing claims owed by the corporate debtor, the CoC should record reasons for this commercial decision ***(Para 6.28.)***. Once the resolution plan is approved by the CoC, it shall be submitted to the Adjudicating Authority for its approval. The extent of judicial review exercised by the Adjudicating Authority while approving resolution plans during the pre-pack process should be similar to CIRP ***(Para 6.29.)***. The regulatory benefits available to a resolution plan during a CIRP should be extended to resolution plans approved during the pre-pack process as well. The approved resolution plan should be binding on all stakeholders, and subject to the requirements of Section 32A, the successful resolution applicant during a pre-pack process should start on a clean slate ***(Para 6.30.)***. Where the approved resolution plan is contravened, the persons prejudicially affected by the contravention may

		apply to the Adjudicating Authority for liquidation of the corporate debtor ***(Para 6.30.)***.
Closure of Pre-Pack Process		
18.	General	The pre-pack process will close in four possible scenarios ***(Para 7.5.)***: – a. Approval of resolution plan; b. Simpliciter termination of the pre-pack process at different stages; c. Termination of pre-pack process and initiation of CIRP; and d. Liquidation in exceptional circumstances.
19.	Termination of the pre-pack process and consequences thereof	The CoC by a voting share of sixty-six percent may agree to terminate the pre-pack process at any stage after the commencement of the pre-pack process but before a resolution plan is approved by the CoC ***(Para 7.7.)***. Additionally, the pre-pack process shall terminate in the following circumstances ***(Para 7.8.)***: – a. On expiry of the ninety days' time-period where the resolution professional does not submit a resolution plan to the Adjudicating Authority; b. The successful resolution plan during the consideration and approval process is not approved by the CoC; or c. The resolution plan approved by the CoC is rejected by the Adjudicating Authority. The limitation period in respect of claims during the continuance of the pre-pack process should be protected.

		Section 60(6) should be made applicable in respect of the moratorium declared during the pre-pack process ***(Para 7.12.)***. Once the pre-pack process is terminated, the corporate debtor should bear the pre-pack process costs incurred during the process ***(Para 7.13.)***. The proceedings in relation to the avoidance of antecedent transactions and fraudulent or wrongful transactions commenced during the pre-pack process shall not be discontinued. The Adjudicating Authority should decide upon the manner of continuation of these proceedings on a case-to-case basis and the stakeholders will be required to act accordingly ***(Para 7.17.)***.
20.	Conversion to a CIRP and consequences thereof	Post-commencement of the pre-pack process and before approving a resolution plan, the CoC should have the option to directly initiate a CIRP during the process for entities eligible under Chapter II of Part II of the Code. The voting threshold for the CoC for taking the decision to initiate CIRP should be sixty-six percent ***(Para 7.18.-7.20.)***. The CIRP should commence from the initial stage i.e., declaration of moratorium, appointment of interim resolution professional and the public announcement stage ***(Para 7.22.)***. An order passed by the Adjudicating Authority for initiating a CIRP shall be deemed to be an order of admission of an application filed under Section 7 of the Code and shall have the same effect ***(Para 7.24.)***. Where the CoC decides to initiate a CIRP, the pre-pack process costs incurred during the process shall form part of the CIRP costs ***(Para 7.26.)***. The proceedings in relation to the avoidance of antecedent transactions and fraudulent or wrongful transactions

		commenced during the pre-pack process should be continued during the CIRP ***(Para 7.27.)***. The look-back period for antecedent transactions shall be calculated from the date on which the Adjudicating Authority admitted the application for initiation of the pre-pack process ***(Para 7.29.)***. Also, the provisions related to antecedent transactions should also apply to any susceptible transactions taken place during the pre-pack process period ***(Para 7.30.)***.
21.	Initiation of liquidation proceedings	Where the management of the company is vested with the resolution professional and the pre-pack process is sought to be terminated, the Adjudicating Authority shall, along-with the termination order pass a liquidation order as per Section 33(1)(b) ***(Para 7.35.)***. Where the management is vested with the resolution professional, the Adjudicating Authority should not approve a resolution plan which does not change the management or control of the corporate debtor. If such a resolution plan is submitted for approval of the Adjudicating Authority, it shall reject such resolution plan and initiate liquidation process ***(Para 7.36.)***.