

Insolvency and Bankruptcy Law in India

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Lecture 20

Insolvency and Bankruptcy Laws in India. Today we are going to discuss the Committee of the Creditors, and in the subsequent lessons, we are going to discuss the voting rights, the powers, and how the meetings will be conducted by the Committee of the Creditors. In the previous classes, we discussed how to make an application and who can initiate an application under the CIRP and the IBC. The financial creditor, operational creditor, and corporate debtor can initiate the proceedings under the IBC themselves. Subsequently, we discussed the concept of moratorium. Today, we are going to discuss the concept of the Committee of the Creditors.

So, what is this Committee of Creditors? The Committee of Creditors is the highest decision-making authority in the CIRP process. During the CIRP process, the committee of creditors makes decisions regarding the debtor's management, how to initiate insolvency, and when to liquidate the company. Therefore, all business decisions are made by the committee of creditors. Once the CIRP process is started, the resolution professional will take over the management of the company, and the existing board of directors will be suspended.

Then the resolution professional will act in accordance with the directions given by the committee of the creditors. What is this committee of creditors? The committee of creditors is the highest decision-making authority in the CIRP process. During the committee meetings, decisions regarding the corporate debtor's management are made based on a majority vote. Whenever they make a decision, we will discuss how they will make it. Whenever they are making decisions, it is always by majority.

So, after complying with the proof of claims. The interim resolution professional must, as per sections 18 and 21 of the code, constitute a committee of creditors. Please remember that an application for the initiation of CIRP may be filed by a financial creditor, an operational creditor, or a corporate debtor. In these three cases, the IRP will be appointed, and once the IRP is appointed, he will make a public announcement, whereby he will invite claims from the creditors. After receiving the claims from the creditors, he is going to form a committee of creditors as per sections 18 and 21 of the Act.

After compiling the proof of claims, the interim resolution professional shall constitute the committee of creditors. Please remember that in the committee of creditors, all the financial creditors of the corporate debtor will be there. Let us now examine the provision. Section 21 of the IBC deals with the committee of creditors. So, if you look at section 21, subsection 1 provides that the interim resolution professional, after collating all the claims received against the corporate debtor and determining the corporate debtor's financial position, shall constitute a committee of creditors.

Section 1 says that the financial professional, okay, so the resolution professional, once appointed, is supposed to make the public announcement. We have already discussed how to make the public announcement in the previous lessons. So once a public announcement is made, it will collate all the claims received from the creditors against the corporate debtor. The financial creditors and operational creditors, whoever the creditor is, will submit claims to the corporate debtor. All these claims will be collated, and then subsequently, the interim resolution professional will constitute a committee of the creditors.

Then who will be on the committee of the creditors? Subsection 2 provides that the committee of creditors shall comprise all financial creditors of the corporate debtor, provided that a financial creditor or the authorized representative of a financial creditor referred to in subsection 6, subsection 6a, or subsection 5 of section 24, if it is a related party of the corporate debtor, shall not have any right of representation, participation, or voting in a meeting of the committee of creditors; thus, as per section 2, all financial creditors will be in the committee of creditors. But if any financial creditor or the authorized representative is a related party, subsequently, we will discuss in detail what the meaning of a related party is and who is considered to be a related party. Subsequently, we are going to discuss, so if any creditor is a related party, then please remember he doesn't have any right of representation, participation, or voting, so he doesn't have any representation. He cannot participate in the meetings or vote. There are exceptions, but under normal circumstances, any creditor who is a related party to the corporate debtor does not have any representation, participation, or voting rights in the creditors' committee.

Provided further that the first proviso shall not apply to a financial creditor regulated by a financial sector regulator if it is a related party of the corporate debtor solely on account of the conversion or substitution of debt into equity shares or instruments convertible into equity shares or the completion of such transactions as may be prescribed prior to the insolvency commencement date. So, in this proviso, they are stating that if there is any financial sector regulator, and a financial services provider to whom the financial sector regulator is applicable, in such cases, suppose we take the example that he has given a loan to the company. Then, maybe because of, or maybe based on, the corporate debt restructuring (CDR) scheme, the debt of the financial service provider is converted into

equity. Now he is a shareholder in the company, so merely because he is a shareholder, you cannot say that he is a related party. Though the debt is converted into equity before the commencement of the insolvency proceedings, that is, before the insolvency commencement date, he is still not considered to be a related party.

Subject to subsections 6 and 6a, where the corporate debtor owes financial debts to two or more financial creditors as a part of a consortium or agreement, each such financial creditor shall be a part of the committee of creditors, and their voting rights or voting share shall be determined on the basis of the financial debt owed to them. So, we are going to discuss this clause in detail subsequently. So, this subsection says that if any financial debt exists where the corporate debtor owes financial debts to one or more financial creditors, it means the financial creditors are giving a loan to the corporate debtor as a consortium, which means two or more people together are providing the loan, possibly because the amount is very large and one banking institution may not be in a position to provide the loan. That's why, as a consortium, they are giving the loan. In such cases, please remember how you are going to have the representation.

It is possible for the consortium to have an authorized representative on the committee of the creditors. Then, please remember they are going to have voting rights in accordance with the financial debt. Suppose we take the example that the total debt of the corporate debtor is 100 rupees, and my debt is 10 rupees; then I'm going to have 10 percent of the voting rights. So, depending on the amount of the debt, I'm going to have voting rights. So, in the case of a consortium, each and every member will have separate voting, though they are represented by one representative only; that is, one author is representative only, but their voting rates will be different.

Subsequently, we'll discuss how they are going to cast their vote in the subsequent lessons. Then, where any person is a financial creditor as well as an operational creditor, the possibility exists that one person is a financial creditor who gave a loan to the company and is also an operational creditor. In such a scenario, that person shall be a financial creditor to the extent of the financial debt. Therefore, he is considered to be a financial creditor to the extent of the financial debt, and to that extent, he shall be included. Please remember that operational creditors are not included in the committee of creditors.

If any person is both a financial creditor and an operational creditor, then he will be included as a financial creditor and shall be included in the committee of creditors with a voting share proportionate to the extent of financial debts owed to such creditor. So, this is a common point. Whenever there is a financial creditor, their voting rights will be proportionate to the amount owed by the corporate debtor. Such a person shall be considered to be an operational creditor to the extent of the operational debt, where an operational creditor has assigned. The possibility is there; the operational creditor is

there; he has assigned, which means he has transferred his right to receive the money to another person, some third party.

He has assigned the rights or legally transferred any operational debt to a financial creditor. Then the assignee or transferee shall be considered an operational creditor to the extent of such assignment or legal transfer. Here, what they are trying to say is, suppose we take the example of me, the operational creditor. I have transferred my rights in favor of Mr. X, who happens to be a financial creditor as well.

In such cases, he is going to have two positions. That is, as a financial creditor, he'll have rights because I have transferred my rights; that is, I have assigned my rights to Mr. X. Then Mr. X will exercise his powers, or Mr.

X will be there in the COC as a financial creditor, and he will also exercise the rights as an operational creditor because I have assigned my rights to Mr. X. Then, where the terms of financial debt are extended as part of a consortium agreement or syndicated facility provided for a single trustee or agent to act for all the financial creditors, the possibility exists that all the financial creditors together have formed a trust. They have syndicated; then this trustee is representing them. In such cases, they can authorize the trustee or agent to act on their behalf in the Committee of Creditors to the extent of their voting rights.

So please remember that whenever any authorized representative is present in the Committee of Creditors, that is the COC. Suppose I am representing the Committee of Creditors on behalf of 100 shares. I am just giving an example. These 100 shares, or 100 votes, I may not cast in favor of one resolution, or I may not cast against the resolution at all. So, there is a possibility, depending on the requirements of the financial creditor.

Suppose we take the example of one financial creditor who has 10 votes out of my 100 votes; he is asking me to cast my vote against the resolution. Another financial creditor is asking me to cast my vote in favor of the resolution, which has 20 votes. Then, accordingly, I will vote 20 votes in favor of the resolution and 10 votes against it. So, because as an authorized representative, I'm not representing a single person, I'm representing all the financial creditors. All the financial creditors, depending on their requirements, I'm supposed to vote.

So, the authorized, in case you're having any syndicate, all these financial creditors can authorize a trustee or agent. Then, he will represent himself in the committee of creditors to the extent of his voting rights. So, if any other representative is also a financial creditor, then their personal interest will also be present. Then, appoint an insolvency professional other than the resolution professional at his own cost to represent him in the committee of creditors to the extent of his voting rights. So, there is a possibility that the financial creditor or consortium can appoint one insolvency professional because they

may not be in a position to properly represent themselves, or they may not have the knowledge, so that's why they can appoint one insolvency professional who is a qualified person.

So, who is considered to be an insolvency professional? In the subsequent lessons, we are going to discuss who is considered to be an insolvency professional, his duties, rights, powers, eligibility, and everything we are going to discuss in the subsequent lessons. They may appoint one insolvency professional other than the resolution professional because a resolution professional is already appointed when you make an application by the financial creditor or corporate debtor. As we have already discussed, you are supposed to propose, except in the case when the application is made by the operational creditor; he need not propose any resolution professional. But whether they are proposing that in the case of a financial creditor or corporate debtor or not in the case of an operational debtor, once it is admitted by the NCLT, the NCLT is going to appoint someone as a resolution professional. So, I am not talking about that resolution professional.

So, appoint an insolvency professional. So, this consortium is supposed to appoint one insolvency professional to represent them. Then what they are going to do is exercise his voting rights to the extent of his voting rights with one or more financial creditors jointly or severally. He is going to exercise the rights under subsection 6(a), where a financial debt is in the form of securities or deposits, and the terms of the financial debt provide for the appointment of a trustee or agent to act as an authorized representative for all. The financial creditors, such as trustees or agents, shall act on behalf of such financial creditors.

Where a financial debt is in the form of securities or deposits, a trustee or agent can be appointed. In such cases, the trustee or agent will represent the financial creditor. Suppose it is the O2 class of creditors exceeding the numbers as may be specified, other than the creditors covered under Clause A or Subclass 6, the interim resolution professional shall make an application to the adjudicating authority, along with a list of financial creditors containing the names of insolvency professionals, other than the interim resolution professional, to act as their authorised representative who shall be appointed by the adjudicating authority prior to the first meeting of the committee of the creditors. Suppose we take the example of whether there is any class of creditors exceeding the limitations specified under the legislative rules. In such cases, they can appoint another professional to represent them because an authorized representative, if he is a person other than the resolution professional, may not have the expertise or knowledge.

Therefore, they can appoint one insolvency professional to represent their interests. Then the next class is represented by a guardian. Suppose any financial creditors are

represented by the guardian, executor, or administrator; such a person shall act as an authorized representative on behalf of the financial creditor. So, if there is any guardian or executor, then he shall represent the financial creditor as the case may be. Then, how much remuneration do we have to pay? The remuneration payable to the authorised representative under clauses a and c of section 6a, subsection 6a, if any, shall be as per the terms of the financial debt or the relevant document.

So, in the relevant document or in the financial debt only, we are going to fix how much remuneration you are going to pay to the representative. So that has to be paid. Or it shall be specified, which shall form part of the insolvency resolution process cost. Okay, so when you are appointing, it shall be part of the insolvency resolution process cost in such cases. Then the board may specify the manner of voting and the determination of the voting share in respect of financial debts covered under subsections 6 and 6a.

So here we have the rules and regulations; in the subsequent lessons, we are going to discuss how voting will be calculated. Suppose a creditor is present, and their representative is present but abstains from voting; the scenario is different. Suppose a creditor is absent from the meeting; then, how do we calculate their voting? So, we have rules and regulations; in the subsequent lessons, we are going to discuss how voting will be considered. Then, the same as otherwise provided in this code, all the decisions of the Committee of Creditors (COC) shall be taken by a vote of not less than 51%. Whenever you want to pass any resolution or take any decision, you are expected to have at least 51% of the vote.

Then, provided that where a corporate debtor does not have any financial creditor, the creditor's committee shall be constituted and shall comprise such persons to exercise such functions in such manner as may be prescribed. So, in subsequent lessons, we are going to discuss. Suppose the creators' committee doesn't have any financial creditors; it may only have operational creditors. In such cases, how do we form a committee of creditors? We will discuss this in the subsequent lessons. Then the committee of the creditors shall have the right to require the resolution professional to furnish any financial information.

It is the responsibility of the resolution professional to ensure that he is collating all the data, and it is the responsibility of the suspended board of directors to cooperate with the resolution professional. The resolution professional will collect all the financial information relating to the corporate debtor so that the COC can make the appropriate decision. So, the committee of the creditors has the right to require the resolution professionals to submit the financial data. The resolution professional shall make available any financial information required by the committee of creditors within a period of seven days. If any information is requested by the committee of creditors, it is the responsibility of the resolution professional to submit such information.

Let us now discuss another section: Section 22, Subsection 2. So, which provides that the committee of the creditors may, in the first meeting, by majority vote of not less than 66%. Please remember that the voting percentages are very, very important. As you observed in the previous section, 51% must make all decisions unless otherwise specified. So here it is specifically stated under section 22, subsection 2: 66% is specifically stated.

So, what they can do with 66% of the voting shares of the financial creditor is either resolve to appoint the interim resolution professional as a resolution professional or replace the interim resolution professional. As we have already discussed in the previous classes. When you apply for the CIRP process before the NCLT, you propose one interim resolution professional. This interim resolution professional will collate all the information about the claims, then subsequently he is going to form a committee of the creditors. At the first meeting of the committee of creditors, they may decide to continue the interim resolution professional as the resolution professional or appoint another person.

They can also replace the interim resolution professional with another resolution professional; that is up to the committee of creditors' discretion. Then please remember that from this we can understand that the COC shall confirm the IRP as RP, or else the replacement of the IRP with another IRP has to be done by 66%. Previously, we discussed that normal decisions will be taken by 51%, but replacing the IRP with another RP is continuing and is not a problem; however, to replace it, you have to pass a resolution by 66%. Then, who is considered to be a related party? As we have already discussed previously, whenever you are forming the committee of creditors, you are not supposed to have a related party. So, in the committee of creditors, who is considered to be a related party? In the case of Phoenix ARC Private Limited versus Spade Financial Services Ltd.

In this case, the Supreme Court held that you are supposed to exclude the related parties while forming the committee of creditors. The purpose of excluding a related party of a corporate debtor from the COC is to obviate the conflict of interest. Why? If I am interested, in the subsequent lesson, we are going to discuss who can be considered to be a related party in detail, but today, we are stating that the related party cannot be a part of the COC.

So, in this case law, Phoenix ARC Pvt. Ltd. vs. Spade Financial Services Ltd., the Supreme Court held that the related party cannot be a part of the COC. Why? Because they are having, obviously, a conflict of interest. So, because they are an interested party, they may not make the decision properly. So that's why they cannot be a part of the committee of creditors.

Then, in another case, Rajdeep Clothing and Advisory Pvt. Ltd. vs. Brijesh Kumar Mishra, RP of Krishna Knitwear Technology Ltd., the NCLT Ahmedabad bench held that the RP is required to have tangible matters material on record. So, whenever you are deciding who is going to form the committee of the creditors, the resolution professional.

IRP is going to form the committee of creditors, so it is its responsibility to verify whether someone is a related party or not. To determine whether someone is a related party, you are supposed to have tangible material, which means you are supposed to have some material. Unless you have some material and relevant information, you cannot decide. Therefore, you are supposed to decide based on the material information that is available to you.

Let us recap what we discussed in today's session. We discussed the committee of the creditors, how to form it, and other related matters. Then, we discussed section 21 of the committee of the creditors, which speaks about the committee of the creditors. Then we discussed section 22, subsection 2 of the code, which states that section 22 also speaks about the committee of creditors. Subsequently, we discussed that a related party of a financial creditor cannot be part of the COC, so if any person is a related party to the financial creditor, they cannot be part of the COC. So, in the next class, we will discuss who is considered to be a related party.

In today's class, we have discussed the committee of the creditors, section 21, and section 22. I can say that today we have discussed at the section level.

Thank you.