

Insolvency and Bankruptcy Law in India

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Week 10

Lecture 48

Hello, welcome to Session 49 on liquidation under the IBC.

Let's quickly recap what we understood and discussed in the previous session. In today's session, we will focus on the IBBI regulations. In the previous session, we gained an understanding of the process overview for the entire liquidation, including the timelines outlined under various IBBI regulations and the provisions of the Act.

Let's quickly move forward today to the regulations. To briefly recall, these regulations are known as the Insolvency and Bankruptcy Board of India Liquidation Process Regulations, 2016. The first and second regulations primarily discuss the applicability, scope, and definitions of various terms used within the provisions. We are not getting into those regulations; we are going straight to the conceptually important regulations. First, of those, Regulation 3 deals with the appointment of the liquidator.

If you want to understand the relation between the Act and the IBBI regulations, section 34 of the Act talks about the appointment of a liquidator, and Regulation 3 of the regulations talks about the appointment of the regulator. And what do they say? The liquidator and their insolvency professional entity must be independent of the corporate debtor; this is the first requirement. What does it mean? It means that a person who is financially interested in the corporate debtor, who is related to the promoters of the corporate debtor, or who has a conflict of interest with the corporate debtor shall not be appointed as a liquidator. At the same time, a liquidator may sometimes be part of an insolvency professional entity. For those who are not aware of an insolvency professional entity, the IBBI allows insolvency professionals to group together and work as a single entity. This can be an LLP or a private company formed under the IBC, which will be referred to as an insolvency professional entity.

Such an entity will comprise a group of insolvency professionals. However, as far as the appointment is concerned, it cannot be made by the entity. The appointment shall always be of the individual. I am sure you understand. I am an individual appointed as a liquidator in a specific case, but I am also part of an insolvency professional entity, and one of the partners in that entity is directly interested in a corporate debtor. Will I then be

qualified or eligible to be appointed as a liquidator of the same corporate debtor? No, because my partner, who is in partnership with me in the Insolvency Professional Entity, has a direct interest in a corporate debtor, and because of that, my independence in the corporate debtor is absolutely affected; therefore, I cannot be a liquidator for this corporate debtor.

Now, look at the second paragraph. The liquidator must promptly disclose any personal or financial relationship with the corporate debtor or its stakeholders to the board and adjudicatory authority. When I mention “board” here, I mean the IBBI and the adjudicatory authorities, specifically the NCLT. Now, the point is, if you have an interest, are you disqualified just because you have that interest? No, what we are saying here is that, to the extent possible, the liquidator must be an independent agency. However, whether before or after being appointed as a liquidator, if the person has acquired any interest in the corporate debtor, they must promptly notify both the liquidator and the IBBI, which is the adjudicatory authority.

Now, the choice to continue with you as a liquidator or not is with the adjudicatory authority, but our duty as resolution professionals or liquidators is to inform the concerned party that we have an interest; after that, the decision rests with the adjudicatory authority. This is Regulation 3. Now, in the same regulation 3, there is one more important line that states the liquidator cannot continue if their insolvency professional entity, or any of its partners or directors, represents another stakeholder in the same liquidation process. Let’s say I am the liquidator conducting the actual liquidation process. I am a partner in a professional entity, and my partner, Mr. X, in this professional entity is actually representing the corporate debtor and its promoters, which completely conflicts with my interest as a liquidator; hence, I am now ineligible to become a liquidator because my partner from this IPE is representing a party that has a conflicting interest with me as a liquidator.

Then, moving forward, we come to Regulation 4, which addresses the regulation of liquidators’ fees. The liquidator is entitled to receive a fee for his or her services, which is a percentage of the realization from the liquidation process. You know some of you are wondering what kind of financial emoluments can flow from this kind of assignment. You must be thinking that there is a great deal of responsibility, risk, and pressure because the entire process is time-bound. What will I gain from this entire process? If you are an insolvency professional, you will know that liquidators and resolution professionals for qualified IPs sometimes have a tremendous opportunity to make money. If you examine Regulation 4 itself, what does it say? It states that the liquidator is entitled to receive a certain percentage of the proceeds from the liquidation process. The liquidator is entitled to receive a fee for his or her services, which is a percentage of the realization from the liquidation process. The fee is paid in stages as the assets are

realized, subject to the approval of the creditors' committee, the adjudicatory authority, or the stakeholders committee.

The liquidator is also entitled to receive reimbursement for other expenses incurred while carrying out liquidation duties. Moving forward, another point in Regulation 4 states that the fee is paid in stages as the assets are realized, subject to approval by the stakeholders' committee or the adjudicating authority. The liquidator is also entitled to receive reimbursement for any other expenses incurred while carrying out liquidation duties. As we mentioned, you can always consult experts. You can also engage registered valuers to carry out the duties of a liquidator. While you carry out these duties, you will incur a lot of expenses. Are you entitled to receive this expenditure? Yes, this is referred to as reimbursement of liquidation costs incurred by the liquidator. Remember, this is in addition to the money you receive as a percentage of the assets' realization; that is the liquidator's fee. What we are discussing here is the reimbursement of expenses. Now, when I mentioned money, I didn't deliberately provide you with the figures.

Now, consider the amount of money that the liquidators can earn. If the realized value of the asset is one crore rupees, then the liquidator can receive a six-percent fee from that entire realized value. Now, when you look at one crore and compute six percent, it comes out to be six lakh rupees. So, we might think that six lakh is not a big deal; it's fine, everybody makes it. However, look at it as you continue to move forward; although the percentage is decreasing, the amount of money the liquidator is making is phenomenal.

I'll take you straight to the fourth row in the table, where the realization value is 50 crores, and the percentage fee charged by the liquidator is 3% of the amount exceeding 50 crores. Additionally, the fee on the previous slab, which is up to ₹50 crores, will be 4%, while anything above that will be charged at 3%. However, if you look at the first 1 crore, it is only 6%, and after the first 1 crore, he will receive 5% up to 10 crores. Let's examine realizable value. If I say the value of an asset is 50 crore, he gets 6 lakhs on the first 1 crore. He gets 5% of the balance of 9 crores; here, 9 crores at 5% is approximately 45 lakhs, plus the first 6 lakhs, which is already 51 lakhs.

Then, from 10 crore to 50 crore, on the 40 lakh surplus, he will get 4 percent. Forty crores, I mean, 40 crores at 4 percent is already 1.6 crores, plus 40 lakhs here; that makes it 2 crores, plus a few more percentages here. So, remember, if I am selling an asset for ₹ 50 crore as a liquidator, I am entitled to receive ₹ 2 crore. So, ₹ 2 crore is not a very small amount. That's why I'm just telling you that as the realization value keeps increasing, though the percentage that he can get keeps falling, the ultimate chunk of money that he is going to get will be huge; therefore, the insolvency professionals' careers are substantially changing, and a lot of people might choose to make money. However, remember one thing: it doesn't look as complicated when you examine the table here. You think that, okay, you said you make money; you sell, you make money, but it is not

as simple as that. To actually sell an asset at a certain value, it takes a phenomenal effort from the liquidator, right? Therefore, the amount of money you receive will be commensurate with the actual effort you put into selling that asset.

That's why this kind of fee is prescribed for the liquidator. Now that we have understood the fees for the liquidator, we will proceed to examine the reporting requirements under the IBC. You can see there are six blocks here. First, we expect a preliminary report to be provided by the liquidator as soon as he receives claims from the claimants. After that, once he is appointed as a liquidator, he will receive claims and form a liquidation estate. He will then prepare an asset memorandum detailing which assets have been identified, which assets are part of his estate, and which are not part of his estate. After that, he will file a progress report from time to time; this is an important provision. Then, after that, when he is selling the assets of the corporate debtor, he is also going to give a sale report to the adjudicating authority and various other stakeholders; afterward, the minutes of the stakeholders' consultations will also be reported to the adjudicating authority regarding the suggestions provided by the stakeholders during the consultation. Lastly, the final report is issued after the assets have been realized and the proceeds have been distributed, so it is only after the final report is received that it is a fit case for dissolution.

Let's move forward to understand other aspects: we have covered Regulation 3, Regulation 4, and we are now covering Regulation 5. It states that the liquidator must preserve both physical and electronic copies of the reports and minutes for a period of eight years after the corporate debtor's dissolution. A stakeholder can request the reports and minutes by submitting a written application and paying the associated costs. Remember, this is an important provision. Let's say that after the company is dissolved, three years later, one of the stakeholders comes and says, "I didn't understand exactly how you distributed the sale proceeds. I want to have minutes of those meetings, and, you know, I want to see the copies of various accounting entries that you've maintained.

Then the liquidator is bound to reply to such a person with the necessary papers and documents within the stipulated time. And you know, therefore, he is bound to maintain all these copies for a period of 8 years, after which he can weed out, I mean destroy, his documents because they are no longer relevant. This ensures that all relevant reports are prepared, preserved, and made available to stakeholders. Promoting transparency and accountability in the liquidation process, reporting is therefore critical.

Let's refer to Regulation 6, which discusses registers and books of accounts. As a liquidator, when handling tremendously valuable liquidation assets and a substantial amount of money, it is crucial to maintain certain books of accounts and registers to ensure transparency throughout the process. This is essential to avoid later questioning or potential criminal negligence. Therefore, it is important to maintain the books of accounts and certain registers. So, what is Regulation 6 saying? If the corporate debtor's books are

incomplete at the commencement date of the liquidation, the liquidator must complete and update them promptly after the liquidation order is issued. Because it is now your duty as a liquidator to maintain the corporate debtor's books of accounts, you cannot blame your predecessor, nor can you blame the corporate debtor for not maintaining its books of accounts. It is now your absolute responsibility. The liquidator must maintain specific registers and books related to the liquidation, preserving them for eight years from the date of the corporate debtor's resolution; this is what we covered earlier. The registers and books can follow the format in Schedule Three; this is an important matter.

We recall that any formats that cannot be incorporated into the core law, specifically the IBC and its sections, are not considered. If you cannot insert a certain aspect into that, you will obviously have schedules created that define specific formats and forms, and those schedules will be placed at the end of the entire act.

There are several schedules under the IBC, and Schedule 3 pertains to the books of accounts that the liquidator must maintain during the liquidation process. The liquidator shall keep receipts for all payments made and expenses incurred. The appointment of a professional liquidator allows for the hiring of professionals in accordance with Regulation 7, as I mentioned earlier. Additionally, if the liquidator is not competent to make certain decisions or lacks knowledge of specific matters, they can engage professionals to perform specific duties and provide them with the necessary input and information. Currently, I am handling a professional case in which we are required to thoroughly examine the financial transactions of a corporate debtor and a personal guarantor to determine if any preferential or extortionate transactions have occurred.

As an insolvency professional and a qualified company secretary, although I possess financial knowledge, I may not have the necessary equipment and tools to perform this audit. Therefore, we are hiring professionals and detective agencies to perform the audits and provide us with a report on any transactions they find to be extortionate, preferential, undervalued, or fraudulent. Now I will have to pay a significant amount of money to these agencies, and this will be part of the liquidation cost. I will actually be reimbursed for the costs involved by the proceeds. Appointed professionals must disclose to the liquidator any personal or financial relationships they have with stakeholders or debtors immediately. After that, whenever I have consultations to make with stakeholders, I can consult with them on various aspects of what is to be done and how. The liquidator must maintain details of these consultations with the stakeholders as specified in Form A of Schedule 2. However, if you recall, we remember one particular line: Are the consultations with stakeholders binding on the liquidator? Should he follow this advice? No. These are non-binding consultations, and hence the liquidator may take his own decisions, though he has consulted the stakeholders and taken their opinions. This brings us to the end of session 49, and we are trying to understand the summary of what we have done in the past few minutes.

We have covered regulation 3 to regulation 8 of the IBBI liquidation process regulations, and there we have seen the appointment of the liquidator, what the eligibility criteria are, and what happens if there is a conflict of interest. We have also seen that liquidators' fees are important. We have seen that there are slabs. The first 1 crore will have a 6% fee to be paid to the liquidator on the realized value of the assets. After that, there is a 5% fee, and after that, there is a 4% fee, and finally, there is a 3% fee on anything realized above 50 crores; this is the liquidation liquidators' fee structure.

After Regulation 5, we have seen a lot of reports to be generated, such as the preliminary report, final report, report on the sale of assets, etc. After that, we have seen Regulation 6, which talks about the registers and books of accounts to be maintained under Schedule 3 for a period of 8 years. After that, we said the liquidator can appoint various professionals under regulation 7, and the fees paid to the professionals will form part of the liquidation process. Lastly, we said you should also have consultations with the stakeholders and report those consultations within the minutes and maintain those minutes for a period of eight years in the form mentioned in Schedule Two of the Act. So, this brings us to the end of session 49, where we have understood the IBBI regulations, ranging from three to eight.

In the next session, we will cover more regulations.

Thank you.