

# Insolvency and Bankruptcy Code 2016 and Winding up of a Company

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## Insolvency Resolution and Liquidation under the Insolvency and Bankruptcy Code, 2016

The Insolvency and Bankruptcy Code 2016 relates to re-organisation and insolvency resolution of companies, partnership firms and individuals in a time bound manner. With notification of the Code in November 2016, the provisions of section 271(2) of the Companies Act 2013 on winding up due to inability to pay debts and voluntary winding up (sections 304 to 323 of the Companies Act 2013) have been deleted and are not applicable.

The Insolvency and Bankruptcy Code 2016 applies to matters relating to the insolvency and liquidation of a company where the minimum amount of the default is Rs. 1 lakh (may be increased up to Rs.1 Cr by the Government, by notification). The Code lays down two stages:

*Insolvency Resolution Process* – It is the stage during which financial creditors assess whether the debtor's business is viable to continue and the options for its re-organisation and re-structuring; and

*Liquidation*– In case the insolvency resolution process fails, the liquidation process shall commence in which the assets of the company are realized to pay to the creditors.

### 1 The Corporate Insolvency Resolution Process

- (i) **Initiation of the Process:** Where a company commits a default in payment of debt of Rs 1 lakh or more, a creditor (financial creditor or operational creditor) or the company itself may initiate corporate insolvency resolution process in respect of such company as under:
  - **A financial creditor**<sup>1</sup> either by itself or jointly with other financial creditors may file an application before the National Company Law Tribunal for initiating corporate insolvency resolution process.

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<sup>1</sup> "Financial creditor" means any person to whom a financial debt is owed and includes a person to whom such debt has been legally assigned or transferred to. "Financial debt" means a debt along with interest, if any, which is disbursed and includes (a) money borrowed against the payment of interest; (b) any amount raised by acceptance under any acceptance credit facility; (c) any amount raised on the issue of bonds, notes, debentures, loan stock or

- **An operational creditor**<sup>2</sup> may, on the occurrence of a default, serve a notice of demand to the company with a copy of the invoice demanding payment of the amount involved in the default.

The company may, within a period of ten days of the receipt of the demand notice or copy of the invoice bring to the notice of the operational creditor (a) existence of a dispute, if any, and record of the pendency of the suit or arbitration proceedings filed before the receipt of such notice or invoice in relation to such dispute; or (b) the payment of unpaid operational debt by sending an attested copy of the record of electronic transfer of the unpaid amount from the bank account of the company; or an attested copy of record that the operational creditor has encashed a cheque issued by the company.

After the expiry of the period of ten days from the date of delivery of the notice or invoice demanding payment, if the operational creditor does not receive payment from the company or notice of the dispute, the operational creditor may file an application before Tribunal for initiating a corporate insolvency resolution process.

- (ii) **Order for Initiation of Insolvency Process:** The Tribunal shall, within 14 days of the receipt of the application of the creditor (financial or operational creditor) ascertain the existence of a default from the records or on the basis of other evidence furnished by the creditor. Where the Tribunal is satisfied that a default has occurred and the application is complete, the Tribunal shall pass the order for initiation of corporate insolvency process.
- (iii) **Time Limit for Completion of Insolvency Resolution Process:** The corporate insolvency resolution process shall be completed within a period of 180 days from the date of admission of the application to initiate such process. However, the Tribunal has the power to grant one-time extension up to further period of 90 days for completing the process on the application of resolution professional.
- (iv) **Moratorium on Claims:** Upon admission of application by the Tribunal, creditors' claims will be frozen for 180 days, during which time Tribunal will hear proposals for revival and decide on the future course of action. The Tribunal shall by an order declare moratorium for prohibiting (a) the institution of

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any similar instrument; (d) the amount of any liability in respect of any lease or hire purchase contract; (e) receivables sold or discounted; (f) any amount raised under any other transaction, including any forward sale or purchase agreement, having the commercial effect of a borrowing; (g) any derivative transaction; (h) any counter-indemnity obligation in respect of a guarantee, indemnity, bond, documentary letter of credit or any other instrument issued by a bank or financial institution; (i) the amount of any liability in respect of any of the guarantee or indemnity for any of the items referred to in sub-clauses (a) to (h).

<sup>2</sup> "**Operational creditor**" means a person to whom an operational debt is owed and includes any person to whom such debt has been legally assigned or transferred. "Operational debt" means a claim in respect of the provision of goods or services including employment or a debt in respect of the repayment of dues arising under any law for the time being in force and payable to the Central Government, any State Government or any local authority.

- suits or continuation of pending suits or proceedings against the company including execution of any judgment, decree or order in any court of law, tribunal, arbitration panel or other authority; (b) transferring, encumbering, alienating or disposing of by the company any of its assets or any legal right or beneficial interest therein; and (c) any action to foreclose, recover or enforce any security interest created by the company, until approval of resolution plan or until initiation of liquidation process.
- (v) **Appointment of Interim Insolvency Professional (IP):** The Tribunal shall appoint an interim resolution professional within 14 days from the insolvency commencement date. (a) Where the application for corporate insolvency resolution process is made by a creditor (financial or operational creditor) or the company, as the case may be, the resolution professional, as proposed respectively in the application; (b) Where the application for corporate insolvency resolution process is made by an operational creditor and no proposal for an interim resolution professional is made, the Tribunal shall make a reference to the Board (Insolvency and Bankruptcy Board) for the recommendation of an insolvency professional who may act as an interim resolution professional. The term of the interim resolution professional shall not exceed 30 days from date of his appointment.
- (vi) **Management of affairs of corporate debtor by interim resolution professional:** From the date of appointment of the interim resolution professional
- the management of the affairs of the corporate debtor shall vest in the interim resolution professional;
  - the powers of the board of directors of the company shall stand suspended and be exercised by the interim resolution professional;
  - the officers and managers of the company shall report to the interim resolution professional and provide access to such documents and records of the corporate debtor as may be required by the interim resolution professional;
  - the financial institutions maintaining accounts of the company shall act on the instructions of the interim resolution professional in relation to such accounts and furnish all information relating to the company available with them to the interim resolution professional.
- (vii) **Committee of Creditors:** The interim resolution professional shall after collation of all claims received against the company determination of the financial position of the, constitute a committee of creditors. The committee of creditors shall comprise all financial creditors of the company: Provided that a related party to whom the company owes a financial debt shall not have any right of representation, participation or voting in a meeting of the committee of creditors. All decisions of the committee of creditors shall be taken by a vote of not less than 75% of voting share of the financial creditors. Operational creditors may be part of creditors' committee (without voting right) if their aggregate dues are not less than 10% of the debt.
- (viii) **Appointment of Resolution Professional:** The first meeting of the creditors' committee shall be held within 7 days of its constitution and decide by 75% of

votes either to replace or confirm interim IP as Resolution Professional. Thereupon, Resolution Professional is appointed by the Tribunal upon confirmation by the Board. The creditors' committee, with a majority of 75% votes, can change Resolution Professional any time.

- (ix) Resolution Professional to conduct Corporate Insolvency Resolution Process:** The resolution professional shall conduct the entire corporate insolvency resolution process and manage the operations of the company during the corporate insolvency resolution process period. The resolution professional shall exercise powers and perform duties as are vested or conferred on the interim resolution professional. The resolution professional shall prepare an information memorandum in such form and manner containing such relevant information as may be specified by the Board for formulating a resolution plan. A resolution applicant may submit a resolution plan to the resolution professional prepared on the basis of the information memorandum. The resolution professional shall examine each resolution plan received by him. The resolution professional shall present to the committee of creditors for its approval such resolution plans which confirm the conditions which are laid down by the Code. The committee of creditors may approve a resolution plan by a vote of not less than 75% of voting share of the financial creditors. The approved resolution plan shall be submitted by the resolution professional to the Tribunal. If the Tribunal is satisfied with the resolution plan as approved by the committee of creditors, it shall by order approve the resolution plan which shall be binding on the company and its employees, members, creditors, guarantors and other stakeholders involved in the resolution plan.

## 2. Liquidation

**(i) Initiation of Liquidation:** The Tribunal shall pass the liquidation order in the following cases:

- failure to submit the resolution plan to the Tribunal within the prescribed period, or
  - rejection of resolution plan for non-compliance with the requirements of the Code,
- or
- decision of creditors' committee based on vote of majority, or
  - contravention of resolution plan by the company.

During liquidation, no suit or other proceedings shall be instituted by or against the company except with permission of the Tribunal. The order for liquidation shall be deemed to be a notice of discharge to the officers, employees and workmen of the corporate debtor, except when the business of the corporate debtor is continued during the liquidation process by the liquidator.

**(ii) Appointment of Liquidator:** The Resolution Professional shall act as liquidator unless replaced by the Tribunal. On the appointment of a liquidator, all powers of the board of directors and key managerial personnel of the company shall cease to have effect and shall be vested in the liquidator. The personnel of the company are required to extend all assistance and cooperation to the liquidator as may be required by him in managing the affairs of the company.

**(iii) Powers and Duties of the Liquidator:** Subject to the directions of the Tribunal, the liquidator shall have the following powers and duties:

- (a) to verify claims of all the creditors;
- (b) to take into his custody or control all the assets, property, effects and claims of the company;
- (c) to evaluate the assets and property of the company in the manner as may be specified by the Board and prepare a report;
- (d) to take such measures to protect and preserve the assets and properties of the company as he considers necessary;
- (e) to carry on the business of the company for its beneficial liquidation as he considers necessary;
- (f) to sell the immovable and movable property and actionable claims of the company;
- (g) to invite and settle claims of creditors and claimants and distribute proceeds in accordance with the provisions of this Code;
- (h) to take all such actions, steps, or to sign, execute and verify any paper, deed, receipt document, application, petition, affidavit, bond or instrument as may be necessary for liquidation, distribution of assets and in discharge of his duties and obligations and functions as liquidator; and
- (i) to perform such other functions as may be specified by the Board.

The liquidator shall form an estate of all assets of company called the liquidation estate.

**(4) Dissolution of company:** Where the assets of the company have been completely liquidated, the liquidator shall make an application to the Tribunal for the dissolution of such company. The Tribunal shall on application filed by the liquidator order that the company shall be dissolved from the date of that order and the company shall be dissolved accordingly.

## Voluntary Liquidation of Company

A company which intends to liquidate voluntarily and has not committed any default and can pay off its debts fully from proceeds of liquidation of its assets may initiate voluntary liquidation proceedings under the provisions of Chapter V of the Insolvency and Bankruptcy Code 2016. The voluntary liquidation requires the following conditions to be met:

- 1. Declaration from the Directors:** A declaration from majority of the directors of the company verified by an affidavit stating that— (i) they have made a full inquiry into the affairs of the company and they have formed an opinion that either the company has no debt or that it will be able to pay its debts in full from the proceeds of assets to be sold in the voluntary liquidation; and (ii) the company is not being liquidated to defraud any person.

The declaration must be accompanied with the following documents: (i) audited financial statements and record of business operations of the company for the previous two years or for the period since its incorporation, whichever is later; (ii) a report of the valuation of the assets of the company, if any prepared by a registered valuer.

- 2 Passing of Special Resolution:** Within four weeks of the declaration, the company is required to pass

- (i) a special resolution of the members of the company in a general meeting requiring the company to be liquidated voluntarily and appointing an insolvency professional to act as the liquidator; or
- (ii) a resolution of the members of the company in a general meeting requiring the company to be liquidated voluntarily as a result of expiry of the period of its duration, if any, fixed by its articles or on the occurrence of any event in respect of which the articles provide that the company shall be dissolved, as the case may be and appointing an insolvency professional to act as the liquidator

- 3. Resolution of the Creditors:** Where the company owes any debt to any person, creditors representing two thirds in value of the debt of the company shall approve the resolution passed by the company within 7 days of such resolution.
- 4. Notice to the Registrar and the Board:** The company is required to notify the Registrar of Companies and the Board about the resolution to liquidate the company within 7 days of such resolution or the subsequent approval by the creditors, as the case may be.
- 5. Commencement of Voluntary Liquidation:** The voluntary liquidation proceedings in respect of a company shall be deemed to have commenced from the date of passing of the resolution. Provisions of the voluntary liquidation shall apply.
- 6. Dissolution:** Where the affairs of the corporate person have been completely wound up, and its assets completely liquidated, the liquidator shall make an application to the Tribunal for the dissolution of such company. The Tribunal shall on an application filed by the liquidator pass an order that the company shall be dissolved from the date of that order.