



Liquidation under IBC

11.11.2021



LIQUIDATION UNDER IBC

ASHISH RATHI
INSOLVENCY
PROFESSIONAL, CA,
MBA (ISB, HYDDERABAD)

ZEENATH JAHAN
CA

23.08.2021

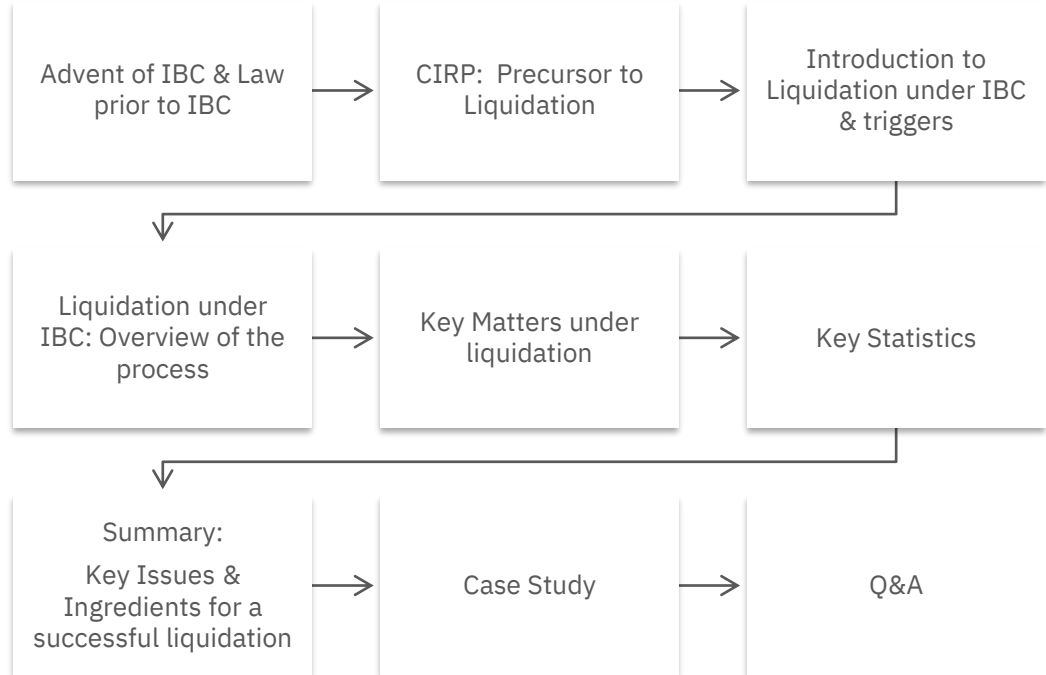
BACKGROUND & COURSE CHART

Background

Presented by Ashish and Zeenath as a part of the certificate course on Insolvency and Bankruptcy Code, 2016 conducted by fortitude learning for professionals and students.

Other speakers in the course included Mr. Bahram Vakil (Founder & senior partner – AZB & Partners), Avinash Subramnium (Partner, AZB & Partners) Ujjwal Ganguly (Director, Duff & Phelps), Archit Grover (VP, Duff & Phelps), Uday Khare (Partner, Link Legal), Anand Srivastava (Partner, Link legal), Divyanshu Pandey (Partner, S&R Associates) Satish Kumar Gupta (Ex-Rp, Essar Steels), Ashwini Mehra (RP, Punj Lloyd Limited), Sumant Batra (Managing Partner, Kesar Das B & Associates) & Raghuram Cabambi (Advocate, Karnataka High Court)

Course Chart





ADVENT OF IBC AND LAW PRIOR TO IBC



ADVENT OF IBC

Introduced in 2016, the IBC,2016 seeks to consolidate and amend all the existing legal frameworks for bankruptcy and insolvency into one. Effective date of implementation – 01st December,2016

OBJECTIVES OF THE CODE:



Effective legal framework for timely resolution



Development of credit markets



Encouraging entrepreneurship

GOVERNING BODY, SERVICE PROVIDERS,ADJUDICATING AUTHORITY



INSOLVENCY AND BANKRUPTCY CODE, 2016

- Insolvency And Bankruptcy Board Of India (IBBI) and Insolvency Professional Agencies (IPAs)
- National Company Law Tribunal And Appellate Tribunal (NCLT and NCLAT)
- Insolvency Professionals and Insolvency Professional Entities
- Committee Of Creditors (CoC)



LAW PRIOR TO IBC & SHORTCOMINGS

SARFAESI Act, 2000
Still in effect

- Resorted to as the first option without following due recovery process.
- Possession of security posed a challenge.

The Presidency Towns
Insolvency Act, 1909 and The
Provincial Insolvency Act, 1920

- Not universally applicable
- Not time bound
- Debtor has no opportunity for resolution before dissolution

Companies Act

- No voluntary liquidation provisions
- No opportunity for revival

RDDBFI Act, 1993

- Delayed decisions

SICA

- Selective application
- Basis of admission - Erosion of net worth and not default
- Bias against liquidation
- No mechanism for distribution of assets

Relevant
provisions
repealed



WHAT ABOUT CDR,SDR AND S4A?

Corporate Debt
Restructuring (CDR)

Stress on maintaining asset classification in the books of bank

Additional cash flow requirement not attended to

Strategic Debt
Restructuring(SDR)

Banks have found it difficult to find investors where SDR was invoked and have faced difficulty in price negotiations

Sustainable Structuring
for Stressed Assets (S4A)

Only applies to entities with commercial operations, requires the companies to have cash flows to service the debt.



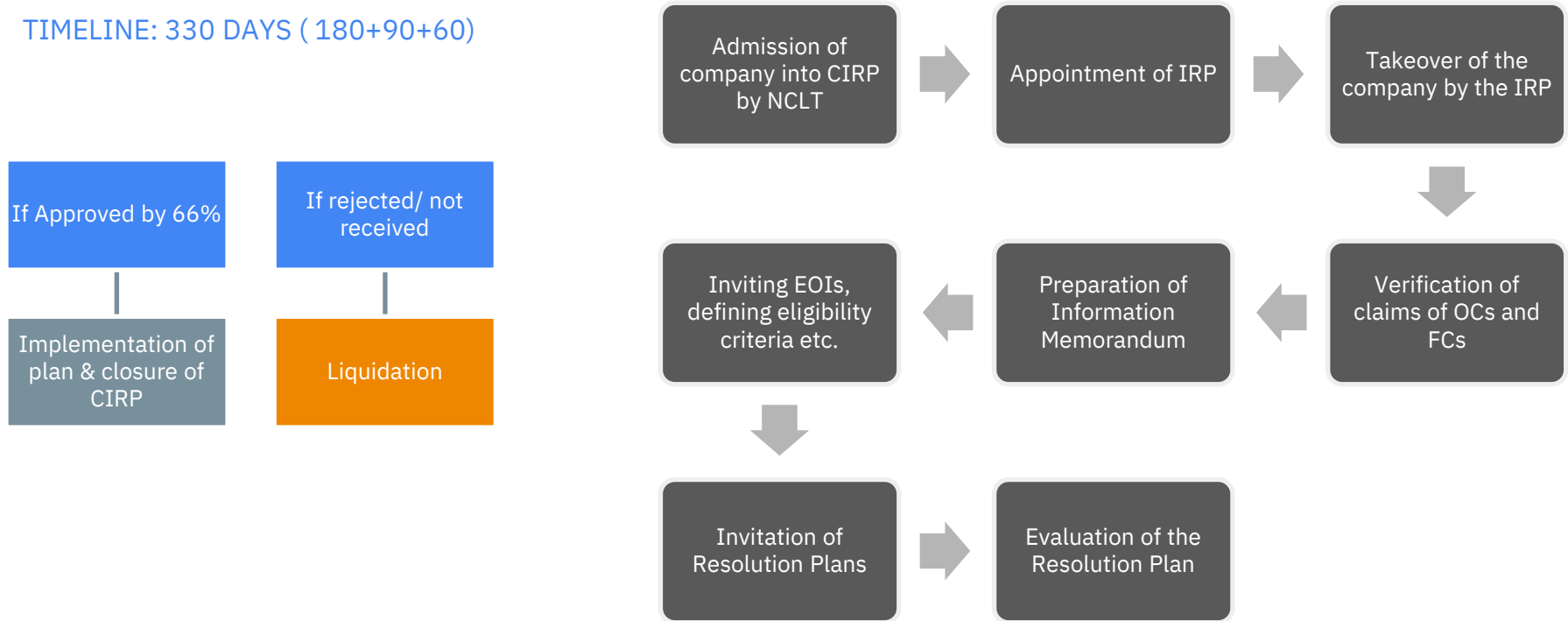
CIRP : PRECURSOR TO LIQUIDATION



CIRP PROCESS FLOW

To understand Liquidation better, it is worthwhile to glance at the precursor to liquidation, CIRP. Under IBC, no company can be referred to liquidation (unless being voluntarily liquidated), without first undergoing CIRP.

TIMELINE: 330 DAYS (180+90+60)

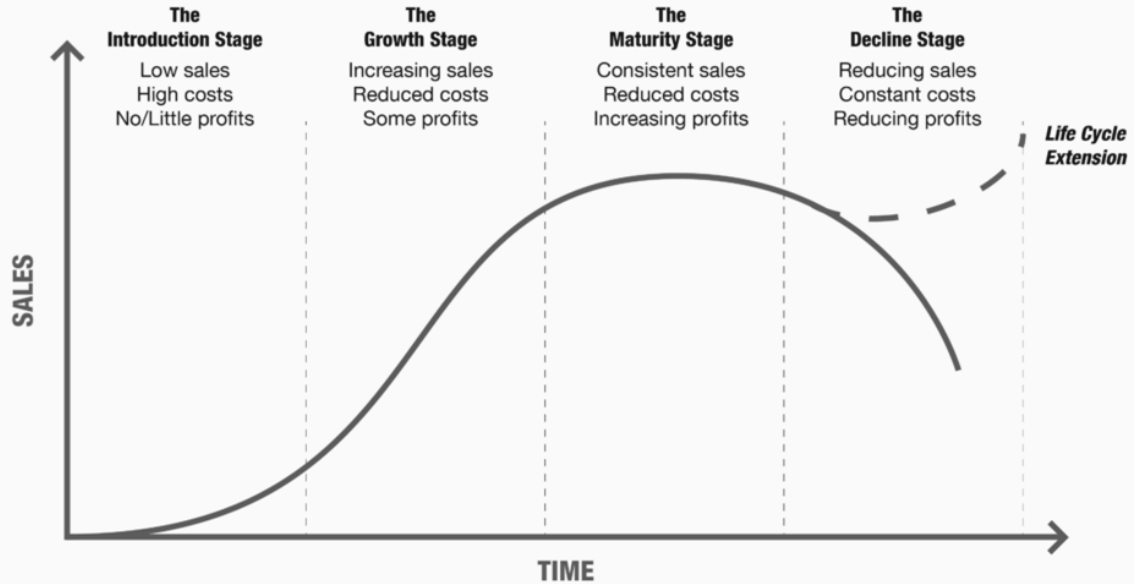




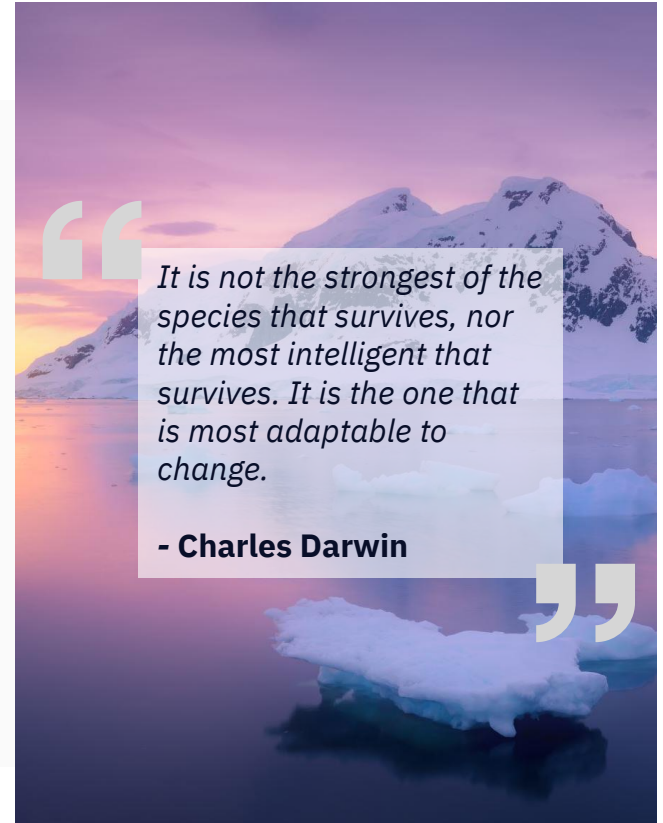
LIQUIDATION IN INDIA

INTRODUCTION

CORPORATE LIFE CYCLE



Source: Data collated from various websites

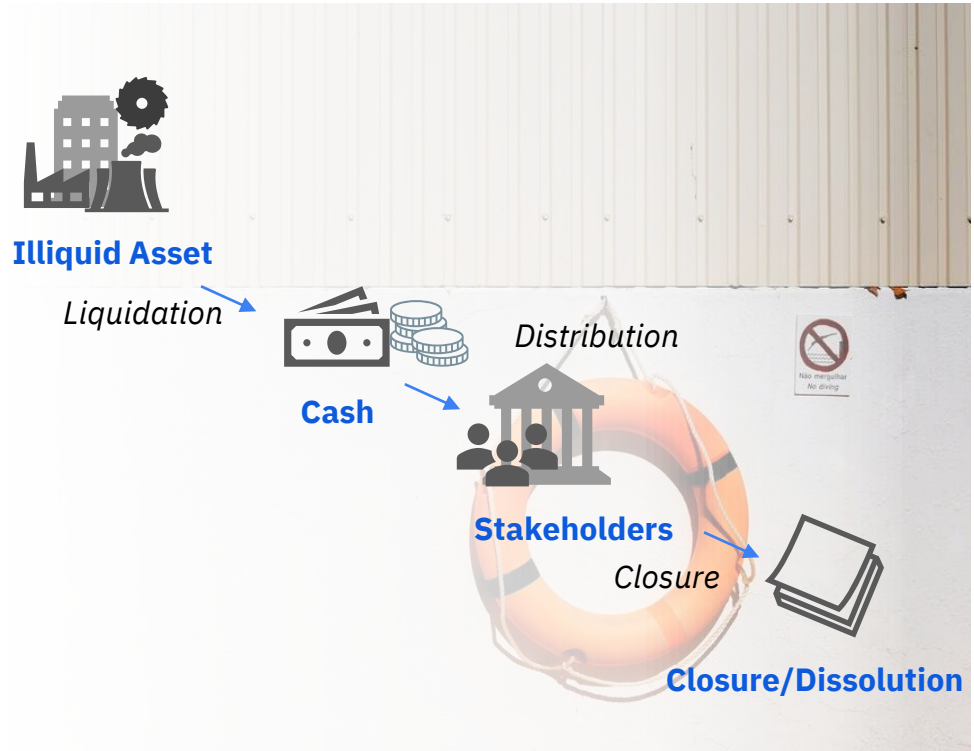


INTRODUCTION TO LIQUIDATION

While there are numerous reasons for liquidation to take place, more generally under IBC, liquidation is a process that is resorted to when the company is **no longer able to meet its financial obligations** from its cash flows or in other words, liquid assets.

It entails “liquidation” of the company’s assets, so that the obligations may be met from the cash proceeds accruing out of the sale of the assets.

It is the last and the least desirable remedy and is only resorted to when all other options are exhausted.





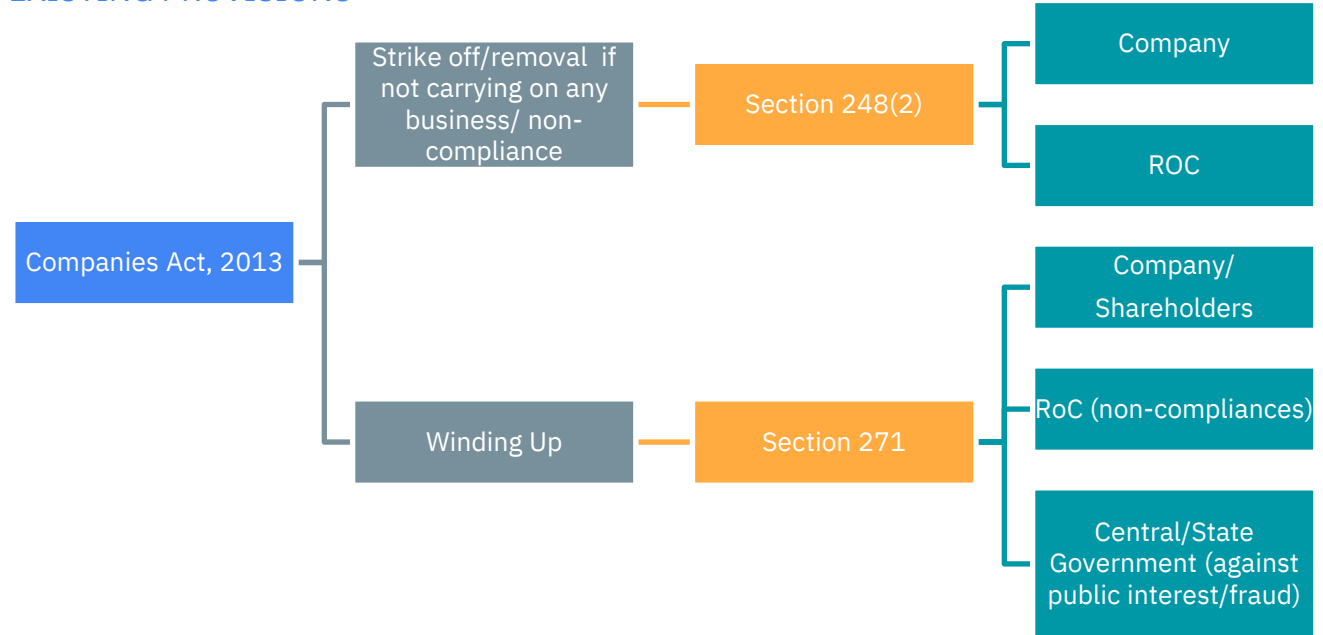
WINDING UP UNDER COMPANIES ACT, 2013

When the Companies Act 2013 was enacted, Section 271 [1] included the ground of “inability to pay debts” and the procedure for voluntary winding up of a company was laid down under Part II of Chapter XX of the Act.

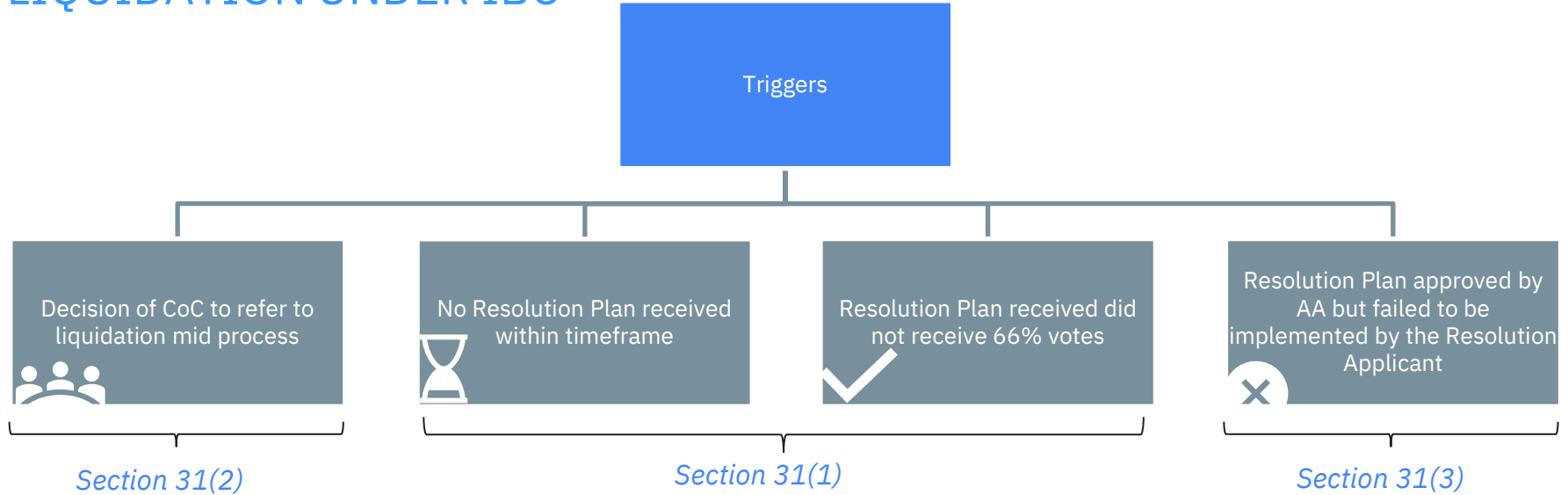
Since then, both the aforesaid have been omitted vide Section 255 of the Insolvency and Bankruptcy Code, 2016. The same are now being governed by IBC.

Summary winding up for smaller companies has been made effective since April 2020 under Companies Act.

EXISTING PROVISIONS



LIQUIDATION UNDER IBC



Case Law – Siva Industries (12.08.2021)

Legal Framework:

- Insolvency and Bankruptcy Code, 2016
- IBBI(Liquidation Process) Regulations, 2016



PROCESS OF LIQUIDATION OVERVIEW

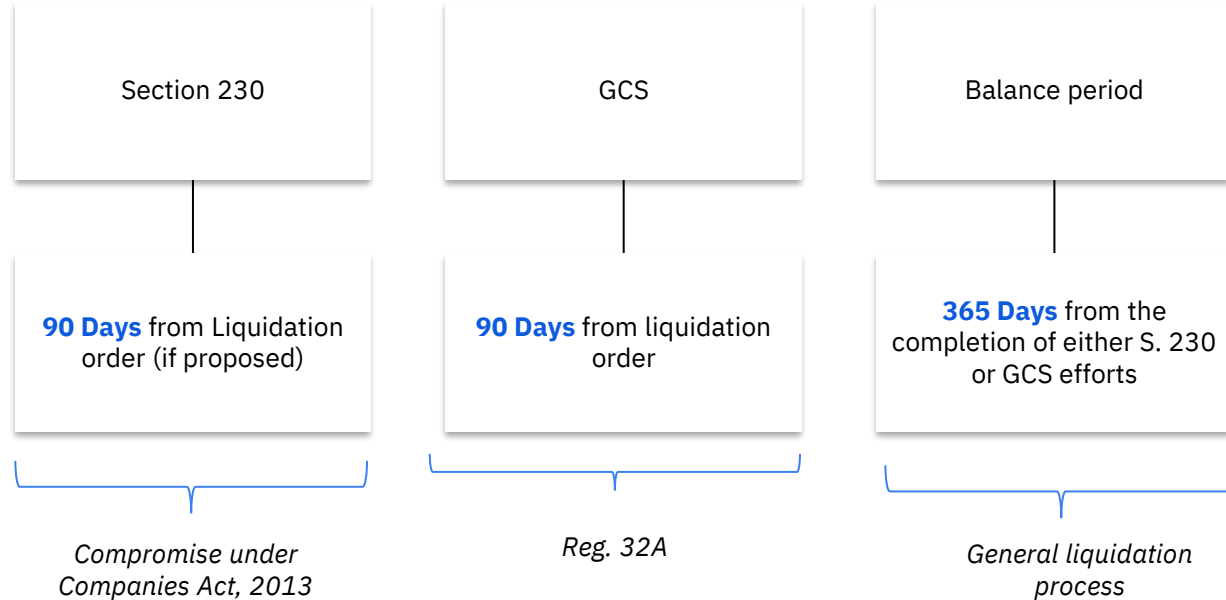


TIMELINES

Regulation 44

Time allowed for liquidation: **1 Year**

(excl. GCS & S. 230)



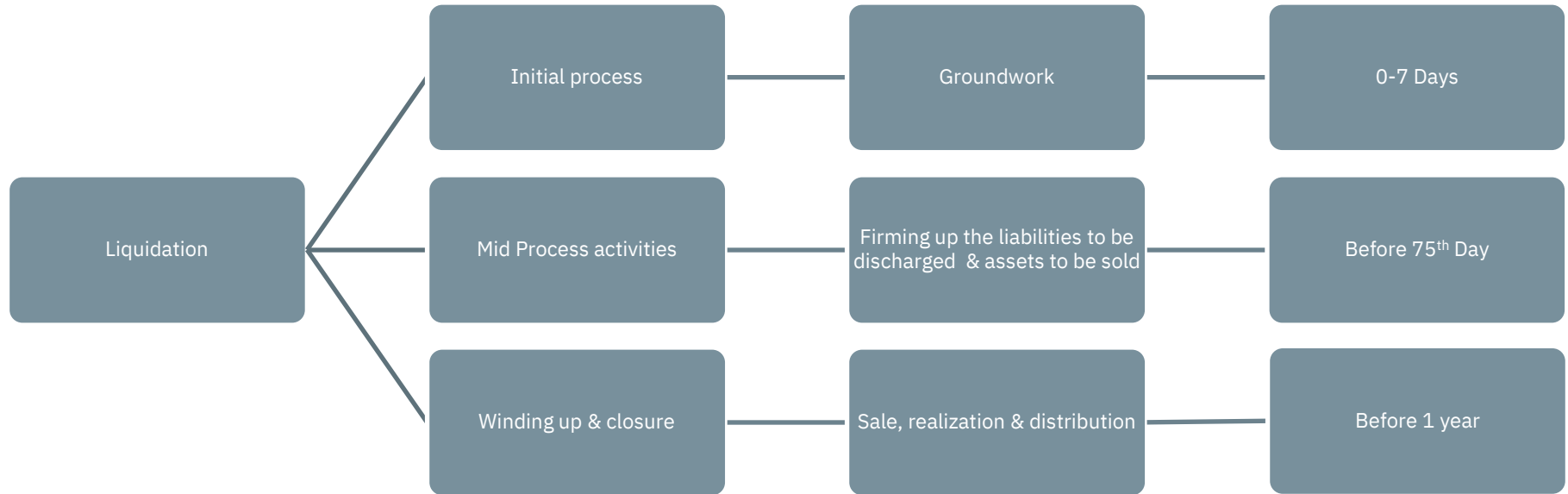
Can the period of 1 year be extended?

Yes, an application has to be made to NCLT, laying out the reasons for delay and the additional time required



LIQUIDATION PROCESS

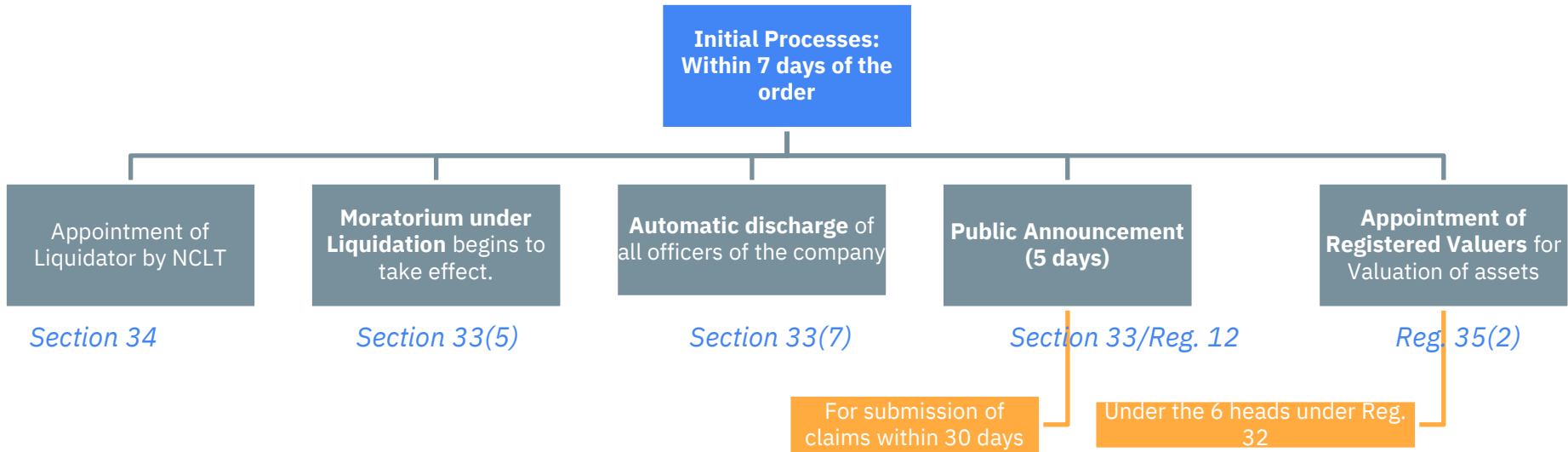
In the following section we are going to get an overview of the salient aspects of the process that contribute towards its closure.





INITIAL PROCESS : WITHIN 7 DAYS OF THE ORDER

TRIGGER: ORDER INITIATING LIQUIDATION & APPOINTMENT OF LIQUIDATOR





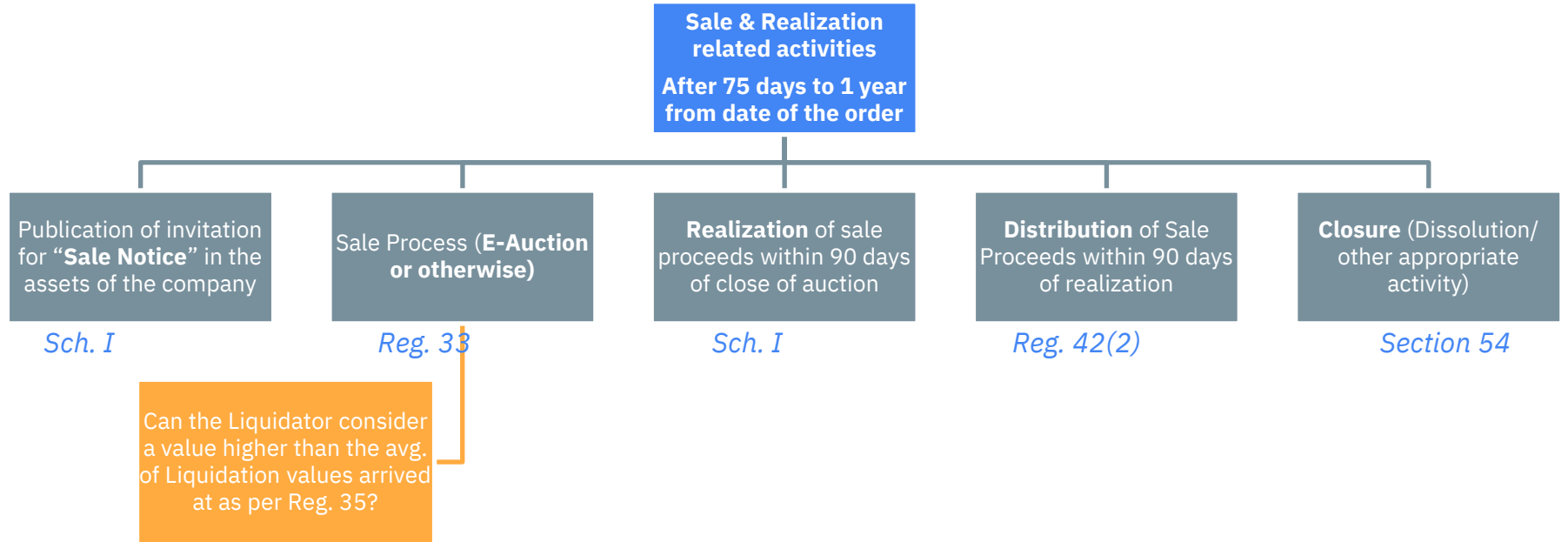
MID-PROCESS ACTIVITIES : BEFORE 75TH DAY

Mid-Process Activities –
Within 30-75 days of the
order





WINDING UP & CLOSURE : BEFORE 1 YEAR





KEY MATTERS IN LIQUIDATION



KEY MATTERS IN LIQUIDATION

Who are the stakeholders?

Stakeholders' consultation committee

Relinquishment by secured creditors

Liquidation Estate : What is and isn't included?

Waterfall Mechanism & Inter-se priorities among creditors

Rights of creditors

Duties & Rights of the liquidator

Liquidator's Remuneration

Valuation & Reserve Price

Mode of sale

Going Concern sale

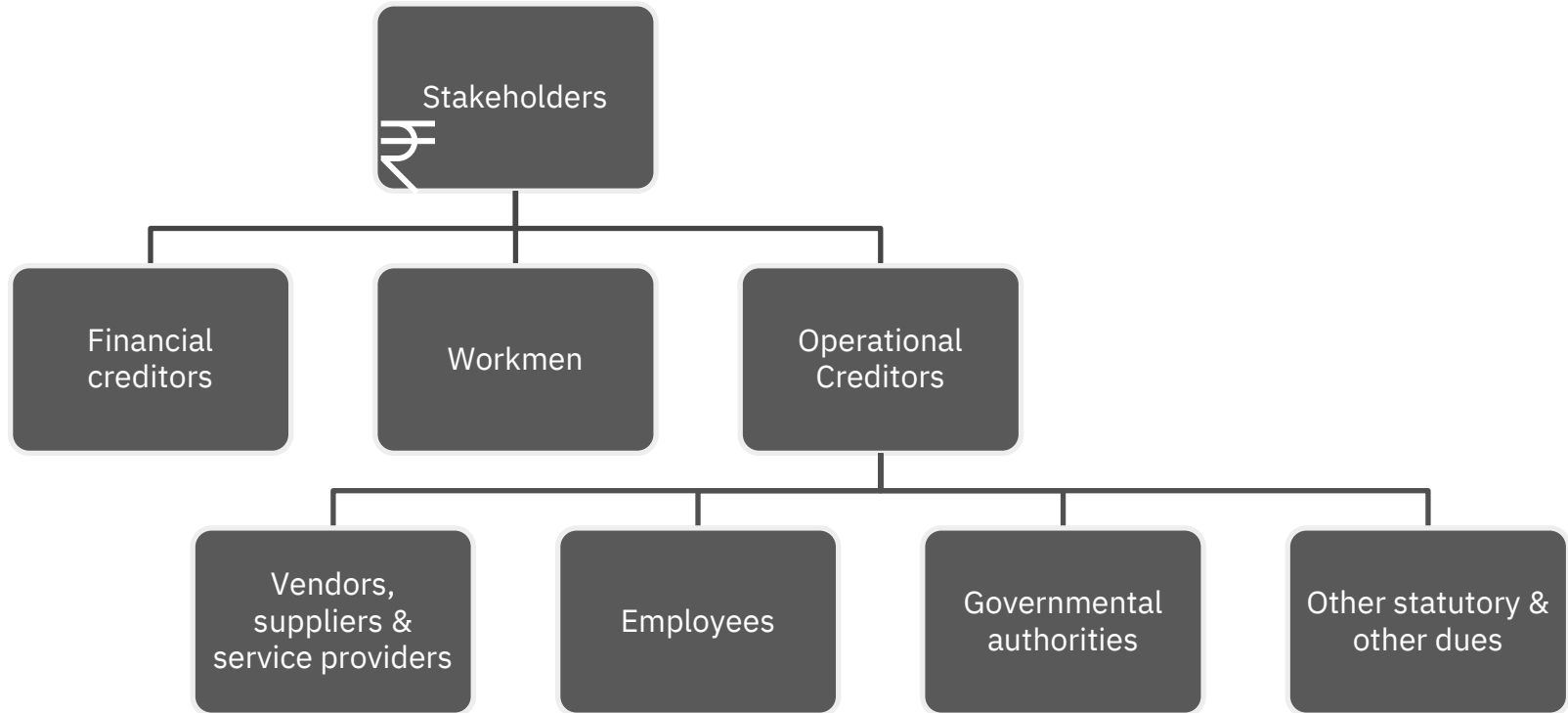
Section 230 Sale

Avoidance Transactions

Powers of NCLT



WHO ARE THE STAKEHOLDERS?





STAKEHOLDERS CONSULTATION COMMITTEE

Inserted vide amendment to give creditors representation as no CoC exists. Here, the liquidator while he does not work under their supervision, he has to assign reasons when he goes against the committee's advisory and is answerable to NCLT

MAXIMUM STRENGTH – 11 MEMBERS

S.no	Category	Members	
		Min.	Max.
1	Secured FCs	2	4
2	Unsecured FCs	1	2
3	Workmen & Employees	1	1
4	Government	1	1
5	OCs (Other than workmen, employees & Government)	2	2
6	Shareholders	1	1
TOTAL		8	11

HOW IS THE MINIMUM OR MAXIMUM NUMBER DECIDED?

The number of representatives allowed depends on the stake of the “class”.

Eg: In case of secured FCs, if their claims are equal to more than 50% of liquidation value, they are allowed to have 4 representatives and if the stake is less than 50%, the number is restricted to 2.

The stake cut-off percentage for unsecured FCs and OCs similarly is 25%



LIQUIDATION ESTATE : WHAT IS AND ISN'T INCLUDED?

Section 36

Liquidation Estate is essentially the group of assets of the company that can be sold by the Liquidator. It typically includes the land, buildings, factories, and other property and equipment owned by the company.

What is formation of the Liquidation Estate, how is it formed and why is it crucial?

The process of putting together the pool of assets is how a liquidation estate is formed. It involves securing [relinquishment](#) from creditors, determining what is and isn't owned by the company and determining if any asset has wrongfully been taken out of the company and bringing it back in via [avoidance](#) proceedings.

Any asset that does not form part of Liquidation Estate cannot be sold by the Liquidator.



LIQUIDATION ESTATE : WHAT IS AND ISN'T INCLUDED?

Section 36

Inclusions:



Assets on which company has ownership rights

Assets subject to the determination of ownership by the court or authority

Any asset recovered through avoidance proceedings

Assets which have been relinquished by secured creditors

Assets owned by third party in possession of the company

Exclusions:



PF, Gratuity & pension fund

Personal assets of directors/partners

Assets of subsidiaries



RELINQUISHMENT OF SECURITY INTEREST

Section 52

WHAT IS RELINQUISHMENT?

A major decision point for secured creditors in a liquidation process is very elementary in nature. The process of relinquishment is one vide which the secured creditors :

- Cede their charge to the “Liquidation Estate”
- Authorize the Liquidator to sell the assets on their behalf and
- Agree to accept the sale proceeds as against their admitted debt.

BY WHEN DOES AN FC NEED TO LET THE LIQUIDATOR KNOW OF ITS DECISION?

30 days from Liquidation date
(w.e.f 25.07.2019)

WHAT IF THE FC DOES NOT DECIDE BY THEN?

The asset is the presumed to have been relinquished to the Liquidation Estate.

The secured creditor has two options:

To **receive the proceeds of sale** the Liquidation Estate.

To **stay out of the Liquidation Process and enforce his security** towards his debt.

This **requires relinquishment of charge.**

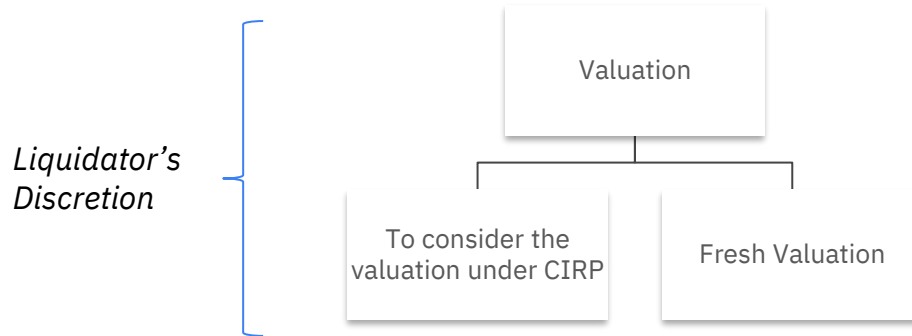
However, **the Code prescribes a few obligations in this case** with respect to costs of the process and workmen’s dues.



VALUATION UNDER LIQUIDATION

Regulation 35

Once the Liquidation Estate is created, the Liquidator is required to assign a value to the estate, so that he can put it up for sale.



If a fresh valuation is being carried out, the Liquidator is required to appoint two independent registered valuers, who will each give their report under each of the [sale options under Regulation 32](#). The average of the figures submitted by the two valuers, shall be taken as the value of the company/assets. This is generally the [Reserve Price](#).

In case valuation under CIRP is being used, this would already be the average of two valuation estimates given by valuers during CIRP and can be taken as is.



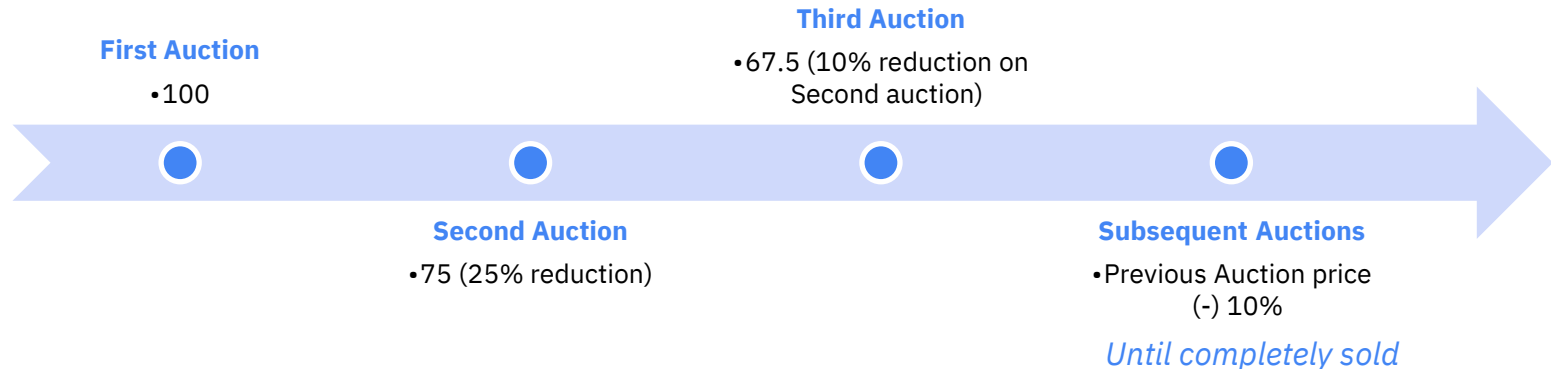
RESERVE PRICE

This is the **floor** price, that is arrived at by averaging out the valuation estimates. The Liquidator is required to put up the company for sale initially at **at least** this price.

Reduction of reserve price:



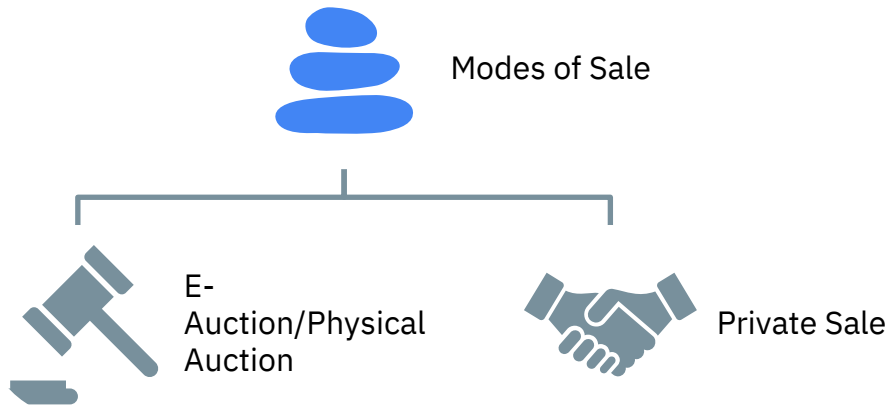
If the auction doesn't go through, what it means that that the market thinks the asset is overvalued. Therefore, the liquidator is empowered to reduce the price with each subsequent auction. In the second auction, a 25% reduction is allowed and thereafter, 10% each time.





MODES OF SALE

In practice, most liquidation cases are disposed off by way of E-Auction, as the process is open for all, transparent and leads to reduced litigation. The competitive bidding also drives up the value for the stakeholders.



PRIVATE SALE IN CASE OF:

The asset is perishable

The asset is likely to deteriorate in value significantly if not sold immediately

The asset is sold at a price higher than the reserve price of a failed auction

The prior permission of the Adjudicating Authority has been obtained for such sale:



SALE OPTIONS UNDER REGULATION 32

The corporate debtor as a going concern

The business of the corporate debtor as a going concern

Slump sale

A set of assets collectively

The assets in parcels

Standalone basis

In order of preference

The Liquidator is required by law to first attempt a “beneficial liquidation”, i.e., a going concern sale under liquidation. Only when he is unsuccessful in doing that, he can explore other options, with sale of assets on standalone basis/piecemeal basis being the last resort

Reserve price is different for each method of sale under Reg. 32



SALE OUTSIDE OF IBC – SECTION 230- COMPROMISE & ARRANGEMENT

Section 230 allows the members of a company to enter into a compromise with the creditors for the debt owed and arrive at “Scheme of Arrangement” that sets out the terms of the settlement. If a liquidator receives a proposal within 90 days of Liquidation process for a compromise, the Liquidator shall file the same with the NCLT. Else, he shall proceed with Liquidation as usual.

What is a Section 230 sale?	It is a compromise, or an arrangement as provided for in the Companies Act, 013
Time Allowed	90 days
Governing Law	Companies Act, 2013 read with IBC
Whether Section 29A Compliance is necessary?	Yes

Is the liquidator obligated to pursue S. 230 compulsorily?

The genesis of S.230 sale under liquidation, came about due to the judgement of The National Company Law Appellate Tribunal (NCLAT) in S.C. Sekaran vs. Amit Gupta and Ors. (Sekaran Case). In this case, the NCLAT directed the liquidator, appointed under the IBC, to “take steps in terms of Section 230” for the revival of the corporate debtor before undertaking the sale of its assets.

It is however, not prescribed within the Code, that S. 230 must be compulsorily resorted to. For S.230 to kick into place, there has to be a proposal from an eligible person.

Conservatively, practically, in a few liquidation processes, a public announcement inviting S.230 proposals is also being made, before auction notice is published to rule out any litigation thereafter.



GOING CONCERN SALE

Reg. 32A

WHAT HAPPENS IN A GCS?

In a GCS, unlike in other modes where the company is dissolved at the end, the company survives the process, while the ownership shall transfer to the new management.

CHALLENGES IN GCS:

Most of the companies under Liquidation/CIRP are likely to be defunct. According to recent statistics of IBBI, ~75% of the asset coming to IBC were defunct to begin with.

HOW CAN GCS TAKE PLACE WHEN THE UNIT IS SHUT?

However, if a unit is closed the generally accepted view of a “going-concern” may not be fulfilled by the company. Hence, Although not fitting the definition of a going concern as per general parlance, sale of the company as a whole along with all its licenses, permissions etc. may be called a going concern sale under liquidation even if the same may not qualify as such under the tax laws.

THE GUJARAT NRE COKE PRECEDENT

The genesis of the concept of “Going Concern” sale under Liquidation can be traced back to the Gujarat NRE Coke order by NCLT, Kolkata which ordered that the company be sold as “ a going concern” under Liquidation. This was a first in the realm of IBC. The underlying rationale was that the employees who were dependent on the company, (Close to 10,000) should not be left without a livelihood.

This paved way for amendment in the Regulations, which now allow and even to a large extent encourage a going concern sale as a first option.

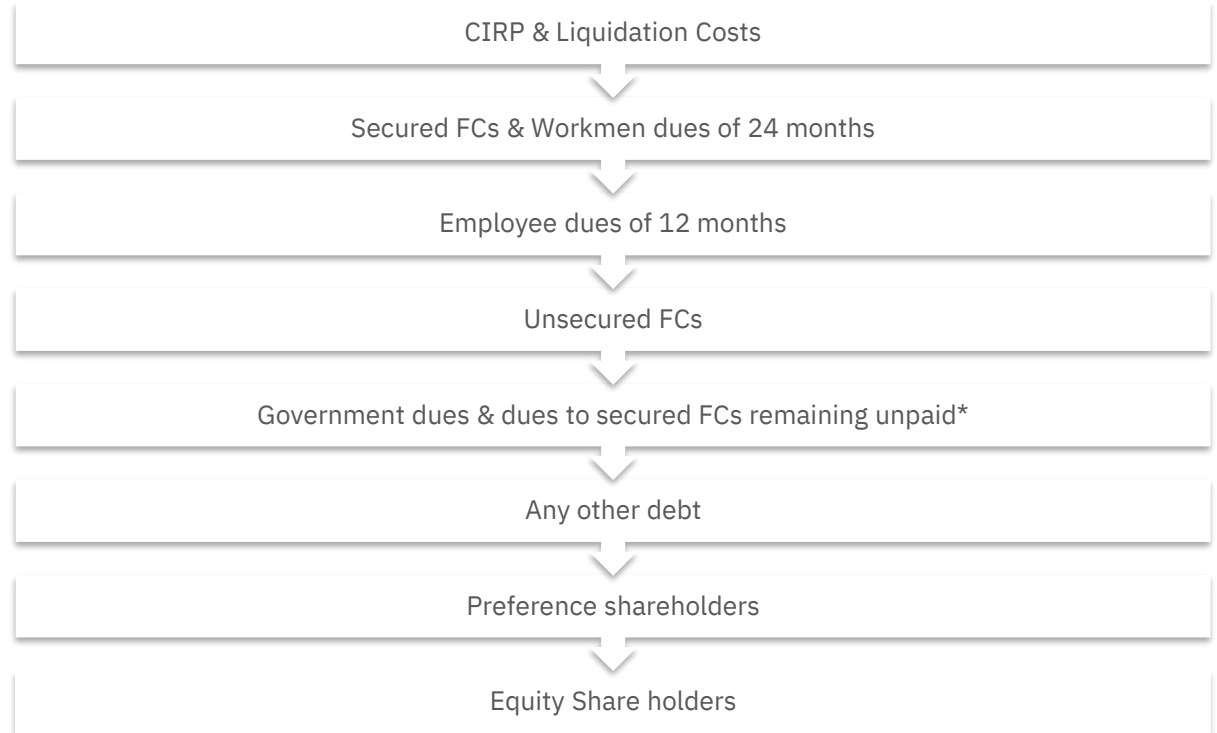


WATERFALL MECHANISM

Section 53

Waterfall mechanism is dictated under Section 53 of the Code. This forms the heart of the liquidation legislation as far as creditors rights are concerned as this determines, who gets paid first out of the liquidation proceeds. This is important as, in most of the cases, the amounts owed to the creditors is much higher than the value that is realized from sale under liquidation.

Section 53, effectively decides who gets paid and who does not.



**remaining unpaid on account of the FC enforcing his security interest on his own*



INTER-SE PRIORITIES BETWEEN CREDITORS

What is the contention?

When the secured creditors relinquish charge to the liquidation estate, there is an argument that, the first charge holders and the subservient/second charge holders shall be paid pari-passu. Effectively, it is being contended that the act of relinquishment takes away the distinction between first charge and second charge.

Relevance of first charge & second charge:

A first charge holder, as the name suggests, is contractually entitled to receive the sale proceeds of the asset held as security by him **first** towards satisfaction of his debt and thereafter, if there is surplus, that would go to the second charge holder. If the above contention is accepted, both the first and second charge holder get paid equally in proportion to their debt, without heeding to priority.

[NCLT, Ahmedabad in Technology Development Board Vs. Anil Goel & Ors. relied on the Supreme Court's decision in ICICI Bank v. SIDCO Leather. Held that:](#)

- Inter-se priorities among secured creditors will remain valid and prevail in distribution of assets in Liquidation.
- Charges are sequential and not proportional.
- Idea of proportionality is only as far as claims of similar ranking are concerned.



RIGHTS OF CREDITORS

To file a claim for their dues before the Liquidator in prescribed form, within prescribed time

To seek timely verification and admission of their claims

To seek reasons for rejection, if their claim is rejected

To appeal against rejection of claim – Within 14 days

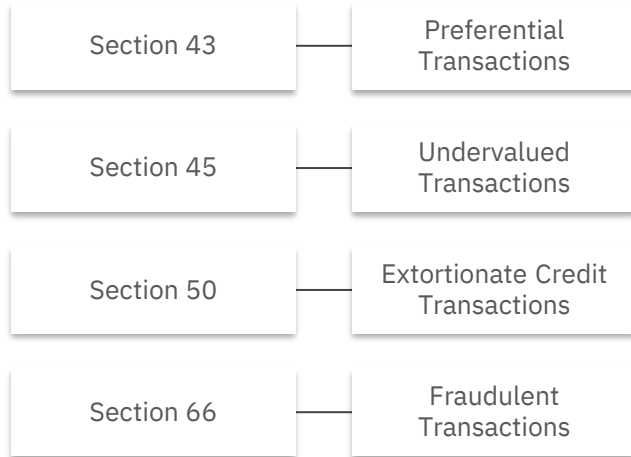
To receive the proceeds of the sale of the liquidation estate as per the waterfall mechanism

To be represented in the Stakeholders 'consultation committee.

To advise the Liquidator at all stages during the process, as may be requested/required



AVOIDANCE TRANSACTIONS



- These are the transactions that, if the company has undertaken prior to CIRP, may have resulted into money/assets flowing out of the company wrongfully to the benefit of a party not entitled to such benefit and detriment of a party, entitled to the sums.
- The RP/Liquidator is required to make an application to NCLT seeking claw back of these assets/monies back into the company upon finding such transactions.
- If recovered under liquidation, the recoveries would form part of Liquidation Estate and would be distributed to creditors.
- Oftentimes, adjudication of these transactions is lengthy process rife with litigation. Hence, IBC provides that CIRP or Liquidation cannot be held in abeyance for adjudication of these applications. However, these applications tend to put brakes on the process.

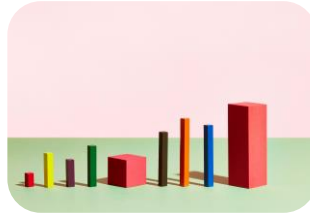
REPORTS TO NCLT



Preliminary Report
75th Day



Asset memorandum
75th Day



Progress Report
(every Quarter)



Receipts & Payments
Account
(every Quarter)



Audited Receipts &
Payments Account
(every FY)



Minutes of consultation
with Stakeholders
As and when



Asset Sale Report
On Sale



Final Report
(prior to dissolution)



APPOINTMENT OF LIQUIDATOR

THE PECULIARITY OF LIQUIDATOR'S APPOINTMENT & STATUS

When an application is made for liquidation by the Resolution Professional (RP), the Code provides for the RP to be appointed as the Liquidator, automatically, subject to him being:

- Not Disqualified
- Providing Consent

Hence, in most cases, the RP on record takes the place of the Liquidator.

BUT WHAT IF THE LENDERS SEEK REPLACEMENT?

DOES THE CODE PROVIDE FOR IT?

No. The Code provides for appointment of RP as the Liquidator, unless he is found ineligible as per the provisions of the Code. However, there have been instances of the Liquidator being replaced on the request of lenders.

NCLT PRECEDENTS:

There is evidence of contradicting rulings across the benches.

While in the case of ORG Informatics (NCLAT) and Tirupati Ceramics Limited (NCLT, Chandigarh), it was ruled that the CoC cannot replace the Liquidator or object to RP's appointment as Liquidator

Interestingly, however, in the case of S Kumars Nationwide Limited (NCLT, Mumbai):

- **Replaced the RP on record with a Liquidator of the CoC's choosing and**
- **While the RP submitted his objections to the same, it ruled that the CoC's decisions calls for no interference.**

DUTIES OF THE LIQUIDATOR



Protect & Preserve



Investigate



Determination of assets & Liabilities



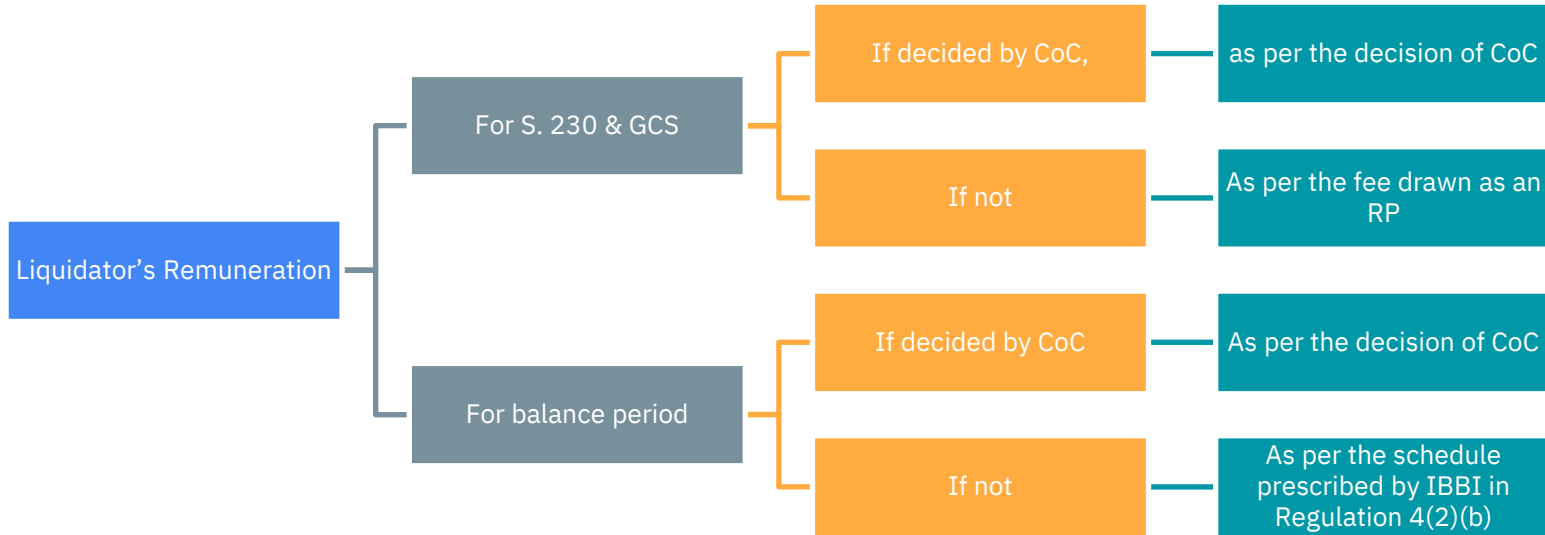
Operational duties



Liquidation Sale & Distribution

- To verify the claims
- Take custody of the assets
- Examine the financial affairs
- Appoint professionals to assist him in the conduct of the process
- Take any action to protect and preserve the assets of the Corporate Debtor
- To carry on business for beneficial liquidation
- To sell the assets, transfer the title to the buyer
- To distribute the sale proceeds as per the law

LIQUIDATOR'S REMUNERATION



The schedule divides the remuneration equally between two events: realization & distribution, where further, half of the fee payable on realization can only be drawn upon distribution.



SCHEDULE AS PER REGULATIONS : LIQUIDATOR'S FEE

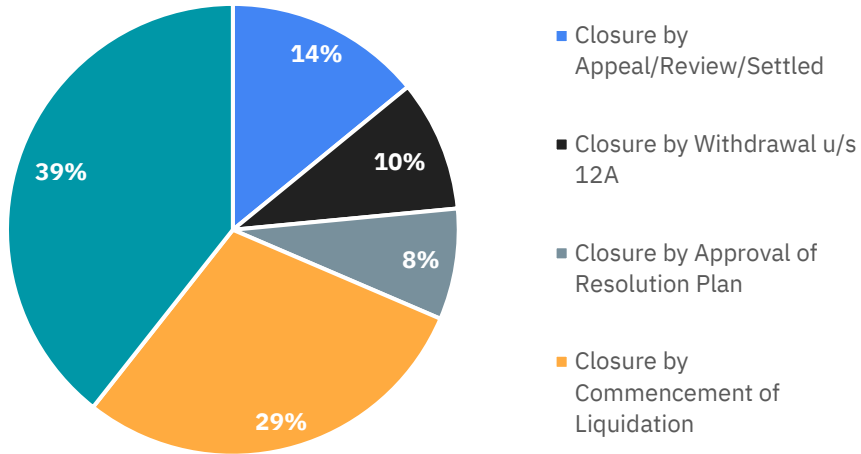
Amount of Realisation /Distribution (In rupees)	Percentage of fee on the amount realised / distributed		
	in the first six months	in the next six months	thereafter
Amount of Realisation (exclusive of liquidation costs)			
On the first 1 crore	5.00	3.75	1.88
On the next 9 crore	3.75	2.80	1.41
On the next 40 crore	2.50	1.88	0.94
On the next 50 crore	1.25	0.94	0.51
On further sums realized	0.25	0.19	0.10
Amount Distributed to Stakeholders			
On the first 1 crore	2.50	1.88	0.94
On the next 9 crore	1.88	1.40	0.71
On the next 40 crore	1.25	0.94	0.47
On the next 50 crore	0.63	0.48	0.25
On further sums distributed	0.13	0.10	0.05



GROUND REALITIES: IN NUMBERS STATISTICS

GROUND REALITIES: IN NUMBERS

Fate of CIRPs:



Quality of asset under liquidation determines the recovery:

7%

Is the liquidation value as a % of claims

74%

Of the companies ending with Liquidation were either in BIFR/non-functional or both on commencement of CIRP

88%

Of the companies ending with Liquidation, the Resolution Plan value was lower than liquidation value.

As per statistics published by IBBI as on 31.03.2021



GROUND REALITIES: IN NUMBERS

88%

Of the cases referred to liquidation are ongoing

43%

Of the cases have been ongoing for more than a year

26%

Of the cases have been ongoing for more than 2 years

3%

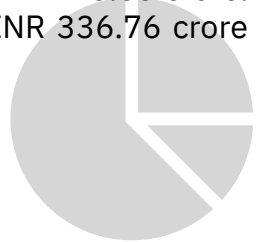
is the recovery that the lenders have gotten so far, out of the 240 liquidation cases that have been closed.

As per statistics published by IBBI as on 31.03.2021

GCS:

Till March 31, 2021, six CDs, namely, M/s. Emmanuel Engineering Private Limited, M/s. K.T.C. Foods Private Limited, M/s. Southern Online Bio Technologies, M/s. Smaat India Private Limited, M/s. Winwind Power Energy Private Limited and M/s. Topworth Pipes & Tubes Private Limited were closed by sale as a going concern under liquidation process.

These six CDs had claims amounting to INR 4325.16 crore, as against the liquidation value of INR 290.03 crore. The liquidators in these cases realized INR 336.76 crore and companies were rescued.



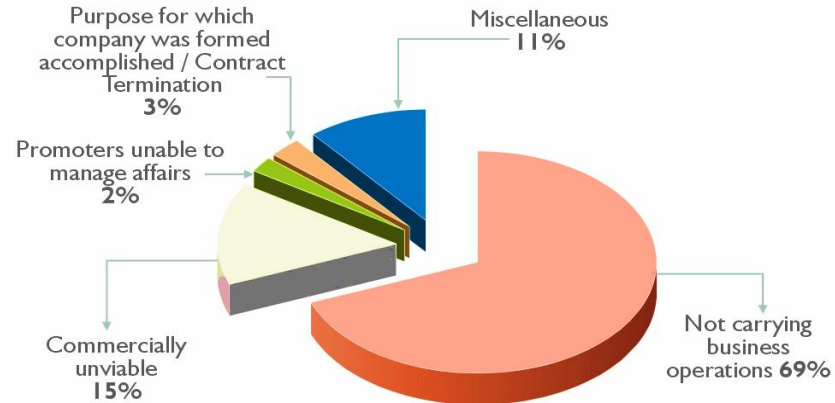
VOLUNTARY LIQUIDATION

Chapter V, Section 59

A company may choose to liquidate itself voluntarily if it has not committed any default. The Application to NCLT to do so, must be accompanied with sufficient declarations and affirmations that the act is not being done to defraud any person.

An important aspect is that the company must be able to pay all its debts in full out of the liquidation proceeds. If there is any haircut envisaged, voluntary liquidation cannot be resorted to.

~900 voluntary liquidations have been initiated so far, out of which 55% are ongoing as on 31.03.2021



As per statistics published by IBBI as on 31.03.2021



SUMMARY

ISSUES & SUCCESS INGREDIENTS

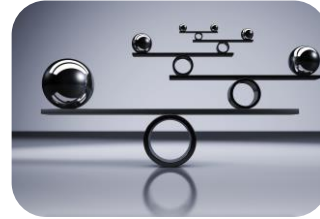
ISSUES SURROUNDING LIQUIDATION



Relinquishment



Remuneration



Avoidance



No ready market



Lack of marketing efforts



Process cost funding



INGREDIENTS FOR A SUCCESSFUL LIQUIDATION UNDER IBC



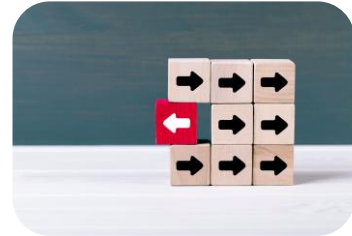
Existence of saleable assets



Relinquishment by secured creditors to the liquidation Estate



Clear title to asset (no litigation)



No avoidance transactions in the company/successful claw back from avoidance applications



Market dynamics



RECAP



CASE STUDY



CASE STUDY

1. Competitive bidding yielded recovery above the reserve price
2. Avoidance transactions & litigation have hampered the process from moving forward

Thank You



Lagrange Point Advisors LLP

3B-116, WeWork Enam Sambhav
C - 20, G Block Rd, G Block BKC, Bandra Kurla Complex,
Mumbai 400051

Email

Ashish.rathi@lpointadvisors.com

Zeenath.Jahaan@lpointadvisors.com

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