

INSOLVENCY AND BANKRUPTCY BOARD OF INDIA
(Disciplinary Committee)

No. IBBI/DC/21/2020
20th April 2020

Order

In the matter of Mr. Koteswara Rao Karuchola, Insolvency Professional (IP) under Regulation 11 of the Insolvency and Bankruptcy Board of India (Insolvency Professionals) Regulations, 2016 read with Section 220 of the Insolvency and Bankruptcy Code, 2016 (Code).

Appearance at Hearing

For Noticee	Mr. Koteswara Rao Karuchola	In person
For Board	Mr. Umesh Kumar Sharma, CGM Mr. Animesh Khandelwal, RA (Law)	

1. Background

- 1.1 This Order disposes of the Show Cause Notice (SCN) dated 22nd October 2019 issued to Mr. Koteswara Rao Karuchola, 2-B, Samrat Residential Complex, #5-9-12, Opp. A.G's Office, Saifabad, Hyderabad (Telangana)- 500004, who is a Professional Member of the Insolvency Professional Agency of Institute of Cost Accountants of India and an Insolvency Professional (IP) registered with the Insolvency and Bankruptcy Board of India (Board) with Registration No. IBBI/IPA-003/IP-N00039/2017-18/10301.
- 1.2 In exercise of its power under section 218 of the Code read with the IBBI (Inspection and Investigation) Regulations, 2017, the Board vide Order dated 17th January 2019 appointed an Inspecting Authority (IA) to conduct an inspection of Mr. Koteswara Rao Karuchola, on having reasonable grounds to believe that the IP had contravened provisions of the Code, Regulations, and directions issued thereunder.
- 1.3 The Board on 22nd October 2019 had issued the SCN to Mr. Koteswara Rao Karuchola, based on findings of an inspection in respect of his role as an interim resolution professional (IRP) and / or resolution professional (RP) in corporate insolvency resolution process (CIRP) of Viceroy Hotels Limited. The SCN alleged contraventions of several provisions of the Code, the IBBI (Insolvency Professionals) Regulations, 2016 (IP Regulations) and the Code of Conduct under regulation 7(2) thereof, the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations 2016 (CIRP Regulations) and IBBI Circular No. IP/003/2018 dated 3rd January 2018. Mr. Koteswara Rao Karuchola, replied to the SCN vide letter dated 21st November 2019.
- 1.4 The Board referred the SCN, response of Mr. Koteswara Rao Karuchola to the SCN and other material available on record to the Disciplinary Committee (DC) for disposal of the SCN in accordance with the Code and Regulations made thereunder. Mr. Koteswara Rao Karuchola availed an opportunity of personal hearing before the DC on 25th February 2020 when he reiterated the submissions made in his written reply and made a few additional submissions. Thereafter, the IP submitted some additional documents vide email dated 4th March 2020 in support of his submissions made during the course of personal hearing.

2. Consideration of SCN

The DC has considered the SCN, the reply to SCN, oral submissions of Mr. Koteswara Rao Karuchola during the course of personal hearing, additional documents, other material available on record and proceeds to dispose of the SCN.

3. Alleged Contraventions, Submissions, Analysis and Findings

A summary of contraventions alleged in the SCN, Mr. Koteswara Rao Karuchola's written and oral submissions thereon and their analysis with findings of the DC are as under:

- 3.1 **Contravention:** Pursuant to regulation 13 (1) of the CIRP Regulations, it is the duty of the IP to verify every claim received by him. Further, the IBBI Circular dated 3rd January 2018 directs that the IP shall not outsource any of his duties and responsibilities under the Code. It has been observed from the minutes of the 1st Committee of Creditors (CoC) meeting that claims received from the creditors have been verified and certified by M/s EzResolve, IPE which shows that the RP has outsourced his responsibility to verify claims of the financial creditors to the IPE.

Submission: RP submits that he did not outsource work of verification of claims to the IPE. He only obtained support services/assistance from the IPE in carrying out the verification and the same was only recommendatory in nature. The RP submits that upon receipt of claims, they were examined by him as to their validity and correctness and thereafter, were sent to the IPE. Further, the RP submits that he has defended the decisions regarding the claims in various Interlocutory Applications (IAs) before the Adjudicating Authority (AA).

Analysis:

One of the core duties of the IP is to receive, collate and verify claims which cannot be outsourced.

Section 18 (1) (b) of the Code provides:

*“The interim resolution professional shall perform the following duties, namely: -
(b) receive and collate all the claims submitted by creditors to him, pursuant to the public announcement made under sections 13 and 15;”*

Regulation 13 (1) of the CIRP Regulations provides:

“13. Verification of claims.

(1) The interim resolution professional or the resolution professional, as the case may be, shall verify every claim, as on the insolvency commencement date, within seven days from the last date of the receipt of the claims, and thereupon maintain a list of creditors containing names of creditors along with the amount claimed by them, the amount of their claims admitted and the security interest, if any, in respect of such claims, and update it.”

Recently, the Apex Court in the matter of *Committee of Creditors of Essar Steel India Limited Through Authorised Signatory Vs. Satish Kumar Gupta & Ors.* (Civil Appeal No. 8766-67 of 2019) also highlighted the role of RP in the revival of the corporate debtor. The Hon'ble Court remarked as under:

"...Thereafter, under Regulation 13, the resolution professional shall verify each claim as on the insolvency commencement date, and thereupon maintain a list of creditors containing the names of creditors along with the amounts claimed by them, the amounts admitted by him, and the security interest, if any, in respect of such claims, and constantly update the aforesaid list – see Regulation 13(1)."

IBBI Circular no. IP/003/2018 dated 3rd January 2018 provides:

“...
...

Sub: Insolvency professional not to outsource his responsibilities

...

4. It is hereby directed that an insolvency resolution professional shall not outsource any of his duties and responsibilities under the Code."

The appointment letter of the IPE dated 30th March 2018 states that, *"You are required to verify claims as per regulations of Insolvency and Bankruptcy Board of India (Insolvency resolution Process for Corporate Persons) (Amendment) Regulations, 2018, as and when received the claims from creditors and verify with Books of the company;"*.

In the present case, it has been observed that the minutes of the 1st meeting of the CoC held on 9th April 2018 provides:

"4. Claims received from Creditors:

...

The claims received have been verified and certified by an IPE from M/s. Ezresolve LLP, who were appointed for claims verification.

6. To Take note and approve the appointment of IPE:

Chairman has briefed the CoC about the appointment of M/s. Ezresolve LLP for verification of claims received from Creditors and verify the claims as per regulations 7, 8, 9, 9A, 10, 12, 13, 14 and 15 of the Insolvency and Bankruptcy Board of India Regulations, 2018 and taking up overall responsibility for claims process. The time period for appointment is up to the date of approval of Resolution Plan by the CoC and the remuneration fee payable is Rs. 3,00,000/- plus GST as per engagement letter dated 30.03.2018.

RESOLVED THAT *pursuant to the provisions of the Insolvency and Bankruptcy Code, 2016, the Committee of Creditors be and hereby unanimously ratified and approved the*

engagement of M/s. EZresolve LLP for a remuneration of Rs. 3,00,000/- plus GST as per engagement letter dated 30.03.2018 for claims received upto 31.05.2018 or till approval of resolution plan by CoC, whichever is later.

7. To take note and vote the CIRP cost incurred by IRP

CMA K.K.Rao informed about the CIRP cost of Rs. 3,11,520/- regarding the paper advertisement and appointment of IPE. Of which, Rs. 1,50,000/- was paid to M/s. Ezresolve LLP, as 50% advance payable on appointment.

...

RESOLVED THAT pursuant to the provisions of the Insolvency and Bankruptcy Code, 2016, the Committee of Creditors be and hereby unanimously ratified and approved the payment of Rs. 1,50,000/- to M/s. Ezresolve LLP..."

Furthermore, an email dated 1st March 2020 was received by the RP from the IPE in response to his email dated 27th February 2020 which clarified, *"During this assignment we have verified claims sent to us for verification under various criteria..."*.

During the personal hearing on 25th February 2020, it was informed by the RP that he had intention to follow the law and the role of the IPE for re-verification of claims has been approved by the CoC. The RP has provided various documents vide email dated 4th March 2020. These include appointment letter of M/s EzResolve LLP dated 30th March 2018, report of the IPE on financial claims dated 3rd April 2018, email dated 1st March 2020 received by the RP from the IPE and specimen letter of M/s Mahal Hotels Private Limited dated 4th July 2019 under which the physical copy of the claim has been returned to them. However, neither the minutes of the CoC meetings nor any document provided by the RP reflect that the IPE was appointment for re-verification of claims.

It is pertinent to note that the appointment letter dated 30th March 2018 clearly states that *"we are appointing you as Claims Verifier for the said company with a professional fee of Rs. 3,00,000 plus applicable GST with terms mentioned in this engagement letter.*

OTHER TERMS

- 1. You are required to verify claims as per regulations of Insolvency and Bankruptcy Board of India (Insolvency resolution Process for Corporate Persons) (Amendment) Regulations, 2018 as and when received the claims from creditors and verify with Books of the company;*
- 2. You shall certify the admissibility or rejection of each claim with reasons after satisfying the regulations and requirements whether proper stamp duty was paid, affidavit enclosed, board resolutions enclosed, authorization letters enclosed etc.,*
- 3. Intimation letters/ mail correspondence shall be prepared if any deficiencies found*

in the claims of creditors or reject the claims with reasons.”

EzResolve, LLP vide its email dated 3rd April 2018 while submitting the report on Financial Claims Submitted up to 3rd April 2018 has intimated the IP that the *“The claims have been verified under regulations of IBC”*.

In the present case, it can be observed from the documents that the IPE has been appointed by the IRP to verify the claims received from creditors. The appointment letter of the IPE, the minutes of the CoC meeting as well as an email dated 1st March 2020 sent by IPE to RP proves the fact that the IPE was appointed for verification of claims, which was the core duty of the RP.

Further, it has also been observed that payment of Rs. 3,00,000/- plus GST has been paid to the IPE for verification of claims which could have been saved, had the verification been done by the RP himself.

IPs, under the provisions of the Code, are required to conduct the entire CIRP and manage the operations of the Corporate Debtor during the CIRP following their appointment. The Code provides for a specific deeming provision that states that IPs are required to exercise all the powers and perform all the duties as are vested or conferred upon them under the provisions of the Code. One of the duties conferred upon IPs include receiving, collating and verifying claims. Such core duties have to be performed by the IPs themselves and they are not permitted to outsource them to third parties.

An IP can take support by appointing accountants, legal or other professionals as may be necessary. However, he cannot outsource duties assigned to himself under the regulations.

Section 5 (13) of the Code defines the term ‘Insolvency Resolution Process Costs’ (IRPC) in the following words -

““insolvency resolution process costs” means—

(a) the amount of any interim finance and the costs incurred in raising such finance;

(b) the fees payable to any person acting as a resolution professional;

(c) any costs incurred by the resolution professional in running the business of the corporate debtor as a going concern;

(d) any costs incurred at the expense of the Government to facilitate the insolvency resolution process; and

(e) any other costs as may be specified by the Board.”

Regulation 31 of IBBI (Insolvency Resolution Process for Corporate Persons) Regulations 2016 provides:

““Insolvency Resolution Process Costs” under Section 5(13)(e) shall mean –

- (a) *amounts due to suppliers of essential goods and services under Regulation 32;*
 - (aa) *fee payable to authorised representative under [sub-regulation (8)] of regulation 16A;*
 - (ab) *Out of pocket expenses of authorised representative for discharge of his functions under [Section 25A];*
- (b) *amounts due to a person whose rights are prejudicially affected on account of the moratorium imposed under section 14(1)(d);*
- (c) *expenses incurred on or by the interim resolution professional to the extent ratified under Regulation 33;*
- (d) *expenses incurred on or by the interim resolution professional fixed under Regulation 34; and*
- (e) *other costs directly relating to the corporate insolvency resolution process and approved by the committee.”*

It is trite to mention that the IRPC is an added financial stress on a Corporate Debtor. Therefore, it becomes crucial to monitor the expenses incurred by the RP to ensure that a Corporate Debtor, who is already entangled in a web of unsustainable liabilities is not further over-burdened with exorbitantly high IRPC. The payment made to the IPE has been included in the IRPC by the RP, thereby creating an additional burden on the Corporate Debtor.

In the present case, the RP failed to produce any document which substantiates that the IPE was engaged for re-verification of claims and thus, the same could not be established. On the other hand, the documents submitted by the RP i.e. the engagement letter issued to the IPE, minutes of 1st CoC meeting and email dated 1st March 2020 received from the IPE clearly provides that the IPE was engaged for the verification of claims.

Findings: Since the RP has outsourced his duty of verification of claims to the IPE as substantiated from various documents, it is found that there is a clear contravention of Section 208 (2) (a) of the Code, Regulation 13 (1) of the CIRP Regulations and Regulation 7 (2) (a), (h) & (i) of the IP Regulations read with clause(s) 2, 3, 10 & 14 of the Code of Conduct as given in the First Schedule of the IP Regulations.

3.2 **Contravention:** Pursuant to regulation 36(2) of the CIRP Regulations, the Information Memorandum (IM) prepared by an IP shall contain list of creditors containing the name of creditors, the amount claimed by them, the amount of their claims admitted and the security interest, if any, in respect of such claims. The RP has failed to include the details of security interest of the admitted claims even though these details were provided to him by the secured financial creditors.

Submission: The RP submits that he had prepared the IM which contained details of securities created in favour of different secured creditors. However, there was an inadvertent omission to suffix the word “interest” along with security. The RP submits that the amended IM depicting “security interest” has been supplied to the stakeholders

vide communication dated 29th December 2018. The RP further submits that the security interest has also been incorporated in the Claims Register and in the list of Financial Creditors sent to the members of the CoC vide email dated 29th January 2019. During the personal hearing on 25th February 2020, RP reiterated his submission. The RP has provided a copy of the IM vide email dated 4th March 2020 and has submitted that the security interest is also included in the IM at Annexure 6.

Analysis: The Code has clearly outlined the duties which must be performed by the RP during the insolvency resolution process. One of the key functions of the RP with respect to conduct of CIRP include preparation of IM. An IM is a very crucial document and provides a holistic view about the operations of the Corporate Debtor.

Section 25 (2) (g) of the Code clearly provides:

“(2) For the purposes of sub-section (1), the resolution professional shall undertake the following actions, namely: -

...

(g) prepare the information memorandum in accordance with section 29;”

Regulation 36 (2) (d) of the CIRP Regulations provides an exhaustive list of details which should form a part of IM which provides as under:

“(2) The information memorandum shall contain the following details of the corporate debtor-

...

(d) a list of creditors containing the names of creditors, the amounts claimed by them, the amount of their claims admitted and the security interest, if any, in respect of such claims;”

Section 3 (31) of the Code provides:

““security interest” means right, title or interest or a claim to property, created in favour of, or provided for a secured creditor by a transaction which secures payment or performance of an obligation and includes mortgage, charge, hypothecation, assignment and encumbrance or any other agreement or arrangement securing payment or performance of any obligation of any person: Provided that security interest shall not include a performance guarantee;”

It has been observed that the IM, obtained by the Board during the course of inspection, does not contain details of security interest even though they were available with the RP. However, from the amended copy of IM shared by the RP, it has been observed that details of the security interest under the heading “security” have been listed.

Further, the copy of the Claims Register maintained by the RP also contain details under the heading “security interest”. In addition to this, the RP has shared details of security interest with the members of the CoC vide emails dated 29th December 2018 & 29th January 2019.

Findings: In the present case, the RP undoubtedly failed to mention the details regarding security interest in the original IM, however, upon perusal of the other documents and emails shared by the RP, it seems that there was no deliberate concealment of information by the RP regarding security interest from the members of CoC. Thus, in the absence of any *mens rea* or *malafide* intention *mens rea*, the RP cannot be strictly held liable for contravening the provisions of the Code.

- 3.3 **Contravention:** Pursuant to Section 43 (1) of the Code, the IP shall apply to the AA for avoidance of preferential transactions made by the corporate debtor. It was observed that the RP filed such an application before the AA. However, the Special Audit Report dated 4th July 2018 provides that the Corporate Debtor had entered into tripartite letters of confirmations/agreements for adjustment of Rs. 63, 20, 43, 151/- (Sixty-three crore twenty lakhs forty-three thousand one hundred and fifty-one only) which were not included in the Section 43 application before the AA as preferential transactions by the RP on the ground that such amount was adjusted against the amounts payable.

Submission: The RP submits that the information regarding the tripartite letters of confirmations/agreements has been brought to the notice of the AA as per para 7 of IA no. 377 of 2018 filed by the RP before the AA (application under Section 43 of the Code). Further, the RP has submitted that the same was also mentioned in the Special Audit Report which was part and parcel of the IA.

Analysis: During CIRP, an IRP/RP possess the highest professional responsibility. His conduct and performance have a substantial bearing on the survival of an ailing entity. He, therefore, is expected to function with a strong sense of urgency and with utmost care and diligence. He is further expected to carefully study and analyse the financial statements of the Corporate Debtor.

Section 43 (1) of the Code provides:

“43. Preferential transactions and relevant time. - (1) Where the liquidator or the resolution professional, as the case may be, is of the opinion that the corporate debtor has at a relevant time given a preference in such transactions and in such manner as laid down in sub-section (2) to any persons as referred to in sub-section (4), he shall apply to the Adjudicating Authority for avoidance of preferential transactions and for, one or more of the orders referred to in section 44.”

Paragraph 7 of IA no. 377 of 2018 filed by the RP is as follows:

“7. It is submitted that from the report it may be seen that NIL transactions have been reported under sections 50 and 66 whereas under section 43 the Auditors made two points giving the details in Annexure-I and Annexure-II. In respect of loans/payable amounts they are set off against the ledger accounts of parties from whom the amounts are receivable. It is seen that against an receivable amount of Rs. 63, 20, 43, 151/- the same has been adjusted against the payable credit balances. This has resulted into

initiation of no action for any recovery since the same has been adjusted against amounts payable.”

As submitted by the RP, paragraph 7 as above-mentioned of the IA no. 377 of 2018 filed before the AA fails to mention about the tripartite letters of confirmations/agreements for adjustment of Rs. 63, 20, 43, 151/- (Sixty-three crore twenty lakhs forty-three thousand one hundred and fifty-one only). However, it has been observed that a copy of the Special Audit Report dated 4th July 2018 which mentions the above required information has been annexed with the IA and, as such, is a part and parcel of the IA.

Further, the IA no. 377 of 2018 was disposed of by the AA vide order dated 25th September 2019 with a direction to the ex-director to pay an amount of Rs. 86,500/- (Eighty-six thousand five hundred only) to the Corporate Debtor whereas no direction was given to the other respondents.

Findings: Undisputedly, the RP did not specifically mention the information regarding tripartite letters of confirmations/agreements in the IA no. 377 of 2018 filed before the AA. However, the Special Audit Report which was annexed with the IA no. 377 of 2018 contained information regarding tripartite letters as mentioned above. In such a scenario, a natural presumption which can be made is that the AA was aware of the information about tripartite letters.

In the absence of any mens rea to hide anything relating to the tripartite agreement specifically when paragraph 7 of IA no. 377 of 2018 mentions that, “*It is seen that against an receivable amount of Rs. 63, 20, 43, 151/- the same has been adjusted against the payable credit balances.*”, the RP cannot be held liable for contravening the provisions of the Code.

4. **Conclusion:**

- 4.1 An IRP or RP is appointed by the AA. He is an officer of the Court and he is duty bound to conduct CIRP with fairness and diligence and must maintain absolute independence in discharge of his statutory duties without any external influences. The entire resolution process of a Corporate Debtor is dependent on the IRP/ RP who is primarily responsible for efficiently and effectively steer it towards resolution. It is due to this reason that the role of the IRP/ RP becomes paramount during CIRP. Further, it is the duty of the IP to follow the guidelines laid down under the Code and the Regulations made thereunder so as to legitimately meet the interests of all stakeholders.
- 4.2 The UNCITRAL Legislative Guide on Insolvency Law as well as the BLRC, the recommendations of which has led to the enactment of the Code, has also laid emphasis on the role of an IP and has identified the role of the IP as central to the entire process as well as one which is of the pillar on which the CIRP exists.
- 4.3 The Code also requires an IP to play a catalytic role in CIRP which requires a right combination of experts acting under the overall supervision of the IP. He is the backbone

of the resolution process under the Code and success thereof hinges on the conduct and competence demonstrated by him. Also, a Corporate Debtor undergoing CIRP is a representation of interests of several stakeholders who pin their hopes on the outcome of CIRP. During CIRP, it is the utmost responsibility of an IP to run the company of Corporate Debtor as a going concern and conduct the entire CIRP in a transparent manner without creating additional insolvency resolution process costs.

4.4 In this matter, the DC observes that

- (a) The RP had outsourced his duty and engaged IPE for verification of claims. He further included the payment made for the same in the IRPC thereby burdening the ailing Corporate Debtor with additional costs.
- (b) The fee of Rs. 3,00,000/- plus GST has been paid to the IPE for verification of claims, which was the primary duty of the RP himself.

4.5 Thus, Mr. Koteswara Rao Karuchola, has displayed a casual attitude towards his duties under the provisions of the Code and Regulations made thereunder. He has, therefore, contravened provisions of:

- a) Sections 208(2)(a) of the Code,
- b) Regulation 13(1) of the CIRP Regulations.
- c) Regulation 7(2)(a), 7(2)(h) and 7(2)(i) of the IP Regulations read with clauses 2, 3, 10 and 14 of the Code of Conduct given in the First Schedule under the said Regulations.

5. Order

5.1 Indeed, an IP is not just another professional. He is dealing with a CD in distress and thus he needs to go beyond the call of duty to address the distress. However, it cannot be disregarded that the insolvency regime in India is in its emerging phase and the profession of Insolvency Professional is also at a nascent stage. This may call for some lenient view in the matter.

5.2 In view of the above, the DC, in exercise of the powers conferred under Section 220 (2) of the Code read with sub-regulations (7) and (8) of Regulation 11 of the IBBI (Insolvency Professionals) Regulations, 2016, issues the following directions:

5.2.1 The DC hereby imposes on Mr. Koteswara Rao Karuchola, a monetary penalty of Rs. 1,00,000/- (Rs. One Lakh only) and directs him to deposit the penalty amount by a crossed demand draft payable in favour of the 'Insolvency and Bankruptcy Board of India'. The Board in turn shall deposit the penalty amount in the Consolidated Fund of India.

5.2.2 Mr. Koteswara Rao Karuchola shall not accept any new assignment as an IP till he deposits the monetary penalty of Rs. 1,00,000/- (Rs. One Lakh only) with the Board and produces evidence to the Board of such deposit.

- 5.3 This Order shall come into force on expiry of 30 days from the date of its issue.
- 5.4 A copy of this order shall be forwarded to the Insolvency Professional Agency of Institute of Cost Accountants of where Mr. Koteswara Rao Karuchola, is enrolled as a member.
- 5.5 A copy of this Order shall also be forwarded to the Registrar of the Principal Bench of the National Company Law Tribunal, New Delhi, for information.
- 5.6 Accordingly, the show cause notice is disposed of.

Sd/-

(Dr. Navrang Saini)
Whole Time Member, IBBI

Dated: 20.04.2020

Place: New Delhi