

Insolvency and Bankruptcy Board of India
7th Floor, Mayur Bhawan, Connaught Place, New Delhi-110001

Facilitation / 001 / 2020

8th May, 2020

To

All Registered Insolvency Professionals
All Registered Insolvency Professional Agencies
All Recognised Insolvency Professional Entities
(By mail to registered email addresses)
Other stakeholders (On website of IBBI).

Dear Madam / Sir,

Subject: Role of Resolution Professional / Liquidator in respect of Avoidance Transactions.

Sections 25 and 37 of the Insolvency and Bankruptcy Code, 2016 (Code) enumerate the duties of a Resolution Professional (RP) and a Liquidator, respectively. These duties include certain actions in respect of avoidance transactions (preferential transactions, undervalued transactions, extortionate transactions, and fraudulent trading). Sections 43, 45, 50 and 66 of the Code mandate the RP and the Liquidator to file applications with the Adjudicating Authority (AA) seeking appropriate reliefs and directions permissible under the Code. Section 47 of the Code, *inter alia*, provides that the AA shall require the Insolvency and Bankruptcy Board of India (Board) to initiate a disciplinary action against the RP or the Liquidator, as the case may be, where he has not reported undervalued transactions to the AA.

2. Regulation 35A of the Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 requires the RP to form an opinion whether the corporate debtor (CD) has been subjected to any avoidance transaction on or before the 75th day of the insolvency commencement date (ICD). Where he is of the opinion that the CD has been subjected to any transactions covered under the aforesaid sections, he shall make a determination, on or before the 115th day of the ICD, under intimation to the Board. Further, he shall apply to the AA for appropriate relief on or before the 135th day of the ICD. These provisions aim to claw back the value lost through avoidance transactions, in sync with objective of maximisation of value of the assets of the CD.

3. The Code, read with Regulations, has demarcated responsibilities of an insolvency professional in corporate insolvency resolution process (CIRP) and liquidation process. To enable the insolvency professional and the committee of creditors (CoC) to have a complete and clear understanding of their roles and responsibilities in a CIRP, the Board, on 1st March, 2019, issued an indicative charter of their responsibilities, prepared in consultation with the three Insolvency Professional Agencies. Since the CoC does not exist in the liquidation process, the Liquidator has independent and exclusive duties. The emerging jurisprudence is bringing further clarity about their roles in corporate insolvency proceedings.

4. The AA has disposed of a few applications relating avoidance transactions. Some matters have travelled up to the Supreme Court. The observations in the following two matters provide guidance to the insolvency professional and stakeholders as well.:

(i) Mr. Ram Ratan Kanoongo Applicant Vs. Mr. Sunil Kathuria & Others. [MA 436/2018 in CP No.172/IBC/NCLT/MB/MAH/2017]

Since certain transactions appeared to be fraudulent or preferential in nature during the CIRP of Saana Syntex Pvt. Ltd. (CD), the RP filed an application Under Section 19, 45 & 66 of the Insolvency and Bankruptcy Code, 2016. . The CD could not be revived and, therefore, liquidation commenced. The AA observed that if there is a syphoning off funds of the CD, it is important that the same be brought back for the completion of liquidation proceedings. It held: *“Section 43 & 45 start with the phrase “Where the liquidator or the RP……”, hence it can be understood that the avoidance or preferential or undervalued transactions can be handled even at the stage of Liquidation.”*

(ii) Anuj Jain Interim Resolution Professional for Jaypee Infratech Limited Vs. Axis Bank Limited Etc. Etc. [Civil Appeal Nos. 8512-8527/2019]

In this landmark judgement, the Supreme Court clarified the duties and responsibilities of the RP in respect of avoidance transactions. It held that the RP shall-

- (i) sift through all transactions relating to the property/interest of the CD backwards from the ICD and up to the preceding two years;
- (ii) identify persons involved in the transactions and put them in two categories: (a) related party under section 5(24), and (b) remaining persons;
- (iii) identify which of the said transactions of preceding two years, the beneficiary is a related party of the CD and in which the beneficiary is not a related party. The sub-set relating to unrelated parties shall be trimmed to include only the transactions preceding one year from the ICD;
- (iv) examine every transaction in each of these sub-sets to find out whether (a) the transaction is of transfer of property of the CD or its interest in it; and (b) beneficiary involved in the transaction stands in the capacity of creditor/surety/guarantor;
- (v) scrutinise the shortlisted transactions to find, if the transfer is for or on account of antecedent financial debt/operational debt/other liability of the CD;
- (vi) examine the scanned and scrutinised transactions to find, if the transfer has the effect of putting such creditor/surety/guarantor in beneficial position, than it would have been in the event of distribution of assets under section 53. If answer is in the affirmative, the transaction shall be deemed to be of preferential, provided it does not fall within the exclusion under section 43(3); and then
- (vii) apply to the AA for necessary orders, after carrying out the aforesaid volumetric and gravimetric analysis of the transactions.

The Supreme Court observed that the parameters and the requisite enquiries as also the consequences in relation to different types of avoidance transactions are different. It clarified that once transactions are held as preferential; it is not necessary to examine whether these are undervalued and/or fraudulent. In preferential transaction, the question of intent is not involved and by virtue of legal fiction, upon existence of the given ingredients, a transaction is deemed to be of giving preference at a relevant time, while undervalued transaction requires different enquiry under sections 45 and 46 where the AA is required to examine the intent, if such transactions were to defraud the creditors.

5. This communication is issued for the sole purpose of educating the IPs and other stakeholders of corporate insolvency resolution and liquidation processes. A stakeholder must refer to the Code and the Rules/Regulations and relevant case laws or seek professional advice if he intends to take any action or decision in any matter under the Code.

Yours faithfully,

- Sd –

(Pawan K Kumar)
Executive Director