

Personal Guarantors under IBC

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About Us

**Vinod Kothari & Co., based in
Kolkata, Mumbai and Delhi**

**We are a team of consultants,
advisors & qualified
professionals having over 25
years of practice.**

AGENDA

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Understanding Terminology

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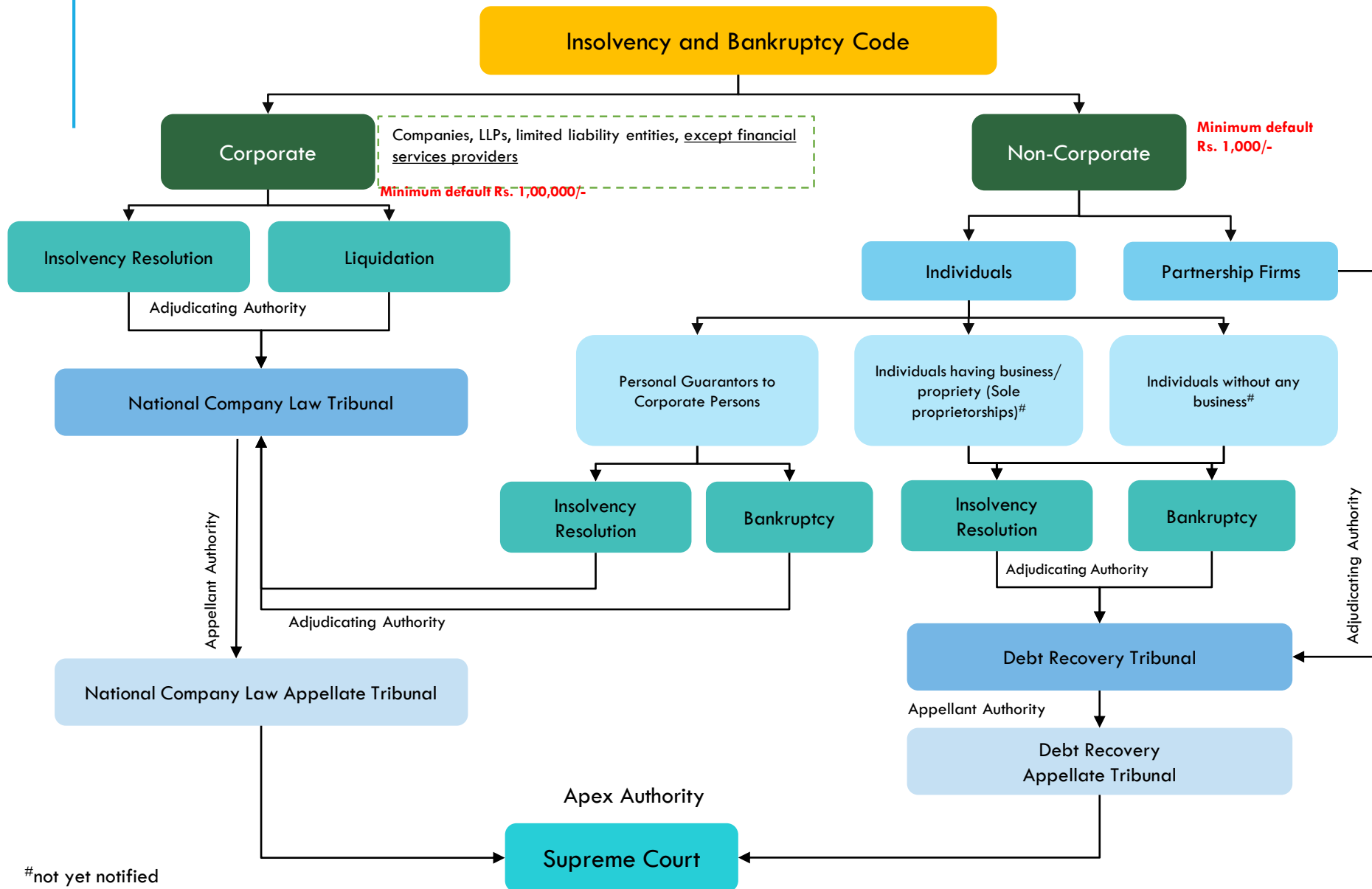
Some Nagging Questions & Way Forward



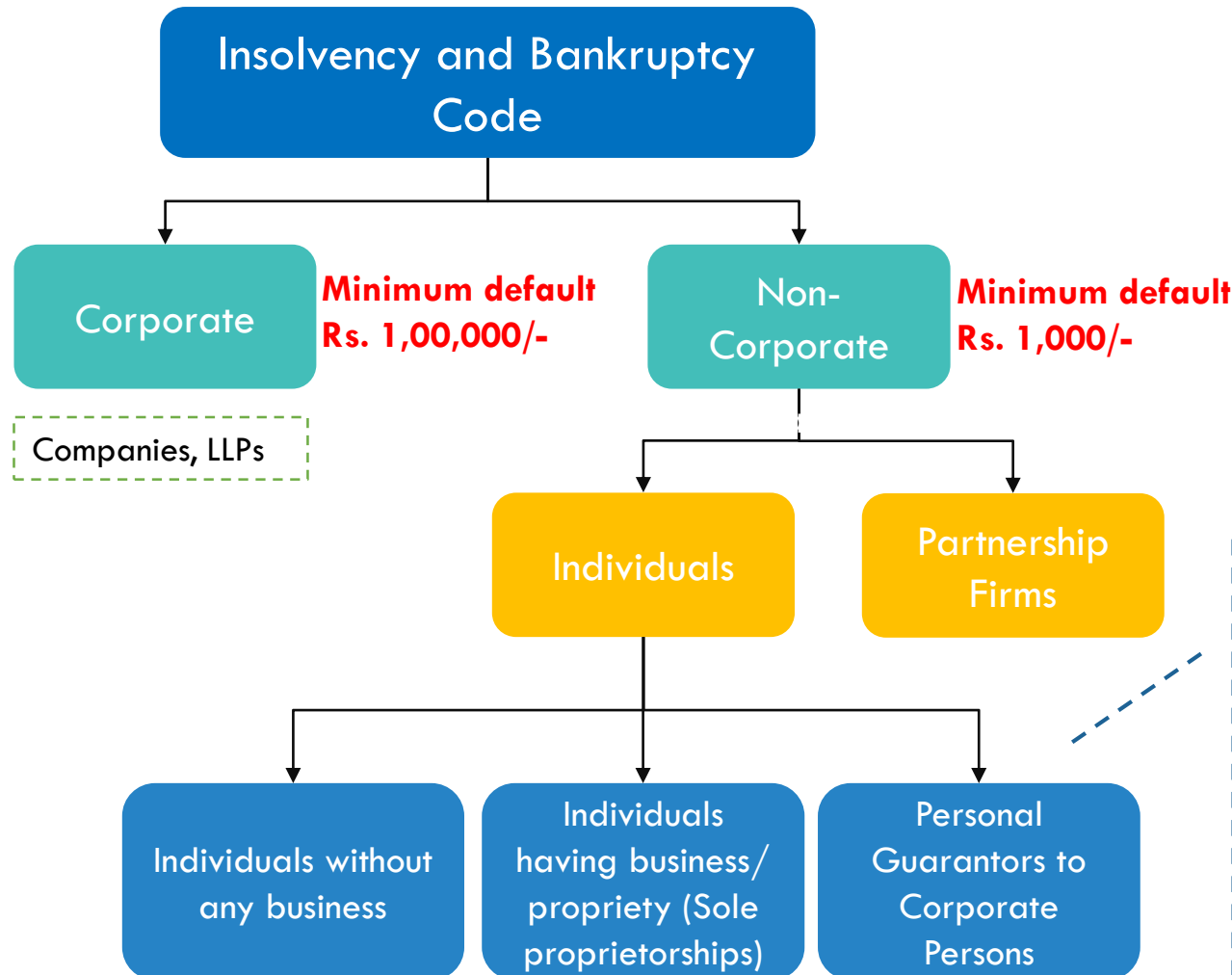


INTRODUCTION

Framework of IBC- Adjudicating Authority



Framework for Personal Insolvency

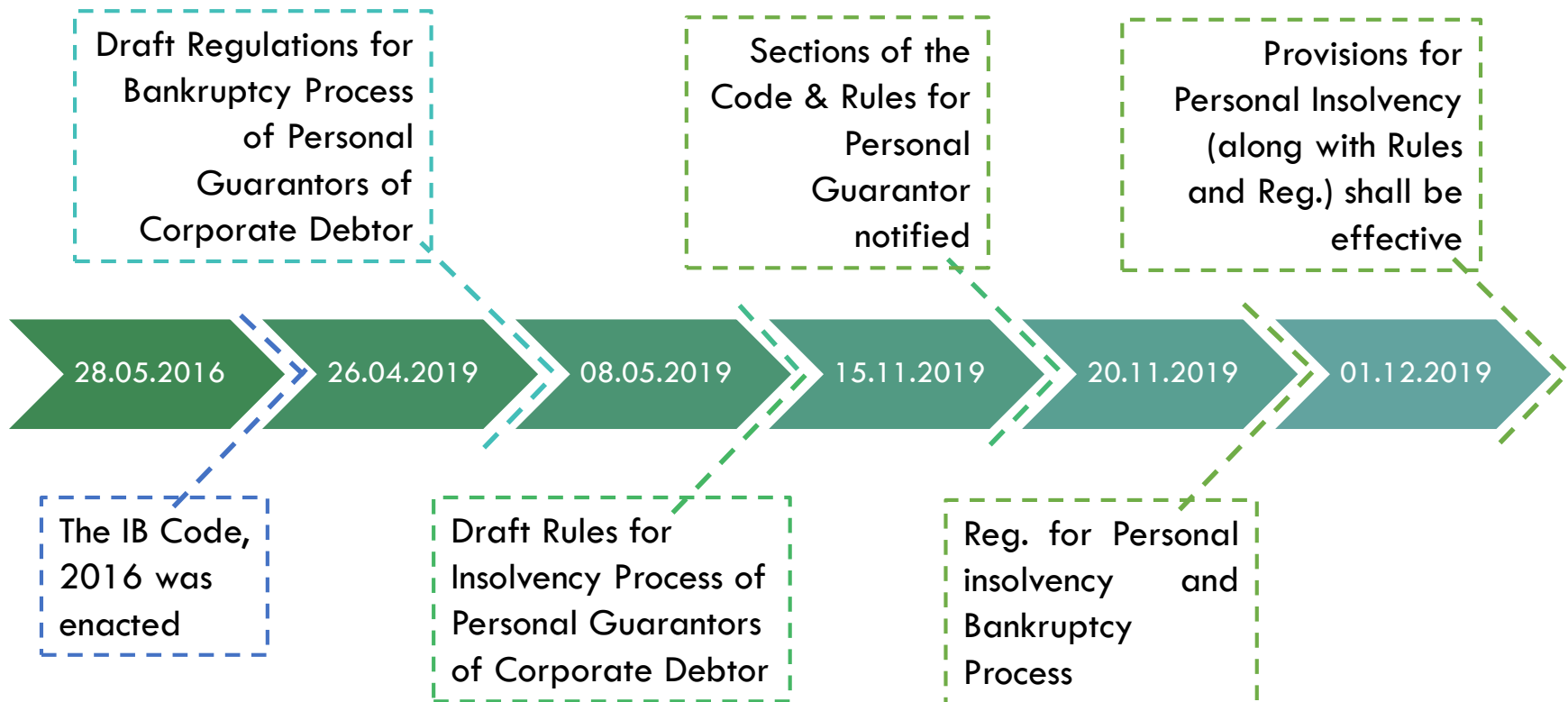


It has been proposed to have separate set of rules and regulations for three classes of non-corporate persons & a phased implementation.

Provisions relating to personal guarantors have been notified.

Framework for Personal Insolvency

Sections 94 to 187 of the Code, read with sec. 60 (1) and (2), w.r.t. insolvency and bankruptcy of personal insolvency of corporate guarantors have been notified vide notification dated 15.11.2019, along with rules and regulations for insolvency and bankruptcy process of Personal Guarantors.



Personal Insolvency v/s Corporate Insolvency

Point of difference	Personal Insolvency	Corporate Insolvency
Distinction between creditors	No classification w.r.t. type of creditor i.e. operational or financial	Three classes of creditors – financial, operational, other
Withdrawal of Application	Yes Requires 90% consent of creditors	Yes Requires 90% consent of CoC
CoC	No concept of CoC- a general list of creditors is formed	Constitution of CoC mandatory- shall comprise of financial creditors only.
Meeting of Creditors	Not Mandatory- shall be conducted if deemed necessary by the RP – subject to conditions	Mandatory to conduct the CoC
Moratorium	Yes	Yes
Interim Moratorium	Yes	No
Approval of Plan	Requires 75% assent of creditors present and voting	Requires 66% assent of CoC
Rejection of plan	Application for bankruptcy may be filed	Leads to compulsory liquidation
Role of the IP	Pre-scrutiny of the insolvency application and repayment plan by the RP	RP does not come into picture until admission

Personal Insolvency Resolution v/s Bankruptcy

Point of difference	Insolvency Resolution	Bankruptcy
Necessary condition	Default by the debtor.	Rejection of application for insolvency resolution; or rejection of repayment plan; or premature termination of the repayment plan.
Eligible applicants	Debtor/creditor.	Debtor/creditor; in some circumstances, only creditor – section 100(4).
Dominant Aspect	Preparation of Repayment plan	Administration, liquidation and distribution of estate
Interim-moratorium	Yes	Yes
Role of insolvency professional	Resolution Professional	Bankruptcy Trustee
Moratorium on creditors	Yes, includes restrictions on creditors too.	Assets of the bankrupt vest in the hands of trustee. Secured creditors may sell
Vesting of estate	No	Yes
Committee of Creditors	Not mandatory	Established u/s 134
Period of Discharge	No default period specified; on implementation of the repayment plan.	Earlier of 1 year or completion of administration is approved by the committee of creditors.
Phases	Insolvency → Resolution → Failure → Bankruptcy/Liquidation → Dissolution	Insolvency → Repayment Plan → Failure → Bankruptcy → Discharge

INSOLVENCY VERSUS BANKRUPTCY

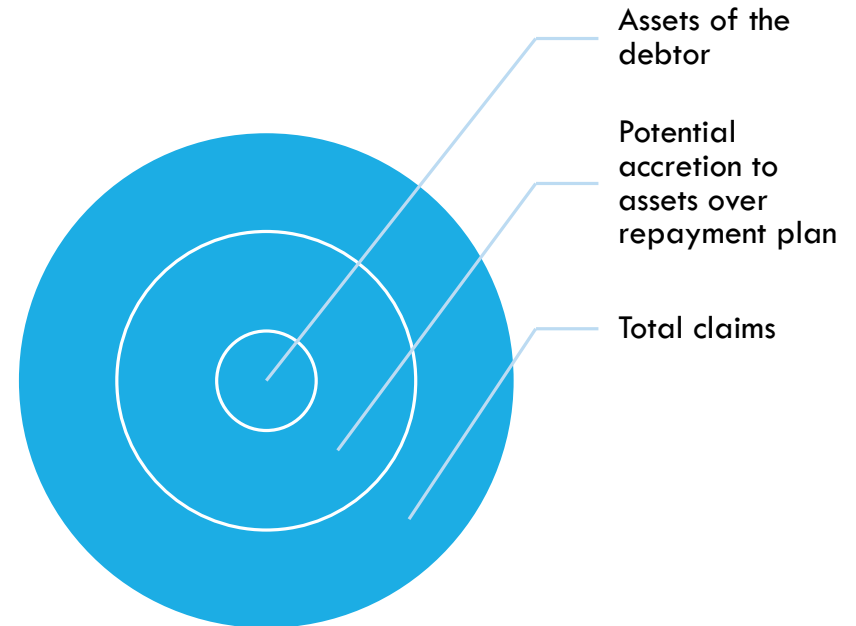
Repayment plan under insolvency is in the nature of a compromise – adherence to repayment plan means the debtor comes out as a non-defaulter

- No question of impairment of credit
- Debtor maintains assets, credit, social reputation, right to borrow

However, why will creditors prefer insolvency over bankruptcy?

- Assets available for immediate liquidation in insolvency are such assets as debtor is willing to liquidate immediately
- However, there may be a repayment plan to pay over time
- Possibility of family assets too

The bargain between insolvency and bankruptcy is the same as between CDR vs OTS



CORPORATE BANKRUPTCY VS. PERSONAL BANKRUPTCY(1 /2)

Point of difference	Liquidation	Bankruptcy
Manner of initiation	Automatically triggered u/s 33	Creditor/debtor become entitled to file for bankruptcy Section 100 – Rejection of insolvency resolution application by AA. Section 115 – Rejection of repayment plan by AA. Section 118 – Premature closing of repayment plan Note undischarged insolvent u/s 92 (2) may also be adjudged as bankrupt
Reversibility/modification or recall	No specific provision – right to appeal against AA’s order – section 61.	Possible – by AA, on application or suo-motu – section 142 (either erroneous initiation or full repayment).
Interim-moratorium	No	Yes – sec. 124 (1)- on application – lasts till bankruptcy order is passed
Moratorium	Sec. 33 - On liquidation order being passed	Sec. 128 - On bankruptcy order being passed
Role of Insolvency Professional	As liquidator	As bankruptcy trustee
Estate of debtor	Liquidation estate held by liquidator as fiduciary for benefit of all creditors – section 36	Estate of the bankrupt vests in the bankruptcy trustee – section 154
Manner of vesting of estate	No conveyance, assignment – the estate is constructive	Section 154(2) provides that there is no need for conveyance, assignment or transfer for vesting of property in the trustee.

PERSONAL BANKRUPTCY V/S CORPORATE BANKRUPTCY (2/2)

Point of difference	Liquidation	Bankruptcy
Involvement of creditors	Liquidator has the constitute Stakeholder's Consultation Committee (including creditors). No provision for a committee of creditors.	Considerable - meeting of creditors is summoned, a committee of creditors is appointed for approval of the report on administration of the estate; the bankruptcy requires approval of the committee for several acts (section 153), and the committee of creditors decides on the release of the bankruptcy trustee.
Priority of pay-out from estate	Sec. 53 – financial debts take priority over operational debts	Sec. 178 – distinction b/w financial creditor and operational creditor does not exist [even if the individual is carrying on business]
Final Stage	Dissolution – the entity loses its existence.	Discharge – releases the bankrupt from all bankruptcy debts.

ROLE OF THE AA

Section	Particulars (in brief)
94	Application by debtor for initiation of insolvency process
95	Application by creditor for initiation of insolvency process
97	Direction to the Board w.r.t. appointment of Resolution Professional, and appointment thereof
98	
100	Admission of application for initiation of insolvency process
102	Public notice to creditors
106	RP to submit report on repayment plan to AA
112	RP to submit report on meeting of creditors on repayment plan
114	Order of AA on repayment plan
116	AA may pass directions w.r.t. implementation of Repayment Plan, if such application is filed by RP
117	Report of completion of repayment plan to AA
118	Order of AA in case of premature termination of repayment plan
119	Discharge order by AA w.r.t. insolvency process

ROLE OF THE AA

Section	Particulars (in brief)
122	Application for bankruptcy by debtor
123	Application for bankruptcy by creditor
126	AA to pass bankruptcy order and appoint bankruptcy trustee in accordance with section 125
130	To send notice to creditors
138	Bankruptcy trustee applies to AA for discharge order, and AA passes discharge order
141	Bankrupt not to maintain any legal action or proceedings in relation to the bankruptcy debts without previous sanction of AA
142	Modification/recall of bankruptcy order
145	Appointment of bankruptcy trustee on replacement
146	Appointment of bankruptcy trustee on resignation

ROLE OF THE AA

Section	Particulars (in brief)
147	Appointment of bankruptcy trustee on vacancy in office
159	AA's approval required to give delayed notice by bankruptcy trustee in respect of after-acquired property
163	Challenges against disclaimed property
164	Application to AA against undervalued transactions
165	Application to AA against preference transactions
167	Application to AA against extortionate credit transactions
176	Application by interested persons to postpone the date of final dividend
177	Order against refusal of bankruptcy trustee to pay dividend
178(3)	Order giving a creditor an advantage in distribution of assets where the creditor has given any indemnity to may payments in respect of assets of the bankrupt

derivation).

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UNDERSTANDING TERMINOLOGY

WHO IS A PERSONAL GUARANTOR?

Elements of the definition:

- Must be a debtor – sec 79 (12) provides an inclusive definition, to include judgement debtor. Meaning should come from “debt” in sec 3 (11)
- Who is a personal guarantor
 - Sec 5 (22) – covers only individuals who are sureties to a contract of guarantee to a corporate debtor.
 - Principal debtor must be a corporate debtor; guarantor must be individual
- Guarantee has been invoked
 - Invocation of guarantee must be in terms of the guarantee deed; provisions of sec 126-147 of the Contracts Act
 - Usually guarantee is invoked by notice
- Remains unpaid in full or part

Does it make a difference if the personal guarantor gave securities as well?

- no

What if there are joint sureties:

- Depending on construction of the guarantee, but proceedings may be filed against one or all – based on joint and several liability

Rule 3 (e) of Personal Guarantor Rules: “debtor who is a personal guarantor to a corporate debtor and in respect of whom guarantee has been invoked by the creditor and remains unpaid in full or part”

A “contract of guarantee ” is a contract to perform the promise, or discharge the liability, of a third person in case of his default. The person who gives the guarantee is called the “ surety”; the person in respect of whose default the guarantee is given is called the “ principal debtor ”, and the person to whom the guarantee is given is called the “ creditor ”. A guarantee may be either oral or written. – Sec 126 of Contracts Act

WHO IS A PERSONAL GUARANTOR?

Know More (some landmark judgements)

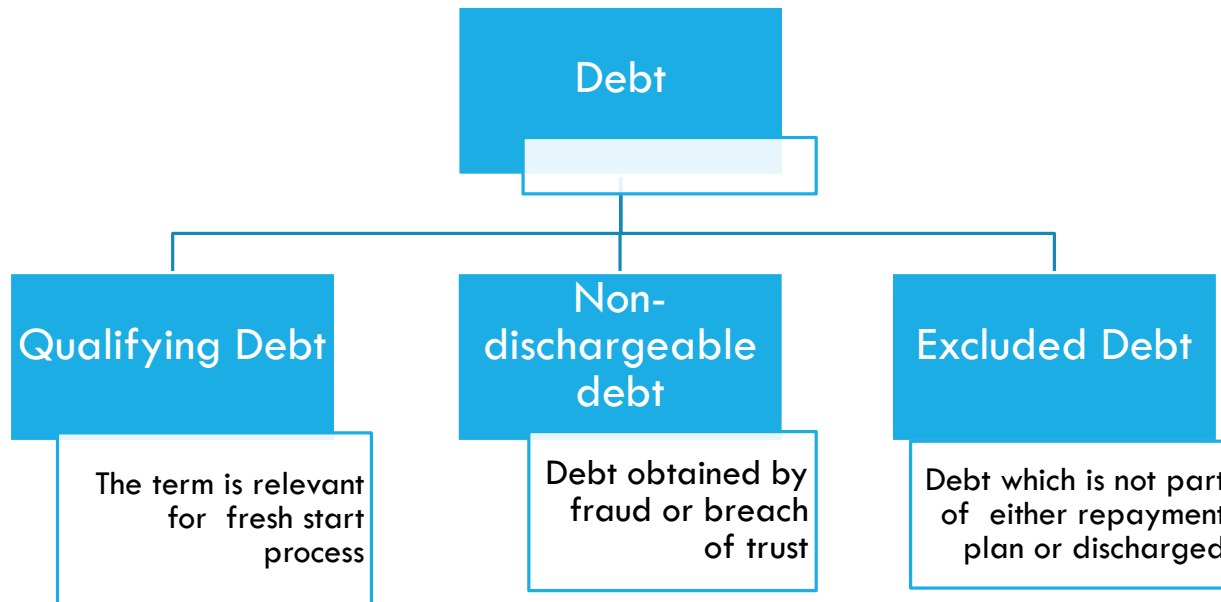
Can guarantee be invoked before claiming the same from the Corporate Person?

The Hon'ble NCLAT in the matter of **Dr. Vishnu Kumar Agarwal v. M/s. Piramal Enterprises Ltd. Company Appeal (AT) (Insolvency) No. 346 of 2018**, held that guarantee can be invoked before claiming the same from the principal debtor.

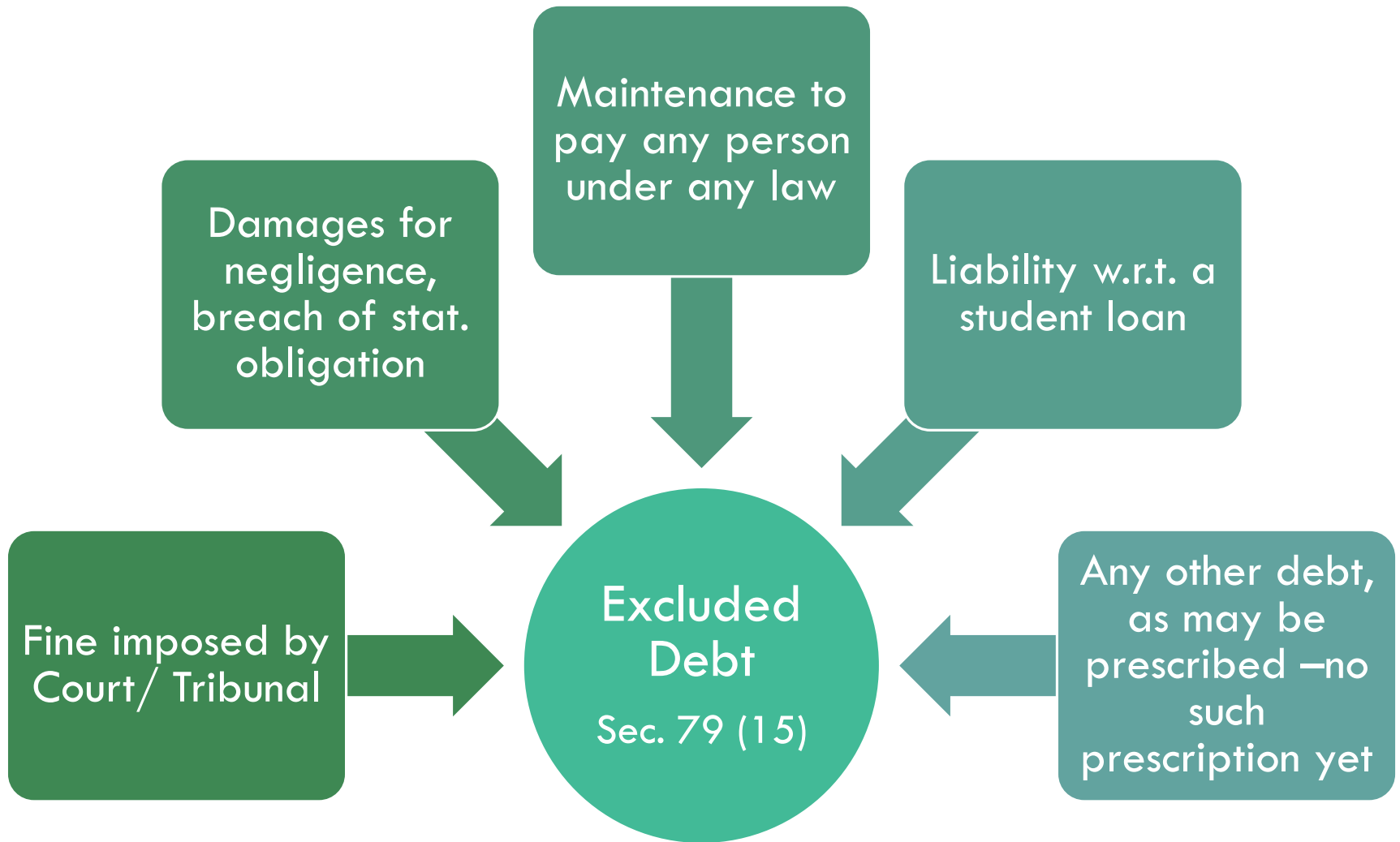
Other landmark judgements in this regard-

- Mukesh Hans & Anr. v. Smt. Uma Bhasin & Ors, Delhi High Court
- Ferro Alloys Corporation Limited v Rural Electrification Corporation Limited (Comp. App (AT) (Ins) No. 92 of 2017)- Hon'ble NCLAT

DEBT



EXCLUDED DEBT



EXCLUDED ASSETS

Sec 79 (14) read with Rule 5



Unencumbered tools, vehicles and other equipments, necessary for employment, business or vocation.



Unencumbered furniture, equipment, necessary for basic domestic needs



Unencumbered personal ornaments, that cannot be parted with in accordance with religious usage

Upto Rs.
1,00,000/-



Unencumbered life insurance policy/
pension plan

Upto Rs. 20,00,000/- in Urban area;
Rs. 10,00,000/- in rural area



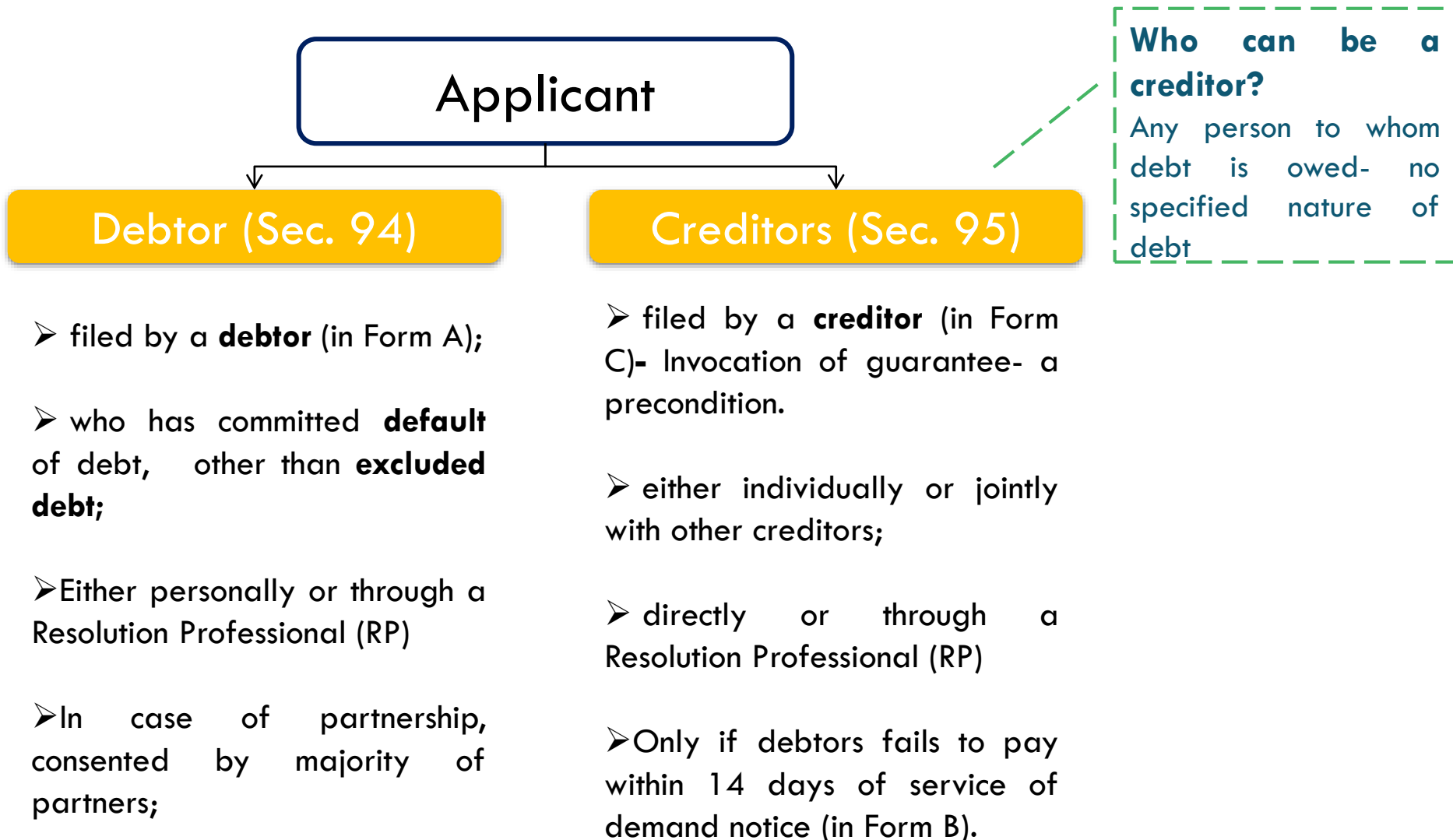
Unencumbered single dwelling unit



INSOLVENCY RESOLUTION PROCESS

-As per Part III of the Code- an “earned start” for the debtor

APPLICATION FOR INITIATION



APPLICATION FOR INITIATION

Debtor's ineligibility to file application

Debtor shall not be entitled to make an application if he is-

- (a) an undischarged bankrupt;
- (b) undergoing a fresh start process;
- (c) undergoing an insolvency resolution process; or
- (d) undergoing a bankruptcy process.

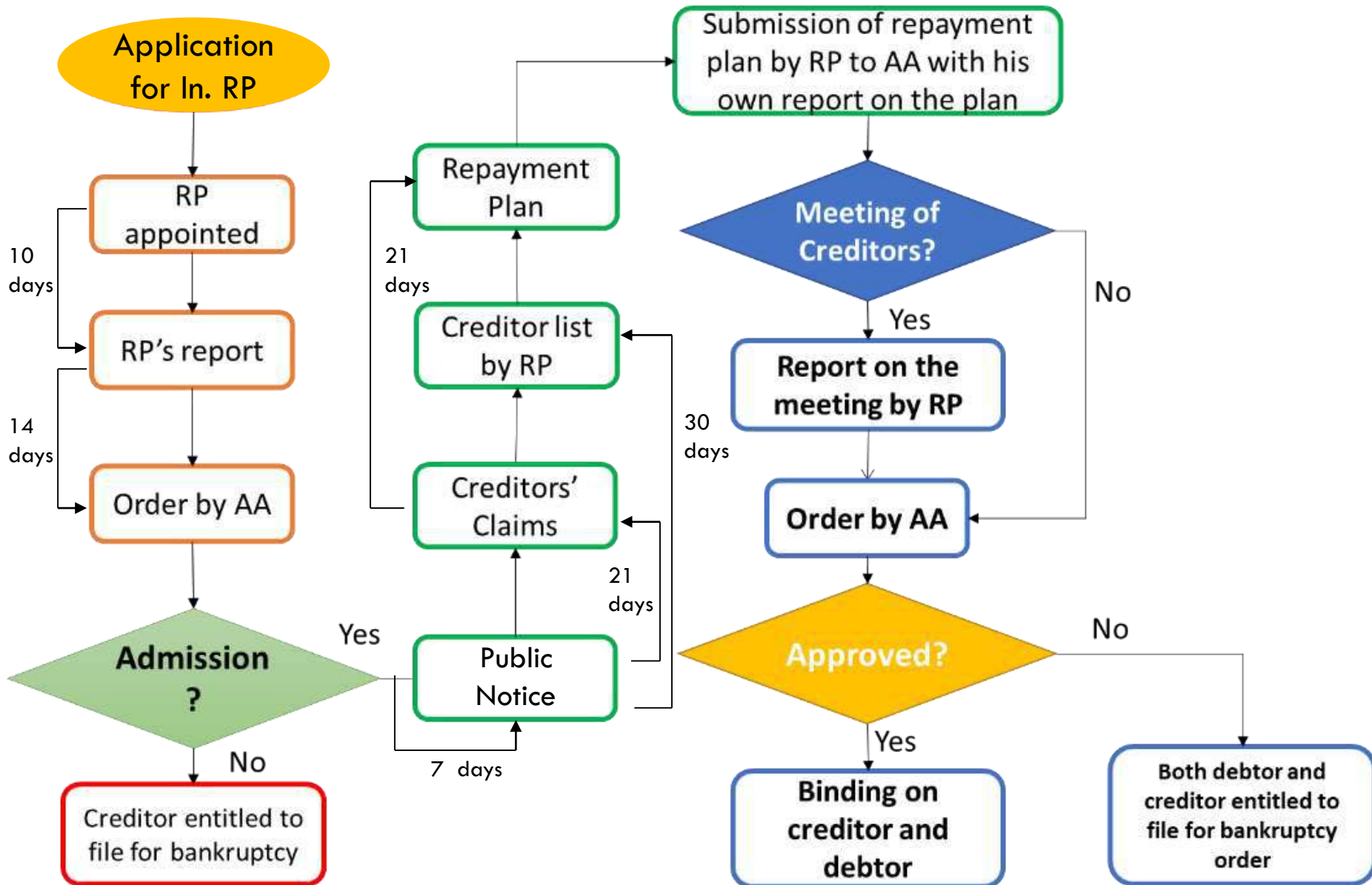
DEMAND NOTICE

Rule 7 (1) -Prior to filing of application, the creditor must serve a demand notice in Form B.

Application can be filed only if the debt stated in the demand notice is not repaid by the debtor within 10 days of service of the demand notice.

Unlike demand notice in Form 3 of the IBBI (Application to Adjudicating Authority) Rules, 2016, the demand notice in case of personal insolvency **does not give a chance of disputing the notice.**

THE PROCESS



MORATORIUM

Stages of Moratorium

Interim (Sec. 96)

- From date of filing of application till its admission
 - No time limit specified
- Against pending legal action w.r.t. **ANY** debt;
- Initiation of proceedings against **ANY** debt
- Applicable to debtor as well

Final (Sec. 100)

- From admission of Application till 180 days or approval of Repayment Plan, whichever is earlier.
- Against pending legal action w.r.t. debt;
- Initiation of proceedings against debt
- The debtor shall not transfer, alienate, encumber, any of his assets or legal rights

CREDITORS & THEIR RIGHTS (1 / 2)

Preparation of List of Creditors (Sec. 104)

The resolution professional shall –

- (a) make the list of creditors available for inspection by the persons who submitted claims with proof;
- (b) serve a copy of the list of creditors to the guarantor;
- (c) make available the list of creditors on the website, if any, of the guarantor;
- (d) present the list of creditors at the meeting of creditors; and
- (e) file a certified copy of the list of creditors with the Adjudicating Authority along with the repayment plan.

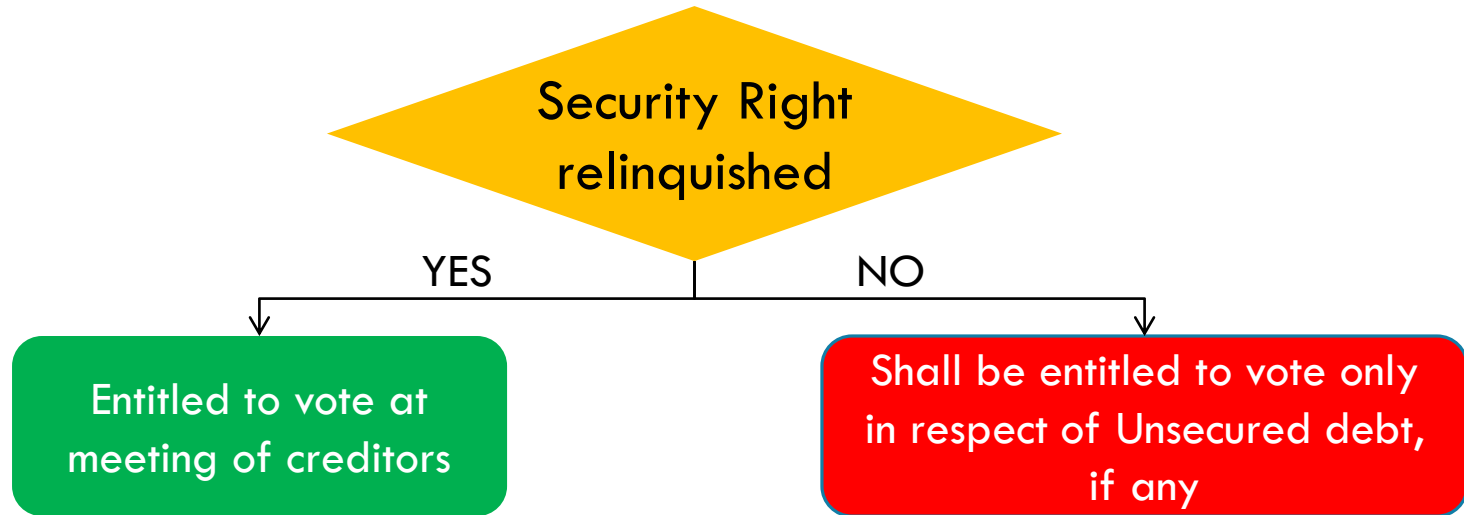
CREDITORS & THEIR RIGHTS (2/2)

General meeting of Creditors

(Sec 107-109 read with Reg. 11-16)

- **No COC – no classification into financial/operational**
 - Classification of creditors of the corporate debtor?
- RP to call general meeting of creditors, if in his opinion, the same is necessary for consideration of repayment plan **OR** on requisition by 33% of list of creditors in value
- **Voting Rights-**
 - Present and voting rule
 - For approval of repayment plan – more than 75% majority
 - For other matters – more than 50% of voting share of those who voted
 - Based on value of the claim as a percentage of **the total claim**;
 - No voting right shall be granted pursuant to an unliquidated debt;
 - Associates of the debtor are not entitled to vote, even if they form part of the list of creditors.
- **Quorum**
 - Creditors representing 33% of voting share
 - Can be modified

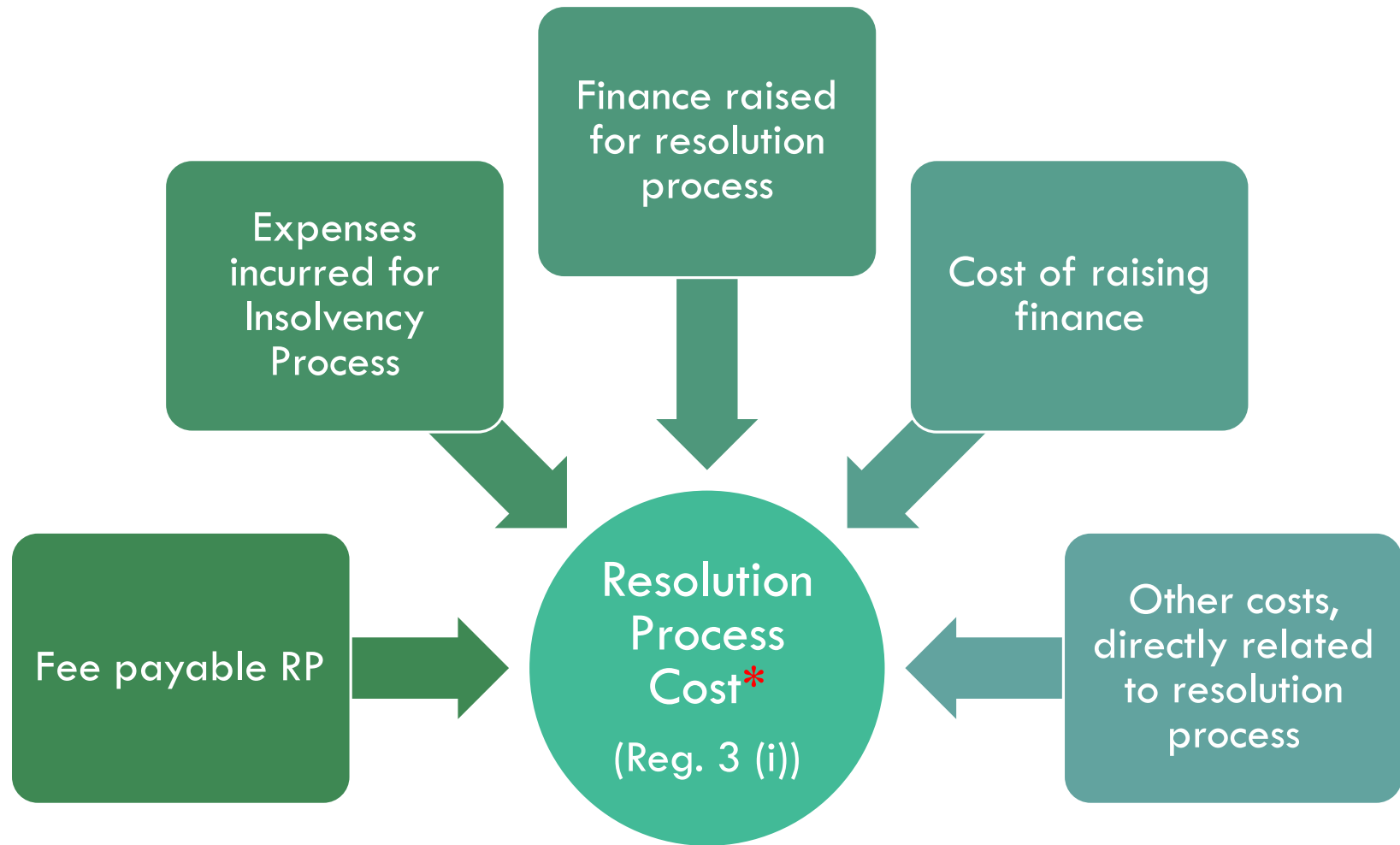
RIGHTS OF A SECURED CREDITOR



NOTE:

"If the Secured creditor does not relinquish his right & the Repayment Plan affects his right to enforce security, his concurrence shall be obtained"

RESOLUTION PROCESS COST



**to the extent approved/ ratified by the creditors*



REPAYMENT PLAN

WHAT IS A REPAYMENT PLAN?

Sec 105 read with Chapter V of Personal Guarantor Regulations

Similar to a “Resolution Plan” in case of corporate insolvency, “Repayment Plan” can be said to be the key to resolution in case of non-corporate insolvency.

It is plan/ proposal, containing terms as per which the debtor will pay his debts to the creditors, and also provides for the manner in which the affairs of the debtors will be carried on.

FEATURES OF A REPAYMENT PLAN

Shall be prepared by the debtor, in consultation with the RP

Contains proposal for restructuring of debtor's debts towards the creditors

Features of a Repayment Plan

May authorise the RP to carry the business/trade of the debtor, on behalf of his name.

Must contain justification for preparation of the plan; and
Reasons why the creditors may agree to it.

CONTENTS OF A REPAYMENT PLAN

Ref. Regulation 17

Term of repayment plan and its implementation schedule

Source of funds that will be used to pay resolution cost

Minimum budget for duration of resolution plan

Finance required for implementation of plan

Variation of onerous terms of a contract or transaction involving guarantor

Details of exclude assets and excluded debts of the guarantor

Terms and conditions for discharge of guarantor

APPROVAL OF THE PLAN (1 / 2)

Approval of Repayment Plan by creditors- Sec 111

Section 111 states that:

“The repayment plan or any modification to the repayment plan shall be approved by a majority of more than three-fourth in value of the creditors present in person or by proxy and voting on the resolution in a meeting of the creditors.”

Illustration:

Mr. A is under going insolvency process, wherein Mr. B is appointed as the RP. On the basis of public announcement, claims have been received from 10 creditors of total value Rs. 5,00,000/-

Repayment Plan is placed before the creditors for approval. Only 6 creditors having dues of Rs. 3,50,000/- are present and entitled to vote in the meeting.

APPROVAL OF THE PLAN (3/3)

Scenario 1:

3 Creditors having dues of Rs. 2,75,000/- approve the Plan

Votes in Favour-

% of total claims- 55%

% of present & voting-
78.57%

Outcome-

Plan approved

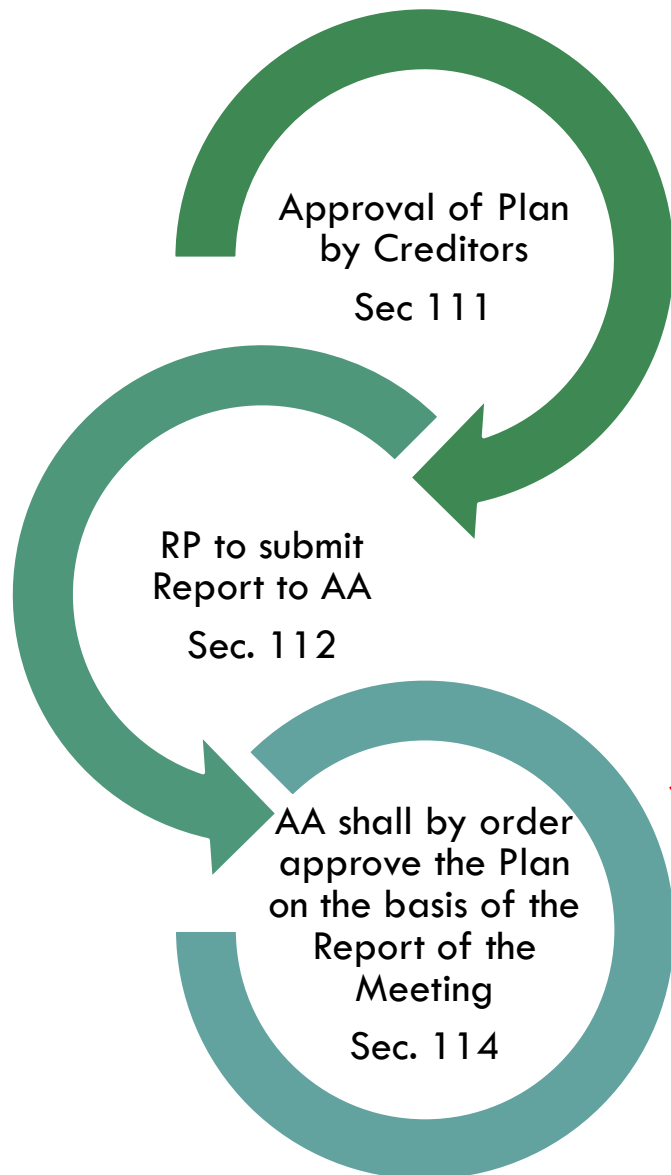
Scenario 2:

Of the 3 creditors who approved the plan, 2 were present in proxy, not in person.

Outcome-

Plan is still considered
approved

ORDER OF THE AA



Repayment plan is to be filed by the RP with AA on or before 120 days from the commencement date.

Where no meeting of CoC is summoned by RP

AA shall by order approve the Plan on the basis of RP's report on Repayment Plan

EFFECT OF APPROVAL OF PLAN

Ref. section 116

Become effective as
if proposed by
debtor

Be binding on the
creditors mentioned
in the Plan

Once approved,
the Plan shall:

RP shall supervise
the implementation
of the Plan

AA may issue
specific direction
w.r.t. implementation

COMPLETION OF REPAYMENT PLAN

Full Completion of Plan (sec. 117)

RP shall notify all persons bound by the Plan, that the Plan has been fully implemented

Report w.r.t. All receipts & payments pursuant to implementation of Plan shall be sent to all persons bound by the Plan

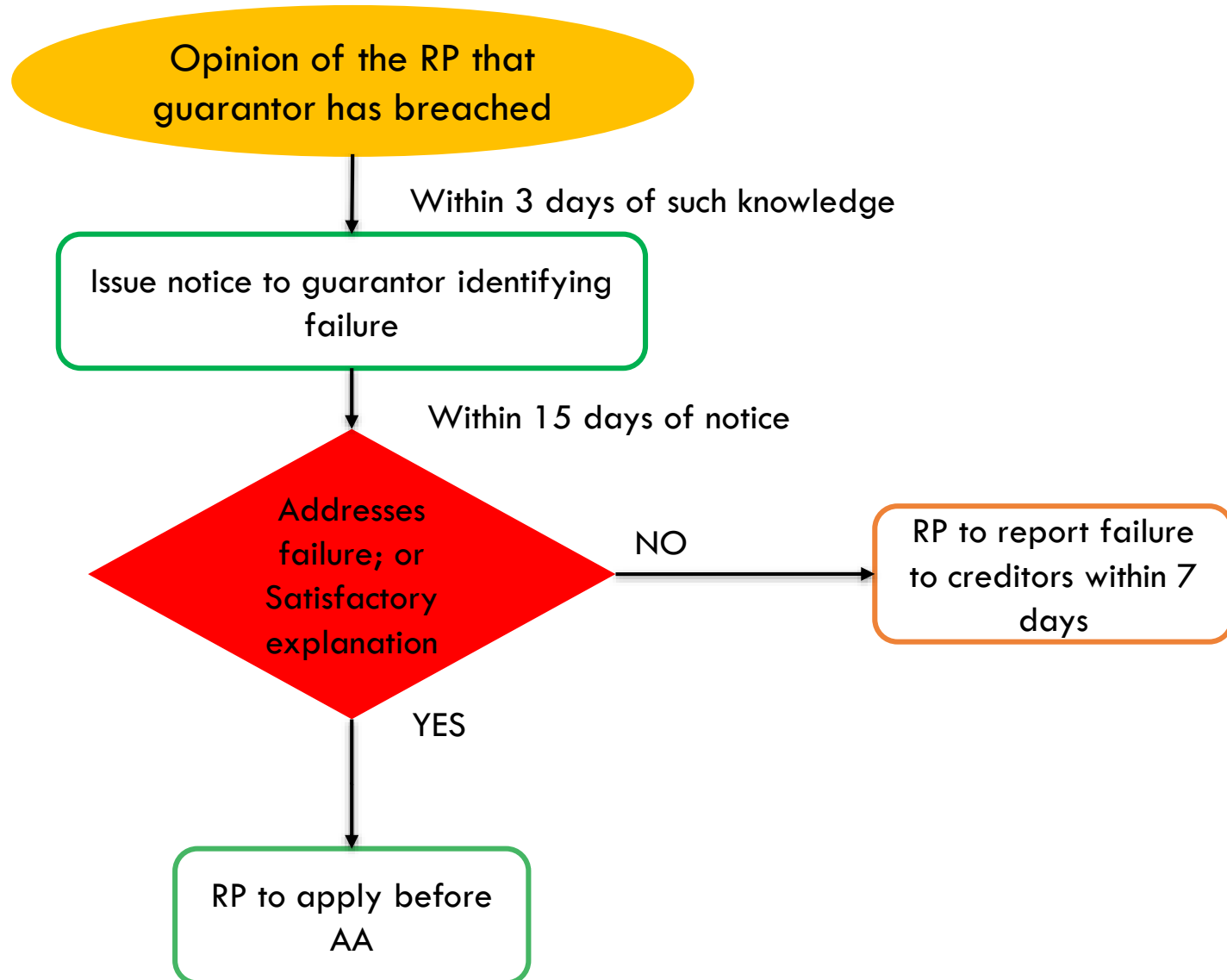
Premature Termination of Plan (sec. 118)

RP shall submit report stating reasons for premature end of repayment plan;
Details of creditors whose dues have not been paid as per Plan

Creditors whose claims have not been fully satisfied may apply for bankruptcy order.

BREACH OF REPAYMENT PLAN

Ref. regulation 20



DISCHARGE ORDER

Application for discharge order (Section 119 read with reg. 21)-

On the basis of the repayment plan, the resolution professional shall apply to the AA for a discharge order in relation to the **debts mentioned in the repayment plan** and the Adjudicating Authority may pass such discharge order.

The repayment plan may provide for -

- (a) early discharge; or
- (b) discharge on complete implementation of the repayment plan.







Discharge order only for the Debtor-

Discharge order under sub-section (3) shall not discharge any other person from any liability in respect of his debt.

PURCHASE OF ASSETS

Purchase of assets by certain persons- Restrictive, not prohibitory (Reg. 18)

The following persons **shall not purchase or acquire any interest** in the property of guarantor, **directly or indirectly, without permission of the Adjudicating Authority**

-  RP, partner/director of related IPE
-  Professional appointed by RP
-  **Any creditor**
-  Company where guarantor is a promoter/director
-  Company where a creditor is a promoter/director
-  Associate of guarantor/RP/creditor

The Adjudication Authority may set aside purchase or acquisition made contrary to the provisions of this regulation and may make such order as it may deem fit.

WITHDRAWAL OF APPLICATION

Rule 11(2)

The Adjudicating Authority may permit withdrawal of the application submitted under rule as the case may be-

(a) before its admission, on a request made by the applicant;

(b) after its admission, on the request made by the applicant, if **90% of the creditors agree to such withdrawal.**

An application for withdrawal shall be in **Form D** appended to the Rules.

SITUATIONS DURING INSOVLENCY PROCESS

There may be various situations during insolvency period, such as-

If provided by Repayment Plan- same shall follow;

If not- most reasonably, shall continue to apply on the estate



Repayment Plan continues to work w.r.t. assets of the debtor

Impact of these may be on the cash-flows of the debtor to the extent the same were dependent on continued availability of the debtor

No explicit restriction- finances must be controlled by the RP



BANKRUPTCY PROCESS

-For Individuals and Partnership Firms

WHO IS A BANKRUPT?

“Bank” + “rupt”

- ‘bank’ means ‘bench or a place of business’
- ‘rupt’ derived from ‘ruptus’ means ‘broken’

‘Bankrupt’ is ‘bankrupt’ only when he is adjudged as such

“Bankrupt” means an individual who has been adjudged bankrupt and, in relation to a bankruptcy order, it means the individual adjudged bankrupt by that order

UK

“*bankrupt*” means a person who has made an assignment or against whom a bankruptcy order has been made or the legal status of that person

Canada

“*bankrupt*” means a person against whose estate a sequestration order has been made; or who has become a bankrupt by virtue of the presentation of a debtor’s petition

Australia

“**bankrupt**” means—

- (a) a debtor who has been adjudged as bankrupt by a bankruptcy order under section 126;
- (b) each of the partners of a firm, where a bankruptcy order under section 126 has been made against a firm; or
- (c) any person adjudged as an undischarged insolvent

Sec 79 (3) IBC, India

Significance of the last limb of the definition:

- After commencement of an insolvency proceeding, if the insolvent fails to get a discharge u/s 92 (2) or 119 (1), the AA may adjudge the insolvent as bankrupt

APPLICATION FOR BANKRUPTCY ORDER

- **Insolvency Process is a pre-condition-** direct application for bankruptcy not allowed.
- **Possible by debtor/creditor**
 - Creditor-individually or jointly
 - In case debtor is a firm, application may be filed by any of its partners
- Within 3 months of the order passed by AA **under Section 100(4), or 115(2), or 118(3)**, as the case may be (refer succeeding slide)
- Applicant may propose an insolvency professional to act as bankruptcy trustee;
- Application shall not be withdrawn without the leave of AA.
- Interim moratorium commences once application is filed (**Sec. 124 (1)(a)**)
 - Terminates on bankruptcy commencement date
 - Debars all actions against properties of the debtor in respect of his debts
 - Creditors not entitled to initiate legal actions against properties in respect of any of the debts of the debtor.
 - Such interim-moratorium provisions not to apply to transactions notified by the Central Government in consultation with any financial sector regulator

WHEN IS APPLICATION FILED

**Creditor
entitled to
file
application**

Application for IRP
is rejected by AA
under Section
100(4)

Order by AA
recording rejection
of repayment plan
by meeting of
creditors (Section
115(2))

**Both debtor and
creditor entitled
to apply**

Order of AA on
premature ending
of the repayment
plan under Section
118(3)

**The debtor or the
creditor, whose
claims have not been
fully satisfied
entitled to apply**

**Application
for
Bankruptcy
(Sec. 122 & 123)**

UNDISCHARGED INSOLVENT

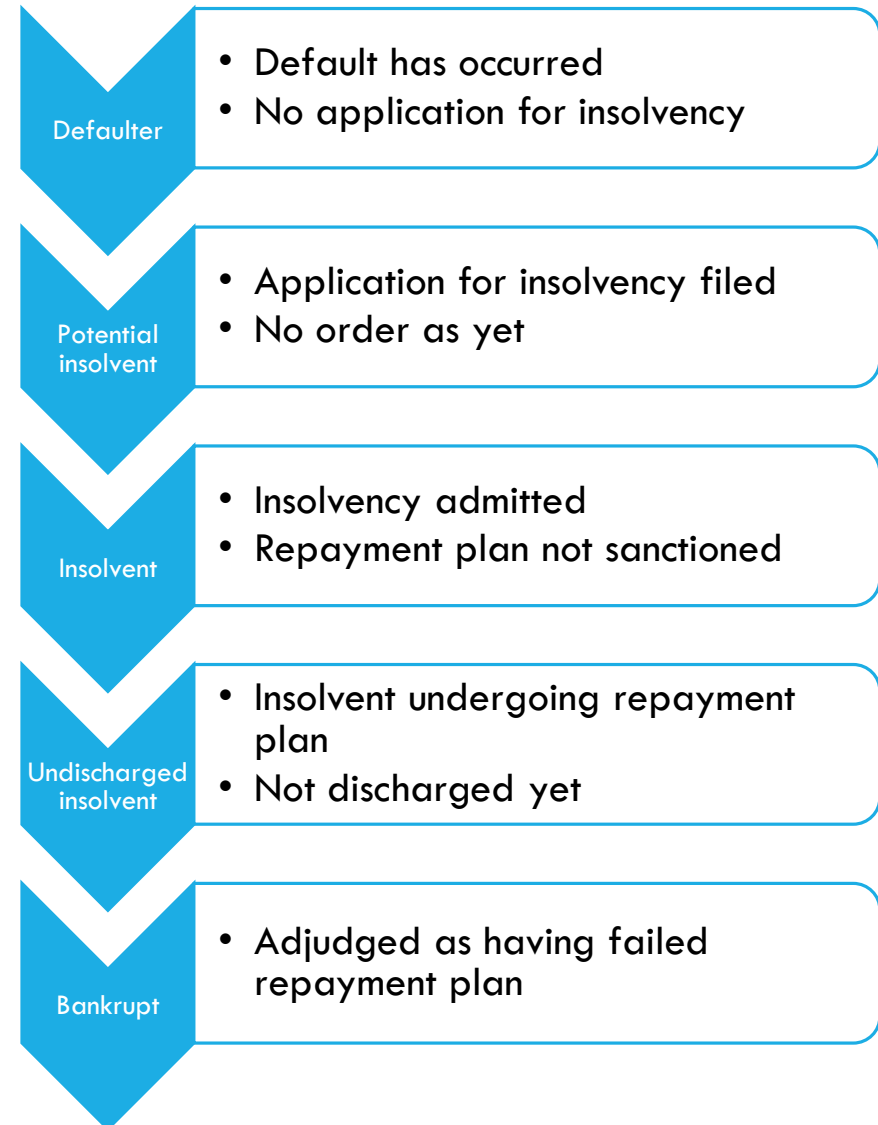
Can a person be undischarged from insolvency and still not undergo bankruptcy?

- Sec 121 suggests that bankruptcy order is only on application
- However, sec 79 (3) (c) provides additional limb to include undischarged insolvent

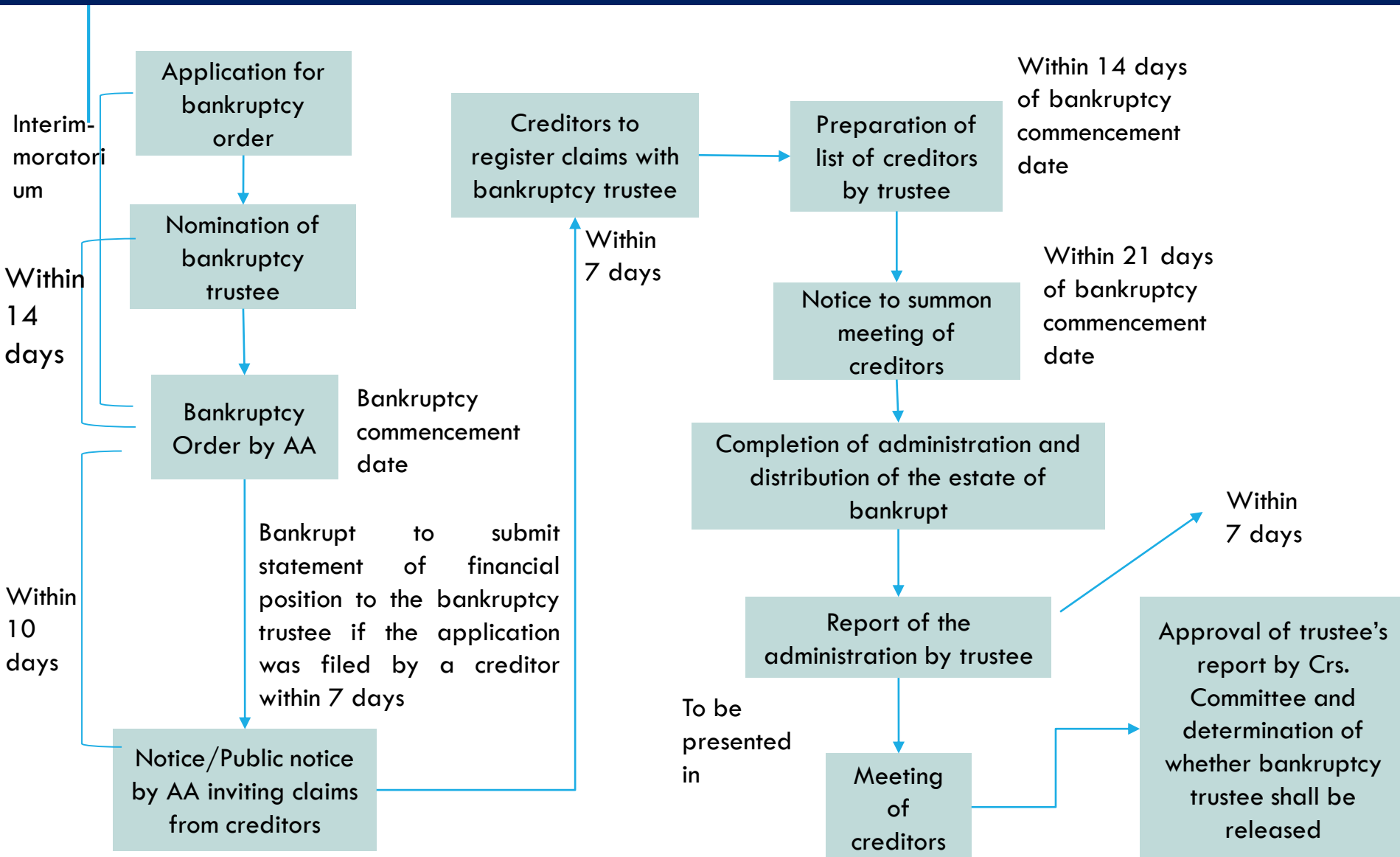
So, if insolvent does not obtain discharge [failure of repayment plan, or unsuccessful completion of repayment plan], insolvency has not been redeemed

Since undischarged insolvent is a bankrupt, this person is still a bankrupt

Bankruptcy order u/s 126 is a process of redeeming the bankrupt from bankruptcy, which will otherwise continue to stay



BANKRUPTCY PROCESS



MODIFICATION OR RECALL OF BANKRUPTCY ORDER

– sec 142

By AA – on application or *suo moto*

Where it appears to AA that –

- **there exists an error apparent on the face of such order**
- both the bankruptcy debts and the expenses of the bankruptcy have, after the making of the bankruptcy order, either been paid for or secured to the satisfaction of the Adjudicating Authority

Effect of modification/recall

- Sale, payments, etc. by bankruptcy trustee remain valid
- Property of the bankrupt shall vest in such person as AA may appoint or may revert to the bankrupt on terms as directed by AA
- Order binding on all creditors so far it relates to bankruptcy debts

Each of these are different

- Recall of the order – the order itself is recalled; the bankrupt has not undergone bankruptcy process
- Discharge on completion of administration – assets have been liquidated
- Setting aside or quashing of the order of the AA on appeal- there never was a bankruptcy order

EFFECT OF BANKRUPTCY ORDER

(Sec 128): Upon passing of the bankruptcy order, the immediate effect is as follows

Bankruptcy Estate

- Bankruptcy estate shall vest with the bankruptcy trustee

Moratorium

- Bankrupt shall be immune from any action by the creditors w.r.t. (a) Property of the bankrupt; (b) any legal proceedings without permission of AA

Division of Estate

- The estate shall be divided amongst the creditors

THE BANKRUPTCY MORATORIUM

– Sec.128 (1) (c)

Blocks these:

- A creditor shall not initiate any action against property of the bankrupt
- A creditor shall not commence any suit or other legal proceeding except with the leave of the AA

Note the bar is only on a creditor – if there is a monetary implication against the debtor, the claimant becomes a creditor

Can excluded debts be recovered? Usually AA should not object to recovery of an excluded debt by any action

- Fines, damages, maintenance obligation, etc

Does not block these:

- Enforcement action by secured creditor – sec 128 (2)
- Punitive action for personal misconduct, such as contempt of court
- Ruling in *Smith vs Braintree DC* [1990] 2 AC 215 – criminal proceedings not stayed; quasi-criminal proceedings, with predominant purpose of enforcing a payment, may get stayed.

STATEMENT OF FINANCIAL POSITION – SEC 129

To be submitted by the debtor in all creditor-filed applications

Format to be prescribed u/s 129 (2)

- Currently, no format prescribed

Usual contents [based on Rule 10.56 of UK Rules]

10.56.—(1) The statement of affairs must contain—

- (a) identification details for the proceedings; (b) identification details for the bankrupt;
- (c) the date of the bankruptcy order;
- (d) a list of the bankrupt’s secured creditors giving in relation to each—
 - (i) the name and postal address,
 - (ii) the amount owed to the creditor, and
 - (iii) particulars of the property of the bankrupt which is claimed by the creditor to clear or reduce the creditor’s debt and the value of that property;
- (e) a list of unsecured creditors giving in relation to each—
 - (i) the name and postal address of the creditor,
 - (ii) the amount the creditor claims the bankrupt owes to that creditor, and
 - (iii) the amount the bankrupt thinks is owed by the bankrupt to that creditor;
- (f) a list of the bankrupt’s total assets (which must include anything not previously mentioned in the statement of affairs which may be of value) divided into the following categories and giving the value of each asset listed—
 - (i) cash at the bank or building society,
 - (ii) household furniture and belongings,
 - (iii) life policies,
 - (iv) money owed to the bankrupt,
 - (v) stock in trade,
 - (vi) motor vehicles, and
 - (vii) other property; and
- (g) the total value of the assets listed under paragraph (f).

RELEVANCE OF STATEMENT OF FINANCIAL POSITION

Besides being a succinct yet comprehensive record of assets and obligations, the SFP is also a way to track the past financial history of the debtor

- Particularly to find any vulnerable transactions

Penal provision of sec 186 (a)

- False representation
- Wilful omission or concealment
- While providing any information during the bankruptcy process

Can creditors seek a copy of the SFP?

- Usually, the SFP is the basis of the bankruptcy proceedings
- UK law specifically empowers creditors to seek a copy of it

Regulation-making may take care of this

DISQUALIFICATIONS OF A BANKRUPT

Sec 140: Upon Bankruptcy Order shall, the bankrupt shall be disqualified from acting as-

- a) being appointed or acting as a trustee or representative in respect of any trust, estate or settlement;
- b) being appointed or acting as a public servant;
- c) being elected to any public office where the appointment to such office is by election; and
- d) being elected or sitting or voting as a member of any local authority.

ADDITIONAL DISQUALIFICATIONS

Additionally, the bankrupt also attracts disqualification from/ under various other laws. Illustrative list is below:

Companies Act, 1956/ 2013

Insurance Regulatory and development Act

Being a member of a professional body viz. ICAI; ICSI. ICWA

Holding office under the Notaries Act, 1952

Being a part of composition of the State Commission under Consumer Protection Act, 1986

Contract Labour (Regulation and Abolition) Central Rules, 1971

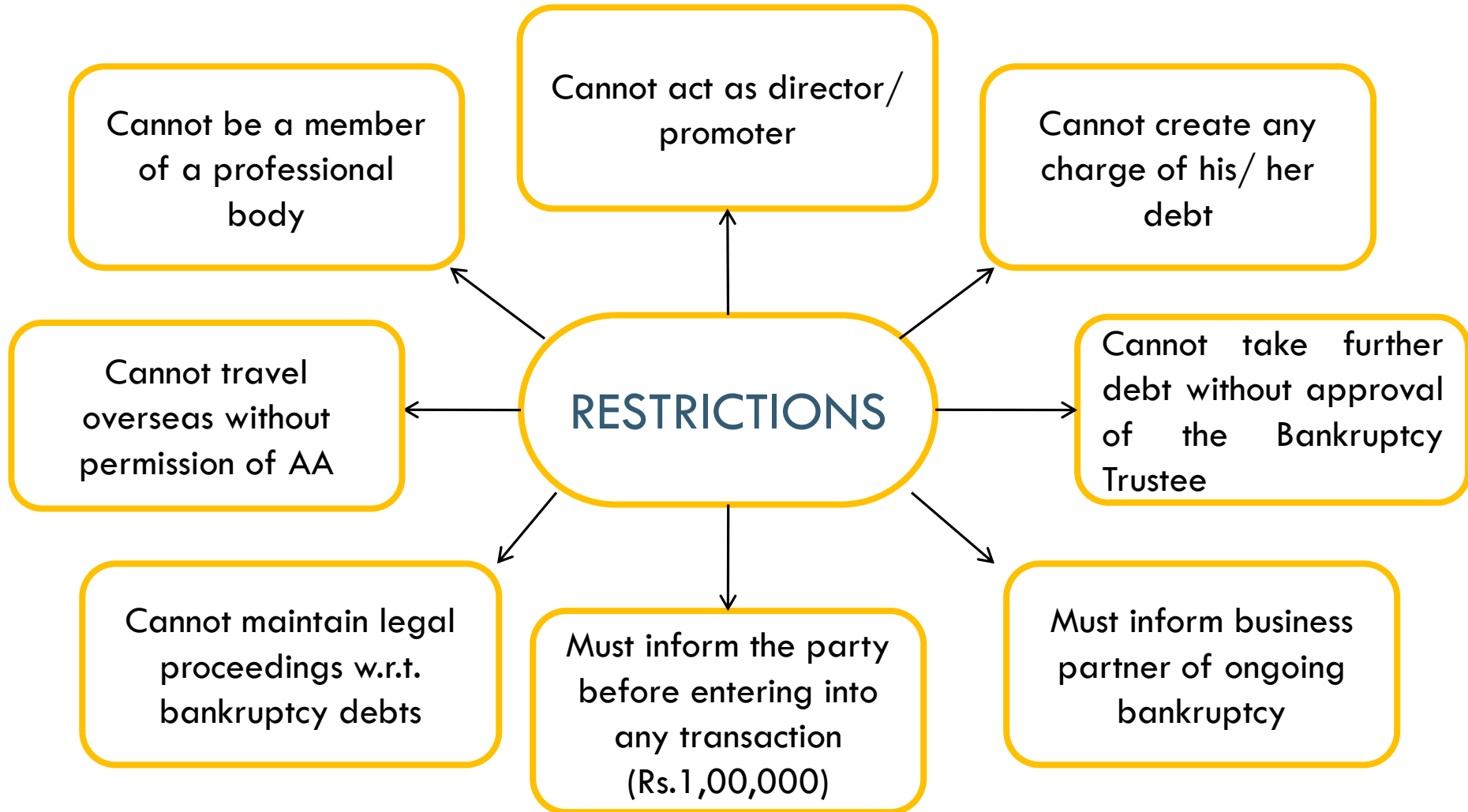
Holding office under the Indian Constitution

Limited Liability Partnership Rules, 2009

Reserve Bank of India Act, 1934

RESTRICTIONS ON A BANKRUPT

Sec. 141: Apart from disqualifications as discussed, bankruptcy order also attracts the following restrictions upon the bankrupt



ROLE OF CREDITORS UNDER BANKRUPTCY

General meeting of creditors	Committee meeting of creditors
<p>The first meeting of creditors will mandatorily have to be called, within 21 days of BCD – sec. 133 (1)</p>	<p>The Committee is constituted by the Trustee. Composition of the Committee is not laid down in the Code or the Regs</p>
<p>Primary business of the first meeting is to constitute the Committee of Creditors</p>	<p>Given the fact that Creditors' Committee has substantial powers to drive the bankruptcy process, including power to replace the trustee, the Committee's composition must reflect the voting share of the general body</p>
<p>Voting percentage for the general meeting is not given in the Code or the Regulations. Sec 134 (3) provides for passing of a resolution</p> <ul style="list-style-type: none">• By common intuition, this should be ordinary majority resolution	<p>Trustee to intimate to the AA the constitution of the Committee within 3 days – reg 20 (2)</p>

VOTING SHARE FOR GUARANTEE CREDITORS

Sec. 135 (3) – a creditor shall not be entitled to vote for an unliquidated amount

- Unliquidated amount normally refers to unliquidated damages for breach of a contract which requires adjudication
- The right of creditor to demand money from guarantor, if clear under the guarantee deed, is an ascertainable claim
- Several rulings of the SC on this point, Biswanath Jhunjhunwala, Ganga Kishun, etc

The Code has several provisions for secured creditor's voting rights – only in respect of surrendered security interest, or unsecured part of his claim

- Sec. 110, 123 (3)

However, is a secured creditor of the CD a secured creditor of the guarantor?

- Answer will be no, unless there assets of guarantor given as security

Hence, the voting shares will be based on claims filed by the guarantee creditors

Claim amount:

- Where resolution plan for CD has been approved – the amount of haircut
- Where the resolution plan for CD is not yet approved – the whole of the amount payable by the CD
- Where the CD is in liquidation, and the creditor has relinquished security interest – the amount claimed, less any distribution
- Where the CD is neither in resolution, nor liquidation – the amount due from CD, as demanded from guarantor

CREDITORS UNDER BANKRUPTCY

Secured Creditors

The bankruptcy order shall not affect the right of any secured creditor to realize or otherwise deal with his security interest in the same manner as he would have been entitled if the bankruptcy order had not been passed:

Who is a secured creditor?

Secured creditor is a lender that provides collateralized debt.

Secured in respect of what?

- His claim against the debtor in question

Under the Code, secured creditor shall have rights of a secured creditor only upto the amount of security not relinquished.

Also, a secured creditor is taken secured only to the extent of value of security interest – sec. 123 (3)

Three options of a secured creditor

1. Relinquish security interest, claim against bankruptcy estate, and get top priority u/s 178
2. Enforce security interest outside of bankruptcy process:
 1. He would have first filed a claim separately for the secured and unsecured portions
 2. Trustee has the right to pit an alternative buyer

PROOF OF DEBT AND ROLE OF CREDITORS

Bankruptcy trustee to give notice to every creditor

Within 14 days from days of preparing list of creditors

Interest on debt - provable as part of the debt

Till bankruptcy commencement date

Mandatory to call meeting of creditors – section 133 (associates not entitled to vote) –

Committee of creditors is to be established – section 134(3)

Creditor approval is mandatory for certain acts by bankruptcy trustee – section 153

Also, the CoC approves the report of bankruptcy trustee on administration of the estate, and determines whether the bankrupt be released

DISCHARGE ORDER

Ref: Sec 138

Application by bankruptcy trustee to AA;

Earlier of –

- Expiry of 1 year from the bankruptcy commencement date
- Within 7 days of the approval of the committee of creditors of the completion of administration of estate of the bankrupt, if the said approval is accorded before the expiry of 1 year from the bankruptcy commencement date

Effects

- Bankrupt is released from **all bankruptcy debts**
- In case the application for discharge is filed within 7 days of the creditors' approval, the discharge does not affect
 - functions of the bankruptcy trustee
 - the operation of the provisions of Chapters IV and V of Part III;

These remain unaffected

- Right of the secured creditor to enforce his security for the payment of a debt from which the bankrupt is discharged
- Bankrupt is not released in respect of debts incurred by means of fraud or breach of trust to which he was a party
- Bankrupt is **not released from any excluded debt**

Undischarged bankrupt – means a bankrupt who has not received a discharge order u/s 138



BANKRUPTCY ESTATE

ESTATE OF THE BANKRUPT

Sec 155- Estate of the Bankrupt shall -

Includes:

- all property belonging to or vested in the bankrupt at BCD;
- the capacity to exercise and to initiate proceedings for exercising all such powers in or over or in respect of property;
- all property which by virtue of any of the provision of the Code

Not include:

- excluded assets; (defined)
- property held by the bankrupt on trust for any other person;
- all sums due to any workman or employee from the provident fund, the pension fund and the gratuity fund;
- such assets as may be notified by the CG in consultation with any financial sector regulator.

EXCLUDED ASSETS — PERSONAL ORNAMENTS AND OTHER ASSETS

Personal ornament exception — sec 79 (14) (c)

- Personal ornaments of debtor “or his immediate family”
 - There is no question of vesting of assets of immediate family members
 - The reference may only for use of the ornaments
- Which cannot be parted with as per religious custom
- Limited in value to Rs 1 lac

Tools, books, vehicle or other equipment

- Necessary for personal use or
- the employment or vocation of the bankrupt
- How many vehicles can be retained?
 - The question is one of necessity
 - Hence, seems exception is only for 1 vehicle
 - Luxury vehicles may also have to be vested

Furniture, household equipment or provisions necessary for basic domestic needs

Unencumbered LIP or pension plan

EXCLUDED ASSETS – DWELLING UNIT

Unencumbered single dwelling unit of such value as may be prescribed

- Unit owned of by the debtor, of upto Rs 20 lacs in urban areas
- Upto Rs 10 lacs in rural areas
- Rural area defined in line with NAREGA law – any area outside the area under a local body or cantonment board

As for determination of value, values' valuations may be relevant

Unlikely that the bankrupt will have a dwelling unit of as much value

Most bankrupt-owned properties may be of value higher than the ceilings:

- Does the bankrupt get as much value from the bankruptcy estate, if he cedes his house to the estate?
- Seems logical, equitable

How to deal with interests in dwelling units:

- Practically, the dwelling unit may be owned in various modes
 - Owned by an HUF, debtor has a co parcener's interest
 - Owned jointly, debtor has a joint owner's interest
 - Owned by spouse, debtor has right to stay
 - Under tenancy – tenancy rights
 - Joint tenancy rights

The only carve out is to leave a dwelling unit owned by the debtor

INCLUSIONS IN THE ESTATE OF THE BANKRUPT

Estate of the bankrupt vests in the trustee

- What is the meaning of estate?
- All the assets owned by the bankrupt as on the bankruptcy commencement date

Sec 155 provides the scope of inclusions

- All property of the bankrupt or vested in the bankrupt on the BCD
- Powers to take proceedings, as the bankrupt would have done
- All property that gets comprised by virtue of any of the provisions – such as preferential transfers, undervalued transactions

Wide definition of “property” in sec 3 (27)

Causes of action personal to the bankrupt do not form part of “property”

- Damages for pain/harm to body, mind or character – Grady v HM Prison Service (2003) EWCA Civ 523
- Damages for unfair dismissal

Family property

- Several rulings under erstwhile insolvency laws that interest of the bankrupt in family property may be liquidated as a part of the bankruptcy estate. Eg. Ramchandra Aiyar, (1922) 43 MLJ 569

Doctrine of reputed ownership has not been incorporated in the Code

Provident fund – sec 10 of the PF Act provides that money lying to the credit of the person shall not be subject to claim under erstwhile Insolvency laws

Gratuity – sec 13 of the Gratuity Act

FUNCTIONS & DUTIES TOWARDS THE ESTATE

Functions of the Trustee

(Sec. 149)

The bankruptcy trustee shall perform the following functions in accordance with the provisions of this Chapter –

- a) Investigate the affairs of the bankrupt;
- b) Realise the estate of the bankrupt; and
- c) Distribute the estate of the bankrupt.

Duties of the Bankrupt

(Sec. 150)

The bankrupt shall perform the following duties-

- a) give to the bankruptcy trustee the information of his affairs;
- b) attend on the bankruptcy trustee at such times as may be required;
- c) giving notice to the bankruptcy trustee of any significant events which have occurred after the BCD

GENERAL POWERS OF THE BANKRUPTCY TRUSTEE

Ref: Sec 152

Sell any part of the estate

Give receipts for any money received by him

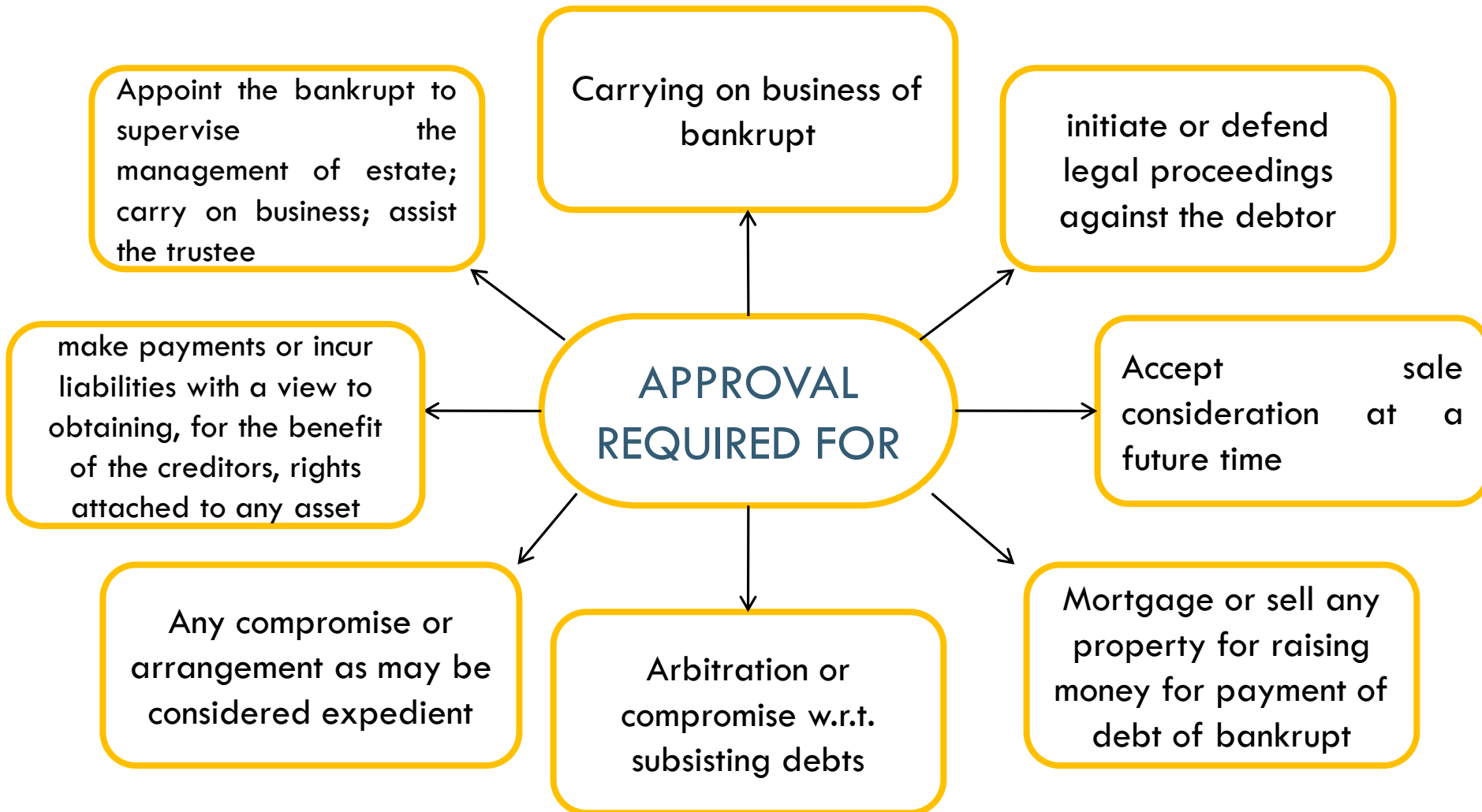
Prove, rank, claim and draw any dividend in respect of such debts due to the bankrupt as are comprised in the estate

Exercise right of redemption w.r.t. any property held in hypothecation

Deal with any property in the bankruptcy estate

APPROVAL OF CREDITORS FOR CERTAIN ACTS

Certain acts that require explicit approval of creditors are: (Sec 153)



VALUATION OF ASSETS

Ref: Regulation 30

No mandatory valuation

Valuation may be done only if:

- (a) Bankruptcy trustee is of the opinion that valuation is necessary;
or
- (b) Resolution in this regard is passed by the committee

Assets to be valued

Valuation may be done of assets which may or may not form part of estate of the bankrupt;

MODE OF SALE[#]

Auction

All assets shall be ordinarily sold by auction, except in case of conditions for private sale mentioned alongside.

Private Sale

In following conditions:

- the asset is perishable in nature;
- Likely deterioration in value of asset;
- the selling price of the asset is higher than the reserve price of a failed auction

[#]Ref: Regulation 27 read with Schedule II

PARTIES DISQUALIFIED FROM PURCHASE OF ASSETS

Purchase of assets by certain persons- Restrictive, not prohibitory (Reg. 27 (3))

The following persons **shall not purchase or acquire any interest** in the property of guarantor, **directly or indirectly, without permission of the Adjudicating Authority**

- (a) the Bankruptcy Trustee or any partner or director of the IPE of which the Bankruptcy Trustee is a partner or director;
- (b) any professional appointed by the Bankruptcy Trustee for the bankruptcy process;
- (c) any creditor or associate of the bankrupt;
- (d) any company where the bankrupt or a creditor is a promoter or director;

The Adjudication Authority may set aside purchase or acquisition made contrary to the provisions of this regulation and may make such order as it may deem fit.

ORDER FOR PRIORITY FOR DISTRIBUTION

Similar to priority set out u/s 53 of the Code for liquidation of a corporate debtor, during bankruptcy, the distribution of the final dividend, the following debts shall be paid in priority to all other debt as per **section 178**.

Costs

- Costs and expenses incurred by the bankruptcy trustee for the bankruptcy process- in full.

Workmen & Secured creditors

- Workmen dues for a period of 24 months prior to BCD;
- Debts to secured creditors

Employee dues

- Wages and any unpaid dues to employees, other than workmen, for a period of 12 months prior to BCD

Government Dues

- Any amount due to CG or SG, for 2 years preceding the BCD

Other debts

- All other debts and dues including unsecured debts

ENHANCING LIQUIDATION ESTATE

All assets of the bankruptcy as on BCD vest in the trustee

All transfers from the date of bankruptcy application to the BCD are void

For incomes/assets after the BCD till the date of discharge

- The trustee has the option of claiming the assets from the bankrupt

Other transfers

- Preferential transfers
- Undervalued transfers
- Fraudulent transfers

Saving the liquidation estate

- Giving up onerous assets

UNCLAIMED PROCEEDS

Ref: Regulation 36

Deposit to the Insolvency and Bankruptcy Fund-

Within 3 days of submission of Final Report, Trustee shall apply to the Adjudicating Authority **for an order for such deposit**, any unclaimed dividends of bankruptcy process or undistributed asset or any other balance amount payable to the creditors, left with him.

Statement for deposit-

Trustee shall submit a statement containing-

- (a) the names and last known address of the creditors entitled to the unclaimed dividend or undistributed asset or any other balance;
- (b) the amount of the unclaimed dividend or any other balance for each creditor under (a);
- (c) the value of the undistributed assets

ONEROUS PROPERTY (1 / 2)

Ref: Sec 160

The term “onerous property” means –

- (i) any unprofitable contract; and
- (ii) any other property comprised in the estate of the bankrupt which is unsaleable or not readily saleable, or is such that it may give rise to a claim.

The bankruptcy trustee may, by giving notice to the bankrupt or any person interested in the onerous property, disclaim any onerous property which forms a part of the estate of the bankrupt.

ONEROUS PROPERTY (2/2)

Person interested in Onerous Property

- (a) Any person who claims an interest in the disclaimed property;
- (b) Any person who is under any liability in respect of the onerous property; or
- (c) where the disclaimed property is a dwelling house, any person who is in occupation of or entitled to occupy the dwelling house, on the date of filing of application.

VULNERABLE TRANSACTIONS

Vulnerable Transactions under the Code

Undervalued Transactions (Sec. 164)

an undervalued transaction between a bankrupt and any person

- entered into during the period of two years ending on the filing of the application for bankruptcy; and
- caused bankruptcy process to be triggered

Preference Transactions (Sec. 165)

The transaction giving preference to an associate of the bankrupt

- entered into during the period of two years ending on the filing of the application for bankruptcy; and

Extortionate Credit Transactions (Sec. 167)

In respect of extortionate credit transactions to which the bankrupt is or has been a party

- entered into during the period of two years ending on the filing of the application for bankruptcy; and



ROLE OF RP/ BANKRUPTCY TRUSTEE

ELIGIBILITY FOR APPOINTMENT

Eligibility of RP/ Bankruptcy Trustee

IP, IPE of which he is partner or director & all partners & directors of that IPE-
Independent* of the guarantor

Regulation 4 & 3 of
Personal Insolvency and
Bankruptcy Regulations,
respectively

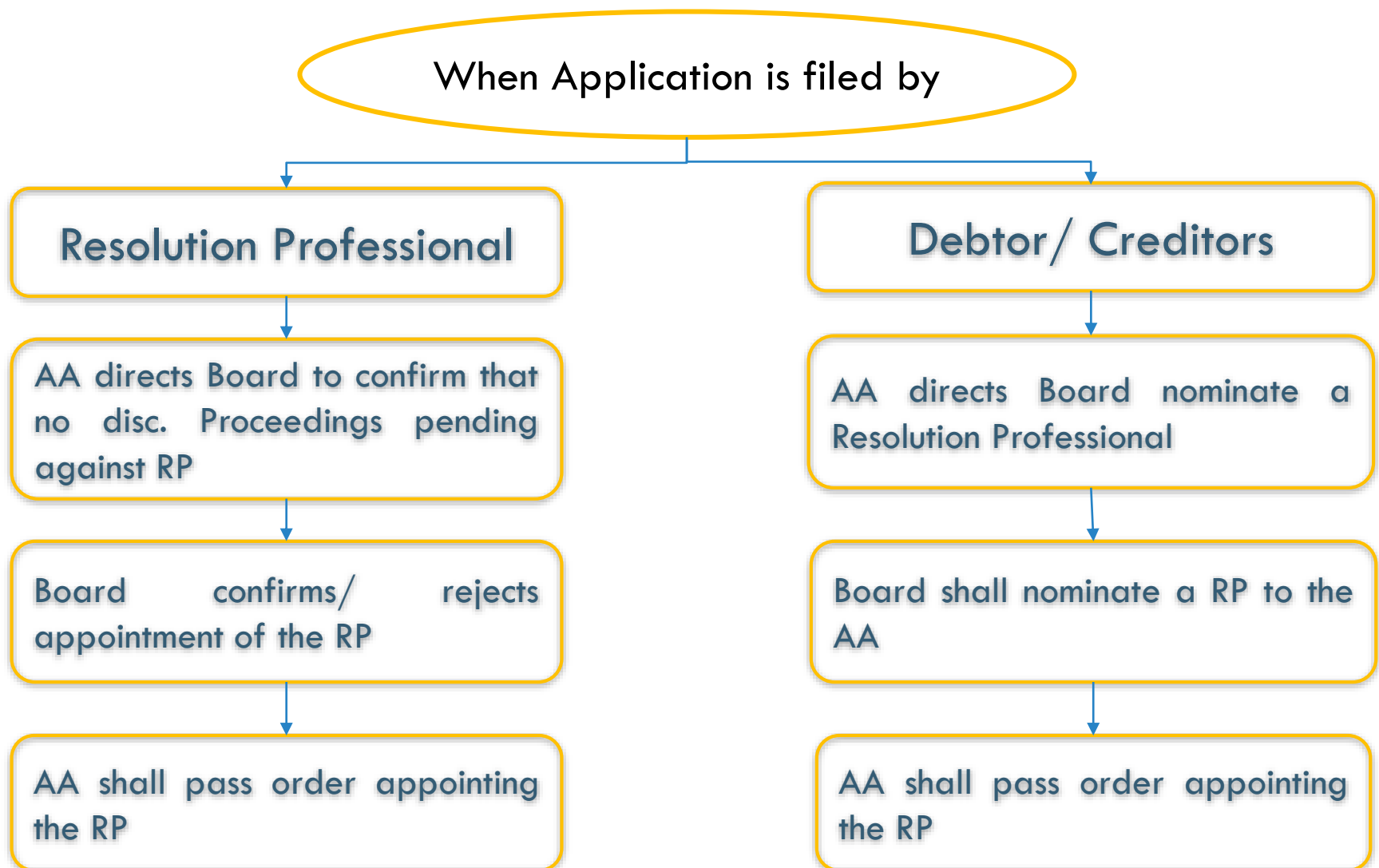
Eligibility of
Resolution
Professional

- Not an associate of the guarantor;
- Not a related party of the corporate debtor;
- Has not acted as the IRP; RP or liquidator of the CD

IP, IPE of which he is partner or director & all partners & directors does not represent any party in resolution process

IP not subject to ongoing proceedings

APPOINTMENT OF RP DURING INSOLVENCY



DUTIES OF THE RP

Duties of the RP in case of personal insolvency process:

■ Report on application u/s 99

RP is required to submit a report within 10 days of his appointment, w.r.t. the Application filed by the debtor (sec 94) or a creditor (sec 95).

■ Invitation for and collation of claim

Sec 102 requires the RP to issue a public notice within seven days of admission, to invite claims from all creditors within 21 days of the public notice.

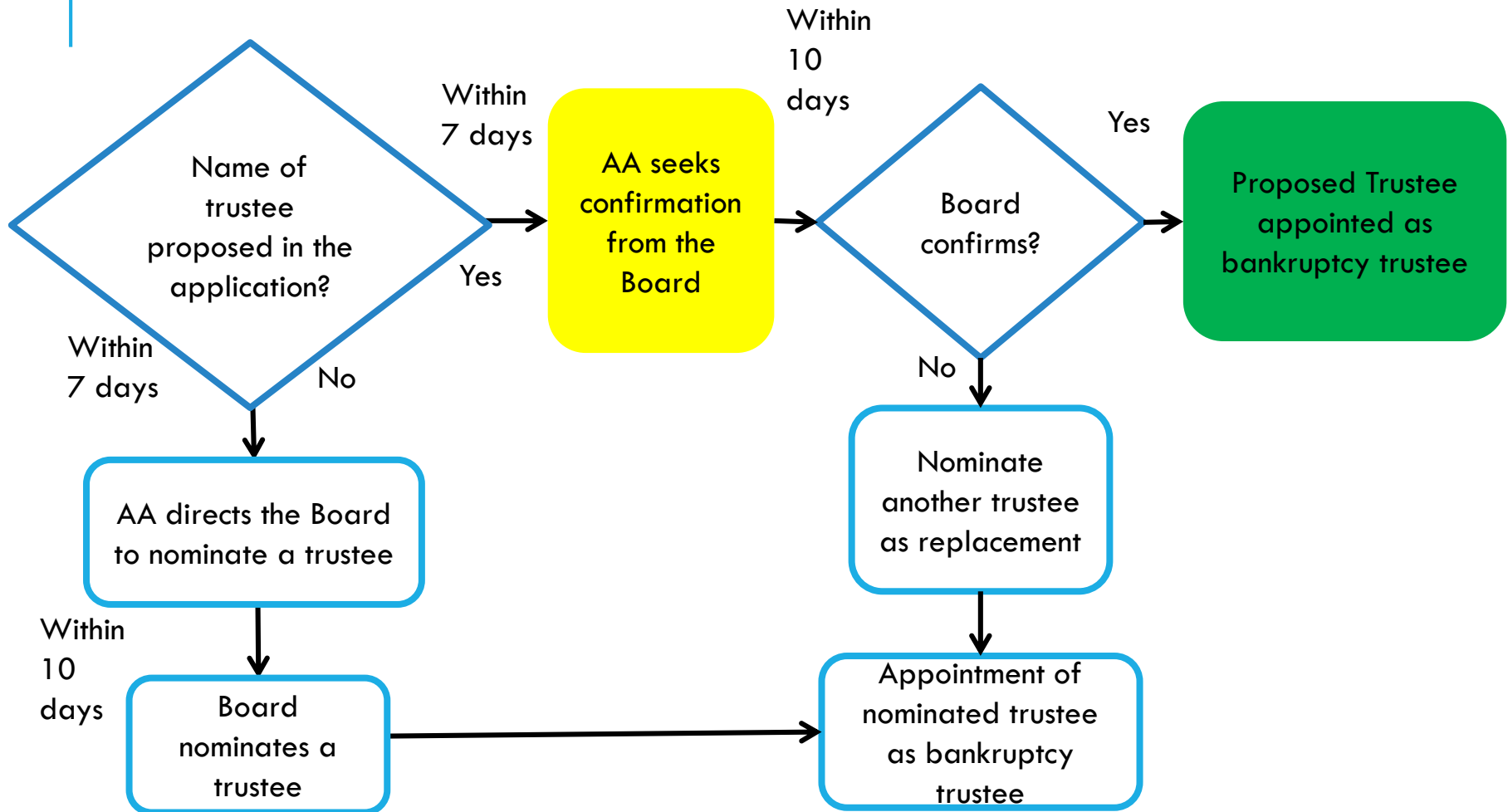
■ Consulting debtor on repayment plan

While making of this Repayment Plan, the RP must endeavour to ensure the following:
The RP must provide consultancy taking into account the personal circumstances of the debtor and the nature of the debtor's finances; To ensure full and accurate disclosure by the RP; Explain the consequences of the Repayment Plan, for which the debtor may be liable.

■ Report on Repayment Plan

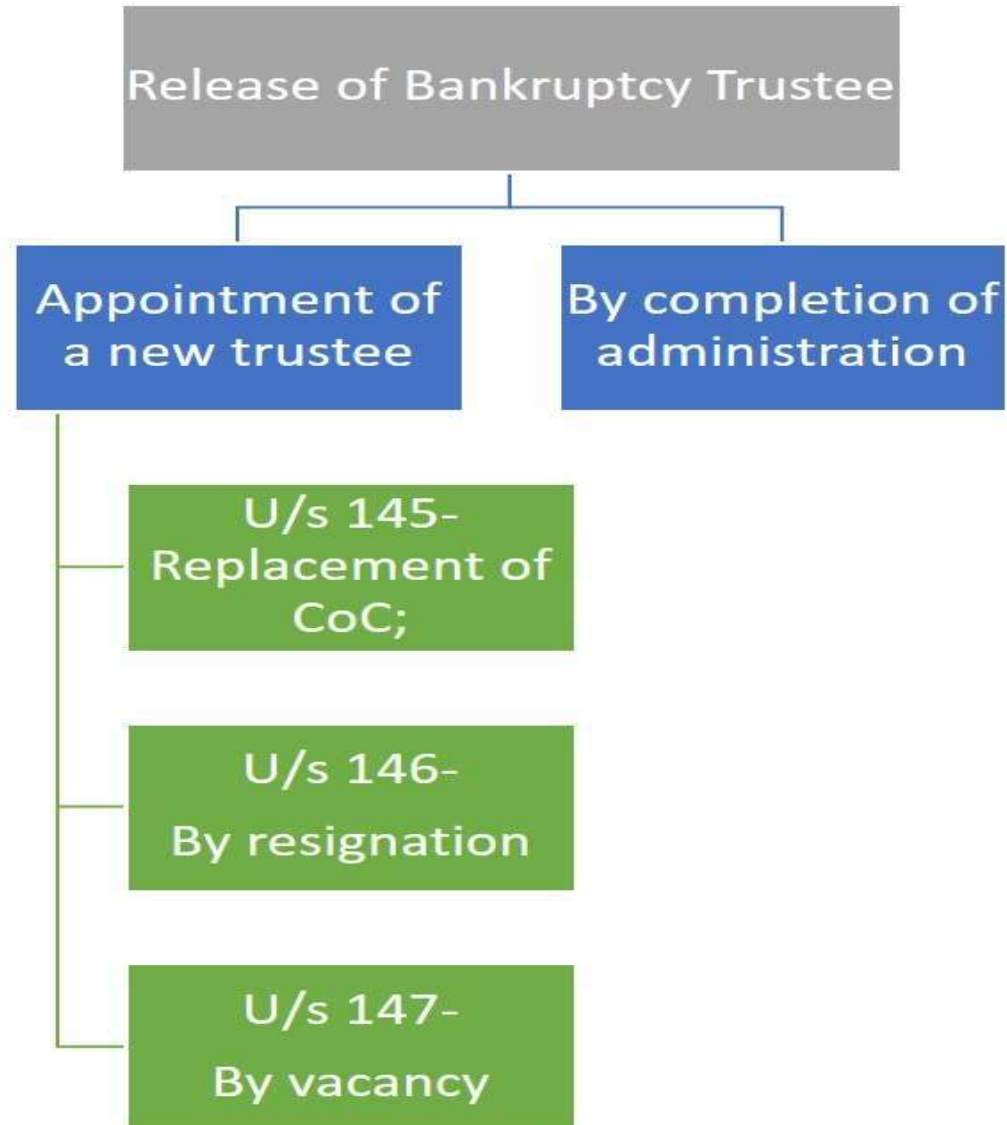
Section 106 of the Code calls for the RP to submit repayment plan within 21 days from the last day of submission of claims of the creditors

APPOINTMENT OF BANKRUPTCY TRUSTEE

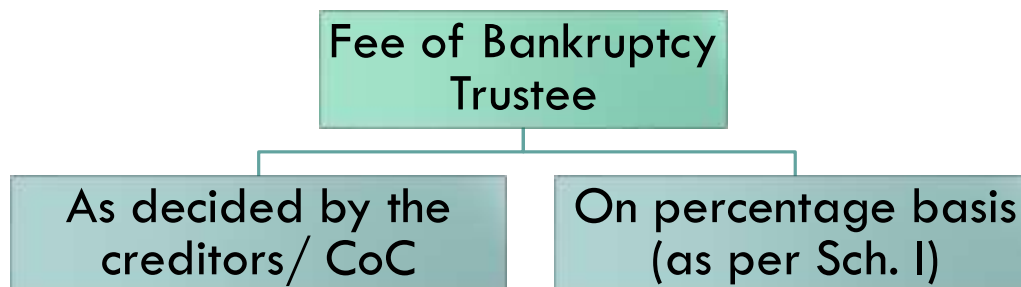


RELEASE OF BANKRUPTCY TRUSTEE

Ref: Sec 148



FEE OF THE BANKRUPTCY TRUSTEE



SCHEDULE I
FEES OF BANKRUPTCY TRUSTEE
 [Under regulation 4(2)]

Amount of realisation in rupees (less bankruptcy process cost)	Percentage of fee on the amount realised			
	in the first six months	in the next three months	in the next three months	thereafter
On the first 25 lakh	10.00	7.50	5.00	3.75
On the next 50 lakh	7.50	5.00	3.75	2.80
On the next 1 crore	5.00	3.75	2.50	1.88
On the next 9 crore	3.75	2.80	1.88	1.41
On the next 40 crore	2.50	1.88	1.25	0.94
On the next 50 crore	1.25	0.94	0.68	0.51
On further sums realised	0.25	0.19	0.13	0.10
Amount of distribution in rupees	Percentage of fee on the amount distributed			
On the first 50 lakh	5.00	3.75	3.00	1.88
On the next 75 lakh	3.75	3.00	1.88	1.41
On the next 1 crore	2.50	1.88	1.25	0.94
On the next 9 crore	1.88	1.40	0.94	0.71
On the next 40 crore	1.25	0.94	0.63	0.47
On the next 50 crore	0.63	0.48	0.34	0.25
On further sums distributed	0.13	0.10	0.06	0.05

REPORTS BY BANKRUPTCY TRUSTEE

Reporting Requirements

Preliminary Report (Reg. 8)

- To the AA & Committee;
- Within 90 days of BCD;
- List of assets and liabilities of the bankrupt as on BCD;
- Proposed plan of action w.r.t. estate;
- Details of the assets forming and not forming part of estate

Subsequent Progress Reports (Reg 10)

- To AA & Committee; within 15 days of every calendar quarter;
- Appointment details of professionals;
- a statement indicating the progress in proceedings;
- an asset sale report
- Details of fee and remuneration;
- Status of material litigation

Final Report (Reg 11)

- manner of realisation of the assets;
- manner of distribution of the dividends;
- details regarding the discharge of the bankrupt;
- unclaimed dividend, if any;
- surplus dividend, if any; and
- if the bankruptcy process cost exceeds the estimated cost provided in the preliminary report, along with reasons for the same