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Critical Analysis Of Legal Gaps And Challenges Arising In Implementation Of Insolvency And Bankruptcy Code, 2016

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ABSTRACT

Insolvency and Bankruptcy Code, 2016 was formulated to provide an easy exit route for Corporations from the market. It was aimed to protect the interests and rights of creditors by providing them an easy route to recover their money from corporations by applying for the initiation of a corporate insolvency resolution process against the corporate debtor. The easy recovery mechanism has enabled Entities to recover debt from the Corporations. This research aims to identify existing legal gaps that hinder stakeholders from effectively executing the Corporate Insolvency Resolution Process (CIRP).

INTRODUCTION

The objective of the Insolvency and Bankruptcy Code, 2016, is to incorporate the laws relating to insolvency resolution and reorganization of corporations in a time-bound manner. The aim was to maximize the value of the debtor's assets and credit availability, promote entrepreneurship, and balance the interests of all stakeholders.

It provided a means to Corporate Persons freedom to exit from the market by resolving their financial distress in a time-bound manner.

It also contains provisions for voluntary liquidation of companies. The code is enacted by the parliament to expedite the insolvency resolution process, reduce red tape, improve investment activities, and attract new businesses. It also helps in improving India's ranking in ease of doing business as now the ease of exit motivates the new entrants.

This code is umbrella legislation that provides level playing fields for all the stakeholders who are interested in the outcome of the process. Fundamental key features of IBC include a time-bound mechanism, early detection of Insolvency, presence of institutional infrastructure, specialized adjudicatory authorities, moratorium protection or 'calm period' preventing the disposal of assets, and a comprehensive framework for revival, rehabilitation, and resolution or liquidation process.

HISTORICAL BACKGROUND

Before the enactment of this Code, Insolvency and Bankruptcy laws were provided into the multiple legislations which were not uniform. In the previous regime, creditor's rights were scattered, and the numerous adjudicatory bodies were dealing with the insolvency issues.

The Companies Act, of 1956, primarily focused on the winding-up or liquidation of companies. It did not include provisions for initiating a rehabilitation process for companies unable to repay their debts. The winding-up process was typically initiated when a company defaulted on its debt obligations, leading directly to liquidation.

With the introduction of the IBC, initiating winding-up due to default or voluntary winding-up is no longer permitted under the Companies Act, 1956 or the Companies Act, 2013. However, involuntary winding-up cases that do not pertain to insolvency are still governed by the provisions of the Companies Act, 2013.

The implementation of the IBC also impacted the enforcement and recovery mechanisms established under debt recovery laws, such as the Recovery of Debts Due to Banks and Financial Institutions Act, 1993, and the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002. These laws were not repealed following the introduction of the Code.

However, their application is limited because the IBC takes precedence over other laws. The IBC holds an overriding effect on all other statutes concerning insolvency and bankruptcy matters. In cases of conflict between the IBC and other laws or proceedings, the provisions of the IBC will prevail. These other proceedings include DRT cases, the SARFAESI Act, civil disputes, criminal cases, and so on.

STATEMENT OF PROBLEM

A strong insolvency framework is designed to achieve two key goals: supporting the preservation of viable businesses and facilitating the exit of companies that cannot be salvaged. The IBC is structured to establish an efficient rescue mechanism, providing defaulting corporate entities with an opportunity to recover and regain stability.

However, following the implementation of the Code, practical challenges have emerged in executing the Corporate Insolvency Resolution Process. The Central Government rolled out the Code in a phased approach.

However, numerous legal challenges have confronted the adjudicatory authorities. These bodies are offering detailed interpretations and clarifications regarding the operational framework of the Code. Despite this, several issues still need the lawmakers' attention. There are specific legal deficiencies or gaps within the corporate insolvency provisions that call for appropriate amendments.

IMPORTANCE OF STUDY

The IBC offers a robust and effective recovery mechanism for defaulting corporate debtors. Despite being in force for years, the Code has undergone numerous amendments to address practical challenges arising from its implementation. Judicial authorities have been interpreting it generously to promote the achievement of its objectives.

To ensure the smooth continuation of the Corporate Insolvency Resolution Process (CIRP), it is essential to identify additional gaps or challenges hindering its effective execution. It is crucial to uncover structural issues that emerge during the CIRP or prior to its initiation. A thorough examination of areas needing reforms is necessary. As a relatively new piece of economic legislation, the IBC cannot anticipate all future challenges or unforeseen circumstances. Therefore, this study will pinpoint critical concerns within the Code that could guide legislative bodies and policymakers in making appropriate amendments to the law.

AIMS AND OBJECTIVES

This research aims to identify existing legal gaps that hinder stakeholders from effectively executing the Corporate Insolvency Resolution Process (CIRP). The key objectives of the research project are as follows:

- To identify provisions that obstruct the implementation of CIRP and are inconsistent with the objectives of the Code.
- To analyze practical issues arising during the corporate insolvency process that impacts the interests of the corporate entity.
- To assess whether a uniform default amount for initiating CIRP is suitable.
- To examine if all stakeholders have a fair and equal playing field during the CIRP.
- To evaluate the role of adjudicatory authorities throughout the CIRP process.

HYPOTHESIS

The Code is designed to safeguard the interests of the corporate entity and ensure a fair and equal playing field for all stakeholders involved in the Corporate Insolvency Resolution Process (CIRP). However, an analysis of the Code reveals several concerns and practical challenges that arise during its implementation. These gaps in the current CIRP framework make it difficult to fully achieve the intended objectives.

RESEARCH QUESTIONS

Based on the above hypothesis, the researcher has formulated the following research questions for this project:

- What is the framework of the Corporate Insolvency Resolution Process under the IBC, 2016?
- Is a uniform default amount for initiating CIRP against the corporate debtor under the Code undesirable?

- Does the Code create arbitrary and unreasonable discrimination between Financial Creditors and Operational Creditors?
- Has the role of the Board of Directors of the corporate debtor been eliminated during CIRP? Could their involvement during CIRP help preserve the corporate entity?
- What is the role of adjudicating authorities during the CIRP? To what extent is court interference permitted during the CIRP proceedings?

RESEARCH METHODOLOGY

The researcher has employed an analytical research method in this project to address the research problems. The study involves analyzing a database of cases, legal provisions, policy decisions, and amendments, all based on the formulated research questions.

Additionally, the doctrinal method has been utilized to examine substantive laws and understand the legal concepts applied to the identified issues.

SCOPE AND LIMITATIONS OF THE STUDY

This study is focused solely on the Corporate Insolvency Resolution Process (CIRP) and does not cover other provisions of the Code. The research examines the issues and challenges that arise during insolvency proceedings involving corporate entities. It excludes matters that are not related to the insolvency of the corporate debtor or fall under other insolvency legislations.

The project does not include case studies from the previous insolvency regime. For the database of authorities, the researcher has relied on cases decided by the Supreme Court, NCLAT, and NCLT between 2017 and 2024. The information for this study has been gathered from amendments made by Parliament, committee reports, Central Government policies related to the IBC, as well as details and regulations published by IBBI.

LITERATURE REVIEW

The article, Differential Treatment Among Creditors under India's Insolvency and Bankruptcy Code, 2016: Issues and Solutions, co-authored by C. Scott Pryor and Risham Garg, offers a data-driven examination of the implementation of India's Insolvency Code. The authors analyze the differential treatment given to various creditors and the issue of granting non-plenary control to the Committee of Creditors, primarily composed of financial creditors. This has led to perceptions of an inequitable distribution of claims among different classes of creditors. The article also examines provisions of the IBC that lack standards of procedural fairness and proposes changes to improve the existing regulations.

The working paper, India's Sustained Economic Recovery Will Require Changes to Its Bankruptcy Law, authored by Anirudh Burman, analyzes India's economic slowdown due to the COVID-19 lockdown and its impact on IBC matters. The author discusses the policy measures adopted by the Indian government post-lockdown and explores the reasons behind the suspension of IBC provisions. The paper examines issues such as judicial delays, including the insufficient judicial capacity of tribunals to handle IBC cases.

The author also highlights the lack of adequate mechanisms in the Code to allow debtors to retain control during insolvency proceedings and suggests the creation of a debtor-friendly IBC.

The article, Corporate Insolvency: Its Operations and Emerging Problems , authored by Navin K. Pahwa, highlights the challenges arising in the implementation and application of the IBC. The article explores various amendments made to the Code over time and the evolving judicial interpretations related to it. The author discusses operational and practical issues encountered during the continuation of business operations, the limitation period, and other related matters. Additionally, the article offers suggestions for appropriate modifications to address these challenges.

The article, The Insolvency and Bankruptcy Code – Not a Brittle Framework, authored by Sourav Sardar, examines the role of government intervention in the working structure of the Code. The author discusses amendments related to financial institutions, standing committee reports, and associated legal challenges. The article also addresses the steps taken by the government and judiciary to strengthen the Code, issues surrounding the commercial wisdom of the Committee of Creditors (CoC), the importance of adhering to timelines, and the overriding effect of the Code.

The article, IBC 2.0 in the Making: A Relook into the Insolvency Regime in India, co-authored by Sandeep Parekh and Sudarshana Basu, highlights the significant developments in the Code since its enactment. The authors discuss the importance given to the Committee of Creditors (CoC) by the judiciary and examine the provisions in the Code that differentiate between financial creditors and operational creditors. Additionally, the article explores areas such as the withdrawal of the corporate insolvency process and provides a roadmap for future reforms in the IBC.

CORPORATE INSOLVENCY

A company becomes insolvent when it defaults on payment or is unable to pay its debts[1]. The Corporate Insolvency Resolution Process (CIRP) is a process through which the insolvency of the corporate debtor is resolved in accordance with the provisions of the Insolvency and Bankruptcy Code, 2016.

An application can be made to the jurisdictional adjudicating authority to initiate the Corporate Insolvency Resolution Process (CIRP). The outcome of this application could result in the resolution of the corporate debtor, or if the CIRP fails, the corporate debtor may proceed into the liquidation process.

Financial Creditors, Operational Creditors, or the corporate debtor himself may initiate the Corporate Insolvency Resolution Process (CIRP) when a corporate person commits a default. An insolvency application is limited to a single corporate person.

For initiating CIRP, "Default" refers to the non-payment of debt when any part or installment of the amount becomes due and payable, and the corporate debtor fails to make the payment. "Debt" refers to a liability or obligation related to a claim that is due from any person, including both financial and operational debt.

[1] *KRISTIN VAN ZWIETEN, GOODE ON THE PRINCIPLES OF CORPORATE INSOLVENCY LAW (5th ed., Sweet & Maxwell) (2018).*

FINANCIAL CREDITOR UNDER IBC

A Financial Creditor for the Corporate Insolvency Resolution Process (CIRP) refers to any person to whom a financial debt is owed, including those to whom such financial debt has been legally assigned or transferred[2]. A financial creditor, either individually, jointly with other financial creditors, or through any other person acting on their behalf, may initiate the insolvency process by applying to the adjudicating authority when a default in the payment of debt has occurred[3]. Financial creditors can be either secured or unsecured when starting the Corporate Insolvency Resolution Process (CIRP). Under Section 7(1) of the Insolvency and Bankruptcy Code (IBC), a financial creditor can initiate CIRP for a default of financial debt owed by the corporate debtor, even if the debt is not owed to the applicant[4].

A financial creditor shall submit the required documents along with the application as per Section 7(3) of the Insolvency and Bankruptcy Code (IBC) and Rule 4 of the Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016. The documents to be provided include a record of the default, which can be obtained from the information utility or other evidence of default as specified. Additionally, the financial creditor must provide the name of the Interim Resolution Professional and any other information prescribed by the Insolvency and Bankruptcy Board of India (IBBI).

Upon receiving the required information, the Adjudicating Authority (AA) verifies the following: the existence of a default in debt payment from the record of the Information Utility (IU) and other evidence, whether the application satisfies all prescribed requirements, and if there are any disciplinary proceedings pending against the proposed Interim Resolution Professional (IRP). The AA is required to accept or reject the Corporate Insolvency Resolution Process (CIRP) application within 14 days of receiving it. If the application is incomplete, the AA will notify the applicant and allow them seven days to rectify the errors[5].

OPERATIONAL CREDITOR

An operational creditor refers to any person to whom an operational debt is owed, including a person to whom such debt has been legally assigned or transferred. An operational debt pertains to claims related to goods and services[6], which include workmen's dues, employment dues, and payments arising under any law[7], such as taxes payable to the central government, state government, or any local authority.

An operational creditor may initiate the Corporate Insolvency Resolution Process (CIRP) under Section 9 of the IBC. However, before initiating the process, the operational creditor must first send a demand notice to the corporate debtor upon the occurrence of default, requesting the payment of the unpaid amount involved in the default.

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[2] *ASHISH MAKHIJA, INSOLVENCY AND BANKRUPTCY CODE OF INDIA (1st ed., 2018)*
[3] *ADITYA SHIRALKAR, COMMENTARY ON THE INSOLVENCY AND BANKRUPTCY CODE, 2016 (1st ed., 2021).*
[4] *Innoventive Industries Ltd. v. ICICI Bank & Another, (2018) 1 SCC 407.*
[5] *Rajinder Kapoor v. Anil Kumar, 2017 SCC OnLine NCLAT 263.*
[6] Mazdoor Morcha v. Juggilal Kamlapat Jute Mills Co. Ltd., (2019) 11 SCC 332.
[7] RMS Employees Welfare Trust v. Anil Goel, 2019 SCC OnLine NCLAT 300.

A corporate debtor shall within ten days of receiving a demand notice, bring to the attention of the operational debtor, the existence of any pre-existing dispute or suit or arbitration proceedings relating to the dispute, including the challenge to the arbitration award, before the notice is received, or evidence that unpaid amount has been settled[8].

If the corporate debtor fails to make the payment or does not provide a notice of the pre-existing dispute within 10 days of receiving the demand notice, the operational creditor may proceed with filing the insolvency application before the adjudicating authority.

An operational creditor must submit the required documents along with the application under Section 9(3) of the Code and Rule 6 of the Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016. If the application is incomplete, the AA will issue a notice to the applicant to rectify the errors within seven days of receiving the notice.

CORPORATE APPLICANT

A corporate applicant refers to the following entities or individuals who are authorized to initiate the Corporate Insolvency Resolution Process under the Insolvency and Bankruptcy Code, 2016:

1. Corporate Debtor: The company or entity that is facing insolvency.
2. Member or Partner of the Corporate Debtor: A member or partner who is authorized under the constitutional document (such as the articles of association or partnership agreement) of the corporate debtor to make an application for CIRP.
3. Individual in Charge of Operations: An individual responsible for managing the operations and resources of the corporate debtor.
4. Person in Control of Financial Affairs: A person who has control or supervision over the financial affairs of the corporate debtor.

This category of applicants is essential for initiating CIRP and ensuring that the process is handled by those with the authority to represent the corporate debtor.

A Corporate Applicant can initiate the CIRP by filing an application with the adjudicating authority if the corporate debtor defaults on its debt obligations.

[8] *K. Kishan v. M/s. Vijay Nirman Company Pvt. Ltd., 2017 SCC OnLine SC 1665; see also Navin K. Pahwa, Corporate Insolvency: Its Operations and Emerging Problems, 30 NAT'L L. SCH. INDIA REV. 111 (2018).*

'CREDITOR IN CONTROL' MODEL

Under the Insolvency and Bankruptcy Code, 2016, a significant shift in control takes place when a Corporate Insolvency Resolution Process is initiated. This shift is from the concept of 'debtor in possession' to 'creditor in control'[9].

Once the Corporate Insolvency Resolution Process (CIRP) is initiated, the adjudicating authority imposes a moratorium to protect the corporate debtor and its assets. It serves the purpose of preserving the status quo, rather than creating new rights concerning the corporate debtor[10]. Its objective is to protect the assets of the corporate debtor, ensuring they remain intact for the benefit of the creditors and to facilitate the maximization of the value of those assets. The moratorium remains in effect throughout the Corporate Insolvency Resolution Process.

During the moratorium, the Directors cannot sell company assets or use funds in Bank for any purpose. It will attract penal provisions under Section 74 of the Code[11].

The moratorium imposed will cease to have effect either when the adjudicating authority approves the resolution plan or when it passes an order for the liquidation of the corporate debtor. This marks the end of the protection provided by the moratorium, allowing the resolution process or liquidation to proceed without further suspension of legal actions or proceedings.[12]

RESOLUTION PROFESSIONAL AND INTERIM RESOLUTION PROFESSIONAL

On the commencement date of insolvency, the adjudicating authority appoints the Interim Resolution Professional as proposed in the CIRP application. Following this, the Committee of Creditors has the authority to either confirm the IRP as the Resolution Professional or replace the IRP with another RP by a majority vote of not less than seventy-five percent. This process ensures that the resolution process is managed by a professional with the confidence and support of the creditors.

Interim Resolution Professionals and Resolution Professionals are granted administrative powers rather than judicial powers under the Insolvency and Bankruptcy Code[13]. The IRP, upon the commencement of the Corporate Insolvency Resolution Process, takes over the management of the corporate debtor's affairs. Once the Resolution Professional is appointed by the Committee of Creditors, he or she continues to manage the corporate debtor's affairs, ensuring the insolvency resolution process is carried out effectively in accordance with the provisions of the IBC.

The Interim Resolution Professional is entrusted with various critical functions during the Corporate Insolvency Resolution Process. These include issuing public announcements regarding the initiation of

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[9] *M S Sahoo, Here's How IBC 2016 Has Taken Corporate Governance to New Heights, Financial Express, Feb. 30, 2020, www.financialexpress.com/opinion/heres-how-ibc-2016-has-taken-corporate-governance-to-new-heights/1866199/.*
[10] *M/s Embassy Property Developments Pvt. Ltd. v. State of Karnataka and Others, 2019 SCC OnLine SC 1542.*
[11] Ssarvi Resolution Services LLP Resolution Professional of Supreme Transport Organisation Private Limited Vs. Kamalkumar Agarwal and Others
[12] Rajendra K. Bhutta v. Maharashtra Housing and Area Development Authority and Another, 2020 SCC OnLine SC 292
[13] *Swiss Ribbons Case*

CIRP and inviting creditors to submit their claims. The IRP is also responsible for gathering comprehensive information about the debtor's assets, financial status, and operations, collecting claims from creditors, and forming the Committee of Creditors. Additionally, the IRP assumes custody and control of the corporate debtor's assets and manages them as required. Importantly, during the moratorium period, the corporate debtor's assets are protected, and any transfer, alienation, or sale of these assets to third parties is strictly prohibited to maintain their integrity for the resolution process[14].

The Resolution Professional is tasked with overseeing the entire insolvency process, including the submission and approval of the resolution plan for the corporate debtor. Among the critical responsibilities of the Interim Resolution Professional is the formation of the Committee of Creditors. The IRP establishes the CoC after consolidating all claims submitted against the corporate debtor and assessing its financial standing, ensuring the proper representation of creditors in the resolution process.

CONSTITUTION OF COMMITTEE OF CREDITORS

The Committee of Creditors consists of all financial creditors of the corporate debtor, including both secured and unsecured creditors. However, related parties of the corporate debtor are explicitly prohibited from participating, representing, or exercising voting rights within the CoC. This inclusive structure aims to foster a collective approach among financial creditors, promoting unified and efficient insolvency resolution rather than fragmented individual proceedings[15].

DIFFERENTIAL TREATMENT BETWEEN OPERATIONAL CREDITORS AND FINANCIAL CREDITORS

Under the Insolvency and Bankruptcy Code, voting rights within the Committee of Creditors are allocated differently for financial creditors and operational creditors. Financial creditors are given voting rights in proportion to the financial debt owed to them by the corporate debtor. This means that the greater the debt a financial creditor holds, the higher their voting power in the decision-making process within the CoC.

On the other hand, operational creditors do not have any voting rights in the CoC. While operational creditors are entitled to be represented and have a say in certain matters, they are excluded from voting on key decisions, such as approving or rejecting the resolution plan. The rationale behind this distinction is that financial creditors are typically seen as having a larger stake in the outcome of the insolvency process due to the nature of their financial claims and the potential for greater loss in the event of liquidation[16].

Under the Insolvency and Bankruptcy Code, financial creditors have the right to initiate the Corporate Insolvency Resolution Process on their own or jointly with other financial creditors upon the occurrence of a default. This gives them an immediate right to file an insolvency application, reflecting their significant financial stake in the corporate debtor's ability to repay debts.

[14] *Commissioner of Customs, (Preventive) West Bengal v. Ram Swarup Industries Ltd. and Others, 2019 SCC OnLine NCLAT 371.*
[15] *Municipal Corporation of Greater Mumbai (MCGM) v. Abhilash Lal and Others, 2019 SCC OnLine SC 1479.*
[16] *Niddhi Parmar, Difference between Operational Creditors and Financial Creditors, (2019), vinodkothari.com/wpcontent/uploads/2019/06/Difference-between-OC-FC.pdf.*

However, operational creditors face a different process. While they can file for CIRP, they must first deliver a demand notice to the corporate debtor for the unpaid debt. If the corporate debtor fails to make the payment or provide a notice of dispute within 10 days of receiving the notice, the operational creditor can then initiate the insolvency process. This requirement creates a distinction between financial and operational creditors under the Code, as operational creditors must first provide an opportunity for the corporate debtor to resolve the issue before resorting to insolvency proceedings. This pre-condition to the right of operational creditors to initiate CIRP is seen as a form of discrimination under the Code, as it imposes additional procedural hurdles on operational creditors compared to financial creditors.

Under the Insolvency and Bankruptcy Code, when filing an insolvency application with the tribunal, financial creditors are required to propose the name of the Interim Resolution Professional. This is a mandatory step for them as part of their application process.

On the other hand, operational creditors are given the option, but not the obligation, to propose the name of the IRP when filing their insolvency application. While operational creditors can suggest an IRP, it is not mandatory for them to do so.

This distinction reflects the greater influence and control that financial creditors have in the insolvency process, as they are more likely to be the primary drivers of the resolution proceedings, while operational creditors have less say in the appointment of the IRP[17].

Under the Insolvency and Bankruptcy Code, the Committee of Creditors is exclusively composed of financial creditors of the corporate debtor. This means that only financial creditors, such as those holding secured or unsecured debts, are included in the CoC. Operational creditors, despite being owed money, are not part of this committee and do not have any voting rights or influence in the decision-making process within the CoC.

This structure highlights the primary role of financial creditors in driving the insolvency resolution process, given their larger financial stake in the debtor's recovery or liquidation. Operational creditors, while crucial for the debtor's operations, are excluded from the CoC, which limits their involvement in major decisions regarding the insolvency process[18].

Under the Insolvency and Bankruptcy Code, financial creditors are required to submit financial information to an Information Utility concerning the assets for which any security interest has been created. This submission is a mandatory requirement for financial creditors as part of the process to verify their claims and establish the extent of their financial interest in the debtor's assets.

On the other hand, operational creditors are not subject to this mandatory obligation. They are not required to submit any information to the Information Utility, making the process optional for them. This distinction arises because financial creditors, with their secured interests and larger financial stakes, are considered to

[17] *Chharia Holdings v. Brys International, 2017 SCC OnLine NCLAT 365.*
[18] *Akshay Jhunjhunwala & Anr. v. Union of India through the Ministry of Corporate Affairs & Ors., AIR 2018 Cal 139*

play a more pivotal role in the insolvency process compared to operational creditors, who primarily deal with goods and services provided to the corporate debtor.

The Supreme Court, in its judgments, has addressed the issue of classification between financial creditors and operational creditors under the Insolvency and Bankruptcy Code, 2016. In upholding the constitutionality of the Code, the Court affirmed that the distinction made between financial creditors and operational creditors is not discriminatory, arbitrary, or violated Article 14 of the Constitution of India, which ensures equality before the law.

The Court recognized that the classification serves a legitimate purpose under the IBC, as financial creditors, who typically deal with substantial financial transactions and secured debts, hold a different position from operational creditors, who are often unsecured and have claims arising from the supply of goods and services. The Supreme Court concluded that this differentiation is reasonable and justified, as it reflects the differing nature of the interests and claims involved, thus not violating the principle of equality under the Constitution.

INSIGNIFICANT REPRESENTATION OF OPERATIONAL CREDITORS IN COMMITTEE OF CREDITORS

Under the framework of the Insolvency and Bankruptcy Code, the Committee of Creditors is composed solely of financial creditors. Operational creditors are only granted representation in the CoC in cases where the corporate debtor has no financial creditors[19]. However, operational creditors do not have voting rights during CoC meetings, which limits their influence over decision-making processes.

Additionally, the rights of operational creditors to attend meetings of the CoC are also restricted under the Code. Their involvement is therefore minimal, primarily serving to ensure that their interests are considered in the context of insolvency resolution, but without the same level of participation or authority as financial creditors. This distinction further reinforces the different roles and interests of financial and operational creditors within the insolvency process.

Operational creditors or their representatives may attend the meetings of the Committee of Creditors only if their aggregate dues amount to at least ten percent of the total debt owed by the corporate debtor. This condition highlights that, in general, operational creditors do not have representation or a say in the decision-making process of the CoC. Given their limited role in the CoC, the protection of their rights becomes a critical issue when analyzing the Insolvency and Bankruptcy Code, as they are often at a disadvantage compared to financial creditors in the insolvency resolution process.

EQUALITY FOR ALL: APPLICABLE OR NOT?

The Supreme Court affirmed that the principle of 'equality for all' does not apply to the rights of financial creditors and operational creditors in the same manner. It noted that the Insolvency and Bankruptcy Code

[19] Sudip Mahapatra, Pooja Singhania & Misha Chandna, Operational Creditors In Insolvency: A Tale of Disenfranchisement, (2020), www.snrlaw.in/operational-creditors-in-insolvency-a-tale-of-disenfranchisement.

does not require equal treatment of creditors who are differently situated. Instead, the Code mandates equitable treatment within each class of creditors, recognizing that financial creditors and operational creditors may have distinct rights and priorities, which are addressed separately under the law[20].

The principle of equitable treatment aims to ensure that creditors who are similarly situated and have identical rights are treated fairly during the collective proceedings related to the distribution of claims and interest. The rationale behind not treating all creditors in the same manner under the Code lies in the fact that creditors enter into different types of debt arrangements with the corporate debtor[21]. As a result, their rights, priorities, and entitlements differ, making it necessary to provide distinct treatment based on the nature of their debt agreements.

The Supreme Court acknowledged the critical role of operational creditors under the Code, as they contribute to the functioning of the corporate debtor's business as a going concern. If the Code were to adopt the equality principle for all creditors, it could incentivize secured financial creditors to vote for liquidation rather than pursuing a resolution. This would undermine the primary objective of the Code, which is to facilitate the resolution of distressed assets. The Code prioritizes resolution, and liquidation is intended to be the last resort when resolution efforts fail.

Despite the efforts made by Parliament to provide equitable rights to operational creditors under the Code, significant issues remain unaddressed. These include concerns about the representation of operational creditors, the differential treatment they face when initiating the insolvency process, the handling of disputed claims, and their limited participatory rights within the Committee of Creditors. Although some modifications have been introduced to improve the position of operational creditors, these changes are still insufficient to fully protect their rights in line with the broader objectives of the Code. The ongoing challenges highlight the need for further reforms to ensure fair treatment of operational creditors in insolvency proceedings.

COMMERCIAL WISDOM OF COMMITTEE OF CREDITORS: PARAMOUNT & SUPREME

The Supreme Court has emphasized that the ultimate control over corporate insolvency lies in the hands of the majority vote of the Committee of Creditors. In line with this, the adjudicating authorities, namely the National Company Law Tribunal (NCLT) and the National Company Law Appellate Tribunal (NCLAT), have limited powers of judicial review regarding the decisions made by the CoC during the insolvency process. Their role is specifically confined to considering the legal and procedural aspects of the resolution plan, rather than delving into its commercial aspects.

[20] *Essar Steel Case, supra note 65; see also, Sandeep Parekh & Sudarshana Basu, IBC 2.0 in the Making: A Relook into the Insolvency Regime in India, 45(2) The Journal for Decision Makers 115 (2020).*

[21] Legislative Guide on Insolvency Law, United Nations Commission on International Trade Law, United Nations Publication, 10 (2005).

Legislative authorities have deliberately not provided adjudicating authorities with the jurisdiction or authority to scrutinize or assess the commercial decisions taken by the CoC. This means that the NCLT or NCLAT cannot question the reasons behind the CoC's rejection or approval of a resolution plan. Their role is to ensure that the resolution plan complies with the legal requirements of the Insolvency and Bankruptcy Code, and not to evaluate the fairness or commercial wisdom of the creditors' decisions[22].

ISSUE FOR CONSIDERATION

The issue at hand is whether adjudicating authorities have the authority to intervene when the Committee of Creditors fails to exercise its commercial wisdom in approving or rejecting a resolution plan. As per the Insolvency and Bankruptcy Code, the CoC's decision is usually considered based on its commercial wisdom, and the role of adjudicating authorities, such as the National Company Law Tribunal (NCLT), is generally limited to ensuring compliance with the statutory requirements.

However, in certain situations, where the CoC's decision is found to be illogical, unreasonable, or lacking in commercial prudence, the adjudicating authorities do have the power to intervene. In one case, the tribunal held that it could reverse the CoC's decision if the resolution plan lacked any element of commercial wisdom or ordinary prudence. This means that while the CoC is given significant discretion in its decision-making, it is not immune to scrutiny if its decision appears to be irrational or not in line with the Code's objectives.

Once it is established that the CoC's decision lacks commercial wisdom, the adjudicating authority can review the plan, and no extraneous interference will occur. In such a case, the tribunal is expected to examine whether the CoC's decision meets the fundamental requirements of maximizing value for creditors and ensuring fairness.

While the adjudicating authorities have this authority, it is essential to have a clear judicial precedent or possibly a legislative amendment to provide more clarity on the circumstances under which the CoC's commercial wisdom can be challenged. The absence of a clear precedent from the Supreme Court or specific provisions in the law may lead to ambiguity regarding the scope of judicial review and the standards of commercial wisdom to be applied in such cases. Therefore, a clearer guideline from higher courts or legislative amendments may be required to address these concerns effectively.

CONCLUSION AND SUGGESTIONS

The Insolvency and Bankruptcy Code (IBC), 2016, is a monumental reform in India's economic and legal landscape, consolidating various fragmented insolvency laws into a comprehensive framework. The Code's introduction marked a paradigm shift, aiming to create a unified mechanism to address corporate insolvency and bankruptcy in a time-bound and efficient manner. By focusing on the resolution of financial distress, the Code seeks to provide a structured approach for corporate debtors to eliminate unsustainable debts while ensuring creditor recovery.

[22] *K. Sashidhar vs. Indian Overseas Bank & Others, 2019 SCC OnLine SC 257.*

Corporate Insolvency Resolution and Its Objectives

The Corporate Insolvency Resolution Process (CIRP), central to the Code, is intended to rehabilitate financially viable businesses and facilitate the exit of non-viable firms. Its primary aim is to strike a balance between supporting distressed corporate entities and ensuring creditors recover their dues. CIRP envisions a recovery mechanism that is not only efficient but also time-bound, fostering an ecosystem that enables the smooth flow of credit in the market.

However, while the Code's objectives are ambitious, its practical implementation has highlighted several challenges. Despite the large-scale litigation it has attracted in a short period, the judiciary has shown considerable restraint in questioning the provisions or amendments of the Code. Courts have generally left such matters to the legislature, underscoring the complexities of balancing economic policy with judicial intervention.

There are many challenges in the implementation of the Code. Since its enactment, the IBC has faced numerous hurdles, particularly in its operational and procedural aspects:

1. **Uniform Default Threshold for All Creditors**: The Code prescribes a single threshold for default amounts to initiate insolvency proceedings, applicable to all types of creditors whether financial or operational. This uniformity has been criticized for failing to account for the differing circumstances and needs of various creditors. Financial creditors, such as banks and lending institutions, are often better equipped to handle defaults compared to operational creditors, who may lack the resources to pursue insolvency litigation effectively.
2. **Favoritism Toward Financial Creditors**: Several provisions of the Code are perceived as favoring financial creditors, often at the expense of operational creditors. For instance, operational creditors are excluded from decision-making in the Committee of Creditors, limiting their role to claim submission and receipt of equitable treatment during resolution plan distribution. This imbalance has led to concerns about the equitable representation of all stakeholders.
3. **Ambiguity in Management Roles During Insolvency**: The suspension of the Board of Directors (BoD) upon the appointment of an Interim Resolution Professional has raised questions about the exclusion of management from insolvency proceedings. While the IRP assumes control, they may lack the in-depth knowledge of the corporate debtor's business that the BoD or management possesses, potentially impacting the formulation of effective resolution plans.
4. **Judicial Intervention and Commercial Wisdom of the CoC**: Courts have consistently upheld the CoC's commercial decisions, emphasizing minimal judicial interference. However, this deference to the CoC has led to debates about the limited scope of judicial review, especially in cases where the CoC's decisions may be influenced by extraneous factors or bad faith.
5. **Litigation Exposure and Delays**: The Code has witnessed a surge in litigation, with stakeholders often contesting procedural and substantive aspects of insolvency proceedings. These legal

challenges, coupled with systemic delays, undermine the Code's goal of providing swift resolutions.

On the basis of the research, following suggestions and recommendations can be adopted by the government in its legal framework to address these challenges and ensure the effective functioning of the IBC.

- **Differential Default Thresholds**: The legislature could consider introducing varying default thresholds based on the nature of the creditor or debtor. For instance, operational creditors might benefit from a lower threshold, ensuring greater access to insolvency remedies.
- **Pre-Packaged Insolvency Processes**: A pre-packaged insolvency framework, allowing out-of-court settlements with debtor involvement in resolution planning, could streamline proceedings. This approach could be particularly beneficial in reducing delays and litigation while promoting collaborative solutions.
- **Enhanced Representation for Operational Creditors**: Operational creditors could be granted participatory rights, including voting power in the CoC, to ensure diverse perspectives in decision-making. This would enhance their role and address concerns about perceived favoritism toward financial creditors.
- **Clarity in Judicial Review**: The legislature or higher courts could establish clearer guidelines for judicial intervention, particularly in cases where the CoC's decisions are influenced by mala fide intentions or extraneous factors. Transparent criteria would strengthen the accountability of all stakeholders.
- **Management Participation in Insolvency:** Policymakers should consider allowing limited participatory roles for the corporate debtor's management during insolvency proceedings. While safeguarding creditors' interests, this would leverage the management's business acumen and ensure resolutions that align with the debtor's operational realities. Exceptions could be made for cases involving fraudulent practices or bad faith by the management.