

Corporate Insolvency Resolution Process (CIRP) – RP's Risks and Challenges

June 2019



Overview: Essar Steel India Limited

Company Overview

- An integrated steel producer with an installed steel making capacity of 9.6 MTPA
 - In top 4 steel manufacturers in India and is the largest integrated steel manufacturer in West India
- Manufacturing operations are strategically located in Western India in close proximity to the major steel market
- Product portfolio includes hot rolled, cold rolled, galvanised and colour coated coils, plates, pipes, etc.
- 7 service centres in various parts of India

Facilities Overview

- Manufacturing facilities primarily comprise:
 - Beneficiation (Odisha and Chhattisgarh) and pelletization plants (Odisha and Andhra Pradesh)
 - Integrated steel complex situated in Hazira, Gujarat Downstream capability hub located in Pune
- Power, ports, shipping are owned by separate legal entities which are not owned by ESIL

ROLE OF THE IRP/ RESOLUTION PROFESSIONAL

- Section 17: Manage the affairs of the corporate debtor
- Section 18: IRP Professional to perform *inter alia* the following duties:
- Collect all financial information relating to the corporate debtor;
 - Receive and collate all claims submitted by creditors; and
 - Constitute committee of creditors (“**CoC**”)
- Section 20: Manage the operations of the Corporate Debtor as a going concern to protect and preserve the value of the Corporate Debtor.
- Section 23: Carry out the entire **CIRP** and manage the operations of the CD
- Section 25: Resolution Professional to perform *inter alia* the following duties:
- Preserve and protect the assets of the Corporate Debtor;
 - Maintain an updated list of claims;
 - Convene and attend all meetings of the CoC;
 - Invite prospective resolution applicants to submit a resolution plan
 - Present all resolution plans at meetings of the CoC

ROLE OF IRP/RESOLUTION PROFESSIONAL

- Section 30(2): Examine each resolution plan to confirm that the plan
Does not contravene any provisions of law
- Section 30(3): Present to the CoC such resolution plans which confirms to the
requirements under Section 30(2) of the Code
- Section 30(6): Submit the resolution plan approved by the CoC to the Adjudicating
Authority for its approval
- Section 28 Prior approval of CoC required for certain actions

Various Risk Buckets resulting in loss of value, litigations, delayed resolution



Various Risks/Potential Litigations emanate from

- 1
 - Differing objectives of various stakeholders, Non-cooperation from certain members – Build consensus

- Compliances issues
- 2
 - Time bound process hence quick decision making
 - Limited Information availability

- Operational issues – may impact ‘Going Concern’ : First few months critical
- 3
 - Related Parties issues
 - Protection & Preservation of assets

- 4
 - Claims of creditors – Amount, disputes, payment etc.

- 5
 - Ongoing and new litigations by Creditors
 - Resolution Plan related from Resolution Applicants (RFP, 29A) etc

Clarity of Role of IRP/RP – Various Relevant Orders

- ESIL SC Order Oct 4, 2018 : RP is not required to take any decision, but merely to ensure that the Res Plans submitted are complete in all respect before they are placed before CoC
- RP to only “examine” and “confirm” that each Res Plan conforms to Sec 30(2)
- RP only required to give a prima facie opinion to the CoC on 29A eligibility – supplemented by Swiss Ribbons SC order
- RP only to provide his prima facie opinion to CoC that a law has not been contravened
- Binani NCLAT Order - Approval of the ‘Resolution Plan’ is in the domain of the ‘CoC’ and not that of ‘RP’ and, therefore, if the ‘Resolution Plan’ provides for the mandatory contents and is in accordance with the ‘I&B Code’ even if in case a ‘Resolution Plan’ does not provide for full satisfaction of claims of ‘OCs’, in absence of any power of the ‘RP’ to reject such ‘Resolution Plan’, the ‘RP’ cannot be blamed
- Swiss Ribbons SC Order- RP is a facilitator of the Resolution Process, whose administrative functions are overseen by the CoC and by the AA
- Swiss Ribbons SC Order- RPs have no adjudicatory (quasi-judicial) powers unlike Liquidators whose determination of claim is a decision

Communication – Key to Success

- 1 - Dissemination of information of initiation of CIRP

- Explain impact to various stakeholders
- Structured reviews with Executive Management
- 2 - Promoters, Directors, KMPs, Banks, suppliers, customers
- Committee of Creditors

- Roles as per IBC to be clearly communicated in writing
- 3 - Make aware of consequences of non-compliance (Sec 19) and failure of Resolution Process – Liquidation

- Statutory Authorities – Moratorium under Section 14
- 4 - Coercive action by authorities

- 5 - Authorizations and signatories

Managing as 'Going Concern'

1 - Control of bank accounts and collections

2 - Focus on liquidity

3 - Pre-payment checks
- Prioritization of payments – critical v. urgent
- Tagging/recovery by banks during CIRP not permitted
- Opening of LCs/BGs, Bill discounting, etc.

4 - Normal capex

5 - Interim Finance

Compliances

- IBBI Circular dated January 3, 2018 – IP to ensure compliance with provisions of the applicable laws
- IP shall exercise reasonable care and diligence and take all necessary steps to ensure that the CD undergoing process complies with the applicable laws
- Compliances can be differentiated into monetary and non-monetary ones
- Sec 17(2)e inserted by way of IBC II Amendment, 2018 as per which RP vested with management of CD to be responsible for complying with the requirements under any law for the time being in force on behalf of the CD

Income Tax

- Sec 140 of Income Tax Act , 1961- Where in respect of a company, an application for CIRP has been admitted by Adjudicating Authority under IBC, the return shall be verified by the IP appointed by such Adjudicating Authority
- Rule 45(3) of IT Rules, form of appeal to be signed by a person who is authorised to sign the return under Sec 140 of the IT Act.

Regulatory Compliances

- 1 - Factory Occupier, Plant related compliances
 - 2 - Issues with statutory authorities & their claims
 - 3 - Companies Act, Annual Accounts, Listing requirements
 - 4 - Reporting to IBBI/NCLT/IPA
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Verification of Claims – Various Relevant Orders

- ESIL NCLT Order dated March 8, 2019 – Role and duty of RP is to collate the information by verifying the claims and update it in the list of creditors and place it before the CoC for its consideration
- RP has not been vested with the power of adjudicating the claim such issues can be dealt with and decide by a competent court/authority.
- Sec 5(7) and 5(20) of IBC – creditors include to whom debt has been **legally** assigned
- All assignments to be legally reviewed as same will impact constitution of CoC and amount of claims
- Fortune Pharma Order- if the assignor is a related party then the assignee shall also be treated in the same status as 'related party' vis-à-vis to the impugned debt
- Pankaj Yadav v. SBI dated 07.08.2018 NCLAT Order- Rights of assignee are no better than those of assignor. Rights and disadvantages also goes along with such assignment
- Related party FC does not have right to be part of CoC and therefore can't vote on assignment

Legal Advisors to RP – Very Critical Role

- 1 - Multi-disciplinary skills – Banking docs, litigations, commercial, etc.

- 2 - Experience in running sale process, due diligence, etc.
- Documents – Simple, no ambiguity

- 3 - Pro-active, prompt advice/opinion rather than reactive one with focus on reduced litigation

- 4 - Up to date with various precedents resulting in quicker decision

- 5 - Independent /No conflict

Challenges to the Resolution Process

Challenges & Difficulties faced

- Res Plan being challenged at various stages – Late bids, 29A eligibility, etc
- Myriad litigations thereby moving away from resolution and resultant delays in resolution due to cross-allegations by the rival resolution applicants
- SC held in ESIL that a resolution applicant has no vested right that his resolution plan be considered by the CoC, in light of which no challenge can be preferred before the NCLT by a Resolution Applicant, at a stage where (a) the Res Plan has been turned down by the RP for non-compliance of Sec 30(2) of the Code or (b) a Res Plan as presented by RP is not approved by CoC. A challenge can be preferred once a Res Plan is approved by the NCLT, before the NCLAT and thereafter the SC.
- K Sashidhar SC Order dated 05.02.2019: If CoC approves the resolution plan by requisite percentage of voting share, it is imperative for the RP to submit the same to the NCLT

Rights of suspended Board of Directors

- Board members (comprising promoters also) invited to all CoC meetings
- SC in the case of Ruchi Soya held that the scheme of the Code makes it clear that the directors, though not members of the CoC, have a right to participate in every meeting of the CoC
- Further, as vitally interest parties, they have right to receive copies of the Res Plan presented to the CoC

Discharge of Duty of RP

Letter issued by IBBI to RPs stating that while conducting CIRP, an IP is an officer of the Court and discharges a statutory public function. Further, any hindrance in the working of the CIRP will amount to contempt of court (Ref NCLT Order in Shivam Water, Jan 2019)

Sec 233- Protection of action taken in good faith

Code has restricted jurisdiction of the civil courts by Sec 63 and Sec 231

Reg 39(7) - No proceeding to be initiated against RP for any action of the CD, prior to the insolvency commencement date

SC Order* Oct 4, 2018 – Key Findings

Purposive interpretation of S. 29A

- ▶ necessitates the lifting of corporate veil, so as to determine the eligibility of 'person' submitting a resolution plan (*Para 29*) – principle can be applied even to group companies so that one is able to look at the economic entity of the group as a whole (*para 34*)
- ▶ antecedent facts reasonably proximate to the time of submission of resolution plan can always be seen, to determine whether the persons referred to in Section 29A are, in substance, seeking to avoid the consequences of the proviso to sub-clause (c) before submitting a resolution plan (*Para 57*)

Relevant time for disqualification - at the time of submission of the resolution plan (*para 43*)

**ArcelorMittal v. Satish Kumar Gupta & Ors., C.A. Nos 9402-9405*

SC Order Oct 4, 2018 – Key Findings

Interpretation of ‘persons acting jointly or in concert’ - to be seen whether certain persons have got together and are acting “jointly” in the sense of acting together - no super added element of “joint venture” required (Para 35)

Interpretation of “management” and “control”

- ▶ “management” refers to the *de jure* management of a corporate debtor
- ▶ “control”, in Section 29A(c), denotes only positive control, which means that the mere power to block special resolutions of a company cannot amount to control - *de facto* control of actual management or policy decisions (Para 48)

Cure of ineligibility under Section 29A(c) – this ineligibility can only be removed if the resolution applicant makes payment of all overdue amounts with interest thereon and charges relating to the non-performing asset in question before submission of a resolution plan.” (Para 54)

SC Order Oct 4, 2018 – Key Findings

Eligibility of Numetal

- Numetal held ineligible as per S. 29 A (c) for both resolution plans on account of presence of Rewant Ruia, a person deemed to be PAC with Ravi Ruia, promoter of ESIL

Eligibility of AM India

- *Held ineligible as per S. 29 A(c) on account of Uttam Galva*
 - Both AM India and AM Netherlands (promoter of UG) managed and controlled by LN Mittal and are deemed to be a PAC
 - Shares of AM Netherlands in UG were sold at a time reasonably proximate to the date of submission of the Res Plan in order to get out of the ineligibility under Section 29A(c) and its proviso
- *Held ineligible as per S. 29 A(c) on account of KSS Petron*
 - Fraseli, a group company of L N Mittal, exercised positive control over KSS Global and in turn KSS Petron
 - Sale of shareholding in KSS Global a transaction reasonably proximate as in UG

Issues/Appeals before NCLAT

Sr. No.	Particulars
1	Distribution to FCs – Distinction between Secured and Unsecured FCs
2	Distribution to FCs – Distinction amongst secured creditors based on security
3	Share of OCs in Resolution Plan
4	Utilisation of EBITA earned during CIRP
5	Claim against Personal Guarantors

Rewards for stakeholders

Sr. No.	Particulars
1	Production increased from 5.47 MT in 2016-17, 6.18 MT in 2017-18 to 6.78 MT in 2018-19.
2	EBIDTA of about Rs 3500 crore during CIRP period
3	Highest ever monthly production of 0.617 million tonne achieved in Dec 2018
4	Amount of Rs 7,500 crore paid by ArcelorMittal to lenders in October 2018 towards eligibility
5	Plan payment on implementation will be more than 50% of total recovery of Rs 75,000 crore made till March 2019 under IBC (Joint Report by Assocham-Crisil)