

Last Updated: 27 June 2018

Article by [Saket Shukla](#), [Akshay Sachthey](#) and [Debottam Chattopadhyay](#)
[Phoenix Legal](#)

The Insolvency and Bankruptcy Code 2016: Time to Wind Up the Winding-up Regime?

The Insolvency and Bankruptcy Code, 2016 (IBC) has impacted companies and assets across various industries and has thrown up a range of opportunities for potential investors. In order to promote investment activity and ensure effective revival of stressed assets, it is critical for the legal framework to be unambiguous and practically workable. While the IBC framework has largely been considered effective so far, there remains a lack of clarity on certain issues that could have practical implications for potential investors and resolution applicants.

This article addresses one such issue – the fate of winding up proceedings pending before High Courts, once an IBC proceeding is subsequently admitted by the National Company Law Tribunal (NCLT).

The New Regime

The IBC introduces the 'corporate insolvency resolution process' (CIRP), an entirely new mechanism that permits defaulting debtors a moratorium period in which to revive their financial woes, under a creditor-in-control approach. The IBC overhauls the regime under the Companies Act, 1956 (**1956 Act**), which provided for winding-up of a company on grounds of its 'inability to pay debts'. The winding-up regime was adjudicated before High Courts, while NCLTs are the adjudicating authority under the IBC.

Transition

The Central Government framed rules (**Transfer Rules**)¹ to determine how pending winding up matters would be dealt with once the IBC comes into force.

The Transfer Rules provided that if a winding up petition had been served on the respondent, the petition would continue before the High Courts under the old regime. If a petition had not been served, it would be transferred to the IBC regime before the NCLTs, subject to the petitioner submitting additional documents. The period for this transition is now over². As on date, matters pending before the High Courts should be those that were required to continue before the High Courts under the Transfer Rules³.

Maintainability of an IBC Action in the face of Winding Up Proceedings

The Transfer Rules did not clarify if fresh proceedings could be initiated under the IBC even where there were pending winding up proceedings for the same debtor company which were being heard

¹ Companies (Transfer of Pending Proceedings) Rules, 2016. The rule in the Transfer Rules relating to transfer of winding-up proceedings has been challenged in the Madras High Court in the matter of Renault Nissan Automotive India Private Limited vs. Union of India (WP 2333 of 2018).

² Winding-up petitioners were required to submit additional documents on or before 15 July 2017, failing which the pending winding up petitions were to abate.

³ The Transfer Rules clarified that where there was even one winding-up proceeding against a company which was to remain before the High Court, then all other pending winding-up proceedings against that company would also have remained with the High Court.

by the High Courts (i.e., winding up proceedings which were not transferred pursuant to the Transfer Rules).

In this regard, a 3-member bench of the NCLT, Principal Bench, New Delhi⁴, has recently held that there is no bar imposed on NCLTs to admit an IBC petition despite pendency of a winding up petition, unless an official liquidator has been appointed and a winding up order has been passed. By implication, where the preceding two conditions are met, an IBC petition would not be maintainable.

The 3-member bench did not clarify what would be the fate of such a pending winding up proceeding, if a subsequent IBC action is admitted.

Moratorium under the IBC

Section 14 of the IBC provides that upon admission of an IBC petition, there would be a moratorium on institution or continuation of pending suits or proceedings against the debtor, including execution proceedings in any court of law, tribunal, arbitration panel or other authority. Section 14 appears to be wide enough to cover pending winding up proceedings and a bare reading of the section suggests that the moratorium would apply to such winding up proceedings. However, Section 14 uses the words "suits or proceedings" and it could be argued that the moratorium under this section was intended to apply only to proceedings that are in the nature of suits.

High Courts appear to have taken conflicting views on the issue. The High Court of Judicature at Hyderabad⁵ has held that an inferior/subordinate tribunal like NCLT, which is constituted under the Companies Act, 2013, cannot grant an injunction on institution/prosecution of proceedings in superior courts like High Courts⁶, which are constituted under the Constitution.

There could be arguments in counter to the above decision. For instance, it can be argued that the High Courts, while adjudicating on winding up matters, are exercising their jurisdiction as a company court under the 1956 Act. Additionally, the IBC provides that it overrides all other laws⁷ and it could be argued that the moratorium under Section 14 should prevail over a pending winding up proceeding under the 1956 Act.

The Bombay High Court, in a later decision, has taken a contrary view and held that the NCLT is not subordinate to the High Court. The Bombay High Court⁸ observed that post-notice winding up petitions (i.e., petitions which have been served on the respondent) are to continue before the High Courts, but this did not bar a new proceeding from being filed under IBC and also indicated that a moratorium order passed by NCLT under Section 14 would apply to such post-notice winding up petitions.

What it Means for Investors and Resolution Applicants

Both the High Court decisions discussed above are in appeal. Until the issue is resolved, it seems that there will be some uncertainty in IBC processes involving corporate debtors who are faced with prior

⁴ Order dated 16 February 2018 passed in Union of India v. Era Infra Engineering Ltd. (C.P. No. (IB)-190(PB)/2017). The 3-member bench was constituted specifically to examine the issue of whether IBC proceedings are maintainable in the face of pending winding up proceedings.

⁵ Paharpur Cooling Towers Ltd. v. Basal Steels and Power Pvt. Ltd. (2017 5 ALD 695).

⁶ The decision, amongst other things, draws reference to Section 41(b) of the Specific Relief Act, 1963, which provides that a subordinate court cannot grant an injunction to restrain a person from instituting or prosecuting any proceeding in a higher (not subordinate) court.

⁷ Section 238 of the Insolvency and Bankruptcy Code, 2016.

⁸ Jotun India Pvt. Ltd. and Ors. v. PSL Limited (2018 145 SCL 601 (Bom)).

winding up actions. This lack of certainty is far from ideal for a potential investor or resolution applicant looking to acquire targets or assets that are subject to the IBC processes.

Another potential implication is that even after a resolution plan is approved and IBC proceedings end, a pending winding up proceeding that predates the IBC action, could potentially revive. The Section 14 moratorium remains in force until a resolution plan is approved or a liquidation order is passed by the NCLT. Therefore, theoretically speaking, a winding up proceeding that predates an IBC action, may potentially revive once the resolution plan is approved.

This poses another cause of concern for investors or resolution applicants, who may need to account for the risk of defending previous winding up proceedings while assessing investments in assets and targets that are subject to IBC processes. There could, of course, be practical considerations involved in such a scenario. For instance, if the winding up petitioner has submitted a proof of claim for its debt to the resolution professional (**RP**) under the IBC process, and such debt is provided for under the resolution plan, the cause of action for the winding up proceedings would cease.

Insolvency Law Committee and IBC Ordinance

In November 2017, the Insolvency Law Committee (**Committee**) was constituted to make recommendations on issues arising from the implementation of the IBC and the Committee recently gave its report⁹. In the report, the Committee recognised the need to avoid multiple and possibly conflicting orders in winding up/liquidation proceedings of the same corporate debtor.

Pursuant to the Committee's recommendations, the Insolvency and Bankruptcy (Amendment) Ordinance, 2018 was brought into force and Section 434 of IBC was amended to permit parties to approach the High Court and request for transfer of a pending winding up proceeding to the NCLT under the IBC regime. As per the amendment, once the transfer is granted, the winding up petition would be treated as an application for initiation of CIRP, or, in other words, an IBC petition.

Conclusion: Towards Resolution

While the intent of the amendment seems to avoid conflicting proceedings, it does not appear to provide a workable solution to the problem. The amendment mentions that a winding up petition can be transferred to NCLT and treated as an IBC petition. Accordingly, the amendment proceeds on the basis that a winding up petitioner would apply for a transfer to the IBC regime only where a fresh IBC petition is maintainable, but not where an IBC petition is already admitted. In the latter situation, another IBC petition would not be maintainable and any creditor that wants its debt to be covered in the resolution plan, would need to submit a proof of claim before the RP. Had the amendment clarified that a pending winding up petition can be withdrawn and used as a basis for submitting a proof of claim, perhaps the intent would have been clearer.

Having said that, it is encouraging to see that legislative cognizance is being taken of the ambiguities in the IBC and there appears to be an intent to iron out practical glitches in implementing the intent of the law. Given the pace at which the law is evolving and the volume of IBC cases which are potential sources of precedent, one can be hopeful that the interplay between winding up and the IBC regime will be settled soon.

The views of the authors are personal and not views of Phoenix Legal. The content of this article is intended to provide a general guide to the subject matter. Specialist advice should be sought about your specific circumstances.

⁹ Report of the Insolvency Law Committee dated 26 March 2018.