PRE-PACKAGED INSOLVENCY: TO UPHOLD THE LEGISLATIVE INTENT OR THE LETTER OF THE LAW?

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Pre-packaged insolvency resolution process ("PPIRP") was introduced by amending the Insolvency and Bankruptcy Code ("Code") in April 2021[1]. This currently applies to Micro Small Medium Enterprises ("MSMEs"). This was enacted to provide 'PPIRP' as an alternative to Corporate Insolvency Resolution Process ("CIRP") to mitigate the financial distress caused by the Covid-19 pandemic to MSMEs.

What Is PPIRP?

- The proposal for PPIRP of a corporate debtor must be approved by at least 66% of its financial creditors before the application for PPIRP is filed before the Adjudicating Authority.
- The minimum amount in default must be INR 10,00,000.
- The creditors and the corporate debtor should have previously agreed upon a base resolution plan for the corporate debtor.
- The entire resolution process is required to be completed within 120 days of commencement of PPIRP.

Application of the provisions of Section 11A of the Code vis-à-vis Applications under Sections 7, 9 or 10 and 54C of the Code

Section 11A[2] of the Code deals with where applications against the same corporate debtor have been filed for CIRP as well as PPIRP. It provides as below:

- If during pendency of the PPIRP, an application for CIRP is *filed*, then the Adjudicating Authority *shall* first pass an order to admit or reject the application for PPIRP.
- If within 14 days from the date of filing of an application for CIRP, an application for PPIRP is filed against the same corporate debtor, then the Adjudicating Authority *shall* first dispose of the PPIRP application.
- If after 14 days from the date of filing of an application for CIRP, an application for PPIRP is filed against the same corporate debtor, then the Adjudicating Authority *shall* first dispose of the application for CIRP.
- If an application for CIRP is pending as on 4th April 2021, then the provisions of Section 11A *shall not apply*.

Lacuna in Section 11A of the Code and dilemma addressed by the NCLT

Recently, a preliminary issue arose before the Principal Bench of the National Company Law Tribunal, New Delhi (**"NCLT"**) in the matter of *CHD Developers* Limited [3] on '*Whether a PPIRP application could be entertained, when an application for CIRP was filed on 21st October 2020, i.e., before 4th April 2021 and has remained pending for admission since long before the enactment of PPIRP itself?'*. In this case, during the pendency of an application for CIRP, an application for PPIRP was filed by the same corporate debtor in July 2022.

The NCLT held that since the provisions under the Code regarding the manner of disposal of applications for CIRP and PPIRP are not applicable[4] in the instant case, therefore, the NCLT would not be restrained from considering a CIRP application already filed and pending for admission[5] in precedence over a PPIRP application.

Other factors, specific to the facts of the said case, also weighed in with the NCLT namely, statement of no-objection to initiation of CIRP given by the corporate debtor during pendency of the applications for CIRP, admission of debt and default by the corporate debtor as a pre-condition at the time of filing the PPRIP application and delay in admission of the CIRP applications for no fault of the applicant-creditor.

The NCLT dismissed the application filed for PPIRP and admitted the applications filed for CIRP.

At first glance, Section 11A of the Code seems watertight when it comes to guiding the NCLT in deciding whether an application for PPIRP will be decided first or not. However, in a situation where an application for CIRP is pending as on 4th April 2021, the non-applicability of the provisions regarding the manner of disposal of applications for CIRP or PPIRP [Section 11A(4)], appears to have left a grey area where *prima facie*, neither admission of an application for CIRP has been assigned priority nor admission of an application for PPIRP. Faced with such an impasse, the question is which application should be decided first, given that the consequence of admission of either application would be same and both applications have been assigned 14 days for adjudication.

Conclusion and Key Takeaways:

While the Adjudicating Authority has not departed from the law enshrined under Section 11A of the Code, it has overlooked the entire scheme and objective behind the introduction of Chapter III-A[6], which is to provide for an efficient alternative to CIRP for an MSME and which has been explained and expounded in detail in the Objects and Reasons of the Amendment itself. Even at ground level, since a PPIRP application entails laborious preparation before filing, a CIRP application (filed before 4th April 2021) may invariably be pending and may even be decided first. This would perpetually deprive MSMEs of the benefits of PPIRP and may result in a situation where the corporate debtor, despite having undergone the strenuous and arduous task of complying with the requirements of a PPIRP, is unable to avail the pre-pack process.

In the long run, such an approach may render the mechanism of PPIRP for MSMEs entirely nugatory and redundant. Besides, even the 14-day period prescribed under Section 11A of the Code may not be pragmatic for filing a PPIRP application, considering the amount of work and labour involved.

The NCLT has possibly overlooked that PPIRP stands on an entirely different footing, which was introduced specifically to meet the urgent requirements of MSMEs to provide quicker, cost-effective and value maximising outcomes for all stakeholders in a manner which is least disruptive to the continuity of their businesses, and which preserves jobs. Besides, a PPIRP application is sealed with the approval of the creditors as required under the relevant provisions of the Code. Whereas an application for CIRP filed at the instance of a creditor or group of creditors, after admission, not only compels other creditors to join the CIRP, but leaves the future of a successful resolution uncertain,

and vulnerable to liquidation. While the outcome of admission of either application would remain the same, but in case of PPIRP, it is the corporate debtor who is in control of the restructuring process, which may lead to a better resolution as opposed to the restructuring process in case of CIRP.

For now, the NCLT has cleared the air around what may have become a recurrent and divergent issue across various benches. But the validity of and rationale behind the approach is subject to further scrutiny by the appellate authorities, as the NCLT order is presently in appeal before the NCLAT[7] and may also be further addressed by the Apex Court, if required.

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