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Swiss Challenge Method: A brief discussion

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This write-up is a brief discussion on the Swiss Challenge Method (**"SCM"**) for selecting a resolution plan under a corporate insolvency resolution process initiated under Chapter II of the Insolvency and Bankruptcy Code, 2016 ("**Code**").

First things first, what is SCM

SCM is a form of public procurement by way of a bidding process, *wherein a bidder (original bidder) makes an unsolicited Bid to the auctioneer. Once approved, the auctioneer then seeks counter-proposals against the original bidder's proposal and chooses the best amongst all options including the original Bid. The original builder in most cases is granted the right to first refusal. If the original bidder match its offer to the challenging proposal, the Bid is awarded to him, else it is awarded to the challenging bidder*[1].

Judicial recognition of SCM in India-

In 2009, the Supreme Court decided on a challenge[2] made by Ravi Development and Maharashtra Housing and Area Development Authority ("**Ravi Development**") against a common order of the High Court of Bombay whereby the tender and conferring preferential treatment by use of SCM to Ravi Development was deemed to be unfair, unreasonable, arbitrary and illegal. In this case, the Supreme court while holding that the contract offered in favour of Ravi Development was correct, clarified that the decision to apply the mode of SCM clearly fell within the realm of the executive discretion and that there was due application of mind by the Housing and Area Development authority, and hence did not foul of Article 14 of the Constitution of India. Further, in the said judgment the Supreme Court also suggested steps that may be kept in mind to avoid ill effects of SCM and encourage transparency and proper execution of the scheme. Since then, many states/ authorities have with time also adopted their own guidelines for SCM.[3]

Advent of SCM under the Indian insolvency regime

On August 27, 2021, the Insolvency and Bankruptcy Board of India's ("**IBBI**") published a discussion paper ("**Discussion Paper**"), whereunder amongst others, the use of SCM was suggested to tackle the issue of delay in passing of resolution plans.

The Discussion Paper observed that while Regulation 39 of the Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 ("**CIRP Regulations**") provides the mechanism for approval of resolution plan by the Committee of Creditors ("**CoC**"), and sub-regulation 3(a) *thereof* provides that CoC shall evaluate the resolution plans

[1] https://ibbi.gov.in/Discussionpaper-CIRP-27Aug2021.pdf.
[2] *Ravi Development vs Shree Krishna Prathisthan & Ors*. [S.L.P.(c) Nos. 11229, 11355-11356,21754-21755 & 21756-21757 of 2008] decided on May 11, 2009.
[3] RBI (guidelines on sale of stressed assets by banks dated September 1, 2016 and draft comprehensive framework of for sale of loan exposures dated June 8, 2020); Haryana (SCM Guideline GoH, 2016); Madhya Pradesh (SCM Guideline GoMP, 2014[6]); Karnataka (para 29 of Suo moto/ innovative proposal for setting up an infrastructure project)

received as per the evaluation matrix, the said regulation was however silent on the exact method to be used for the selection of the best resolution plan.

The Tribunals ("**NCLT/ NCLAT**[4]") had on previous occasions approved Resolution Plans received by the use of SCM, where:

a) the SCM process was approved by the CoC, and it was not based on any *suo moto* process adopted by the successful resolution applicant[5];
b) the process document was prepared as per the mandate of Section 25(2)(h) of the Code read in conjunction with Regulation 36B of the CIRP Regulations[6];
c) The SCM procedure to select the 'Resolution Plan' was fair, transparent and in consonance to the object of the Code was followed by CoC and RP; and
d) there was sufficient time granted to the resolution applicants to follow the process.

While it is true that resolution professionals, COCs and resolution applicants were already resorting to SCM for maximization of the value of the assets of corporate debtors, and the Tribunals were allowing resolution plans selected basis SCM, there was a looming uncertainty on its acceptance without *ado*, owing to certain precedents which disapproved the use of SCM while selecting a resolution plan.[7]

Owing to the above, the Discussion Paper proposed certain amendments to the CIRP Regulations, including to bring in a provision that the CoC could decide whether it considers appropriate to opt for an SCM and if it so decides, then such decision should be provided in the request for resolution plan ("**RFRP**") on *ex-ante* basis.

Process determined for SCM within the Code

Accordingly, Regulation 39(1A)(b) was introduced in the CIRP Regulations on September 30, 2021[8], which provides that, "*The resolution professional may, if envisaged in the request for resolution plan-*

(a) […]; or
(b) use a challenge mechanism to enable resolution applicants to improve their plans.

In view of the above amendment, a resolution professional can now resort to using the SCM or any other such challenge procedure as a statutory mandate for selecting the best resolution plan. However, it is imperative to note that as per the said regulation, such challenge procedure can be used only if the same is envisaged in the RFRP.

Kochhar & Co. view

As per the Discussion Paper, out of 4541 CIRPs which were initiated till June 2021, only 396 CIRPs culminated in the approval of a Resolution Plan. Here it is important to keep in mind that till June 2021, SCM was being implemented during the CIRP where the CoC was in agreement of its implementation. However, if we look at the CIRPs where the same was implemented, owing to lack of defined guidelines for implementation of the same, there were several objections that were preferred by stakeholders during the CIRP, thus causing a delay which was unavoidable. It is also important to note that in the past, the risks of lack of transparency, favouritism and adequate competition along with absence of symmetry in the bidding process, did cause speculations against SCM. However, with the amendment to the CIRP Regulations, the prospective resolution applicants can at least be aware beforehand that a challenge procedure is envisaged, if at all, under the RFRP for improvement of their plans.

One question however which begs an answer is, can a resolution professional use the SCM or any other challenge procedure if the RFRP for a corporate debtor does not explicitly provide for the same. Considering the number of precedents upholding the commercial wisdom of CoC, one would like to believe that if in the opinion of CoC and resolution professionals, the best outcome of the

[4] National Company Law Tribunal/ National Company Law Appellate Tribunal
[5] Saket Tex Dye Private Limited v. Kailash T. Shah [C.P.1981(IB)/MB/2019] decided on May 12, 2020 - para 12
[6] Binani Industries Limited vs. Bank of Baroda [CP (AT) (Insolvency) No. 82 of 2018] decided on Nov 14, 2018
[7] *Ibid* Fn 5
[8] Notification No. IBBI/2021-22/GN/REG078, dated September 30, 2021.

resolution plan is achieved by SCM, in our view, the CoC ought to be free to negotiate with the prospective resolution applicants by way of such SCM. In other words, even if possible use of SCM is not mentioned in the RFRP, if the CoC considers it appropriate to use SCM where there is enough time and a transparent process is followed, the said process should be allowed to achieve the maximization of assets of the corporate debtor. However, owing to the statutory requirement under Regulation 39(1A)(b) to stipulate the possibility of using such challenge procedure in the RFRP itself, it will have to be seen if the Tribunals will go by a strict interpretation or will allow use of SCM de hors such stipulation, by deferring to the commercial wisdom of the CoC.

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