IBC - PUFE transaction article

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This write-up is a brief discussion on the continuance of proceedings in relation to avoidance of preferential, under-valued, fraudulent or extortionate transactions ("**PUFE transactions**")[1] as defined under the Insolvency and Bankruptcy Code, 2016 ("**Code**"), after approval of a resolution plan.

As per the 5th report of Insolvency Law Committee, sections 43-51, 66 and 67 of the Code which deal with avoidance of PUFE transactions, are amongst others primarily aimed at swelling the asset pool that is available for distribution to creditors and preventing unjust enrichment of one party at the expense of other creditors.

In tandem with such aim, regulation 40A of the Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 ("**CIRP Regulations**") requires the resolution professional to determine PUFE transactions on or before the 115th day from the commencement of the corporate insolvency resolution process ("**CIRP**"), and to file applications before the Adjudicating Authority for avoidance of PUFE transactions within 135 days of commencement of CIRP. However, given that the CIRP of a corporate Debtor has to be mandatorily concluded within a period of 330 days (including all extensions from the date of admission into CIRP), coupled with the delay that commonly occurs in disposal of ordinary *lis*, applications in relation to avoidance of PUFE transactions in relation to a corporate debtor often remains unadjudicated by the time the CIRP of such corporate debtor is concluded.

As a result, applications for avoidance of PUFE transactions were considered infructuous upon conclusion of the CIRP. This issue was highlighted in the matter of *Venus Recruiters Private Limited vs. Union of India & Ors*. (decided on November 26, 2020)[2]. The High Court of Delhi in the said matter held that the Adjudicating Authority did not have jurisdiction to hear applications under section 43 of the Code after the approval of a resolution plan. It observed that the applications qua PUFE transactions are neither for the benefit of the resolution applicant, nor for the corporate debtor after completion of CIRP, and that such applications are for the benefit of the committee of creditors ("CoC") of the corporate debtor. It was also observed by the court that the resolution professional whose mandate ends with the conclusion of the CIRP, cannot indirectly seek to give benefit to the corporate debtor who is under the control of the new management/ resolution applicant, by pursuing such applications. However, the above was subject to the existence of any clause in the resolution plan which permitted

[1] Sections 43-51, 66 and 67 of the Insolvency and Bankruptcy Code, 2016
[2] 2020 SCC OnLine Del 1479

the resolution professional to function for any specific purpose beyond the approval of resolution plan.

The Insolvency Law Committee in its 5th report of May 2022, deliberated on the issue which was highlighted in the matter of Venus Recruiters Private Limited vs. Union of India & Ors., and considering the import of section 26 of the Code, suggested that proceedings related to PUFE transactions should be considered independent of the CIRP. Accordingly, the Committee concluded that proceedings in respect of PUFE transactions may continue beyond the timeline for the CIRP.[3]

Consideration the suggestion of the Committee, regulation 38(2)(d) was inserted to the CIRP Regulations on June 14, 2022, vide which it was made mandatory for a resolution applicant to set out in the resolution plan itself, the manner in which the proceedings for PUFE transactions were to be conducted after approval of the resolution plan, and the manner in which the proceeds, if any, from such proceedings shall be distributed.

There is no doubt that this amendment would certainly hold the suspended management of the corporate debtor to a greater degree of accountability and allow the corporate debtor to recover and distribute amounts which it otherwise may not have been able obtain owing to completion of CIRP. However, while a resolution applicant appears to have been given the discretion to decide the manner in which such proceeds would be distributed, one can only wonder if the COC would be agreeable to approve a plan which provides for distribution of such proceeds to creditors other than to itself. Further, while such proceeds or part thereof, may be received well after the approval of a resolution plan, since the manner of its distribution has to be spelt out in the resolution plan itself, the distribution envisaged may have to be in consonance with the principle of non-discriminatory payouts to creditors of the same class. While most resolution applicants would choose to err on the side of caution, it would be interesting to see if resolution applicants may also choose to distribute such proceeds as additional amounts to strategic partners who are essential for the survival of the corporate debtor post the approval of the resolution plan. Given the objective of the Code, there appears to exist good reasons for both the COC and the judicial forums to approve such a choice.

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The Article is also published on MONDAQ

https://www.mondaq.com/india/insolvencybankruptcy/1260426/continuation-of-proceedings-in-relation-to-avoidance-transactions-after-acceptance-of-resolution-plan

[3] Section 2.22 of the 5th report of Insolvency Law Committee of May 2022