

## ***A Hanging Sword of Damocles Over Preferential Transactions***

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### **ABSTRACT**

*Everyone is in a hurry, but no one is on time. In a complex and interconnected system with numerous variables, anticipating timely outcomes is akin to setting lofty expectations. This is particularly true in the context of the Corporate Insolvency Resolution Process (CIRP) under the Insolvency and Bankruptcy Code, 2016 (IBC).*

*One of the critical challenges in ensuring an efficient CIRP is the handling of asset transfers and financial transactions during insolvency proceedings. The absence of strict time-bound enforcement mechanisms often creates loopholes that allow financially distressed entities to manipulate transactions before the resolution process concludes. Section 43(2) of the IBC defines a preferential transaction as one where an asset transfer benefits a creditor, surety, or guarantor, disadvantaging other creditors in the waterfall mechanism during asset distribution. If not identified and reversed promptly, such transactions can erode the corporate debtor's financial health and disrupt the fair and equitable resolution process.*

*To safeguard creditor interests and maintain fairness, an efficient CIRP requires the appointment of a Resolution Professional (RP) by the*

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*Committee of Creditors (CoC) under Section 21 of the IBC. A crucial responsibility of the RP is to audit transactions made by the corporate debtor during the “relevant time” or “lookback period” – which extends two years for related parties and one year for others under Section 43(4) of the IBC. Additionally, the RP must determine whether these transactions comply with Regulation 35A of the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 (CIRP Regulations). If transactions are found to be avoidable or preferential, the RP is obligated under Section 25(2)(j) of the IBC to report them to the Adjudicating Authority (AA) under Chapter III of the Code. This process ensures that no creditor, surety, or guarantor gains an unfair advantage during the period leading up to the Insolvency Commencement Date.*

*The question of whether preferential transactions can be challenged even after the resolution process “concludes” remains a subject of debate. The key issue revolves around whether procedural requirements under the insolvency framework are mandatory or merely directory. Specifically, can the RP pursue avoidance of preferential, undervalued, or fraudulent transactions post-CIRP, even if the RP has already confirmed the ability to recover improperly transferred assets? The interpretation of the term “shall” within Regulation 35A of the CIRP regulations rests with the AA. Additionally, timelines: Do they enhance or hinder the overall effectiveness of the CIRP? Striking a balance between an expeditious resolution and a thorough examination remains crucial, as courts consider whether rigid adherence to timelines ensures fairness or compromises decision quality.*

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### I. INTRODUCTION

When a debtor incurs debt, their moral obligations and personal alliances are subordinated to their legal obligation to repay debts. This standard was prominently highlighted with the introduction of the IBC. The IBC is a transformative piece of legislation that consolidated the previously fragmented and cacophonous insolvency framework into a cohesive and effective system.<sup>1</sup> It has facilitated the reduction of the “cost of credit” while simultaneously improving India’s global ranking in “*the World Bank’s Ease of Doing Business index*.” India’s rank improved by 14 places, from 77<sup>th</sup> among 109 countries in 2018 to 63<sup>rd</sup> in 2019.<sup>2</sup> By 2021, India’s rank had further improved by 84 places, underscoring the

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<sup>1</sup> Ministry of Commerce and Industry, ‘Insolvency and Bankruptcy Board of India in association with INSOL India organises International Conclave 2024 on “Insolvency Resolution: Evolution & Global Perspective” at New Delhi’ (Press Information Bureau, 08 December 2024) <<https://pib.gov.in/PressReleaseIframePage.aspx?PRID=2082086>> accessed 16 April 2024.

<sup>2</sup> Trading Economics, ‘Ease of Doing Business in India’ (2019) <Ease of Doing Business in India (tradingeconomics.com)> accessed 12 August 2024.

IBC as a “*game-changer reform*.”<sup>3</sup> This demonstrates the efficacious insolvency norms being followed in India, positioning the IBC not merely as a “*recovery legislation*” but also as a “*beneficial legislation*”.<sup>4</sup>

The aforementioned ideology is grounded in two significant doctrines, the “*doctrine of equitable subordination*” and the “*doctrine of even-handedness*.”<sup>5</sup> These doctrines delineate the duties and obligations of a debtor towards its creditors. The doctrine of equitable subordination, particularly within the context of the IBC, empowers the AA to scrutinize the nature of transactions and subordinate or reverse the ones which are inequitable<sup>6</sup>, thereby ensuring fairness and the equitable distribution of claims among all creditors. This doctrine is explicitly reflected in Section 53<sup>7</sup> of the IBC, which mandates the AA to adhere to a hierarchical structure while distributing claims arising from the liquidation of an insolvent company’s assets.

Furthermore, the doctrine of even-handedness encompasses two critical aspects within the insolvency framework. *Firstly*, it posits that a debtor, in the event of insolvency, should not prioritize certain creditors over others or engage in a preferential treatment based on kinship. *Secondly*, it requires creditors to avoid such preferential treatment, thereby

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<sup>3</sup> Ministry of Commerce & Industry, ‘Insolvency and Bankruptcy Code (IBC), 2016 a “gamechanger reform”: Shri Piyush Goyal’ (Press Information Bureau, 25 November 2021) <Press Release: Press Information Bureau (pib.gov.in)> accessed 24 August 2024.

<sup>4</sup> *Swiss ribbons Pvt. Ltd. & Anr. v Union of India & Ors.* AIR 2019 SC (CIV) 1041  
<sup>5</sup> Robert Charles Clark, ‘The Duties of the Corporate Debtor to its Creditors’ (1977) Harv L Rev <<https://www.jstor.org/stable/1340335>> accessed 22 August 2024.

<sup>6</sup> Insolvency and Bankruptcy Code 2016, s 44.

<sup>7</sup> Insolvency and Bankruptcy Code 2016, s 53.

upholding the principles of equitable treatment and fairness.<sup>8</sup> These foundational concepts further find their basis in the *Jaypee Infratech case*<sup>9</sup>, wherein it was contended that if a corporate entity in financial distress faces insolvency or liquidation, any transaction that adversely affects its financial health or unfairly benefits certain creditors or third parties over others is viewed with “*considerable disfavour.*”

While the IBC has enabled the filing of numerous insolvency cases by both financial and operational creditors, several concerns about its effectiveness have surfaced. As of March 2024, the state of cases under liquidation reveals significant inefficiencies and delays, with over half of the 2,476 insolvency cases languishing for more than two years and only a small fraction being resolved through alternate means<sup>10</sup>. Additionally, significant value remains stuck in unresolved cases, with an average pendency of 340 days<sup>11</sup>, highlighting the need for streamlined processes and increased judicial capacity to ensure timely resolutions. The IBC is increasingly being used as a recovery tool rather than a resolution mechanism, contrary to its original aim, as evidenced by the high number of filings by operational creditors and withdrawals under Section 12A<sup>12</sup>.

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<sup>8</sup> Robert Charles Clark (n 5).

<sup>9</sup> *Jaypee Infratech Ltd. Interim Resolution Professional v. Axis Bank Ltd.* (2020) 8 SCC 401.

<sup>10</sup> Mukesh Chand, ‘The Evolution And Effectiveness Of The Insolvency And Bankruptcy Code, 2016: An Analytical Perspective’ (2024) Mondaq <[<sup>11</sup> \*ibid.\*](https://www.mondaq.com/india/insolvencybankruptcy/1505536/the-evolution-and-effectiveness-of-the-insolvency-and-bankruptcy-code-2016-an-analytical-perspective#:~:text=Pendency%20and%20Value%20Stuck:%20Significant%20value%20remains,increased%20judicial%20capacity%20to%20ensure%20timely%20resolutions.></a> accessed 15 April 2024.</p>
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<sup>12</sup> Insolvency and Bankruptcy Code 2016, s 12A.

The prescribed timeline for the CIRP is 180 days, extendable to 330 days, yet the average time taken is approximately two years.<sup>13</sup> Therefore, it is crucial not only to recognise preferential transactions during insolvency proceedings but also to ensure timely outcomes to achieve effective resolutions and uphold the IBC's objectives.

In this paper, an attempt has been made to highlight the issue of the untimely resolution of insolvency proceedings. The first part of the paper deals with applications, procedural framework and timeline that are mandated by the IBC to curtail avoidance transactions. The second part, deals with the interpretation of the directory or mandatory nature of the timeline prescribed under Regulation 35A of the CIRP Regulations through critical dissection of various judicial precedents. Lastly, the third section offers recommendations for improving the efficiency of the current insolvency system with respect to the procedural timeline enshrined under the code and its ancillary regulations.

## **II. OVERVIEW OF PREFERENTIAL TRANSACTIONS UNDER IBC**

Imagine a scenario where company A is facing financial difficulties and files for bankruptcy. Mr. X, the CEO of company A, also owns company B. Before filing for bankruptcy, "A" repays a substantial loan to "B", despite owing money to other creditors. In this situation, the court may invoke the doctrine of equitable subordination. The court determines that Mr. X leveraged his position as CEO to ensure "B", which he owns,

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<sup>13</sup> Insolvency and Bankruptcy Board of India, IBBI Quarterly Newsletter (Jan.-Mar. 2024), <<https://ibbi.gov.in/uploads/publication/21aa7620a9e809f7a20b432eec89888b.pdf>> accessed 20 August 2024.

was repaid before other creditors. This conduct is deemed unfair and inequitable as it prioritizes his interests over those of other creditors. Consequently, the other creditors receive less money due to the preferential repayment to “B”. To address this, the court decides to subordinate B’s claim, meaning B’s claim will be treated as a lower priority compared to other creditors. Essentially, “B” will only be paid after all other creditors have been fully compensated, or this particular transaction will be reversed and redistributed in accordance with the creditor’s hierarchy. By subordinating B’s claim, the court ensures a more equitable distribution of A’s assets among all creditors, preventing Mr. X from exploiting his insider position.

The aforementioned scenario aptly illustrates the importance of Preferential, Undervalued, Fraudulent, and Extortionate (PUFE) transactions under the IBC. PUFE transactions encompass *preferential, undervalued, fraudulent, and extortionate transactions* as outlined in Sections 43 to 55<sup>14</sup>, and Section 66<sup>15</sup> of the IBC. While all these transactions fall under the category of suspect and avoidance transactions, this article aims to delve specifically into the nuances and statutory provisions pertaining to preferential transactions. Section 43<sup>16</sup> addresses the look-back period for preferential transactions, indicating that any transactions made to a related party within two years or to an unrelated party within one year of the insolvency commencement date

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<sup>14</sup> Insolvency and Bankruptcy Code 2016, s 43-55.

<sup>15</sup> Insolvency and Bankruptcy Code 2016, s 66.

<sup>16</sup> Insolvency and Bankruptcy Code 2016, s 43.

will be considered preferential. These transactions are subject to the orders specified in Section 44<sup>17</sup> of the IBC.

Further Regulation 35A<sup>18</sup> acts as an ancillary while dealing with avoidance transactions. Regulation 35A<sup>19</sup> of the CIRP regulations mandates that the resolution professional (RP) must form an “*opinion*” on whether the corporate debtor has been involved in any transactions covered under Sections 43<sup>20</sup>, 45<sup>21</sup>, 50<sup>22</sup>, or 66<sup>23</sup> of the IBC within seventy-five days of the insolvency commencement date. If such transactions are identified, the resolution professional must make a determination by the *one hundred and fifteenth day* and apply to the AA for appropriate relief by the *one hundred and thirtieth day*. Additionally, the RP must forward a copy of the application to the prospective resolution applicants for consideration, while submitting their resolution plans. Creditors are required to provide the relevant audit extracts to assist this process. The term “*opinion*” in this context, as interpreted in *M.A. Rasheed v State of Kerala*<sup>24</sup>, refers to the subjective judgment or assessment made by an authority based on their evaluation of the facts and circumstances. If lacking reasonable grounds, the court may invalidate the opinion for being formed without the proper application of mind.

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<sup>17</sup> Insolvency and Bankruptcy Code 2016, s 44.

<sup>18</sup> Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations 2016, reg 35A.

<sup>19</sup> *ibid.*

<sup>20</sup> Insolvency and Bankruptcy Code 2016, s 43.

<sup>21</sup> Insolvency and Bankruptcy Code 2016, s 45.

<sup>22</sup> Insolvency and Bankruptcy Code 2016, s 50.

<sup>23</sup> Insolvency and Bankruptcy Code 2016, s 66.

<sup>24</sup> *M.A. Rasheed v. State of Kerala*, (1974) 2 SCC 687.

Furthermore, in light of the NCLAT’s decision in the *Venus Recruiters judgment*<sup>25</sup> it is established that the RP becomes “*functus officio*” immediately upon the approval of the resolution plan by the AA. This constrains the RP’s timeframe to identify and address the avoidance transactions, often resulting in the conclusion of the resolution process before such transactions can be properly investigated. Consequently, the CoC might be compelled to accept a financial haircut, thereby granting a few beneficiaries an undue advantage over others. This judgment implicitly affects the cases where the resolution plan fails to account for pending avoidance applications, allowing beneficiaries of avoidable transactions to evade accountability, leading to unjust enrichment.

### III. THE SWORD OF PRECEDENT: DISSECTING JUDGEMENTS

In the case of *Aditya Kumar Tibrewal v Om Prakash Pandey & Ors.*<sup>26</sup> (NCLT Kolkata), the Bank of India initiated the CIRP against M/s. Sri Balaji Forest Products Private Limited, by applying Section 7<sup>27</sup> of the IBC, 2016. Subsequently, the suspended directors of the corporate debtor failed to cooperate with the RP and provide the necessary documents, leading to an order under Section 19(2)<sup>28</sup> of the Code, directing the directors to cooperate. The suspended directors shared a Lease Deed which leased all the Corporate Debtor’s land, plot, and machinery to the respondent no. 3 for 29 years. The RP then filed an Interim application

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<sup>25</sup> *Venus Recruiters (P.) Ltd. v. Union of India* 2020 SCC Del 1479.

<sup>26</sup> *Aditya Kumar Tibrewal v. Om Prakash Pandey & Ors.* (2023) 24 Comp Cas-OL 552.

<sup>27</sup> Insolvency and Bankruptcy Code 2016, s 7.

<sup>28</sup> Insolvency and Bankruptcy Code 2016, s 19 (2).

under Sections 43<sup>29</sup>, 45<sup>30</sup>, 49<sup>31</sup>, 66<sup>32</sup>, and 60(5)<sup>33</sup> of the Code, seeking various reliefs, including the declaration of the lease deed as fraudulent and void.

The NCLT rejected the application, citing non-compliance with the Regulation 35A<sup>34</sup> of the CIRP Regulations, which prescribes a timeline for the RP to form an opinion and apply to the AA regarding avoidable transactions. The judgment emphasized that the timelines under Regulation 35A are directory, not mandatory. The RP's failure to comply with these timelines does not automatically invalidate the application, but the specific circumstances must be considered on a case-to-case basis.

Moreover, the word “shall” in Regulation 35A can be leniently construed as held in the *State of Uttar Pradesh v Manbodhan Lal Shrivastava*,<sup>35</sup> where the court clarified that while “shall” is generally understood as mandatory, its effect depends on the legislative intent rather than the wording alone. The ruling emphasised that statutory provisions must be evaluated based on their nature, design, and potential consequences, rather than a strict textual approach. This principle suggests that the timelines prescribed in Regulation 35A are directory rather than mandatory, meaning non-compliance does not automatically invalidate an application but must be assessed on a case-by-case basis.

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<sup>29</sup> Insolvency and Bankruptcy Code 2016, s 43.

<sup>30</sup> Insolvency and Bankruptcy Code 2016, s 45.

<sup>31</sup> Insolvency and Bankruptcy Code 2016, s 49.

<sup>32</sup> Insolvency and Bankruptcy Code 2016, s 66.

<sup>33</sup> Insolvency and Bankruptcy Code 2016, s 60 (5).

<sup>34</sup> Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations 2016, reg 35A.

<sup>35</sup> *State of Uttar Pradesh v. Manbodhan Lal Shrivastava*, AIR1957 SC 912.

In the case of *Venus Recruiters (P.) Ltd. v Union of India*<sup>36</sup>, the State Bank of India started the CIRP against M/s. Bhushan Steel Ltd. (now Tata Steel BSL Ltd.) by invoking Section 7<sup>37</sup> of the IBC. After that, an IRP was appointed. The CoC approved the resolution plan put forward by Tata Steel Ltd., and the RP submitted it before the NCLT. Then, the RP filed an avoidance application under Sections 25(2)(j)<sup>38</sup>, 43<sup>39</sup> to 51<sup>40</sup>, and 66<sup>41</sup> of the IBC, identifying various suspect transactions, including excessive payments to manpower contractors like Venus Recruiters.

The NCLT approved the resolution plan but did not specifically address the avoidance application, effectively disposing of all pending applications. Subsequently, the NCLT issued a notice in the avoidance application, which led to Venus Recruiters challenging the jurisdiction of the NCLT to hear the application post-approval of the Resolution Plan. The Delhi High Court, in its judgment, addressed the survival of an application under Section 43<sup>42</sup> for the avoidance of preferential transactions beyond the conclusion of the resolution process and the role of the RP in pursuing such applications. The court clarified that the RP has a defined role within the CIRP. Under Section 23<sup>43</sup>, the RP manages the corporate debtor only during the resolution process and must cease involvement post-approval of a Resolution Plan under Section 31<sup>44</sup>. Once new management takes over, the RP cannot file applications indefinitely,

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<sup>36</sup> *Venus Recruiters (P.) Ltd.* (n 25).

<sup>37</sup> Insolvency and Bankruptcy Code 2016, s 7.

<sup>38</sup> Insolvency and Bankruptcy Code 2016, s 25(2)(j).

<sup>39</sup> Insolvency and Bankruptcy Code 2016, s 43.

<sup>40</sup> Insolvency and Bankruptcy Code 2016, s 51.

<sup>41</sup> Insolvency and Bankruptcy Code 2016, s 66.

<sup>42</sup> Insolvency and Bankruptcy Code 2016, s 43.

<sup>43</sup> Insolvency and Bankruptcy Code 2016, s 23.

<sup>44</sup> Insolvency and Bankruptcy Code 2016, s 31.

as extending their role beyond the plan's approval contradicts the intent of their appointment.

However, the interpretation of post-CIRP avoidance applications underwent a shift in a subsequent case, *Tata Steel Bsl Limited v Venus Recruiter Private Limited & Ors*<sup>45</sup>. The court overruled the decision made in the *Venus Recruiters (P.) Ltd. case*, holding that avoidance applications can continue even after the CIRP. The court also highlighted that Section 26<sup>46</sup> emphasises the distinction between resolution proceedings and adjudication of avoidance applications, making it clear that filing an avoidance application under Section 25 (2) (j)<sup>47</sup> by the RP will not impact the CIRP proceedings. The court clarified that while the resolution plan should ideally provide for the treatment of pending avoidance applications, failure to do so due to practical constraints does not render them infructuous. Such an interpretation would make the provisions related to suspect transactions otiose, allowing beneficiaries of questionable transactions to evade scrutiny. The judgment underscored the principle that money borrowed from creditors is essentially public money, and permitting parties to unjustly appropriate such funds through suspect arrangements would undermine the insolvency framework.

Consequently, the court held that unresolved avoidance matters must continue to be heard by the AA, ensuring that the integrity of the insolvency resolution process is upheld. Furthermore, certain

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<sup>45</sup> *Tata Steel Bsl Limited v. Venus Recruiter Private Limited & Ors.* 2023 SCC DEL 155.

<sup>46</sup> Insolvency and Bankruptcy Code 2016, s 26.

<sup>47</sup> Insolvency and Bankruptcy Code 2016, s 25 (2) (j).

suggestions of IBBI discussion papers were also highlighted in this case, according to which any funds recovered after the dissolution of the corporate debtor should be distributed according to Section 53<sup>48</sup> of the Code, and any excess recoveries and unclaimed amounts may be credited to the insolvency and bankruptcy fund.

Besides that, the Insolvency Law Committee (ILC) Report, 2020, also took an effort to analyse the two hypothetical situations which were found to be crucial to understand the scope of avoidance proceedings, *firstly*, where the AA would mandatorily be required to determine the conclusion of avoidance proceedings prior to approval of the resolution plan under Section 31<sup>49</sup>. This would inordinately delay the conclusion of CIRP proceedings, the timely resolution of the corporate debtor.<sup>50</sup> The resolution of the corporate debtor should not be hindered by pending ancillary proceedings. Investigating and adjudicating avoidable transactions can be time-consuming, requiring a thorough examination of the transactions conducted by the corporate debtor before the commencement of insolvency or liquidation proceedings.

This process can be especially challenging when dealing with companies whose financial records fail to document all past transactions accurately. The RP is tasked with assessing whether suspicious transactions meet the criteria for avoidable transactions or improper trading as outlined in the Code.

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<sup>48</sup> Insolvency and Bankruptcy Code 2016, s 53.

<sup>49</sup> Insolvency and Bankruptcy Code 2016, s 31.

<sup>50</sup> Ministry of Finance and Corporate Affairs, 'Insolvency Law Committee Report 2020' <[https://www.mca.gov.in/Ministry/pdf/ICLReport\\_05032020.pdf](https://www.mca.gov.in/Ministry/pdf/ICLReport_05032020.pdf)> accessed 20 August 2024.

Additionally, the investigation, filing, and adjudication of such transactions are time-consuming processes. Findings of avoidable transactions and improper trading involve subjective assessments and require addressing legal and factual questions. For instance, determining if a particular transaction qualifies as a preference transaction involves ascertaining if it falls within the legal framework created under Section 43(2)<sup>51</sup> or within the exceptions under Section 43(3)<sup>52</sup>. Consequently, concluding proceedings for the avoidance of transactions or improper trading within the 330-day time limit for CIRP may be quite challenging in this scenario.

*Secondly*, where the avoidance applications have not been concluded before the approval of a resolution plan under Section 31<sup>53</sup>, they would be deemed ineffective, effectively terminating such proceedings. This would create a situation where corporate debtors could evade scrutiny for pre-commencement transactions, gaining undue benefits while allowing beneficiaries of suspect transactions to walk away without consequences. Given the inherently time-consuming nature of investigating and adjudicating avoidable transactions, this loophole could be exploited by errant promoters and management, undermining the insolvency resolution framework<sup>54</sup>. Recognising these risks, the ILC observed that both scenarios—either requiring avoidance proceedings to conclude within CIRP or allowing them to lapse due to procedural constraints — would lead to undesirable outcomes.

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<sup>51</sup> Insolvency and Bankruptcy Code 2016, s 43(2).

<sup>52</sup> Insolvency and Bankruptcy Code 2016, s 43(3).

<sup>53</sup> Insolvency and Bankruptcy Code 2016, s 31.

<sup>54</sup> Insolvency Law Committee Report 2020 (n 50).

The IBC does not specify a deadline for commencing proceedings to avoid transactions and improper trading, whether in the context of the CIRP or liquidation. Additionally, the Code does not set a time limit for the completion of such proceedings once initiated. However, the CIRP Regulations stipulate that the RP must assess whether the corporate debtor has engaged in any avoidable transactions by the *one hundred and fifteenth* day from the date of insolvency commencement and inform the IBBI accordingly. Furthermore, it requires that the resolution professional should seek appropriate relief from the AA by the *one-hundred-thirty-fifth* day from the date of insolvency commencement. Although these timeframes are considered as guidelines, the 2020 report of the Committee<sup>55</sup> noted that prescriptive timelines for initiating proceedings against avoidable transactions and improper trading during the CIRP or liquidation proceedings may not be necessary.

Furthermore, the timelines outlined within the IBC and its regulations, such as regulation 35A<sup>56</sup> of the CIRP Regulations, serve to enhance time efficiency. However, it is important to note that proceedings under the IBC often receive extensions granted by the NCLT. The ILC Report 2020 further supports this perspective, asserting that the RP should initiate proceedings for avoidable transactions during the CIRP. The report also emphasises that strict timelines for initiating such proceedings may not be necessary and that resolution plans may include provisions for pursuing these proceedings post-implementation without being constrained by rigid timelines<sup>57</sup>. It is crucial to emphasise that

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<sup>55</sup> Insolvency Law Committee Report 2020 (n 50).

<sup>56</sup> Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations 2016, reg. 35.

<sup>57</sup> Insolvency Law Committee Report 2020 (n 50).

Regulation 35A<sup>58</sup> only mandates the RP to form an opinion, determine, and file an application before the NCLT without specifying a timeline for the NCLT to adjudicate such applications. This interpretation reaffirms the flexibility and procedural nuances inherent in the IBC framework, aligning with the cases at hand.

#### **IV. SHARPENING THE BLADE: STRATEGIC RECOMMENDATIONS FOR IMPROVEMENT IN PROCEDURAL TIMELINE**

Amendments to the Code are necessary to provide clarity on conducting proceedings for the avoidance of transactions and wrongful trading after the approval of a resolution plan. As per the recommendations of the ILC report 2020<sup>59</sup>, it is proposed that the resolution plan should specify the manner of undertaking proceedings for the avoidance of transactions and wrongful trading if such proceedings are to be continued after the plan's approval, as well as whether the resolution professional or any other person will pursue such transactions/trading after the plan's approval. Moreover, detailed provisions such as the eligibility requirements for the appointed person, the mechanism for sharing relevant details of pending proceedings with prospective resolution applicants, and the manner of distribution of expected recoveries from proceedings related to the avoidance of transactions and wrongful trading should be laid down in the subordinate legislation. The AA should consider these details when issuing final orders in such proceedings.

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<sup>58</sup> Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations 2016, reg. 35.

<sup>59</sup> Insolvency Law Committee Report 2020 (n 50).

Further, it is important to note that filing an avoidance application during the CIRP should not impact the CIRP timeline. In the case of liquidation, such proceedings should conclude before the corporate debtor's dissolution. If that is not feasible, the AA should provide a method for continuation of avoidance applications post-dissolution.

Furthermore, in the recommendations of the ILC report 2022<sup>60</sup>, emphasis had been supplied to the need for the accountability of individuals responsible for the conduct of the corporate debtor's business at the time of the commission of insolvency period. They should continue to be liable for such offenses, even if the corporate debtor's liability has ceased. It is recommended that a clarificatory amendment be made to Section 26<sup>61</sup> to ensure that the completion of the CIRP proceedings does not affect the continuation of proceedings for avoidable transactions or improper trading. Additionally, the regulations should lay down a mechanism for reviewing late submissions of (or revisions to) resolution plans, with suitable amendments to be made in the Code to ensure that the procedure provided in the regulations has due sanctity.

## V. CONCLUSION

The intent of the legislature plays a critical role in determining whether a statutory provision is mandatory or directory, considering the nature, design, and practical consequences of its application. While the use of "shall" in Regulation 35A<sup>62</sup> of the CIRP Regulations is generally

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<sup>60</sup> Ministry of Corporate Affairs, '5th Insolvency Law Committee Report' 2022 <<https://ibbi.gov.in/uploads/whatsnew/7c9bde175431a4abb8c33bb105e1f2dd.pdf>> accessed 25 August 2024.

<sup>61</sup> Insolvency and Bankruptcy Code 2016, s 26.

<sup>62</sup> Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations 2016, reg. 35.

understood as mandatory, its interpretation as directory allows for flexibility in procedural adherence. A key concern remains whether the RP can pursue avoidance of Preferential transactions post-CIRP. An amendment to Section 26<sup>63</sup> is necessary to ensure that the completion of CIRP does not hinder proceedings for avoidable transactions or improper trading. Additionally, the necessity of establishing a clear review mechanism for late submissions or revisions to resolution plans, ensuring procedural timelines do not weaken the efficiency of CIRP. Going forward, enhancing procedural clarity and ensuring strict accountability will be crucial in safeguarding creditor interests while maintaining the integrity and efficiency of the insolvency framework. Continuous improvements to the IBC and its regulations will help resolve emerging challenges and reinforce the equitable resolution of insolvency cases.

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<sup>63</sup> Insolvency and Bankruptcy Code 2016, s 26.