



Back Door Entry Closed for Defaulters: SC

Why in News

Recently, the [Supreme Court \(SC\)](#) has **closed the back-door entry of defaulting promoters** by using a **special provision of compromise** or arrangement during the liquidation phase of the insolvency proceeding.

- The ruling **reaffirms the spirit of the [Insolvency and Bankruptcy Code \(IBC\)](#).**

Key Points

▪ Background:

- In a case involving the liquidation of a Limited Company, the [National Company Law Appellate Tribunal \(NCLAT\)](#) in 2019 held that any person who was ineligible, under **Section 29A of Insolvency and Bankruptcy Code (IBC)**, to bid for his company, **was also barred from proposing a scheme of compromise and arrangement** under **Section 230** of the [Companies Act 2013](#).
 - The Companies Act 2013 is an **Indian company law** which **regulates incorporation of a company, responsibilities of a company, directors, dissolution of a company**.
 - Company means a company incorporated under this Act or under any previous Company Law.
 - **Section 230** of the Companies Act allows promoters or creditors of the company to propose a scheme of arrangement or compromise under which the debt of the company can be restructured.

▪ Recent Ruling of the SC:

- SC upheld NCLAT's decision and said that while **Section 230 would be applicable for promoters and creditors in the normal course** of the workings of the company, it would **not be applicable if the company is facing liquidation under IBC**.

▪ Reason Given by SC:

- The **company has to be protected** from its **management and a corporate death**.
- It would lead to a **manifest absurdity** if the very **persons who are ineligible for submitting a resolution plan**, participating in the sale of assets of the company in liquidation or participating in the sale of the corporate debtor as a 'going concern', **are somehow permitted to propose a compromise or arrangement under Section 230 of Companies Act 2013**.

▪ Significance of the Judgement:

◦ Speed up the Resolution:

- The clarification by the SC with respect to participation of promoters in the liquidation process of an insolvent company will **speed up the [corporate](#)**

[insolvency resolution process.](#)

- **Maximisation of the Asset Value:**
 - Since the **objective of the IBC** is to find a suitable buyer for the company and liquidation is ordered only in cases where there are no viable plans submitted, experts believe that a **quick liquidation is of utmost importance to maximise the value of assets of the company.**
- **Settled Conflicting Judgements:**
 - **It settles down the conflicting judgments given by different benches of the NCLT**, wherein these forums had, in order to follow the IBC's principle of value of asset maximisation, allowed some of the promoters to re-bid for the company or propose some arrangement when it was sent to liquidation.

Insolvency and Bankruptcy Code, 2016

▪ **About:**

- It provides a **time-bound process** for resolving insolvency in companies and among individuals.
- It covers all **individuals, companies, Limited Liability Partnerships (LLPs) and partnership firms.**

▪ **Objective:**

- To **streamline and speed up the resolution process** of failed businesses.
- To **consolidate provisions of the existing legislative framework** to form a common forum for debtors and creditors of all classes to resolve insolvency.
- To **stipulate that the resolution process** of a stressed company will **have to be completed in a maximum of 270 days.**

▪ **Section 29A:**

- It is a **restrictive provision**, it specifically lists down the **persons who are not eligible to be resolution applicants.**
- Section 29A in its entirety not only restricts promoters but **also the people related/connected with the promoters.**
- This section was introduced **to disqualify those who had contributed in the downfall of the corporate debtor** or were unsuitable to run the company.

▪ **Adjudicating Authority:**

- **National Company Law Tribunal (NCLT)** for companies and LLPs.
- **[Debt Recovery Tribunal \(DRT\)](#)** for individuals and partnership firms.

National Company Law Appellate Tribunal

- The NCLAT was **constituted under Section 410 of the Companies Act, 2013** to hear appeals against the orders of the National Company Law Tribunal (NCLT).
 - NCLT is a **quasi-judicial body** that adjudicates issues relating to companies.
- It is **also the appellate tribunal for orders passed by the NCLT(s)** under Section 61 of the IBC, 2016, and for orders passed by the Insolvency and Bankruptcy Board of India (IBBI) under Sections 202 and 211 of the IBC.
- Any **person aggrieved by any order of the NCLAT may file an appeal to the SC.**

[Source:IE](#)

PDF Refernece URL: <https://www.drishtias.com/printpdf/back-door-entry-closed-for-defaulters-sc>