

# **EXAMINING THE PRE-PACKAGED INSOLVENCY RESOLUTION PROCESS IN INDIA**

## **Abstract**

The shift from the contemporary insolvency law towards a corporate rescue mechanism has been well incorporated in the Insolvency and bankruptcy code 2016 (hereinafter “the code”). In a short span of six years, the code has brought sweeping reforms in the insolvency landscape of India. The code provides a comprehensive and time-bound insolvency resolution process for the corporate debtor offering their creditors the legal right to press claims for recovery of default. The recovery mechanism under the code either results in corporate rescue or liquidation of the corporate debtor. The purpose of the code is to rehabilitate and revive the financially troubled corporate debtor and prevent the extreme liquidation route. The code has undergone various amendments since its inception. An innovative approach to corporate restructuring that has emerged over the years is the pre-pack mechanism which incorporates the virtues of formal judicial proceedings and informal out-of-court settlement. The pre-pack method of insolvency resolution has been prevalent in various developed nations like the United Kingdom and the United States. It was recently introduced in India through chapter iii-a on the pre-packaged insolvency resolution process (hereinafter “PPIRP”) in the code. The essence of pre-pack is formulating a restructuring or resolution plan before the commencement of insolvency. It offers a hybrid ‘debtor-in-possession’ and ‘creditor-in-control’ model for the Micro, Small, and Medium Enterprises (hereinafter “MSME”). The paper analyses the provisions of PPIRP under the Code and whether it can provide an efficient and effective insolvency regime to the MSMEs. The paper further examines the impact of pre-packs on the insolvency framework in India.

## **I Introduction**

A CORPORATION faces financial distress in its life span due to inherent distress, use of obsolete technology in production, financial or operational failure, change in consumer demand, access to funds or capital and other factors that might not be in control of the corporation. As a result, the corporation fails to pay the debts it owes to its creditors.

The two terms widely used to determine the financial failure of an enterprise are insolvency and bankruptcy. Insolvency of a debtor company refers to its inability to pay to its creditors, whereas bankruptcy refers to a formal declaration of insolvency by the court or the tribunal. Various terminologies such as cash-flow insolvency, balance sheet insolvency, liquidation, and reorganization is associated with a corporation’s insolvency. For example, cash flow insolvency is when the company’s cash inflow is less than its cash outflow, resulting in its inability to pay the debts. Balance sheet insolvency arises when the book value of the company’s assets is less than its liabilities. Liquidation results in the dissolution of the company and precisely refers to the sale of assets for cash to repay the creditors. Another term, reorganization, has become

popular in recent years, and it denotes restructuring a financially distressed firm using financial and corporate restructuring techniques. Economic viability is an essential factor that determines the projections and prospects of the financial performance of the product or the service of the business. The corporation goes into economic and financial distress if the business does not have economic viability.<sup>1</sup>

The erstwhile regime regulating corporate insolvency in India was highly fragmented and lacked clarity in its application and implementation. The Insolvency and Bankruptcy Code, 2016, enacted under the recommendations of the Bankruptcy Law Reforms Committee, provides comprehensive insolvency legislation ensuring a time-bound process, maximizing the value of corporate debtor's assets and balancing stakeholders' interests. It applies to companies, limited liability partnerships, individuals and partnerships. The emphasis of the Code is on the revival and rescue of a viable entity. The Code has been instrumental in revamping the insolvency framework in India by providing a streamlined Corporate Insolvency Resolution Process (*hereinafter* "CIRP") to resolve financially distressed companies. In addition, it provides a mechanism for equitable distribution of the debtor's assets. The prime aim of the Code is to avoid the creditor's frenzied attempt to recover the dues from the financially distressed debtor and thus preserve the common pool of assets of the debtor.<sup>2</sup> The success of the CIRP depends on the resolution applicant's (*hereinafter* "RA") availability and willingness to invest in the distressed entity. In the COVID-19 era, most companies have been facing financial distress, and in such times, the likelihood of finding a RA is minimal. Moreover, economies worldwide are experiencing the ongoing waves of the pandemic. It would be difficult to ascertain when it will entirely subside and the business will function as usual.

Under the Code, CIRP is available only to defaults of more than rupees 1 crore. In such a situation, the business would be under stress for longer, and the creditors would enable recovery through other means because the recovery under the Code is not possible as the default threshold would not be met. Moreover, the companies are generally disincentivized to initiate CIRP voluntarily while experiencing financial hardship due to the displacement of the current management. Similarly, the resolution professional or the liquidator is often unable to identify avoidable transactions and apply to NCLT to reverse them within the prescribed time limits.<sup>3</sup>

---

1 Karen Hopper Wruck, *Financial Distress, Reorganization, and Organizational Efficiency* 27(2) *J. Fin. Eco.* 419 (1990).

2 Barry E Adler, *Financial and Political Theories of American Corporate Bankruptcy*, 45(2) *Stan. Law Rev.* 311 (1993).

3 Karthik Somasundram and Khyati Mehrotra, *IBC Valuations May Spike with Proceeds of Avoidable Transactions*, *Law Asia* (Jan. 22, 2023, 9:30 AM), available at : <https://law.asia/ibc-valuations-avoidable-transactions/> (last visited on Apr. 30, 2023).

Business failures are inevitable, and the best way to deal with them is to adopt semi-formal insolvency mechanisms specifically tailored to the corporate debtor's requirement, blending elements of both formal and informal resolution processes that result in better sanctity and balances the stakeholders' interests. The prominent semi-formal insolvency resolution option is pre-pack, employed widely across jurisdictions. Developed nations like the United States and the United Kingdom have utilized pre-packaged reorganization procedures and pre-packaged administrations, enabling financially troubled firms to emerge from bankruptcy quickly. Even Singapore has introduced pre-packaged schemes to prevent the dissolution of the corporate debtor (*hereinafter* "CD"). Pre-pack is typically time-effective, flexible, cost-effective, and less disruptive to the business. Though the inclusion of pre-pack has been the talk of the town for a while, the Code introduced the pre-packaged insolvency resolution process for the micro, small, and medium enterprises in the year 2021.

## II Micro, small and medium enterprises in India

MSMEs are the critical accelerator of production, employment, entrepreneurship, financial inclusion and economic growth in India. The contribution of MSMEs to the Gross Domestic Product is significant, and thus they are referred to as the power engines of the economy. MSMEs create job opportunities at a meagre cost and employ a vast population. It also boosts entrepreneurship, especially in rural and semi-urban areas. MSME-related products export share of All India Exports stood at 49.4% and 49.8% for FY21 and FY20, respectively. Data from the Ministry of Micro, Small and Medium Enterprises epic that the number of micro, small and medium enterprises, respectively, are 11,735,117; 426,864; 39,467 as of November 25, 2022, in India.<sup>4</sup>

MSMEs are distinctly vulnerable to financial disruptions due to the inaccessibility of funds, hiring and retaining qualified workforce, and difficulty in penetrating domestic and global markets. As a result, even though MSMEs are the foundation of the economy's growth, they face difficulty in accessing the insolvency system. Moreover, the ongoing COVID-19 pandemic has further impacted the business of corporations, especially MSMEs, exposing them to financial distress for which the sector was unprepared.

The COVID-19 pandemic has struck the world as a 'crisis like no other,' shaking the economy of several countries. It has caused recession and disrupted the global value chain. It has impacted the production and distribution of goods and services, bringing the operations of many corporations to a standstill as the COVID-19 virus continues to spread. The World Bank has characterized the pandemic as one of the most severe recessions since World War II. The crisis has declined the per capita output in most

---

<sup>4</sup> *Indian MSME Industry Analysis*, IBEF, available at: <https://www.ibef.org/industry/msme-presentation> (last visited Apr. 23, 2023).

economies across the globe and has resulted in business failure and potential unemployment, causing profound financial system risk. The economic impact of the COVID-19 crisis is graver than what has been witnessed in the Great Depression of 1930.<sup>5</sup>

The definition of MSME is provided in the Micro, Small, and Medium Enterprises Development Act, 2006, which classifies MSME based on investment in plant, machinery or equipment and annual turnover. MSME are further classified in two classes *i.e.*, Manufacturing Enterprises and Service Enterprises. The enterprises are further categorized based on investment in equipment and annual turnover.<sup>6</sup> When the Code was enacted in 2016, the minimum default threshold to initiate CIRP was prescribed as rupees one lakh.<sup>7</sup> MSMEs have been the worst affected by this minimum threshold. This is because the creditors could initiate the insolvency proceedings against them before the NCLT on default of an amount as meagre as “rupees one lakh.” As a result, it was difficult for the distressed MSMEs to receive a resolution plan as financially sound corporate entities were unwilling to invest in a financially distressed small-scale company. However, the government revised the default threshold and increased it to rupees 1 crore during the 1<sup>st</sup> wave of the COVID-19 pandemic, thus relieving the MSMEs from a lower threshold.<sup>8</sup>

The Insolvency and Bankruptcy Code (Second Amendment) Ordinance, 2018, has aided the MSMEs as it relaxed the applicability of section 29A of the Code on *persons not eligible to be a resolution applicant*. The provision discusses a person’s ineligibility to be RA and their eligibility to submit a resolution plan, thus restraining untrustworthy promoters from buying back assets at a subsidized price. In order to provide an exemption from section 29A to the MSMEs, the government introduced section 240A under the said amendment. The provision grants exemptions to the MSMEs by allowing a promoter who is not a wilful defaulter or has any specific disqualification as provided under section 29A to bid for the MSME’s resolution plan.<sup>9</sup> These exemptions will

---

5 COVID-19 to Plunge Global Economy into Worst Recession Since World War II, The World Bank, available at: <https://www.worldbank.org/en/news/press-release/2020/06/08/covid-19-to-plunge-global-economy-into-worst-recession-since-world-war-ii> (last visited Apr. 24, 2023).

6 S.O. 1702(E), Revised classification applicable *m.e.f.* July 1, 2020 for Micro, Small, and Medium Enterprises, available at: <https://msme.gov.in/know-about-msme> (last visited on Apr. 24, 2023).

7 Insolvency and Bankruptcy Code, No. 31 of 2016, s.4, India Code (2016).

8 Samir Malik and Aditya Sharma, *Quietus on the Threshold Limit for Filing Insolvency Proceedings*, SCC Online Blog (Dec. 24, 2022, 10:00 AM), available at: <https://www.scconline.com/blog/post/2022/06/14/quietus-on-the-threshold-limit-for-filing-insolvency-proceedings/#:~:text=The%20threshold%20was%20enhanced%20by%20the%20Central%20Government> (last visited on May 20, 2023).

9 Prachi Apte and Sushant Kumar Das, *Treatment of MSME Insolvency under IBC*, IBBI (Dec. 20, 2022, 10:00 AM), available at: <https://ibbi.gov.in/uploads/resources/b7dfd3332bc133fde5783cf70b9371a1.pdf> (last visited on May 20, 2023).

benefit the relatively smaller companies to find takers and prevent them from liquidation.<sup>10</sup>

Irrespective of the amendments under the Code, the number of MSMEs liquidated has been relatively high and in total conflict with the purpose of enactment of the Code, which promises rescue, revival and rehabilitation of distressed entities. Henceforth, the need of the hour is to have an efficient alternative insolvency resolution structure for the MSMEs, providing value-maximizing outcomes while being cost-effective.

### III Pre-packs under the Insolvency and Bankruptcy Code, 2016

#### Meaning of pre-pack

Pre-pack insolvency resolution is a combination of formal and informal debt restructuring methods aimed at restoring a financially troubled company to a stable state, thereby allowing creditors to receive their repayments in a timely manner. This process combines elements of both court-supervised insolvency proceedings and out-of-court settlements. Pre-packaged insolvency contains a reorganization plan approved by the creditors and offers a unique mechanism by giving flexibility of informal workouts and the legal sanctity of formal proceedings with appropriate defence for the stakeholders.<sup>11</sup>

The mechanism of CIRP under the Code is time-consuming and incurs direct and indirect costs, just like any other formal proceeding. On the contrary, informal workouts like PPIRP are a flexible and low-cost alternative for resolving insolvency. The pre-pack process allows for a quick sale of the business and its assets, preserving value and potentially saving jobs. By reorganizing the company's debts and assets, a pre-pack can increase the chances of the company's long-term success.<sup>12</sup>

In the United Kingdom, pre-packs involve sales to connected parties or persons of the debtor, for example, sales to the associates or directors of the company. Pre-packs have multiple benefits; when the company faces financial distress, the solvent corporations in the market might not be interested in purchasing an insolvent company. In such a situation, the incumbent management alone is the one interested in buying the business of the insolvent debtor. Furthermore, it would be incorrect to state that

---

10 Varsha Banerjee and Garima Mehra, "India: MSME's and Insolvency and Bankruptcy Code" *MONDAQ* (Dec. 23, 2022, 10:30 AM), available at: <https://www.mondaq.com/advicecentre/content/3826/MSMEs-And-Insolvency-And-Bankruptcy-Code> (last visited on May 20, 2023).

11 Debanshu Mukherjee *et al.*, "Pre-Packaged Insolvency Resolution under the Insolvency and Bankruptcy Code: An Overview", *Vidhi Legal Policy* (Jan. 25, 2023, 1:00 PM), available at: <https://vidhilegalpolicy.in/blog/pre-packaged-insolvency-resolution-under-the-insolvency-and-bankruptcy-code-ibc-an-overview/> (last visited on Apr. 20, 2023).

12 *Ibid.*

insolvency results from bad management practices. Thus, pre-packs grant the promoters and directors a second opportunity to run the company.<sup>13</sup> Further business failure is unavoidable, and pre-packaged insolvency provides a chance to restructure the business with lesser costs. Thus it results in a quick insolvency process focusing on the rescue and reorganization of the company.<sup>14</sup>

Initially, the Interim Report of the BLRC rejected pre-packs citing the infeasibility of the out-of-court settlement in the Indian context. But then, the COVID-19 pandemic disrupted the economic process, severely affecting businesses and increasing insolvency cases in India. The worst affected were the small businesses and start-ups that could not sustain in the market due to reduced sales and lockdown restrictions. The drastic impact of the pandemic on small businesses necessitated the policymakers to look into the feasibility of pre-packs in the Indian scenario. Henceforth, on April 4, 2021, the Insolvency and Bankruptcy Code (Amendment) Ordinance, 2021 introduced PPIRP for MSMEs. The amendment proposes an efficient insolvency resolution mechanism for MSMEs. It provides for a quicker, cost-effective, and value-maximizing insolvency process with less disruption to the business.

### Chapter III-A in the Code

The PPIRP is provided in the chapter III-A of the Insolvency and Bankruptcy Code, 2016. The salient provisions of the PPIRP are as follows:

#### *S. 54A. Corporate debtors eligible for PPIRP*

PPIRP application can be initiated for a Micro, Small and Medium Enterprise under section 7(1) of the Micro, Small and Medium Enterprises Development Act, 2006, when it commits a default, subject to the below-mentioned conditions:

- i. Not undergone PPIRP or completed CIRP during three years before initiation date;
- ii. Not undergoing CIRP;
- iii. Liquidation order not passed under section 33;
- iv. Eligible to submit a resolution plan under section 29A;
- v. Financial creditors have provided the name of the Insolvency Professional to act as Resolution Professional (*hereinafter* “RP”) for conducting PPIRP;

---

13 M.P. Ram Mohan and Vishakha Raj, “Pre-packs in the Indian Insolvency Regime”, *IIMA* (Jan. 27, 2023, 11:00 AM), *available at*: [https://www.researchgate.net/publication/344351741\\_Prepacks\\_in\\_the\\_Indian\\_Insolvency\\_Regime](https://www.researchgate.net/publication/344351741_Prepacks_in_the_Indian_Insolvency_Regime) (last visited on Apr. 20, 2023).

14 Sanjana Rao, *Insolvency Procedures- Investigating the Pre-Pack Paradigm in India*, 10 *L. Rev. Glc.* 69(2019), *available at*: <https://www.glcmbai.com/lawreview/volume10/Sanjana%20Rao.pdf>. last visited on Apr. 20, 2023).

- vi. Approval of proposal by the financial creditors with a minimum of 66 percent of financial debt due to creditors.
- vii. Declaration by the majority of directors & partners stating:
  - i. filing of the application to initiate PPIRP by the CD within 90 days;
  - ii. name of the Insolvency Professional to be appointed as RP;
  - iii. PPIRP is not initiated to defraud any person.
- viii. Special resolution by the members or resolution by a minimum of 3/4<sup>th</sup> of the total partners of the CD approving the filing of the PPIRP application.

Before seeking approval from the financial creditor, the CD must furnish the declaration, special resolution or resolution and base resolution plan to its financial creditor.

*S. 54B. Duties of insolvency professional*

The RP shall perform the below-mentioned duties:

- i. Preparing a report stating whether the CD fulfils the requirements and whether the base resolution plan is in conformity to the mandates in section 54A;
- ii. filing of reports and other documents with the Insolvency & Bankruptcy Board of India;
- iii. performing other duties as specified.

*S. 54C. Application to initiate PPIRP*

A corporate applicant has to apply with the NCLT to initiate PPIRP and has to provide the following information-

- i. the declaration, resolution, or special resolution, and financial creditors' approval;
- ii. insolvency professional's name and written consent;
- iii. declaration of any transactions of the CD on avoidance of transactions or fraudulent or wrongful trading;
- iv. information on books of account of the CD.

Within 14 days of receiving the application, NCLT has to admit or reject the application. On rejection, the applicant will be given seven days' notice to rectify the defect. The PPIRP commences from the date of admission of the application.

*S. 54D. Time limit for completion*

PPIRP should be completed within 120 days from the commencement date. A resolution plan needs to be submitted by the RP after approval by the committee of creditors (*hereinafter* "CoC") to the NCLT within ninety days starting from the commencement

date. If the CoC does not approve the resolution plan, the RP will file an application with the NCLT to terminate PPIRP.

*S. 54E. Declaration of moratorium and public announcement*

The NCLT shall declare a moratorium, appoint an RP and make a public announcement of the initiation of the PPIRP on the commencement date. The moratorium will be applicable until the date on which PPIRP ends.

*S. 54F. Duties and powers of RP*

The RP will conduct PPIRP and perform the duties as provided:

- i. confirming the list of claims;
- ii. informing creditors of their claims;
- iii. maintaining a list of claims;
- iv. monitoring the management of the company's affairs;
- v. informing the CoC of any breach of obligations by the BoD or partners of the CD;
- vi. constituting the CoC, convening and attending all its meetings;
- vii. preparing the information memorandum;
- viii. filing applications for the avoidance of transactions or fraudulent or wrongful trading.

The RP can access the books of account, records and information available with the CD, information utility, government authorities, statutory auditors, accountants or other persons. In addition, the RP will attend meetings of members, BoD, CoC, or partners of the CD, along with appointing accountants, legal professionals and other professionals.

*S. 54G. List of claims & preliminary information memorandum*

The CD has to submit a list of claims, details of the respective creditors, their guarantees, security interests, and preliminary information memorandum to the RP within two days of the commencement date. A promoter, director, or partner who has authorized the list of claims or the preliminary information memorandum submitted by the CD must compensate every person who has sustained loss/ damage due to the omission of material information or the inclusion of misleading information in the said documents.<sup>15</sup>

---

15 Insolvency and Bankruptcy Code, No. 31 of 2016, s. 77A.



*S. 54H. Management of CD's affairs*

The management of the affairs of the CD shall be vested in its BOD or its partners, who shall protect and preserve the property's value and manage the operations as a going concern. The members, promoters, personnel, and partners of CD shall exercise and discharge their contractual rights, statutory rights and obligations concerning the CD.

*S. 54I. Committee of creditors*

Within seven days of the insolvency commencement date, the RP shall constitute a CoC based on the list of claims. The first meeting of the CoC shall be held within seven days of its constitution.

*S. 54J. Vesting management of CD with the RP*

By a minimum vote of sixty-six percent of the voting shares, the CoC may resolve to confer the management of the CD with the RP during the PPIRP period. The RP shall make an application for the same to the NCLT. NCLT shall pass an order vesting its management with the RP if it believes that the business of CD has been conducted fraudulently or there has been gross mismanagement during the PPIRP.

*S. 54K. Consideration and approval of resolution plan*

The CD will submit the base resolution plan to the RP within two days of the pre-packaged insolvency commencement date, which shall be presented to the CoC. The CoC may allow the CD to revise the base resolution plan before approval or invitation of prospective resolution applicants. The resolution plan and base resolution plan shall comply with the requirements u/s 30 on *submission of the resolution plan*.

The CoC may approve the base resolution plan if it doesn't affect the claims of the operational creditors. If the CoC rejects the base resolution plan, the RP shall invite prospective applicants to submit a resolution plan to compete with the base resolution plan. The CoC will evaluate the resolution plans submitted by the RP and select the ones that are better than the base resolution plan. The RP will submit the resolution plan to the NCLT after approval of the CoC by a vote of a minimum of 66 % of the voting shares. If CoC rejects the resolution plan, the RP will apply for termination of PPIRP.

*S. 54L. Approval of resolution plan*

NCLT will approve or reject the resolution plan within 30 days of receiving the same. If the resolution plan is rejected, NCLT will pass an order u/s 54N for terminating the PPIRP.

*S. 54M. Appeal against an order under section 54L*

Any appeal can be filed against an order approving the resolution plan u/s 54L(1) can be filed if the approved resolution plan contravenes the law in force, or there is a

material irregularity in the exercise of RP's powers, or if the resolution plan is not in conformity to criteria provided by the Board and other conditions as mentioned u/s 61(3).

#### *54N. Termination of the PPIRP*

Where the RP files an application with the NCLT for termination of the PPIRP, the NCLT shall, within thirty days of the date of application, pass an order terminating the PPIRP and provide for a procedure for the continuance of proceedings relating to avoidance of transaction or wrongful/ fraudulent trading. The NCLT will pass an order of liquidation of the CD and declare that PPIRP costs will be included in the liquidation costs.

#### *54-O Initiation of the CIRP*

The CoC may resolve to initiate a CIRP in respect of the CD at any time after the pre-packaged insolvency commencement date but before the approval of the resolution plan under section 54K by a vote of a minimum 66% of the voting shares. NCLT can pass an order within 30 days of the intimation by the resolution professional of the decision of the CoC either to terminate PPIRP, to initiate CIRP, to appoint the RP as the interim resolution professional or to declare that PPIRP costs are to be included in the CIRP costs.

### **IV Assessing the impact of pre-packs**

#### **Advantages**

PIRP is a commendable step in providing a flexible, speedy and collaborative process for resolution of financial stress in the MSME sector. Especially in a scenario where the base resolution plan is accepted, the process is potentially far speedier and more cost effective than a CIRP process. The possibility of liquidation is a significant threat to the CD, especially to the MSMEs. There are various *advantages* of the pre-packs, which have been detailed as follows:

#### *Cost-effective, swift resolution and flexible approach*

PPIRP has served as a cost-effective insolvency resolution mechanism offering quicker resolution as compared to CIRP under the Code. CIRP works on a set process and is inflexible, limiting its use in specific scenarios, whereas pre-packs lessen a formal procedure's cost and offer higher flexibility.

#### *Continuity of the business*

Under CIRP, the company's control is shifted to an Interim Resolution Professional, then to a Resolution Professional, and finally to a successful Resolution Applicant. On the contrary, PPIRP offers flexibility, and the existing management comprising suppliers, investors, employees, customers, etc., remains in control of the CD before the parties

reach the final agreement. PPIRP causes minimum disruption to the business of the debtor. An attractive feature of the PPIRP mechanism is that the corporate debtor's business continues as a going concern, and the control is retained in the hands of the management, resulting in higher employee retention, unlike the conventional CIRP.

*Better returns to the creditors and lessens the burden on the adjudicating authorities*

Under the PPIRP scheme, the possibility of the liquidation of the CD reduces, yielding better returns to the creditors and maximizing the economic value of the property. In addition, since it is an out-of-court settlement, it minimizes the burden on the adjudicating authorities. Further, the mechanism under PPIRP is quicker, as a substantial portion of the proceedings is completed before approaching the NCLT.

*Avoids the possibility of hostile and conflicting takeover or buyout*

The PPIRP involves detailed negotiation and discussion with the investor or buyer, and thus there is a solid understanding of the long-term vision and business process. The possibility of conflicting or hostile buyout reduces as pre-packaged insolvency is initiated after COC's and NCLT's approval. There is the sanctity and strong credibility involved in the restructuring process.<sup>16</sup>

### **Challenges**

*Balancing the interests of financial and operational creditors and lack of transparency*

The PPIRP scheme is not devoid of challenges, and a significant concern in the scheme is to balance the interests of financial and operational creditors. It is evident that the framework is biased toward financial creditors. The scheme also lacks transparency, as there is a possibility that the financial creditors will agree with the potential investor privately, which might result in unfair treatment to the operational creditor.

*Price discovery mechanism is not followed*

Moreover, in PPIRP, the insolvency practitioner is under no legal compulsion to assess the business's future viability resulting from the pre-pack sale. Further, the price discovery mechanism is not followed, in contrast to the mandate under the CIRP. Instead, the NCLT only evaluates the resolution plan based on submissions made by the creditors.

*Stringent timeline*

Pre-pack has not proved feasible due to its tight timeline, precisely the 90-day window, which makes it difficult to resolve cases. Furthermore, with the automatic initiation of liquidation, the CD and its stakeholders might not even have a reasonable shot at

---

<sup>16</sup> Santosh Kumar and Vaishali Jain, "Pre-packaged Insolvency- Exploring an Alternative Framework for Bankruptcy Resolution in India" 107(1) *Ecs Transactions* 4129 (2022).

reviving the business. On the other hand, the related parties may benefit from pre-packs by taking advantage of re-engineering the balance sheet.

Currently, the pre-pack scheme is only limited to MSMEs, and according to the latest report of September 2022, only two cases- Delhi-based Loon Land Developers and Ahmedabad-based GCCL Infra-structure and Projects have been admitted under the pre-packaged mechanism so far. The poor response could result from hesitancy on the part of financial institutions and lack of awareness of PPIRP amongst businesses.

Even though IBC aims to facilitate exit from failed units so that capital can be reallocated to better ones, banks are uncomfortable initiating PPIRP due to voluntary haircuts, which might lead to subsequent scrutiny and investigations.<sup>1718</sup> Moreover, since the involved assets are not very large, the lenders do not feel inclined to take further risks.

### V Conclusion

MSMEs play a significant role in the growth and development of an economy. They are key players in promoting job creation, encouraging entrepreneurship, and fostering innovation. In addition, they drive economic activity by supplying goods and services to consumers and in supporting larger businesses through the supply chain. MSMEs also play a vital role in reducing poverty and improving living standards in rural and semi-urban areas. Furthermore, MSMEs are a foundation for local economic development and contribute to regional and national economic growth. Overall, MSMEs are a crucial component of a thriving economy.

The government has been proactively supporting the growth of MSMEs through various schemes, such as the Pradhan Mantri Mudra Yojana, the Credit Guarantee Trust Fund for Micro & Small Enterprises, Credit Linked Capital Subsidy for Technology Upgradation, and various other financial schemes. In addition, the pre-packaged insolvency resolution process for the MSMEs has further strengthened the insolvency regime in India. The mechanism helps achieve a steady and smoother tailor-made insolvency resolution of the distressed organization.

Though the government has been bringing out many schemes for the smooth functioning of MSMEs, there are no mechanisms to check the success of these schemes. Further, these schemes would require better grass-root implementation, which is not taking place in India. Under the insolvency mechanism in the Code, the resolution plan becomes final not based on the agreement of 66% of financial creditors but on

---

17 *Pre-Pack IBC Resolution, Civils Daily*, available at: <https://www.civilsdaily.com/news/pre-pack-ibc-resolution/> (last visited Apr. 18, 2023).

18 Banikinkar Pattanayak, “*Pre-pack insolvency May Get a Facelift*”, *Financial Express* (Jan. 23, 2023, 6:30 AM), available at: <https://www.financialexpress.com/industry/sme/pre-pack-insolvency-may-get-a-facelift/2705278/>. (last visited Apr. 18, 2023).

approval by the NCLT. This mandatory involvement of the judiciary impedes the speed of the pre-pack process, thus undermining its intended purpose.<sup>19</sup>

Further, given that pre-pack does not involve the public bidding process, it would be critical for the NCLT to satisfy that all stakeholders' interests are considered before approving the scheme.<sup>20</sup> Pre-packed insolvency will not be successful if a company's financial position is weak without any scope for recovery. Thus, the CD must be aware of the actual financial value of the business.

Further, there are concerns about the balance of interests of financial and operational creditors. The operational creditors do not have a decisive say in negotiations, nor the fair share, making the plan biased towards secured creditors. Further, there are possibilities of the advantage of pre-pack being taken by the related parties from restructuring the balance sheet.<sup>21</sup> Therefore, addressing the issue of transparency in the entire PPIRP and preventing collusion between the CD and the purchaser will also strengthen the pre-packaged framework.

Lately, the government has been trying to rework the scheme of PPIRP to make it more feasible after it has failed to attract debtors and creditors. In addition, the government plans to launch a campaign to raise awareness about the scheme amongst the masses. In the wake of the COVID-19 pandemic, a PPIRP for MSMEs envisaging a hybrid mechanism of negotiated debt restructuring, which is binding on all stakeholders on approval of the NCLT, would be a game-changer in the insolvency landscape if implemented cautiously.

The Deputy Governor of the Reserve Bank of India, M Rajeshwar Rao, at the International Research Conference on Insolvency and Bankruptcy held at IIM Ahmedabad, has also quoted that *"it is prudent that the lenders should perform periodic stress tests to estimate possible trajectories that the credit exposure is likely to take and calibrate their responses accordingly. Ultimately, they are responsible for safeguarding their and stakeholder's interests."* Further, he also emphasized that the group resolution process is particularly crucial in an economy like India, where credit contracts are traditionally linked with cross obligations and credit mitigating covers provided by the parent and group companies of the borrower. He also necessitated extending the applicability of pre-packs on

---

19 Tariq Khant, "Pre-Packs for MSMEs: A Positive Step with Implementation Hurdles" SCC OnLine (Jan. 23, 2023), available at: <https://www.scconline.com/blog/post/2021/07/20/pre-packs-for-msmes-a-positive-step-with-implementation-hurdles/> (last visited on Apr. 20, 2023).

20 Akriti Shikha, "Pre-packs – A Speedy Resolution Process?" ILJ (Jan. 22, 2023), available at: <https://www.indialawjournal.org/pre-packs-a-speedy-resolution-process.php> (last visited on Apr. 20, 2023).

21 *Supra* note 20.

corporates other than MSMEs.<sup>22</sup> The policymakers should revisit the PPIRP mechanism under the Code and introduce the necessary amendments. Since the pre-pack is in its nascent stage, there is immense scope for improvisation, which should be addressed timely to ensure effective implementation of the pre-packaged insolvency resolution process in the Indian framework.

*Puja Kumari\**  
*Prachi Tyagi\*\**

---

22 Resolution of Stressed Assets and IBC, [https://m.rbi.org.in/scripts/BS\\_SpeechesView.aspx?Id=1306](https://m.rbi.org.in/scripts/BS_SpeechesView.aspx?Id=1306) (last visited Jan. 20, 2023).

\* Research Scholar, School of Law, Bennett University.

\*\* Associate Professor, School of Law, Bennett University.