

Study Group Report on Taxation and Company Law Compliances Under IBC– Best Practices

(...continued from the previous edition)

4. Analysis of Challenges in Statutory Compliances during CIRP & Liquidation

While the statutory imperative for an Insolvency Professional (IP) to ensure compliance is unequivocal, the practical application of this duty is fraught with significant challenges. The interplay between the Insolvency and Bankruptcy Code, 2016, and other existing statutes creates numerous legal ambiguities and operational impediments. These challenges are not uniform and vary significantly depending on the specific legislation in question. This section provides a detailed analysis of the key challenges faced by IPs in ensuring compliance under various pivotal laws. It draws upon the extensive research, stakeholder consultations, and practical experiences gathered by the Study Group. The analysis is structured to first identify the specific legal or procedural issue, then to explore its practical impact on the CIRP or Liquidation process, thereby laying the groundwork for the best practices and legislative reforms recommended in subsequent sections.

4.1 Compliances under the Companies Act, 2013, and SEBI Regulations

The Companies Act, 2013, and the regulations issued by the Securities and Exchange Board of India (SEBI) govern the fundamental corporate and governance obligations of a company. For listed entities, these two legal frameworks are inextricably linked. During a CIRP or Liquidation, while the Board of Directors is suspended, the company as a legal entity continues to exist and remains subject to these provisions. This creates an immediate conflict between the normal functioning envisaged by company and securities law and the altered reality of a company managed by an IP. The primary challenges identified in this domain are

as follows:

4.1.1 Conundrum of Statutory Meetings and Corporate Approvals

The mechanism of corporate approvals under the Companies Act is predicated on a functional Board of Directors and an engaged body of shareholders. The initiation of CIRP renders this mechanism largely unworkable.

- **Board and Committee Meetings:** With the powers of the Board suspended under Section 17 of the Code, the convening of Board meetings and its various committees (e.g., Audit Committee, Nomination & Remuneration Committee, Stakeholders Relationship Committee) becomes a legal impossibility. All powers are vested in the IP, who acts in consultation with the Committee of Creditors (CoC). This suspension creates a governance vacuum that the law does not formally address with exemptions.
- **Annual General Meetings (AGMs):** The requirement to hold an AGM under Section 96 of the Companies Act presents a significant challenge. The primary purpose of an AGM is to consider and adopt the annual financial statements. However, with the Board suspended, the accounts cannot be approved by directors in the conventional manner before being presented to the shareholders. Furthermore, as the erstwhile promoters and their relatives often constitute the majority of shareholders, their cooperation in convening an AGM and adopting the accounts (which may contain qualifications or reflect poor performance) is frequently withheld. This creates a procedural deadlock, making a fundamental compliance of the Companies Act impracticable.

4.1.2 Preparation, Signing, and Auditing of Financial Statements

The finalisation of financial statements is a cornerstone of corporate compliance, yet it is an area fraught with obstacles for the IP.

- **Access to Information:** IPs frequently encounter non-cooperation from the suspended management and face situations where financial records are incomplete, missing, or inaccessible. This severely hampers the ability to prepare accurate financial statements for the period prior to and during the CIRP.
- **Signing of Financial Statements:** A significant point of contention is the legal responsibility for signing the financial statements. Section 134(1) of the Companies Act requires financial statements to be signed by directors. Suspended directors often refuse to sign, arguing that they no longer control the company's affairs. While IPs have the authority to manage the company, they are not designated as directors and may be hesitant to sign off on accounts for periods they did not oversee. The Hon'ble NCLAT, in the matter of *Mr. Mukund Choudhary vs. Mr. Subhash Kumar Kundra (RP for CLC Industries Ltd.)*, has clarified that the suspension of powers does not absolve directors of their duties and they are obligated to cooperate and sign the financial statements. Despite this judicial clarification, non-cooperation remains a persistent ground-level challenge requiring the IP to seek directions from the Adjudicating Authority, causing delays.
- **Appointment and Role of Statutory Auditors:** The process for appointment or re-appointment of a statutory auditor, which requires shareholder approval in an AGM, is disrupted. IPs often struggle to have auditors appointed or to secure the cooperation of existing auditors, who may have outstanding fees from the pre-CIRP period or may be unwilling to continue due to the complexities and risks involved.

4.1.3 Impediments in Statutory Filings with Regulatory Portals

Even when an IP manages to prepare the requisite documents, procedural and technical hurdles in filing them with the Registrar of Companies (ROC) present a major challenge.

- **MCA Portal Architecture:** The MCA-21 e-filing portal is designed for filings to be made by directors or other Key Managerial Personnel (KMP) using their Digital Signature Certificates (DSCs). The system architecture is not inherently equipped to recognise the role of an IP.
- **Workarounds and Their Limitations:** While the Ministry of Corporate Affairs (MCA) has issued circulars (e.g., General Circular No. 08/2020) providing workarounds—such as requiring the IP to first file Form INC28 to notify the appointment, and subsequently file other forms like AOC-4 and MGT-7 as attachments to Form GNL-2, signing as “CEO” for filing purposes—these are ad hoc solutions. They indicate a responsive approach from the Ministry but also highlight a deeper systemic issue: the lack of seamless integration between the IBC process and the standard corporate filing infrastructure. This multi-step, manual-override process is cumbersome, prone to error, and can lead to delays.

4.1.4 Specific Form-wise Filing Challenges

The general challenges in filing manifest as specific, acute problems when dealing with individual statutory forms. The following are key examples:

- **Form AOC-4 (Financial Statements) & Form MGT-7 (Annual Return):** These are the most critical annual filings and face the most significant hurdles.
- **Interdependency:** The filing of MGT-7 is contingent on the date of the AGM, and the filing of AOC-4 requires financial statements to be duly signed and adopted at the AGM. Since holding an AGM is often impracticable, a cascading failure occurs.

- **Data Field Constraints:** Form MGT-7 contains mandatory fields for details of Board and Committee meetings held during the year. As no such meetings are held post-CIRP initiation, the form cannot be accurately filled, leading to validation errors on the portal.
- **Form DIR-12 (Particulars of Appointment of Directors and KMP):**
- **Inapplicability during CIRP:** This form is used to report changes in the Board of Directors. During CIRP, the Board is suspended, not changed. The IP's appointment is notified via Form INC-28. There is no standard procedure to reflect the "suspension" status of existing directors in the MCA master data, leading to an inaccurate representation of the company's governance.
- **Post-Plan Complications:** Upon approval of a resolution plan that requires the appointment of a new Board, filing DIR-12 for the new directors can be problematic if the records for previous directors are not in order.
- **Form ADT-1 (Auditor Appointment):** The inability to convene an AGM makes it impossible to follow the standard procedure for auditor appointment or ratification, rendering the filing of this form problematic.
- **Forms for Charges (CHG-1, CHG-4):** Modifying or satisfying charges as part of debt restructuring is a key CIRP activity. However, filing these forms can be challenging without the active cooperation of the charge holders (lenders), who may be slow to provide the necessary authorisations.
- **Forms for Corporate Actions (e.g., PAS-3 - Return of Allotment, SH-7 - Notice for Alteration of Capital):**

These forms are critical for implementing a resolution plan that involves issuance of new shares to a resolution applicant or alteration of the company's capital structure. The successful filing of these forms is often hindered by the need for precedent actions (like shareholder resolutions) which are typically waived by the NCLT in the

resolution plan approval order. However, the portal's validation checks may not recognize such waivers, creating filing impediments that delay the legal and financial closure of the resolution plan.

- **Form DPT-3 (Return of Deposits):** The IP may not have access to complete historical records of deposits accepted by the company, making it difficult to file an accurate return.

4.1.5 Heightened Challenges for Listed Entities under SEBI Regulations

For companies whose securities are listed, the compliance burden is magnified due to the stringent and time-sensitive disclosure regime of the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 (LODR). The IP must effectively function as the Board, CEO, and Compliance Officer combined.

- **Continuous Disclosure Obligations (Regulation 30):** The LODR mandates disclosure of all material events. An IP, who is primarily focused on the resolution process, faces the immense challenge of identifying and disclosing such information within the stipulated timelines. This includes quarterly financial results, which suffer from the same finalisation and audit issues detailed above, leading to significant delays and potential non-compliance.
- **Specialised SEBI Filings:** The IP is confronted with numerous specialised compliance requirements for which they may lack historical data or context, including:
 - **Annual Secretarial Compliance Report (LODR 24A):** Requires a comprehensive review of past compliance, which is difficult for an IP to certify.
 - **Insider Trading Compliance (PIT Regulations):** The IP assumes responsibility for implementing the code of conduct, including maintaining a Structured Digital Database (SDD) and monitoring the trading window for designated persons, tasks complicated by the potential lack of a complete list of such persons from the erstwhile management.

- **Scheme of Arrangement Approvals:** If a resolution plan involves a scheme of arrangement, navigating the SEBI Master Circular on Schemes can be complex and time-consuming.
- **Related Party Transaction Disclosures (Regulation 23):** While SEBI has granted exemptions from shareholder approvals for related party transactions forming part of an NCLT-approved resolution plan, the IP must still ensure compliance with all other facets of the regulation during the CIRP, including identification of related parties and maintaining proper records, which can be difficult without historical context and cooperation.
- **Compliance with Minimum Public Shareholding (MPS):** A resolution plan that involves significant equity infusion to a new promoter can lead to the public shareholding falling below the mandated 25%. While rules provide a window to restore the MPS, this adds another layer of complexity for the incoming resolution applicant and must be factored into the plan, potentially affecting its attractiveness.

4.1.6 The Inherited Burden of Pre-CIRP Non-Compliance

The IP does not start with a clean slate. Upon appointment, the IP inherits a history of the corporate debtor's operations, which often includes a significant backlog of statutory non-compliances under both the Companies Act and SEBI regulations.

- **Unfulfilled Filing Obligations:** Typically, a company spirals into insolvency after a period of financial distress, during which statutory filings such as annual returns (MGT-7), financial statements (AOC-4), and various SEBI disclosures for one or more preceding years are often neglected. The IP is then faced with the monumental task of rectifying these historical defaults, a task made difficult by the aforementioned issues of data unavailability and non-cooperation.
- **Penalties and Prosecution:** This inherited non-compliance carries the risk of substantial

additional fees for delayed filings and potential prosecution against the company and its “officers in default.” The IP must then expend valuable time and resources seeking condonation of these delays or waivers from regulatory authorities, diverting focus from the core resolution activities.

4.1.7 Post-Resolution Plan Implementation Challenges

The challenges do not cease upon the approval of a resolution plan by the Adjudicating Authority. The new management, installed by the Successful Resolution Applicant (SRA), faces its own set of compliance hurdles as it seeks to regularise the company's affairs.

- **Rectification of Past Defaults:** The new Board of Directors assumes responsibility for a company whose public records with both the ROC and stock exchanges are often outdated and reflect a history of noncompliance. Bringing these records up to date, filing for condonation of delays for the pre-CIRP and CIRP periods, and ensuring the company master data is accurate is a complex and time-consuming process.
- **Transition of Authority:** Transitioning filing authority on the MCA portal and stock exchange portals from the IP back to the newly appointed directors of the revived company can be procedurally challenging. It requires proactive coordination with multiple regulators to ensure a smooth handover and to update the signatory details in the respective systems, failing which the new management may find itself unable to make statutory filings.
- **Impact of Waivers:** While a resolution plan approved under Section 31 of the Code is binding on all stakeholders, the extent to which it grants a blanket waiver for all past non-compliances under the Companies Act and SEBI Regulations is still a matter of debate. The new management often has to engage with authorities to have historical defaults formally addressed, even if they are covered by the plan's provisions.