



PREFERENTIAL TRANSACTIONS UNDER INSOLVENCY & BANKRUPTCY CODE, 2016

MAY 2020

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Table of Contents

I. Introduction	1
II. The Object Behind Permitting Avoidance of a Transaction.....	1
III. Brief Background on the Law Pertaining to Avoidance Transactions	2
IV. Important Concepts to Understand Avoidance Transactions	3
V. Preferential Transaction & Relevant Time:.....	4
i. Meaning of the term “Preferential Transaction”	4
ii. Who can approach the Adjudicating Authority?	4
iii. What would amount to a preferential transaction?	4
iv. Relevant time period for the preferential transaction	11
v. “Deemed to be given’	12
vi. Transactions which shall not be treated as preferential	13
vii. Remedies available against preferential transactions.....	15
viii. The persons upon whom Section 43 & 44 do not apply	16
VI. Summary of the Analysis of Section 43 of the Code	16

PREFERENTIAL TRANSACTIONS UNDER IBC, 2016

I. Introduction:

The Insolvency and Bankruptcy Code¹ (“Code”) is a beneficial legislation aimed to put the corporate debtor back on its feet.² It was enacted in 2016 by the Parliament of India to consolidate the law on reorganisation and insolvency resolution of corporate persons, partnership firm, individuals in a time bound manner.³ The objective of the Code was *inter alia* promoting entrepreneurship, innovation and managing interests of all stakeholders.⁴ This article discussed the law legislative background and objective behind the inclusion of provisions pertaining to ‘Avoidance Transactions’ under the Code, with special focus on preferential transactions.

II. The Object Behind Permitting Avoidance of a Transaction:

Under the Code, the Insolvency Resolution Professionals⁵ (“RP”) have been assigned the task of overseeing and managing the commercial aspects of Corporate Insolvency Resolution Process (“CIRP”).⁶ The RP is entrusted with the duty to protect and preserve the assets of the Corporate Debtor and manage the operations of the Corporate Debtor as a going concern.⁷ One of these duties include avoiding transactions which were made by the erstwhile management of the corporate debtor

¹ Act 31 of 2016.

² *Swiss Ribbons and Anr. v. Union of India and Ors.*, (2019) 4 SCC 17 ¶ 28.

³ The Insolvency and Bankruptcy Code, Preamble (2016).

⁴ Parliament passes the Insolvency and Bankruptcy Code, PIB, MoF, GOI, May 11, 2016, 10:44 IST, available at <https://pib.gov.in/newsite/printrelease.aspx?relid=145286>.

⁵ The Insolvency and Bankruptcy Code, s. 3(19) (2016).

⁶ Parliament passes the Insolvency and Bankruptcy Code, PIB, MoF, GOI, May 11, 2016, 10:44 IST, available at <https://pib.gov.in/newsite/printrelease.aspx?relid=145286>.

⁷ The Insolvency and Bankruptcy Code, s. 20(1) (2016).

in bad faith to protect its own interests over those of corporate debtor's. These transactions include Preferential, Undervalued, Extortionate Credit Transactions.⁸

The object behind the provisions regarding avoidance transaction is that once a transaction amounting to Preferential, Undervalued, Extortionate Credit is committed by the erstwhile management, then such transaction can be avoided or reversed, and such assets can be utilised by the RP or the liquidator to achieve the purpose of CIRP i.e. make the corporate debtor a running concern again.⁹ It ensures that a creditor is not placed in a beneficial position more than what such creditor would otherwise receive through the distribution of bankruptcy estate. Moreover, it ensures that *"the defaulters should not go scot free, if the funds have been syphoned away"*¹⁰.

III. Brief Background on the Law Pertaining to Avoidance Transactions:

The relevant provisions of Avoidance transaction are based on the UNCITRAL Legislative Guide on Insolvency Law¹¹ However, the avoidance transactions are not a new scheme under the laws of India. The Presidency Town Insolvency Act, 1909 and the Provincial Insolvency Act, 1920 dealt with such provisions.¹² These Acts barred the alienation of an asset by an insolvent individual to any person which would negatively affect the interest of bona fide creditors of such insolvent individual. U.S. Bankruptcy Code¹³ and the UK Insolvency Act¹⁴ also follow the same scheme.

The law pertaining to avoidance transactions is given under Chapter III of Part II of the Code and it applies to both insolvency proceedings and liquidation proceedings.

⁸ The Insolvency and Bankruptcy Code, s. 43, 45, 50(1), 66 (2016).

⁹ Swiss Ribbons v. Union of India, (2019) 4 SCC 17 ¶ 28.

¹⁰ SBI Global Factors Ltd. v. Sanaa Syntex Private Ltd., MA 436/2018 in CP No. 172/IBC/NCLT/MB/MAH/2017.

¹¹ UNCITRAL Legislative Guide on Insolvency Law, ¶ 173(b), 177 (2005).

¹² The Presidency Town Insolvency Act, s. 56(1909) and the Provincial Insolvency Act, s. 69 (1920).

¹³ 11 U.S.C. §547-8.

¹⁴ The UK Insolvency Act, s. 238-9, 244 (1986).

Sections 43, 45, 50¹⁵ lay down the substantive law on avoidance transactions. They deal with preferential transactions and relevant time, avoidance of undervalued transaction and extortionate credit transactions.

At the outset, it is imperative to note that even though the RP/liquidator has the power to decide whether according to him, a transaction is preferential/extortionate/undervalued/fraudulent, he cannot take any action by himself. He needs to approach the Adjudicating Authority (“AA”) for such determination and seek appropriate order.¹⁶

IV. Important Concepts to Understand Avoidance Transactions:

- i. A "corporate person"¹⁷ means:
 - a. A company as defined under the Companies Act, 2013 (Act 18 of 2013);
 - b. A limited liability partnership defined under the Limited Liability Partnership Act, 2008 (Act 6 of 2009); or
 - c. Any other person incorporated with limited liability under any law for the time being in force.
 - d. It does not include any financial service provider.

- ii. A "corporate debtor" means *“a corporate person who owes a debt to any person; financial creditor, an operational creditor, a secured creditor, an unsecured creditor and a decree-holder”*.¹⁸

- iii. A "debt"¹⁹ means:

¹⁵ Came into force on 15.12.2016.

¹⁶ The Insolvency and Bankruptcy Code, s. 25(2)(j); The Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, s. 39(2) (2016); CIRP Regulations, Reg. 35A; *Swiss Ribbons v. Union of India*, (2019) 4 SCC 17 ¶ 59-60.

¹⁷ The Insolvency and Bankruptcy Code, s. 3(7) (2016).

¹⁸ The Insolvency and Bankruptcy Code, s. 3(8) (2016).

¹⁹ The Insolvency and Bankruptcy Code, s. 3(11) (2016).

- a. A liability relating to a claim which is due from any person.
- b. It includes financial debt and operational debt.

V. Preferential Transaction & Relevant Time:

i. Meaning of the term “Preferential Transaction”

Section 43 and 44 of the Code pertain to preferential transactions. It is first important to understand the meaning of the term ‘Preferential Transaction’. The term preference has been defined in the Black’s Law Dictionary as *“the favouring of one person over one thing”*²⁰. The term ‘Transaction’ under the Code includes an *“agreement or arrangement in writing for the transfer of assets, or funds, goods or services, from or to the corporate debtor”*²¹. In turn the term ‘Transfer’ under the Code, *“includes sale, purchase, exchange, mortgage, pledge, gift, loan or any other form of transfer of right, title, possession or lien”*²². Finally, ‘Transfer of Property’ is defined as *“transfer of any property and includes a transfer of any interest in the property and creation of any charge upon such property”*²³ Thus, in the literal sense, ‘Preferential Transaction’ can be defined as an arrangement to transfer any asset to a person who is favoured/preferred amongst others.

ii. Who can approach the Adjudicating Authority?

The Code grants the power to the Liquidator/Resolution Professional to approach the Adjudicating Authority to avoid a transaction mentioned under Sub-section (2) of Section 43, which is made by the corporate debtor in the relevant period of time.

iii. What would amount to a preferential transaction?

²⁰ 10th Edn. Pp. 1369-70.

²¹ The Insolvency and Bankruptcy Code, s. 3(33) (2016).

²² The Insolvency and Bankruptcy Code, s. 3(34) (2016).

²³ The Insolvency and Bankruptcy Code, s. 3(35) (2016).

Section 43(2) of the Code lays down the conditions under which the liquidator or the RP can approach the Adjudicating Authority. It is a deeming provision and lays down twin considerations which needs to be proved before the Adjudicating Authority by the applicant.²⁴ First, a transfer of a property or interest therein of the corporate debtor is made for the benefit (intended or unintended)²⁵ of a creditor or a surety or a guarantor for or on account of an antecedent financial debt or operational debt or other liabilities owed by the corporate debtor. Second, such transfer should have the effect of putting such creditor or a surety or a guarantor, in whose favour the transfer is made, in a beneficial position than it would have been in the event of a distribution of assets being made in accordance with Section 53^{26, 27}

The Hon'ble Supreme Court in the matter of *Anuj Jain v. Axis Bank* (supra) set aside the mortgage transactions done by Corporate Debtor holding them as preferential transaction. The facts of the case were that Jaiprakash Associates Ltd. ("Jaiprakash") is the holding company of Jaypee Infratech Ltd. ("Jaypee"). Jaiprakash received working capital from certain banks. Jaypee put parcels of land under mortgage with the lenders of Jaiprakash. These transactions created security interest benefiting Jaiprakash. Jaiprakash had agreed to provide certain services to Jaypee, thus Jaypee owed financial and operational debts to Jaiprakash. As Jaiprakash was an operational debtor to Jaypee, and would have stood much lower in priority in case Jaypee went into liquidation, as such transfer of land put Jaiprakash in a beneficial position in relation to other creditors in terms of Section 53 of the Code. Further, the transfer/mortgage was made within 2 years of initiation of CIRP. Jaiprakash being a related party, these transactions fell within the time period mentioned under Section 43 of the Code. Finally, they were not carried within ordinary course of business as

²⁴ *Anuj Jain Interim Resolution Professional for Jaypee Infratech Ltd. v. Axis Bank Ltd. etc. etc.*, Civil Appeal Nos. 8512-8527 of 2019, 6777-6797 of 2019, 9357-77 OF 2019.

²⁵ *Id.*

²⁶ It regulates the distribution of proceeds from the sale of the liquidation assets.

²⁷ *The Insolvency and Bankruptcy Code, s. 43(2) (2016); Mr. S. V. Ramkumar, RP v. M/s. Orchid Health Care Pvt. Ltd.*, MA/86/2018 in CP/540/IB/CB/2017.

Jaypee was under tremendous financial stress and therefore could not have been providing mortgages to secure finances of its holding company.

The relevant extracts of the aforesaid judgement of The Hon'ble Supreme Court are as under: -

18.1. Looking at the broad features of Section 43 of the Code, it is noticed that as per sub-section (1) thereof, when the liquidator or the resolution professional, as the case may be, is of the opinion that the corporate debtor has, at a relevant time, given a preference in such transactions and in such manner as specified in sub-section (2), to any person/persons as referred to in sub-section (4), he is required to apply to the Adjudicating Authority for avoidance of preferential transactions and for one or more of the orders referred to in Section 44. If twin conditions specified in sub-section (2) of Section 43 are satisfied, the transaction would be deemed to be of preference. As per clause (a) of sub-section (2) of Section 43, the transaction, of transfer of property or an interest thereof of the corporate debtor, ought to be for the benefit of a creditor or a surety or a guarantor for or on account of an antecedent financial debt or operational debt or other liabilities owed by the corporate debtor; and as per clause (b) thereof, such transfer ought to be of the effect of putting such creditor or surety or guarantor in beneficial position than it would have been in the event of distribution of assets under Section 53.

18.2. However, merely giving of the preference and putting the beneficiary in a better position is not enough. For a preference to become an offending one for the purpose of Section 43 of the Code, another essential and rather prime requirement is to be satisfied that such event, of giving preference, ought to have happened within and during the specified time, referred to as "relevant time". The relevant time is reckoned, as per sub-section (4) of Section 43 of the Code, in two ways: (a) if the preference is given to a related party (other than an employee), the relevant time is a period of two years preceding the insolvency commencement date; and (b) if the preference is given to a person other than a

related party, the relevant time is a period of one year preceding such commencement date. In other words, for a transaction to fall within the mischief sought to be remedied by Sections 43 and 44 of the Code, it ought to be a preferential one answering to the requirements of sub-section (2) of Section 43; and the preference ought to have been given at a relevant time, as specified in sub-section (4) of Section 43.

18.3. However, even if a transaction of transfer otherwise answers to and comes within the scope of sub-sections (4) and (2) of Section 43 of the Code, it may yet remain outside the ambit of sub-section (2) because of the exclusion provided in sub-section (3) of Section 43.

18.4. Sub-section (3) of Section 43 specifically excludes some of the transfers from the ambit of sub-section (2). Such exclusion is provided to:

- (a) a transfer made in the ordinary course of business or financial affairs of the corporate debtor or transferee;*
- (b) a transfer creating security interest in a property acquired by the corporate debtor to the extent that such security interest secures new value and was given at the time specified in sub-clause (i) of clause (b) of Section 43(3) and subject to fulfilment of other requirements of sub-clause (ii) thereof. The meaning of the expression "new value" has also been explained in this provision.*

.....

19.1. To put it more explicit, the sum total of sub-sections (2) and (4) is that a corporate debtor shall be deemed to have given a preference at a relevant time if:

- (i) the transaction is of transfer of property or the interest thereof of the corporate debtor, for the benefit of a creditor or surety or guarantor for or on account of an antecedent financial debt or operational debt or other liability;*
- (ii) such transfer has the effect of putting such creditor or surety or guarantor in a beneficial position than it would*

have been in the event of distribution of assets in accordance with Section 53; and

(iii) preference is given, either during the period of two years preceding the insolvency commencement date when the beneficiary is a related party (other than an employee), or during the period of one year preceding the insolvency commencement date when the beneficiary is an unrelated party.

.....

19.4. Even when the above-stated indicting parts of Section 43 as occurring in sub-sections (4) and (2) are satisfied and the corporate debtor is deemed to have given preference at a relevant time to a related party or unrelated party, as the case may be, such deemed preference may yet not be an offending preference, if it falls into any or both of the exclusions provided by sub-section (3) i.e., having been entered into during the ordinary course of business of the corporate debtor or transferee or resulting in acquisition of new value for the corporate debtor.

Net concentrate of Section 43

19.5. Thus, the net concentrate of Section 43 is that if a transaction entered into by a corporate debtor is not falling in either of the exceptions provided by sub-section (3) and satisfies the three-fold requirements of sub-sections (4) and (2), it would be deemed to be a preference during a relevant time, whether or not in fact it were so; and whether or not it were intended or anticipated to be so.

20. The analysis foregoing leads to the position that in order to find as to whether a transaction, of transfer of property or an interest thereof of the corporate debtor, falls squarely within the ambit of Section 43 of the Code, ordinarily, the following questions shall have to be examined in a given case:

(i). As to whether such transfer is for the benefit of a creditor or a surety or a guarantor?

(ii). *As to whether such transfer is for or on account of an antecedent financial debt or operational debt or other liabilities owed by the corporate debtor?*

(iii). *As to whether such transfer has the effect of putting such creditor or surety or guarantor in a beneficial position than it would have been in the event of distribution of assets being made in accordance with Section 53?*

(iv). *If such transfer had been for the benefit of a related party (other than an employee), as to whether the same was made during the period 73 of two years preceding the insolvency commencement date; and if such transfer had been for the benefit of an unrelated party, as to whether the same was made during the period of one year preceding the insolvency commencement date?*

(v) *As to whether such transfer is not an excluded transaction in terms of sub-section (3) of Section 43?*

Ordinary course of business or financial affairs

25. *Even when it is held that the impugned transactions answer to the requirements of sub-section (2) of Section 43 and fall within the period specified in sub-section (4) thereof, the question still remains as to whether the impugned transactions do or do not fall within the exclusion provided by subsection (3) of Section 43 of the Code? As noticed, two types of transfers, as specified in clauses (a) and (b) of sub-section (3) of Section 43, are not to be treated as preference for the purpose of sub-section (2). It has been the mainstay of respondent-lenders that, in any case, the transfers in question were made in the ordinary course of their business and hence, fall within clause (a) of Section 43(3) that excludes the transfer made in the ordinary course of business or financial affairs of the corporate debtor or the transferee. It has been forcefully argued that the lenders of JAL are the transferees in the transactions in question and their ordinary course of business being of providing financial support with loans and advances, such transfers are not included in sub-*

section (2) of Section 43 by virtue of the exclusion provided in sub-section (3) thereof. On the other hand, the main plank of submissions on behalf of the appellants has been that the expression “or” occurring in clause (a) of sub-section (3) of Section 43, seemingly disjunctive of corporate debtor on one hand and transferee on the other, is required to be read as “and” so as to be conjunctive and covering only the transfers made in the ordinary course of business or financial affairs of the corporate debtor and the transferee. It is submitted on behalf of the appellants that such mortgage transactions had neither been in the ordinary course of business or financial affairs of the corporate debtor JIL nor secure new value in the property acquired by the corporate debtor and hence, are not excepted transactions within the meaning of sub-section (3) of Section 43 of the Code.

29.1. However, we are impelled to make one comment as regards the application made by IRP. It is noticed that in the present case, the IRP moved one composite application purportedly under Sections 43, 45 and 66 of the Code while alleging that the transactions in question were preferential as also undervalued and fraudulent. In our view, in the scheme of the Code, the parameters and the requisite enquiries as also the consequences in relation to these aspects are different and such difference is explicit in the related provisions. As noticed, the question of intent is not involved in Section 43 and by virtue of legal fiction, upon existence of the given ingredients, a transaction is deemed to be of giving preference at a relevant time. However, whether a transaction is undervalued requires a different enquiry as per Sections 45 and 46 of the Code and significantly, such application can also be made by the creditor under Section 47 of the Code. The consequences of undervaluation are contained in Sections 48 and 49. Per Section 49, if the undervalued transaction is referable to sub-section (2) of Section 45, the Adjudicating Authority may look at the intent to examine if such undervaluation was to defraud the creditors. On the other hand, the provisions of Section 66 related to fraudulent trading and wrongful trading entail the liabilities on the persons

responsible therefore. We are not elaborating on all these aspects for being not necessary as the transactions in question are already held preferential and hence, the order for their avoidance is required to be approved; but it appears expedient to observe that the arena and scope of the requisite enquiries, to find if the transaction is undervalued or is intended to defraud the creditors or had been of wrongful/fraudulent trading are entirely different. Specific material facts are required to be pleaded if a transaction is sought to be brought under the mischief sought to be remedied by Sections 45/46/47 or Section 66 of the Code. As noticed, the scope of enquiry in relation to the questions as to whether a transaction is of giving preference at a relevant time, is entirely different. Hence, it would be expected of any resolution professional to keep such requirements in view while making a motion to the Adjudicating Authority.

The NCLT, Special Bench at Chennai²⁸ dealt with one such transaction where a transfer is made to a creditor by the corporate debtor in pursuance of mutual dealings and obligations between the parties. The Ld. Tribunal held that as the adjustments are made in respect of payments to be made against each other, it cannot be held as preferential transaction. As these adjustments do not have the effect of putting such a creditor in a beneficial position as to the other creditors, in the event of waterfall.

- iv. Relevant time period for the preferential transaction to have deemed to have taken place

Further, the aforementioned transaction is only deemed to be a preferential transaction if it is made within a stipulated period of time. There are two scenarios of such period mentioned under Section 43(4) of the Code:

²⁸ Mr. S. V. Ramkumar, RP v. M/s. Orchid Health Care Pvt. Ltd., MA/86/2018 in CP/540/IB/CB/2017.

- a. Where transfer is made to a related party: The look back period is of 2 years preceding the insolvency commencement date.
 - b. Where transfer is made to a person other than a related party: The look back period is of 1 year preceding the insolvency commencement date.
- v. “Deemed to be given”

Section 43(2) and (4) use the phrase “*deemed to have given a preference*” and “*deemed to be given at a relevant time*”. This has the effect of making Section 43 of the Code a deeming fiction. The true meaning of deemed provision was discussed extensively in *Hindustan Cooperative Housing Building Society Ltd. v. Registrar, Cooperative Societies and Anr.*²⁹, wherein it was observed that:

- a. Sometimes “deemed” is used to impose an artificial construction of a word that would otherwise not prevail.
- b. Sometimes it is used to put beyond a doubt a particular construction that otherwise may be uncertain.
- c. Sometimes when a statute adds certain things as deemed to be covered in a definition, it does not matter whether without such addition, the definition would have covered them or not.
- d. The conclusive or rebuttable nature of the deemed provision depends upon the context in which the statute is used.

The Hon’ble Supreme Court in *Anuj Jain Interim Resolution Professional for Jaypee Infratech Ltd. v. Axis Bank Ltd.*³⁰ applied the principles of dealing with meaning of “deemed” to Section 43 and held that:

19.3. ... any transaction that answers to the descriptions contained in sub-sections (4) and (2) is presumed to be a

²⁹ (2009) 14 SCC 3012 pp. 13-16; *Pioneer Urban Land and Infrastructure Ltd. v. Union of India*, (2019) 8 SCC 416.

³⁰ Civil Appeal Nos. 8512-8527 of 2019, 6777-6797 of 2019, 9357-77 OF 2019.

preferential transaction at a relevant time, even though it may not be so in reality. In other words, since sub-sections (4) and (2) are deeming provisions, upon existence of the ingredients stated therein, the legal fiction would come into play; and such transaction entered into by a corporate debtor would be regarded as preferential transaction with the attendant consequences as per Section 44 of the Code, irrespective whether the transaction was in fact intended or even anticipated to be so.

[Emphasis Supplied]

vi. Transactions which shall not be treated as preferential

a. Sub-section (3) of Section 43 lists down certain exceptions to the general definition of transfer which are deemed to be made for the purpose of this section.

- (i) Such transactions are made in the ordinary course of the business or financial affairs of the corporate debtor or the transferee.
- (ii) Any transfer creating a security interest in property acquired by the corporate debtor to the extent that such security interest secures new value³¹. It should have been given at the time of or after the signing of a security agreement that contains a description of such property as security interest. Also, it should be used by corporate debtor to acquire such property. It is also subject to the fulfilment of requirements mentioned under sub-clause (ii), which are that such transfer should have been registered with an information utility on or before thirty days after the corporate debtor receives possession of such property.

³¹ The Insolvency and Bankruptcy Code, s. 43 (2016) “*Explanation.*—For the purpose of sub-section (3) of this section, "new value" means money or its worth in goods, services, or new credit, or release by the transferee of property previously transferred to such transferee in a transaction that is neither void nor voidable by the liquidator or the resolution professional under this Code, including proceeds of such property, but does not include a financial debt or operational debt substituted for existing financial debt or operational debt.”

- b. Meaning of “*Ordinary Course of Business*”: The term “Business” has been defined by the Hon’ble Supreme Court in the matter of *Barendra Prasad Ray v. ITO*³², as “one of wide import and it means an activity carried on continuously and systematically by a person by the application of his labour or skill with a view to earning an income. It does not necessarily mean trade or manufacture only and includes within its scope professions, vocations and callings from a fairly long time” Further, the term “Ordinary” has been defined by the Hon’ble Supreme Court in the case of *Bajaj Allianz General Insurance Co. Ltd. and Another v. State of Madhya Pradesh*³³ as follows:

*P. Ramanatha Aiyar's Law Lexicon, defines the expression “ordinary”:
 “Regular; usual; normal; common; often recurring; according to established order; settled; customary; reasonable; not characterised by peculiar or unusual circumstances; belonging to, exercised by, or characteristic of, the normal or average individual.*

Thus, ‘Ordinary Course of Business’ means any normal business task, which does not arise out of a special or particular situation for the meaning of the Code. Such task should fall in place as a part of the undistinguished common flow of the business. Hence, for the purpose of the section³⁴, transactions made during the usual course of business do not fall under the scope of preferential transactions.³⁵

- c. It is important to be highlighted here that lack of intention or knowledge is not a valid defense to such transactions.³⁶

³² (1981) 2 SCC 693.

³³ 2020 SCC OnLine SC 401.

³⁴ The Insolvency and Bankruptcy Code, s. 43 (2016).

³⁵ *Tirumala Balaji Alloys Private Ltd. v. Sumit Binani, CA (AT) (Ins.) No. 600 of 2018*; *Anup Kumar, Resolution Professional of M/s. Shivkala Developers Pvt. Ltd. v. BDR Builder & Developers Pvt. Ltd., CA (AT) (Ins.) No. 679 of 2018*.

³⁶ *Supra* note 24.

vii. Remedies available against preferential transactions

Once the applicant before the Adjudicating Authority (the liquidator or the RP) is able to satisfy the Authority that the impugned transaction is preferential in nature, the Adjudicating Authority may grant such reliefs as mentioned under Section 44 of the Code. These remedies “operate towards annulling the effect of such transactions”³⁷.

The remedies mentioned under Section 44 are that the Adjudicating Authority may:

- a. require the impugned property to be vested in the corporate debtor;
- b. require any property to be vested if it represents the application
 - (i) of the proceeds of sale of property so transferred; or
 - (ii) of money so transferred;
- c. release or discharge the whole or a part of any security interest created by the corporate debtor;
- d. require any person to pay such sums in respect of benefits received by him from the Corporate Debtor, such sums to the Liquidator or the Resolution Professional;
- e. direct any guarantor, whose financial debts or operational debts owed to any person were released or discharged (in whole or in part) by the giving of the preference, to be under such new or revived financial debts or operational debts to that person as the Adjudicating Authority deems appropriate;
- f. direct for providing security or charge on any property for the discharge of any financial debt or operational debt, to be treated with the same priority as a security or charge released or discharged by the giving of the preference; and
- g. direct for providing the extent to which any person whose property is so vested in the corporate debtor, or on whom financial debts or operational debts are imposed by the order, are to be proved in the liquidation or the corporate insolvency resolution process for financial debts or operational debts which

³⁷ Supra note 24.

arose from, or were released or discharged wholly or in part by the giving of the preference.

- viii. The persons upon whom Section 43 & 44 do not apply

The proviso to Section 44 states that an order cannot be passed under Section 44 of the Code which:

- a. Interferes with the interest in a property owned by a person who is not the corporate debtor; or
- b. Interferes with the interest in the property owned by a person who has acquired such interest from the corporate debtor in good faith and for value;
- c. Involves a person who received a benefit from the preferential transaction in good faith and for value and necessitate him to pay a sum to the liquidator or the RP.

It is to be noted that if in the forestated circumstances, such a person had sufficient information³⁸ of the initiation or commencement of CIRP of the corporate debtor, or was a related party, then there arises a statutory rebuttable presumption at the interest was acquired or the benefit was received otherwise than in good faith.

VI. Summary of the Analysis of Section 43 of the Code

The Hon'ble Supreme Court in the matter of *Anuj Jain v. Axis Bank* (supra) has in clear and simple terms mentioned the ingredients a liquidator or RP would need to satisfy to avail the remedies available under Section 44 of the judgment. The relevant extracts of the judgment are reproduced hereinunder:

20. ...

(i). *As to whether such transfer is for the benefit of a creditor or a surety or a guarantor?*

³⁸ The Insolvency and Bankruptcy Code, s. 44 (2016) "Explanation II.—A person shall be deemed to have sufficient information or opportunity to avail such information if a public announcement regarding the corporate insolvency resolution process has been made under section 13."

(ii). As to whether such transfer is for or on account of an antecedent financial debt or operational debt or other liabilities owed by the corporate debtor?

(iii). As to whether such transfer has the effect of putting such creditor or surety or guarantor in a beneficial position than it would have been in the event of distribution of assets being made in accordance with Section 53?

(iv). If such transfer had been for the benefit of a related party (other than an employee), as to whether the same was made during the period of two years preceding the insolvency commencement date; and if such transfer had been for the benefit of an unrelated party, as to whether the same was made during the period of one year preceding the insolvency commencement date?

(v) As to whether such transfer is not an excluded transaction in terms of sub-section (3) of Section 43?

Thus, the provisions of avoidable transactions ensure that no dishonest promoter or director of a corporation can manipulate the process of waterfall by wrongfully entering into preferential transactions agreeing to transfer its assets just prior to initiation of CIRP in favour of a few to the detriment of creditors at large. The negation of such transactions help protects *bona fide* creditors from fraud by a corporation which attempts to abuse the provisions of the Code at the point when insolvency which, to the knowledge of the management, is right around the corner.

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Ashish Aggarwal (D-455/89)
Gurkamal Hora Arora (D-1617/95)
Amit Bhatnagar (D-1554/02)
Subodh K Pandey (D-3860/12)
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