

# ASSET RECONSTRUCTION COMPANIES (ARCs) AND IBC: AN INTERPLAY BETWEEN SECURITIZATION AND RESOLUTION IN THE IBC REGIME

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## ABSTRACT

Asset Reconstruction Companies (ARCs) under the SARFAESI Act, 2002 are the fulcrum point in the realization of dues to the secured creditor by Asset Reconstruction or Securitisation. However, a third mechanism can be adopted by the ARCs for the realization of dues by way of the Resolution of the company under the Insolvency and Bankruptcy Code (IBC), and this has a two-fold benefit- Realisation of dues of the secured creditor and the Resolution of an Insolvent company. This confluence between the SARFAESI Act and IBC through the medium of ARCs is possible by the insertion of Section 29A in IBC, coupled with the Proviso to Section 15(4) of the SARFAESI Act. However, these positive confluences between the SARFAESI Act and the IBC by way of ARCs acting as Resolution Applicants are marred with certain lacunas like the recent RBI notification in 2022 requiring the ARCs to have a minimum of Rs. 1000 Crores as the Net Owned Fund (NOF) creating a vacuum for small ARCs in resolution of certain companies, an exception like provision for ARCs to be the Resolution Applicants only upon joint acquisition of property with the secured creditors under Section 15(4), and so on. These vacuums can be filled by amendments to the SARFAESI Act by expanding the function of ARCs from just Realisation to Realisation as well as Resolution of distressed companies, inserting a provision, creating a class of ARCs to be resolution applicants and their approval by RBI, into the IBC regime itself, and so on. By incorporating excerpts from websites, articles, and books, the paper aims to rectify the contemporary landscape of ARCs in the domain of Insolvency and Bankruptcy under the IBC, their role as a Resolution Applicant, the lacunas creating hindrances to ARCs in entering the IBC regime, and the possible solutions to it by paying heed to the foreign practices dealing with Realisation to Banks and Restructuring of Companies simultaneously. This paper aims to showcase the confluence of the SARFAESI Act in the domain of IBC through ARCs.

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## I. INTRODUCTION

The growing effect of loan borrowing in India on an individual capacity by the consumers on the retail market level proliferated the liquidity in the market lent by Financial Institutions<sup>1</sup> [‘Entities’] due to the rise in per capita income of the public after the onset of the LPA policy. On one side, the liquidity in terms of loan borrowing increased, and on the other side, the default by the debtors on the loan so committed to them started increasing which started increasing the distress on the Entities, thus creating an economic imbalance. So, the lawmakers formulated legislation to curb the menace of default by the debtors due on the Secured Creditors [‘Creditors’], the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act 2002 [‘SARFAESI’] created “with the object of expediting and overhauling the process of reconstruction of financial assets in favour of secured creditors, implementing the recommendations of the Narasimham Committee II by greenlighting the setting up of ARCs in India”.<sup>2</sup> Under this legislation, the main actors facilitating the object of the Act are- Debtor, Creditor, and Asset Reconstruction Companies [‘ARCs’].

<sup>1</sup> Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act 2002, s 2.

<sup>2</sup> Manmeet Kaur, Anjali Dwivedi, Gurtejpal Singh, 'ARCs as Resolution Applicants under IBC?' (Mondaq, 20 July 2022) <<https://www.mondaq.com/india/insolvencybankruptcy/1213590/arcs-as-resolution-applicants-under-ibc>> accessed 19th January 2025.

The ARCs are the entities “that are endowed with the responsibility of taking over bad and doubtful assets off the balance sheets of the Entities and allow lenders to recycle their funds and direct the same into generating new productive assets, and are designed to allow Creditors to focus on their core function of lending, by removing sticky stressed financial assets from their books”.<sup>3</sup> The ARCs are the independent entities that divest themselves upon the application of the creditor to reconstruct the default due to the creditor by two processes- Securitization<sup>4</sup> and Asset Reconstruction<sup>5</sup>. They play a crucial role under the SARFAESI Act in realizing dues for the creditor through the usage of Security Interest and channelizing the proceeds of the interest to the creditor by taking measures for reconstructing the secured assets<sup>6</sup> or any other measure.<sup>7</sup> Although the entire gamut of the ARC framework is discussed under the SARFAESI Act, a lacuna remains in expediting the process of asset reconstruction and mitigating the debt default when their role in the Insolvency and Bankruptcy Code [‘IBC’] is left untouched and the plight of the distressed debtors is not taken into consideration when the route of SARFAESI is taken into consideration by the Creditors.

Therefore, this paper will discuss how the mechanism of ARCs under the SARFAESI regime which is primarily of Securitization can be utilized simultaneously under the IBC framework (for only Corporate Entities and not Individual or Partnership Firms), thereby maintaining a fair balance of the interests of the Creditors and the Debtors and providing an inclusive

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<sup>3</sup> Reserve Bank of India, Report of the Committee to Review the Working of Asset Reconstruction Companies, September 2021.

<sup>4</sup> Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act 2002, s 2(z).

<sup>5</sup> Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act 2002, s 2(b).

<sup>6</sup> Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act 2002, s 9.

<sup>7</sup> Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act 2002, s 5.

framework for the ARCs to function both as a Resolution Applicant [‘RA’] and the Resolution Professional [‘RP’] in a Corporate Restructuring (in general), and Liquidation (in particular cases).

## II. CORRELATION BETWEEN ARCS AND SECURITIZATION

The SARFAESI Act provides a definite framework for the functioning of ARCs for the realization of dues by the process of Securitization (generally). Securitization, in common parlance, is a “financial process of pooling and repackaging debt into securities that are sold to investors.”<sup>8</sup> The IMF defines Securitization as follows-

“Securitization is the process in which certain types of assets are pooled so that they can be repackaged into interest-bearing securities, and the interest and principal payments from the assets are passed through to the purchasers of the securities.”<sup>9</sup>

Taking into consideration the definition of Securitization under the SARFAESI Act, ‘Securitization’ in toto means the acquisition of financial assets by an ARC from the creditor, raising the claim of realization of dues, and converting it into securities (can be a bond, debenture, or another type of security) which is to be sold to qualified buyers as selected by the ARC in order to offset the debt liability of the Debtor and to make proceeds of such sale to the Creditor. These Securities, which are created out of such distressed assets/collateral, are usually in the form of Debentures and are backed by such assets.

The mechanism of Securitization under the SARFAESI Act works in such a way that the interests of creditors are kept at the highest consideration. Under

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<sup>8</sup> John A Pearce II and Ilya A. Lipin, ‘Special Purpose Vehicles in Bankruptcy Litigation,’ (2011) 40 Hofstra L.R. 177, 178.

<sup>9</sup> Andrew Jobst, ‘What is Securitization?’ (*IMF*, 21 August 2008) <<https://www.imf.org/external/pubs/ft/fandd/2008/09/pdf/basics.pdf>> accessed Jan 19, 2025.

this framework, the ARCs for securitization “create trusts that are governed by the provisions of the Indian Trust Act 1882 wherein, the Security Receipts [‘SR’] are secured in the Trust in the name of Qualified Buyers [‘QB’] (as decided by the ARCs).”<sup>10</sup> This trust is created for the sole purpose of transacting SRs to Qualified Buyers, created out of the security interest of the debtor,<sup>11</sup> whose existence becomes defunct as soon as the payment of dues to the Creditor is made, ARCs receive their remuneration and incentives (if any), and the QBs receive their SR making a consideration to the Trust for such SRs. So, the Trust Route to facilitate Securitization under the SARFAESI Act consists of a tri-partite body- ARCs as Trustees, QBs as Beneficiaries, and the Debtor as Settlers, and out of such tri-partite structure, the dues are realized to the creditor. Within this structure, the Sudarshan Sen Committee on the working of ARCs has recommended “that the ARCs maintain a minimum threshold of 15% of the SRs in their account.”<sup>12</sup>

On the other side, another pivotal function of ARCs under the SARFAESI regime is that of Asset Reconstruction. In this, an ARC performs multi-fold functions to secure the realization of dues to the Creditors which are- “taking over the affairs of the company in terms of its management, making a sale or lease of the security interest, rescheduling of payment by the debtor, settlement of dues by the debtor, enforcement of Security Interest, and so on.”<sup>13</sup> These functions replicate the functions of an RP whose sole object of functioning under IBC is to restructure the distressed company and make the realization of dues to the creditors, thereby playing the role of the Trustee and

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<sup>10</sup> Reserve Bank of India (n 3).

<sup>11</sup> Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act 2002, s 7.

<sup>12</sup> Reserve Bank of India (n 3).

<sup>13</sup> SARFAESI (n 6).

facilitating the expeditious delivery of dues to the creditors and mitigating the distressed situation of the debtor.

### **III. RESOLUTION APPLICANTS AND RESOLUTION PROFESSIONALS: THE CHIEFTAINS IN THE IBC REGIME**

One of the similarities between the SARFAESI Act and the IBC is that both legislations aim at mitigating the financial wreckage due to a high number of defaults and claims of bankruptcy. However, what makes both the legislations different is that while the former deals only with the realization of dues of the Creditor, whereas the latter provides for the realization of dues to different kinds of Creditors in a hierarchical formula (Waterfall Mechanism)<sup>14</sup> as well as the restructuring of the Debtor whose financial stakes are at distressed end thereby providing an inclusive mechanism for maintaining a healthy and sound economic and financial ecosystem in the market. Both legislations strive for an official in the form of a supervisor, ARCs in the former case and the RPs in the latter case, and both of them facilitate the financial means of alleviating the financial distress of a Debtor by offsetting his debts due to the creditor, one by Securitization and Asset Reconstruction, and the other by Corporate Restructuring and Liquidation (worst case scenario).

The IBC has been formulated as a complete code to fill the vacuum of restructuring any sick/distressed/bankrupt Debtor and simultaneously working at realizing the claims of the Creditor. There are two species under the IBC regime that play a chief role in fulfilling the ambition of IBC- Resolution Applicants (RA) and Resolution Professionals (RP). In the IBC framework, RA is “an individual who, either individually or with others, submits a

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<sup>14</sup> Insolvency and Bankruptcy Code 2016, s 53.

Resolution Plan to the RP under Section 30 IBC.”<sup>15</sup> An RP, on the other hand, is “an individual who supervises the Corporate Insolvency Resolution Process (CIRP) and can also be an Interim Resolution Professional.”<sup>16</sup> Both of them facilitate the CIRP by outlining a sketch of the claims of the Creditor in the form of a Resolution Plan in which, the RA prepares and submits such plan and the RP verifies it and executes it leading to the restructuring of the Debtor from financial sickness and the realization of claims made by the Creditor.

Stating the brief outline of the IBC framework, an insolvency process can commence only “upon the application for initiation of CIRP by the Debtor or the Creditor, as the case may be”<sup>17</sup> after which, the Creditor (in our case, the Financial Creditor since as far as SARFAESI Act is concerned, only the claims regarding financial debt is made) shall “make an application for initiation of CIRP before the Adjudicatory Authority [‘Adjudicator’], stating- a) Record of Default; b) Name of the RP; c) Any other information as may be prescribed.”<sup>18</sup> After an interim RP is appointed by the Adjudicator<sup>19</sup> He shall verify the claims of all the creditors, collate their claims, and then constitute a Committee of Creditors [‘COC’]<sup>20</sup> which shall be the oversight body enhancing the CIRP and maintaining the corporate governance alongside the RP. The RP shall receive the Resolution Plan from the RAs and, along with 66% of the concurring votes of the COC, shall approve the Resolution Plan and refer it to the Adjudicator<sup>21</sup> which, if approved, shall then be executed by the RP, making all the proceeds of the claims in accordance with the Waterfall Mechanism under Section 53 IBC.

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<sup>15</sup> Insolvency and Bankruptcy Code 2016, s 5(25).

<sup>16</sup> Insolvency and Bankruptcy Code 2016, s 5(27).

<sup>17</sup> Insolvency and Bankruptcy Code 2016, s 6.

<sup>18</sup> Insolvency and Bankruptcy Code 2016, s 7.

<sup>19</sup> Insolvency and Bankruptcy Code 2016, s 5(1).

<sup>20</sup> Insolvency and Bankruptcy Code 2016, s 21.

<sup>21</sup> Insolvency and Bankruptcy Code 2016, s 30.

#### **IV. COMPLEXITY IN THE ROLE OF ARCS AS RESOLUTION APPLICANTS AND RESOLUTION PROFESSIONALS**

Under the SARFAESI Act, an ARC is broadly involved in financial, accounting, and law-related matters to expedite the process of Securitization and Asset Reconstruction which may take the painstaking efforts of an ARC in collating the accounts of the Debtor and the Creditor, rescheduling of payment, managing the affairs of the company, converting the collateral into shares, and others, and all these may require a good command in accounting, financial, management and law related compliances. These technicalities may augur well for the ARCs to fit in the IBC framework because the RPs also dive into and have expertise in such domains to expedite the CIRP. Hence, there remains a firm position for the ARCs to delve into the IBC framework either as RA or as RP. However, although much of the negotiations have taken place on the role of ARCs as RAs, none of the analyses has sought for ARCs as the RPs. So, this portion of the paper shall deal with the dilemma of designating the ARCs with the position of RAs and RPs, thereby enforcing them to undergo the CIRP.

##### ***A. ARCs as Resolution Applicants***

Section 10 SARFAESI Act restricts the “ARCs from undertaking business activities on the Securitization or Asset Reconstruction of the Debtor’s assets, and any other business activity can be undertaken by the ARCs upon the prior approval of the RBI.”<sup>22</sup> However, since one of the key functions of an ARC is to reschedule the debts due to the creditor and to take over the management of the company, the ARCs are the fittest entities who are well-versed with the financial whereabouts of a Debtor and the claims of the Creditor and hence

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<sup>22</sup> Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act 2002, s 10.



can make an inclusive and comprehensive Resolution Plan which consists of payment of claims made by the Creditors and the management and supervision of the Resolution Plan as and when approved by the Adjudicator.<sup>23</sup> Keeping all these averments in consideration, ARCs can be fit for submitting the Resolution Plan to the RP so as to balance the interests of the Creditor and the Debtor (which may not be the case for ARCs to enforce under the SARFAESI Act).

Moreover, RBI, the watchdog of the SARFAESI Act, since the onset of this legislation, is witnessing the growing usage of ARCs in the finance market (due to the sudden increase in defaults) and seldom can be found unhindered by the institutional incapacity of the ARCs to grant approval to take the position of RAs. Currently, the front door entry of the ARCs into the IBC regime has been institutionalized by the RBI by its 2022 notification, in which, it has been held as follows-

“It has now been decided under the provision of Section 10(2) of the SARFAESI Act to permit ARCs to undertake those activities as a Resolution Applicant (RA) under IBC which are not specifically allowed under the SARFAESI Act.”<sup>24</sup>

However, this grant of taking over the role of an RA is subject to certain conditions. In addition to this, IBC has also recognized the role of ARCs as RAs by way of a 2018 amendment to “Section 29A IBC which now does not debar the ARCs from taking the position of RAs merely because it is a financial entity and is not related to the corporate debtor.”<sup>25</sup> Moreover,

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<sup>23</sup> Aritra Mitra, ‘Asset Reconstruction Companies as Resolution co-applicant – Interplay of SARFAESI and Insolvency and Bankruptcy Code’ (*CBCL*, 7 August 2023) <<https://cbcl.nliu.ac.in/insolvency-law/asset-reconstruction-companies-as-resolution-co-applicant-interplay-of-sarfaesi-and-insolvency-and-bankruptcy-code/>> accessed Jan 19, 2025.

<sup>24</sup> RBI Guidelines on Regulatory Framework for Asset Reconstruction Companies, s 13.

<sup>25</sup> Insolvency and Bankruptcy Code 2016, s 29A.

Explanation 1 to Section 29A IBC also explains how a financial entity like an ARC is not the related party to the Debtor merely because it is the financial creditor of the Debtor and has converted the security interest of the Debtor into the Securities.<sup>26</sup>

Although ARCs are now institutionally permitted to play the role of RAs under the IBC, there are certain lacunas attached to such institutional backing that can deter the entry of ARCs into the IBC regime. Firstly, the condition of an ARC to have a net owned fund of Rs. 1000 Cr in order to make itself eligible to be an RA may not augur well when a consonant reading with Section 29A IBC read with the “RBI 2017 notification since this notification, which allows the ARCs to go for 100% conversion of debt into equities for any purpose as mandated by RBI,”<sup>27</sup> is done since the 2017 RBI notification on debt conversion into equities by an ARC is only permitted when an ARC has a net owned fund of Rs. 100 Cr as a requirement whereas, the 2022 RBI notification mandates the ARC to have a net owned fund of Rs. 1000 Cr to fulfil the responsibilities of the RA; in hindsight, explanation 1 to Section 29A IBC provides for financial entities like ARCs to become a RA even if it has converted debt of the debtor into equities before the initiation of CIRP. So, this wide ambiguity in the criteria to be met by an ARC may lead to the ineligibility of an ARC under Section 29A IBC to become an RA when it has led the conversion of 100% debt into equities but has a NOF of Rs. 200 Cr (hypothetical), and such lacuna needs to be rectified by the appropriate authorities.<sup>28</sup>

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<sup>26</sup> *ibid.*

<sup>27</sup> Reserve Bank of India, Conversion of debt into equity-Review, Circular No. 04/26.03.001/2017-18, November 23, 2017.

<sup>28</sup> Arshit Kapoor & Srilagna Dash, ‘Asset Reconstruction Companies as Resolution Applicants: Revisiting the SARFAESI’s Limitations’ (*Indiacorplaw* 5<sup>th</sup> January 2023) <<https://indiacorplaw.in/2023/01/asset-reconstruction-companies-as-resolution-applicants-revisiting-the-sarfaesis-limitations.html>> accessed 19<sup>th</sup> January 2025.

### ***B. ARCs as Resolution Professionals***

An RP is the supervisory authority in the CIRP of a debtor taking all actions for the corporate debtor's restructuring and realizing the claims of the Creditor on the concurring decision of the COC, a replica of the role of a Director of a Company under the Companies Act 2013 who takes all the governing decisions for a company only upon the concurring decision of the Shareholders of the Company. Under the IBC regime, an RP enjoys a wide gamut of powers ranging from a coalition of claims of the creditor to taking over the management of the debtor's estate, from rescheduling of payment by the debtor to executing the Resolution Plan as approved by the Adjudicator.

Similar roles are also performed by an ARC under the SARFAESI regime, ranging from taking over the management of the security interest of the debtor to rescheduling of payment, from selling, leasing, or disposing of the debt collateral to enforcement of the security interest for realization of due to the creditor. All these functions can be performed by an ARC only when its directors have experience in the domain of finance, securitization, or reconstruction. The only difference in the functionality of an ARC and the RP is that the latter only ponders upon the realization of dues, whereas the latter focuses on the realization of dues as well as striking out the distressed financial condition of the debtor. However, not much debate has been made regarding the role of ARCs as RPs since professional expertise in certain domains like finance, accounting, law, management, and others is all that is required first-hand by an RP, and ARCs are such entities which are well equipped with all such technical aspects. So, this part of the paper shall deal with the international practices of an RP along with its delicate relationship with Securitization, and backing the role of ARCs as RPs through such international practices.

In the international domain, the mechanism of Securitization is very delicately connected with the Bankruptcy mechanism, especially in the USA. Securitization, as earlier stated, is “a process whereby a debtor raises funds through the sale and repackaging of certain assets, in which, the securitizing firm sells its cash flows to a Special Purpose Corporation, commonly referred to as an SPC, and the SPC in turn, transforms these cash flows into securities and sells the securities, backed by the cash flows (ABS), to private or public investors”.<sup>29</sup> There are three parties to the Securitization transaction- Originator, Investor, and the Special Purpose Vehicles [‘SPV’],<sup>30</sup> and this transaction is based upon the asset-based collateral of the Obligor. This transaction is very similar to the one explained above, taking place under the SARFAESI regime (the trust route by the ARC). So, by the very process of Securitization, the liability of the debtor is offset from its account book when his assets are managed by an independent SPV.

Chapter 11 of the US Bankruptcy Code<sup>31</sup> provides for the reorganization process of the distressed debtors wherein the process of Securitization is tied up with that of the Bankruptcy mechanism. Now, in securing the debt due on the creditor by the process of Securitization in isolation, what may deter in achieving the overall interests of the creditors is that “if under securitization, all the claims so made are realized, and then if the debtor goes for bankruptcy, then a dearth of receivables is left for the bankruptcy trustee to proceed it towards the creditors which may not augur well for the secured and unsecured creditors, since secured creditors get the value of the collateral and not the

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<sup>29</sup> Lois R. Lupica, ‘Revised Article 9, Securitization Transactions and the Bankruptcy Dynamic’, (2001) 9 AM. BANKR. Inst. L. REV. 287, 288.

<sup>30</sup> PWC, ‘Parties involved in securitisation transactions’ (*PWC Luxembourg*) <[<sup>31</sup> Bankruptcy Code, ch 11.](https://www.pwc.lu/en/securitisation/parties-involved-in-securitisation-transactions.html#:~:text=The%20Originator%20is%20the%20entity,securitised%20the%20claims%20(loans)>” accessed 19<sup>th</sup> January, 2025.</a></p></div><div data-bbox=)

collateral itself, and the unsecured creditors can claim only when any receivable is left to make for the proceeds of the claim after the secured creditors' dues are paid.”<sup>32</sup> So, the overall interest of the creditors is not so referenced under the Securitization process gets hampered to a large extent. A similar problem can be witnessed in the Indian context with reference to Section 9 SARFAESI Act read with the Waterfall Mechanism under Section 53 IBC.

An ‘Insolvency Representative’ under the UNCITRAL Legislative Guide on Insolvency Law, is an individual “who is authorized to make decisions on a number of issues, such as verification and admission of claims, the need for post-commencement funding, surrender of encumbered assets of no value to the estate, sale of major assets, commencement of avoidance actions and treatment of contracts, without the court being required to intervene, except in the case of a dispute concerning one of these matters.”<sup>33</sup> The UNICTRAL guide also speaks about the attributes that need to be imbibed by an Insolvency Representative which is “a requirement for certain levels of experience in relevant areas, for example, finance, commerce, accounting, and law, as well as in the conduct of insolvency proceedings.”<sup>34</sup> The guide also mandates that an Insolvency Representative should fulfil the function of “representing the insolvency estate and submitting a final report on the management of the insolvency estate to the court of creditors.”<sup>35</sup>

Apart from the UNICTRAL Guide, Principle 2 to the EBRD Insolvency Office Holder Principles provides as follows-

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<sup>32</sup> Lois (n 29).

<sup>33</sup> UNCITRAL, Legislative Guide on Insolvency Law, 34.

<sup>34</sup> UNCITRAL, Legislative Guide on Insolvency Law, 175.

<sup>35</sup> UNCITRAL, Legislative Guide on Insolvency Law, 179.

“The work of an office holder requires a diverse skill set and includes knowledge of the law as well as commercial, financial, and accounting matters.”<sup>36</sup>

Similarly, “candidates vouching for the insolvency office holder should have previous work experience with an acting, licensed office holder in insolvency-related matters, and where specific insolvency-related work experience or training is not readily available, other relevant practical experience may be an appropriate substitute.”<sup>37</sup> Therefore, a consonant reading of the UNCITRAL Guide and the EBRD Principles suggests that the minimum qualification an Insolvency Representative should have is to have expertise in law, management, accounts, and financial matters, and if there is not, then it can be attained by alternative methods such as practice courses and training. All that is required for an Insolvency Representative is to verify the claims (if bona fide and undue), collate all such claims, constitute the COC, collate the resolution plan (if submitted by any), and execute it, which may require the due expertise in accountancy and managerial domain. Therefore, in the context of ARCs, they being the professional entities delving themselves only into the object of securitization and asset reconstruction have due expertise in accountancy, managerial, and law domains, thus making them a fit case for the role of RPs.

In the Indian context, the Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations 2016 prescribes the eligibility criteria for an RP to attain maximum independence of the debtor, so to say “that the Directors or Partners of the RP entity are independent of the Debtor wherein, the Directors or Partners of the RP entity

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<sup>36</sup> European Bank for Reconstruction and Development, EBRD Insolvency Office Holder Principles, 8.

<sup>37</sup> *ibid.*

are not a related party neither did they have any transaction amounting to 5% of the gross turnover of the debtor's company in the last three financial years.”<sup>38</sup> However, the crux matter of the eligibility criteria is that the RP concerned should be eligible to be an Independent Director under Section 149 Companies Act 2013. Regulation 3 has to be read with Section 2(24) IBC which provides a leeway for the ARCs to be a fit case to fulfil the role of the RP since the ARCs do not come within the purview of ‘related party’ with respect to the debtor.

One of the key roles of an RP is to constitute the COC under Section 21 IBC and reading it with Regulation 17 of the CIRP Regulations 2016, the RP is mandated to “constitute the COC within two days of the verification of the claims of the Creditors and is also mandated to convene its first meeting within seven days of the filing of the report of constituting such committee.”<sup>39</sup> If the above averments are read along with Regulation 8 and 8A of the CIRP regulations 2016, then the class action claim of the creditors can be expedited by the ARCs as well if they are fitted to the position of the RPs and thus, the claims so made by the Creditors under SARFAESI Act can be proceeded to make class action claims under the IBC, thereby mitigating the burden on the Courts/Tribunals to enforce the Security Interest under Section 13 SARFAESI Act.

However, such an averment needs to be considered with caution as the class action claims of the creditors can only be done under the IBC regime when there is a minimum of 100 such creditors so making the claim. This may not seem pragmatic as far as the harmonious construction between the SARFAESI Act and the IBC has to be developed since this may be possible

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<sup>38</sup> The Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations 2016, reg 3.

<sup>39</sup> The Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations 2016, reg 17.

only when the ARCs collate such claims against a single debtor in numbers amounting to 100 which practically seems unreasonable as the minimum claim value under the SARFAESI Act and IBC does not match. Therefore, the author opines that the ARCs should have the option of collating the claims of the creditor under the SARFAESI Act against a Corporate Debtor and facilitating the process towards IBC thereby mitigating the burden on the court, and facilitating the intent of the IBC to expedite the realization of dues to the creditor and restructuring the debtor's business.

Also, "once the application for initiation of CIRP is accepted by the Adjudicator, the Adjudicator has to declare a Moratorium for 270 days during which, all the claims of the creditor either under IBC or under any other statute are kept at abeyance to give a cooling off period to the debtor to restructure the business, and the vigilance over the abatement of claims of the creditor is overseen by the IRP"<sup>40</sup>. During such a Moratorium, no application for enforcing the security interest can be filed by the creditor under the SARFAESI Act due to the non-obstante clause and overriding effect of IBC over the SARFAESI Act due to Section 238 IBC<sup>41</sup>. The effect of the Moratorium will be that apart from the creditor's claim languishing for 270 days, the cost so borne upon the enforcement of the Security Interest would go in vain. However, such an effect can be alleviated if the ARCs play the role of RPs which if done, the ARCs beforehand direct the Creditors to proceed towards the CIRP and avoid making any enforcement of Security Interest under the SARFAESI Act, thus making the creditors invest them in a single process.

Also, "the RPs perform quasi-judicial functions and are the office bearers of the court in expediting the process of restructuring the business of the debtor

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<sup>40</sup> Insolvency and Bankruptcy Code 2016, s 14.

<sup>41</sup> Insolvency and Bankruptcy Code 2016, s 238.



and making proceeds of the claim of the creditors to them. So, they hold a fiduciary relationship with the debtor's company till the resolution plan is approved since they are authorized to represent such a company in all the legal proceedings. However, this requires the duty of care on the front of the RPs and hence they are not immune from complying with the provisions of IBC as a Debtor or Creditor may have to, and hence the duty of the board of directors or directors are transferred to the RPs during the CIRP.”<sup>42</sup> Hence, this requires professional ethics from the RPs to be manifested during the CIRP.

Also, since due care and diligence need to be manifested by the RP during the CIRP, this professional duty can very well be served by an ARC since their modus operandi is well suited for expediting the process of Securitization and Asset Reconstruction dealing broadly with the financial, managerial and accountancy matters of the debtor's company. Therefore, this due diligence can very well be maintained by the ARCs (if authorized to fulfil the responsibility of the RP). Further, due diligence on the part of RPs can be alleviated by using independent expert advice, and ARCs having a whole corporate structure is well-resourced by a body of experts in the domain of law, management, accounts, finance, and others. Hence, with all these averments made, the ARCs are now fit to fulfil the role of the RP under the IBC regime.

## V. SUGGESTIONS BY THE AUTHOR

Although the ARCs are yet to achieve their stand in the IBC regime and need to be institutionalized under this codified legislation. There are some suggestions by the author made under the averments made above and the suggestions put forth are-

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<sup>42</sup> Sumant Batra, *Corporate Insolvency: Law and Practice* 306 (1st ed. 2017).

Firstly, the concept of ‘Bankruptcy Remote’ must be considered with utmost vigour since the “Bankruptcy Remote entities are the ones which are formed to develop, risk and minimize bankruptcy risk, such as SPVs and such entity is typically prohibited from incurring debt or other obligations and is limited in its purpose and the activities in which it may engage”<sup>43</sup>. These SPVs/Bankruptcy Remote entities have the same role as done under the US Bankruptcy Code, as done by the ARCs under the SARFAESI Act, the only difference being that the former deals with Securitization as well as Bankruptcy process at one go according to the debtor’s financial status, whereas the latter deals with Securitization in isolation. So, ARCs should be facilitated to verify the all financial weather condition of the debtor and when an application to it is made by the creditor, then it should have the authority to divert such case towards IBC so that, all the claims are collated and verified beforehand, the RP as mandated by the Creditor is selected at the time of application beforehand, and then the creditors so verified are selected to constitute the COC under Section 21 IBC, thereby facilitating the entire IBC mechanism during CIRP.

Secondly, as stated earlier, Section 29A IBC needs to be seen to give a harmonious reading of Section 10(2) of the SARFAESI Act read with the 2017 RBI notification allowing 100% debt conversion into equities by the ARCs, and the 2022 RBI notification allowing the ARCs to be selected as RAs since if both the guidelines are not brought in consonance to each other, then the ARCs so institutionally getting an entry into the IBC regime, may become ineligible to become a RA under Section 29A IBC (since this discrepancy may lead to ARCs being designated as a related party to the debtor).

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<sup>43</sup> Thomson Reuters, ‘Glossary’ (*Thomson Reuters Practical Law*) <[https://uk.practicallaw.thomsonreuters.com/8-386-1827?transitionType=Default&contextData=\(sc.Default\)&firstPage=true](https://uk.practicallaw.thomsonreuters.com/8-386-1827?transitionType=Default&contextData=(sc.Default)&firstPage=true)> accessed 19<sup>th</sup> January, 2025.

Thirdly, to facilitate the role of ARCs as RPs and give them a front-door entry to the IBC framework, the minimum number of creditors to make claims to the RP under IBC needs to be reduced from a count of 100, so that the creditors against the single debtor (very often under SARFAESI Act) even if not in such numbers, can make their claims to the RPs, or thereby to the ARCs to enable them to undergo CIRP.

Fourthly, although the ARCs have a slightly different role and modus operandi in their current functioning under the SARFAESI Act with reference to the RPs under IBC, a separate training program and separate set of provisions needs to be instituted in IBC on the lines of the EBRD Insolvency Office Holder Principles wherein, they are mandated to undergo a test as well as licensing program including training and developing some professional skills and ethical code of conduct which takes place for the RPs under the IBBI (Insolvency Professional) Regulations 2016.

## VI. CONCLUSION

IBC as a code of rules aims at providing a comprehensive mechanism for debt restructuring as well as the debtor's restructuring which is not the case under the SARFAESI Act. The IBC comprises RAs and the RPs as the chief proponents facilitating the restructuring process of the debtor by the concurring decision of the COC, thereby maintaining Corporate Governance on the other side, ARCs under the SARFAESI regime strive for debt restructuring and making expedited proceeds towards the claim of the Creditors. However, the role of ARCs though now institutionalised for the position of RAs subject to certain conditions, no such deliberation has been taken towards the role of the ARCs as Resolution Professionals which if done, may augur well in lubricating the harmonious construction between the SARFAESI Act and the IBC.

Therefore, the ARCs which have institutionalised their place as RAs have yet to become eligible for the designation of RPs and due to the growing trend of interplay between the SARFAESI Act and the IBC, it is hoped to be seen in future. ARCs which traditionally have been playing the role of facilitating only the process of Securitization, must also be given some authority in restructuring the debtor's business with its prior professional skills and the debtor and creditor database (created out of the Securitization process), so as to lessen the burden on the courts, mitigate the labour of the creditors towards SARFAESI as well as IBC (if opted), and lastly adding professionalism to the Restructuring process under IBC due to the whole body of experts present in an ARC company having knowledge across different domains be it law, management, accounts, finance, etc. In conclusion, the role of ARCs is gaining trend to be institutionalised into the IBC regime since the "IBC mechanism is proving to be more cost-friendly, efficient and wealth maximizing since in 2022-23 alone, the recovery rate of IBC is 52.8% as compared to 30.5% under the SARFAESI mechanism, and this rate of recovery is further the highest for resolution and liquidation among the Scheduled Commercial Banks (the largest recipient in the SARFAESI Act)."<sup>44</sup>

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<sup>44</sup> Ministry of Finance, Economic Survey 2022-23, January, 2023, 94.