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DECODING FRAUDULENT TRANSACTIONS UNDER INSOLVENCY AND BANKRUPTCY CODE

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ABSTRACT

The Insolvency and Bankruptcy Code (IBC) was passed to integrate and update all corporate restructuring laws and to conduct the time-bound Insolvency Resolution Process. One of the essential provisions under the IBC pertains to avoidance transactions. These transactions include undervalued transactions, extortionate credit transactions, preferential transactions, and transactions defrauding creditors. All these avoidance transactions are intended to protect the interests of creditors by ensuring that assets are not siphoned off before the commencement of insolvency proceedings.

This research provides a comprehensive analysis of the legal framework governing transactions defrauding creditors under the IBC. It examines the definitions, criteria, and implications of these transactions, with a particular focus on the challenges faced in identifying and adjudicating such transactions. The research delves into the lack of look back period in these provisions, transactions done in good faith with emphasis on the intent of the corporate debtor and the practical difficulties encountered by resolution professionals and adjudicating authorities.

Furthermore, the paper critically assesses whether the provisions effectively deter fraudulent transactions and protect the interests of creditors. It highlights the lacunae and loopholes within the current legal framework and suggests potential reforms to enhance the efficiency and effectiveness of the IBC in dealing with transactions defrauding creditors.

Keywords: CIRP, IBC, Avoidance transaction, Fraudulent transactions, corporate debtor

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INTRODUCTION

A fraudulent transaction is one of the avoidance transactions that is entered to place the assets of the corporate debtor out of the reach of certain creditors. This transaction intends to prevent corporate debtors from engaging in fraudulent activities that may cause losses to creditors. Fraudulent trade is the accumulation of debt and the transfer of assets when there are good reasons to believe that the company will not be able to settle its obligations to its creditors. IBC incorporates provisions for undervalued transactions entered for defrauding the creditors[2], fraudulent trading[3], and punishment for transactions that defraud creditors.[4] The research investigates the effectiveness of these provisions when a fraudulent transaction occurs and the difficulty in restoring the assets if the person to whom the property was transferred acted in good faith. One of the most important turning points in the evolution of insolvency laws in both UK and Indian jurisdictions was the introduction of separate remedies for fraudulent and unlawful trading.[5] Unlike other avoidance transactions, a period is absent in fraudulent transactions that benefit the creditors. Other than IBC, fraudulent transactions are dealt with within the Companies Act 2013 and Transfer of Property Act 1882.

TRANSACTIONS DEFRAUDING CREDITORS

IBC provides a remedy for undervalued transactions done to defraud creditors.[6] This happens when the adjudicating authority has reason to believe that the corporate debtor engaged in an undervalued transaction to shield its assets from any suit or to negatively impact the interests of those who may have such a claim to the assets.[7] Resolution professionals and liquidators may file a complaint with the adjudicating authority upon discovering any transaction described by this provision. If the complaint is deemed valid, the adjudicating authority may issue an order to:

i. Restore position before the transaction and

2. Insolvency and Bankruptcy Code, 2016, s 49, Acts of Parliament,2016, (India)
3. Insolvency and Bankruptcy Code 2016, s 66.
4. Insolvency and Bankruptcy Code 2016, s 69.
5. Vinod Kothari, A note on fraudulent trading and wrongful,(20 March 2024),https://vinodkothari.com/wp-content/uploads/2019/06/A-note-of-Fraudulent-and-Unlawful-Trading.pdf.
6. Insolvency and Bankruptcy Code 2016, s 49.

49. Where the corporate debtor has entered an undervalued transaction as referred to in sub-section (2) of section 45 and the Adjudicating Authority is satisfied that such transaction was deliberately entered into by such corporate debtor—

(a) for keeping assets of the corporate debtor beyond the reach of any person who is entitled to make a claim against the corporate debtor; or

(b) in order to adversely affect the interests of such a person in relation to the claim, the Adjudicating Authority shall make an order—

(i) restoring the position as it existed before such transaction as if the transaction had not been entered; and

(ii) protecting the interests of persons who are victims of such transactions:

Provided that an order under this section—

(a) shall not affect any interest in property which was acquired from a person other than the corporate debtor and was acquired in good faith, for value and without notice of the relevant circumstances, or affect any interest deriving from such an interest, and

(b) shall not require a person who received a benefit from the transaction in good faith, for value and without notice of the relevant circumstances to pay any sum unless he was a party to the transaction.

7. Insolvency and Bankruptcy Code 2016, s 49(1).

ii. Protect the rights of creditors who are affected by these kinds of transactions. [8]

Nevertheless, the orders issued by the adjudicating body will not impact the rights of an individual who obtained the asset from a party other than the corporate debtor in a bona fide transaction and without knowledge of the relevant circumstances.[9] The person shall not be made to pay any sum unless he was party to the transaction. It was made to protect the interests of persons who acted in good faith as it is necessary to ensure that the bona fide transactions are not affected by any order of the adjudicating authority.[10] The burden of proving that the transactions have all the elements of bona fide transactions is on the person claiming that the transactions are bona fide and, therefore, exempted.[11]

Looking back at the history of provisions pertaining to undervalue transactions, the Department of Economic Affairs, Ministry of Finance, chaired by Mr. T.K. Vishwanathan, established the Bankruptcy Law Reform Committee ("BLRC" or the "Committee") in August 2014 with the goal of studying the "corporate bankruptcy legal framework in India" and to present a report to the government for systemic reform.[12] The Bankruptcy Law Reform Committee recommended in its Interim Report that, in the United Kingdom, Section 423 of the Insolvency Act 1986 invalidates transactions at undervalue if they aim to place assets out of reach or harm the interests of a person with present or potential claims against the company. This provision bears a resemblance to the one concerning the avoidance of undervalue transactions (Section 238, IA 1986), yet Section 423 actions distinguish themselves by lacking a timeframe for such transactions and being applicable both within and outside formal insolvency procedures. Introducing such a clause in the Companies Act 2013 would enhance creditor safeguarding under avoidance legislation by empowering the liquidator to cancel transactions made prior to the one-year period before the company's insolvency. Such a measure is essential in preventing the depletion of corporate assets by corporate debtor who have knowledge to the company's financial situation in scenarios where a prolonged period of financial distress ends in insolvency.[13] The committee recommended at the end that a clause be incorporated into the Companies Act of 2013, like Section 423 of the UK Insolvency Act of 1986, which nullifies transactions aimed at defrauding creditors. This clause would have perpetual applicability, both within and beyond the formal bankruptcy processes.[14]

IBC did not exist when the committee recommended incorporating the UK Insolvency Act into the Companies Act of 2013. However, the provision of fraudulent transactions in IBC was also adopted from the UK Insolvency Act 1986.

FRAUDULENT TRADING OR WRONGFUL TRADING

IBC specifically incorporates fraudulent trading. If the corporate debtor continues to operate the business during the CIRP or liquidation process with the intention of defrauding the creditors, the

8. *Id.*
9. Insolvency and Bankruptcy Code, 2016, s 49(1), Acts of Parliament, 2016
10. Sheth DK, Treatise on the Insolvency and Bankruptcy Code, 2016: (Law and Practice), vol 1 (Snow White Publications Pvt Ltd 2023)
11. Insolvency and Bankruptcy Code, 2016, s 49.
12. Ministry of Micro, Small & Medium Enterprises, (25 April 2024) https://msme.gov.in/interim-report-bankruptcy-law-reforms-committee-blrcdated-10th-february-2015-0
13. Richa Saraf,'Corporate Insolvency: Fraudulent Transactions and Look-Back Period', IndiaCorpLaw, (9 May 2024) https://indiacorplaw.in/2018/07/corporate-insolvency-fraudulent-transactions-look-back-period.html
14. *Id.*

adjudicating authority can upon the resolution professional's application, pass any order requiring any person who is held responsible for contributing to the corporate debtor's assets.[15] The party, in the absence of any limitation of liability, should assume personal liability for the losses incurred as a result of their deceptive trading practices.[16] This stipulation applies solely when the individual knowingly engages in fraudulent activities.

If the corporate debtor knew that there was no reasonable chance of avoiding the CIRP process before it started, but the corporate debtor continued to operate the business, and the director or partner did not take appropriate steps and due diligence to reduce the potential loss to the creditors, then the adjudicating authority could make any order to reverse the transaction.[17] Therefore, directors have to face penalties according to this particular provision, regardless of their lack of fraudulent intent, as long as they displayed negligence and recklessness in their actions, thereby increasing the company's vulnerability to additional risks.[18] In this context, directors are unable to use ignorance or lack of awareness as a defence under the aforementioned regulation.

In Renuka Devi Rangaswamy, IRP of M/s. Regen Infrastructure and Services Pvt. Ltd. Vs. Mr. Madhusudan Khemka[19], there was a sale of Immovable Properties of 16.02 Acres in favour of the third Respondent. Land was purchased in the name of the third Respondent, utilizing the funds of the corporate debtor; it was not in the ordinary course of business and provided no profit or gain to RISPL (Corporate Debtor). The third Respondent was also a related party to the corporate debtor as director. The Respondent has submitted that the money for the lands that the third Respondent purchased was given by RPPL to the corporate debtor, which in turn provided that money to the third Respondent, one of the Special Purpose Vehicle (SPVs) created by the Regen Group. Respondents submitted that they had funded the corporate debtor for the project's development and that the transaction had happened within the group. The appellant claimed that the property was purchased by the third respondent with the money given by the corporate debtor.

The issue was whether transferring assets within the group companies per se would constitute 'fraudulent trading' as stipulated under IBC. NCLT

15. *Supra note* 1
16. Insolvency and Bankruptcy Code, 2016, s 66(1), Acts of Parliament,2016

66. (1) If during the corporate insolvency resolution process or a liquidation process, it is found that any business of the corporate debtor has been carried on with intent to defraud creditors of the corporate debtor or for any fraudulent purpose, the Adjudicating Authority may on the application of the resolution professional pass an order that any persons who were knowingly parties to the carrying on of the business in such manner shall be liable to make such contributions to the assets of the corporate debtor as it may deem fit.

(2) On an application made by a resolution professional during the corporate insolvency resolution process, the Adjudicating Authority may by an order direct that a director or partner of the corporate debtor, as the case may be, shall be liable to make such contribution to the assets of the corporate debtor as it may deem fit, if— (a) before the insolvency commencement date, such director or partner knew or ought to have known that the there was no reasonable prospect of avoiding the commencement of a corporate insolvency resolution process in respect of such corporate debtor; and

(b) such director or partner did not exercise due diligence in minimising the potential loss to the creditors of the corporate debtor. Explanation. —For the purposes of this section a director or partner of the corporate debtor, as the case may be, shall be deemed to have exercised due diligence if such diligence was reasonably expected of a person carrying out the same functions as are carried out by such director or partner, as the case may be, in relation to the corporate debtor.

17. Insolvency and Bankruptcy Code, 2016, s 66(2),Acts of Parliament,2016
18. *Supra note* 1
19. Renuka Devi Rangaswamy,IRP of M/s. Regen Infrastructure and Services Pvt. Ltd. v. Mr. Madhusudan Khemka, Company Appeal (AT) (CH) (INS.) No. 356 of 2022

held that the respondents had not made a case of fraud or dishonest intention, and it would not constitute fraudulent trading. NCLAT held that dishonesty is an essential ingredient in fraudulent trading. Dishonesty is to be established and cannot be inferred in any manner. Whether a director had exercised his skill, experience, and general knowledge to be expected of a person in carrying out the duties of his functions is to be determined for imposing liability. The Adjudicating Authority held that, the appellant must establish that a person knowingly carries on the business with the corporate debtor with a dishonest intention to defraud the creditors and it held that the Appellant could not establish fraud or dishonest intent, and thus the appeal was dismissed.

In the provisions of Fraudulent trading, liability can be imposed upon any person, including outsiders [20], and can be imposed specifically upon the director or partner of a company.[21] If the adjudicating authority issues an order in accordance with the provisions of this section, it can issue additional instructions to carry out its orders. It has the authority to impose liability on anyone for any obligation or debt owed by the corporate debtor, as well as a charge on any assets of the corporate debtor that are vested in them.It can occasionally provide further directions for enforcing any charge under this section.[22]

PUNISHMENT FOR FRAUDULENT TRANSACTIONS

Punishment serves the purpose of deterrence for those who follow fraudulent trading, as restoring assets alone is insufficient.[23] Punishment for fraudulent transactions is given under the Code.[24] Officers of a company involved in fraudulent transactions face imprisonment of five years and a fine of one crore rupee. Undervalued transactions are not subject to this kind of penalty under the IBC. The element of intent must be established in order to be punished under the applicable provision. The intent must be to deprive or adversely affect the rights of any persons regarding their claim. It must be proven for a transaction to be considered fraudulent, while in an undervalued transaction, it is not necessary to have an intent.

In Aditya Kumar Tibrewal vs. Om Prakash Pandey[25], This appeal was filed by the resolution professional challenging the Order passed by the National Company Law Tribunal. A corporate Insolvency Resolution Process was initiated against the corporate debtor M/s. Sri Balaji Forest Products Private Limited in 2019.The corporate debtor refused to provide relevant documents to the Resolution Professional. The resolution professional commenced ‘Contempt Proceedings’ against the suspended directors in the year 2020. Subsequently, the suspended directors disclosed the Lease Agreement dated 30th November 2016, carried out by the corporate debtor in the interest of Respondent No. 3, through which the corporate debtor has leased out all its land, parcels, and equipment to Respondent No. 3 for a duration of 29 years.

The resolution professional submitted an Interim Application (I.A.) pursuant to Sections 43 and 45, in conjunction with Section 49, as well as Sections 66 and 60(5) of the Code. Nevertheless, the National Company Law Tribunal (NCLT) dismissed the I.A. filed by the resolution professional, citing that it was precluded by Regulation 35A of the Insolvency and Bankruptcy Code (CIRP) Regulations, 2016, and Section 46 of the Code. A subsequent appeal

20. Insolvency and Bankruptcy Code, 2016, s 66(1)
21. Insolvency and Bankruptcy Code, 2016, s 66(2)
22. Insolvency and Bankruptcy Code, 2016, s 67(1)
23. Preetha S, The Fraudulent Trading Offence: Need for a Relook, 4 NUJS L. Rev. 231 (2011)
24. Insolvency and Bankruptcy Code, 2016, s 69
25. Aditya Kumar Tyrewala v. Om Prakash Pandey, Company Appeal (AT) Insolvency No. 583 of 2021

was lodged by the RP. The appellant contended that the lease transaction involving the corporate debtor's related party was executed for a nominal amount and constituted a fraudulent act aimed at prejudicing the interests of creditors. The RP further argued that the adjudicating authority erred in its decision to not entertain the application since the transaction occurred more than two years before. Furthermore, the respondents opted not to furnish any response affidavits in opposition to the one provided by the resolution professionals, as they lacked a valid defense against the application. Appellants thus claimed that the Adjudicating Authority should have drawn adverse inferences against the respondents based on all those factors, which was not done. The respondents, nevertheless, argued that the Lease Agreement signed by the corporate debtor on November 30, 2016, exceeded the lookout period of two years as stipulated in Section 46 of the Code.

The issue at hand pertained to the necessity of applying in accordance with Sections 43, 45, 49, and 66 within the 135th day of the initiation of insolvency proceedings, and, if not done so, whether it ought to be dismissed for failing to adhere to Regulation 35A of the Corporate Insolvency Resolution Process (CIRP) Regulations, 2016.

The I.A. was filed by the RP beyond the 135th Day of Insolvency Commencement date because he learned about the transaction undertaken in 2016 only after the respondents produced the sale deed in 2020. The NCLAT determined that the time frame stipulated in Regulation 35A of the CIRP Regulations is merely directory, and any steps executed by the RP after the specified duration outlined in Regulation 35A of the CIRP Regulations should not be deemed invalid solely due to exceeding the time frame prescribed under the CIRP Regulations. There might exist genuine justifications for resolution professionals refraining from submitting an application to circumvent the transactions within the stipulated time frame, as the matter necessitates scrutiny on an individual basis and evaluation based on merits. The transactions defrauding creditors and fraudulent trading or wrongful trading[26] and the timeline prescribed[27] are not applicable as the timeline is prescribed explicitly under Section 66, five years before the Insolvency Commencement date. The NCLAT held that substantial evidence was in the application within Sections 49 and 66 of the Code and that the NCLT committed an error even though the IBC specifically empowers the Adjudicating Authority to make decisions regarding transactions to maximize the corporate debtor's assets. It is also held that assets are subject to undervalued transactions, fraudulent transactions, or transactions to defraud creditors, necessitating appropriate interventions and instructions to safeguard the interests of the corporate debtor.

Thus, when we talk about punishment for fraudulent transactions under section 66, if the offense to succeed, the applicant (IRP/RP/Liquidator) must satisfy the following:

a. Intention of the corporate debtor to defraud the creditors.

b. b. Business/Trading of the corporate debtor has been carried out fraudulently.

c. c. Assessment of the extent of the impact of such fraudulent business/trading on the interests of the creditors and undue benefit to the corporate debtor must be established. [28]

In the case of Edelweiss Asset Reconstruction Company Limited Vs. RTIL Limited[29], this was

26. Insolvency and Bankruptcy Code, 2016, s 66
27. Insolvency and Bankruptcy Code, 2016, s 49
28. Mangla A, 'IBC - Contesting Section 66(1) Application.' LinkedIn, (26 April 2024), https://www.linkedin.com/pulse/ibc-contesting-section-661-application-arvind-mangla/
29. Edelweiss Asset Reconstruction Company Limited v. RTIL Limited,C.P. No. 382/I&BP/MB/2018

filed by the liquidator against the directors of the corporate debtor under Section 66 of the Insolvency and Bankruptcy Code, based on the Audit Report by the Auditor. The auditor identified specific transactions conducted by the corporate debtor as fraudulent. The provision outlined in Section 66 of the Insolvency and Bankruptcy Code pertains to instances where the corporate debtor engages in transactions with the deliberate intention of deceiving its creditors or for any other fraudulent objectives. An extensive sum was declared as a loss and the reasons attributed to the write-off were the challenges within the manufacturing sector, such as a lack of working capital and issues related to doubtful recovery. It was discussed and recorded in the minutes of the Audit Committee and in the Board of the corporate debtor. The court held that the write-off process aligned with the accounting norms, and any subsequent actions should not be deemed as fraudulent.[30]

THE SIMILAR PROVISIONS

Provisions that were implemented to defraud creditors are found in both sections 49 and 66. However, the former necessitates the deliberate intent to deceive creditors through engaging in such transactions, whereas section 66(2) penalizes negligent acts that similarly impact the creditors' interests. Section 49 specifically addresses the actions of the corporate debtor in engaging in fraudulent transactions, whereas Section 66 imposes personal liability on any party responsible.

If a corporate debtor or one of its officers engages in activities that deceive creditors, they may be punished under Section 69. The differences between sections 66 & 69 are:

a. An application pursuant to Section 66 is permissible solely within the confines of the corporate insolvency resolution process or liquidation process, as carried out by the resolution professional. Nevertheless, the enactment of the Insolvency and Bankruptcy Code (Second Amendment) Bill, 2018 has extended the scope to enable the submission of an application in instances when any such transactions occur.[31]

b. The outcome of acts carried out pursuant to Section 66 involves the involvement of the director or any individual accountable for the assets of the corporate debtor. This section does not entail any criminal responsibility. However, the consequences outlined in Section 69 encompass both civil and criminal liability. Section 69 specifies that the punishment may entail imprisonment ranging from a minimum of one year to a maximum of five years, or a fine of one lakh rupees to a maximum of one crore rupees, or both.

One of the defenses provided under Section 69 pertains to instances where the specified actions occurred over five years prior to the insolvency date and if it can be substantiated by the corporate debtor to have done the transactions without any intent to defraud the creditors. If due diligence was done in accordance with Section 66 or there was no dishonest intention, those transactions are protected under Section 66 (1). [32]

The main distinction between section 45 and section 49 is that the former is concerned with undervalued transactions with the intention not necessary to constitute an offense, and in the latter, malafide intention is necessary. Similarly, section 45 has a look-back period like all other avoidable transactions, but section 49 does not have a look-back period because once fraud is committed, it is

30. Supra note 3
31. Insolvency and Bankruptcy Code, 2016, s 69
32. Supra note 1

committed without doubt.[33] The reason behind the clause is that anyone who has committed a criminal act with malice in mind cannot get away with it by invoking a justification like the passage of time.[34]

LACK OF LIMITATION PERIOD

While a look-back period is specified for transactions deemed undervalued, there exists no statute of limitations for fraudulent transactions.[35] This means that there is no specific time frame within which a transaction must have occurred in order to be contested as a transaction defrauding creditor. It is based on the doctrine, "once a fraud, always a fraud." The principle that "fraud vitiates every transaction into which it enters applies to judgments as well as to contracts and other transactions" forms a fundamental aspect of common law jurisprudence.[36] Embedding a time restriction within the sections would contradict the objectives of the Insolvency and Bankruptcy Code (IBC).[37] The inclusion of provisions addressing undervalued and fraudulent transactions represents a distinctive feature of the Code, derived from the Insolvency Act, 1986 of the United Kingdom. The Bankruptcy Law Reform Committee proposed the addition of a clause that would nullify transactions aimed at defrauding creditors, drawing inspiration from section 243 of the UK Insolvency Act, 1986. It is crucial to emphasize that when deliberating on the rationale behind incorporating this provision into the statute, the Committee highlighted that the statutory framework concerning fraudulent transactions should not be constrained by limitations on time period.[38]

If there is a lack of a specified limitation period in a statute, legal recourse may be pursued within a three-year timeframe in accordance with the Limitation Act of 1963. Against this backdrop, the National Company Law Appellate Tribunal (NCLAT) deliberated on the matter of the non-existence of time for fraudulent transactions under the Code in Mr. Thomas George v. K. Easwara Pillai and Others[39] . Thomas George was the suspended director of the corporate debtor Mathstraman Manufacturers and Traders Private Limited (Appellant). The corporate debtor was subject to CIRP proceedings, and RP was assigned as the resolution specialist. The RP discovered undesirable business activity by the corporate debtor during the CIRP.It was argued that the RP had prepared the annual accounts for 2014–15 with incomplete information because the corporate debtor was dormant during the 2015–16 fiscal year. Starting in 2015, the corporate debtor neglected to submit the required statutory accounts to the company's registrar. It was claimed that all current and movable assets were transferred to the third respondent and sold to pay off the corporate debtor's debts in full, outside the company's books of accounts, using cash. Additionally, it was argued that neither employers nor employees were on the payroll of the corporate debtor. Respondents 3 to 6 were served notice but chose not to show up in front of the adjudicating authority; as a result, the order was made ex parte. Consequently, the RP made an interim application against the appellant under Section 66 of the IBC, requesting the following reliefs:

- To issue a directive instructing the respondents to compensate the creditors

33. 'Avoidable Transaction under IBC: Key Factors', Reedlaw,(20 March 2024), https://www.reedlaw.in/articles/avoidable-transaction-under-ibc%3A-key-factors.
34. *Id.*
35. Insolvency and Bankruptcy Code, 2016, ss 49 & 69
36. Supra note 12
37. *Id.*
38. *Id.*
39. Mr. Thomas George v. K. Easwara Pillai and Others, Company Appeal (At)(Ch) (Insolvency) No. 293 of 2021.

of the corporate debtor for any damages incurred.

- To impose individual responsibility on the part of the respondents for their deliberate and intentional failure.
- To declare the transaction as Fraudulent Transactions.

The NCLT allowed the application filed by the RP and observed that the suspended Directors of the corporate debtor had carried on the business in the factory illegally, and the respondents utilized the corporate debtor's assets. From this, the suspended Directors did the act with the intent to defraud the corporate debtor's creditors for fraudulent purposes. Considering these conclusions, the application was permitted by the Adjudicating Authority to classify the transactions as fraudulent and ordered the respondents to reimburse the losses incurred by the creditors, thereby establishing their personal liability for the willful and intentional default. The respondents were instructed to provide all the necessary documents as per the request of the resolution professional to ensure the efficient execution of the Corporate Insolvency Resolution Process. The respondents, feeling aggrieved by the decision made by the National Company Law Tribunal, decided to file an appeal. The issue was whether a three-year limitation period, as per the Limitation Act of 1963, should be applied to Section 66 of the IBC. The NCLAT found that the three-year period of limitations cannot be applied to fraudulent transactions under the Code and that the Code does not expressly allow for a lookback period for fraudulent transactions. As a result, the Insolvency Professional can identify fraudulent transactions more than three years before CIRP began to operate. According to the NCLT, the suspended directors who participated in these fraudulent transactions are personally liable for compensating MMTPL for its losses. As a result, the suspended director's appeal was rejected. In the Thomas George case, the NCLAT decided in favor of creditors who would lose money because of corporate debtors' wrongdoing. The NCLAT has made sure that past transactions by the corporate debtor that were carried into fraudulently misleading the creditors are not spared from prosecution by refusing to restrict the lookback period to three years. The NCLAT's approach also aligns with the Code's objective to maximize the value of corporate debtors' assets.[40]

COMPANIES ACT 2013

The Companies Act 2013 also deals with fraudulent and wrongful business trading.[41] Previously, the Companies Act was silent on defining fraud; however, the 2013 Act does define fraud precisely. [42]"fraud" in relation to affairs of a company or anybody corporate includes any act, omission, concealment of any fact or abuse of position committed by any person or any other person with the connivance in any manner, with intent to deceive, to gain undue advantage from, or to injure the interests of, the company or its shareholders or its creditors or any other person, whether or not there is any wrongful gain or wrongful loss.[43] If any director, manager, officer, or other individual continues to operate the business fraudulently or operate with the intention of defrauding creditors, without regard to any limitations on responsibility, the Adjudicating Authority may decide that such person be held personally liable for all or any of the obligations or liabilities as the Tribunal may direct.[44]

40. Ganguly S, Qureshi A and Mishra S, 'No Look Back Period for Fraudulent Transactions under Insolvency Laws', Lexology, (13 March) https://www.lexology.com/library/detail.aspx?g=86576e57-1eb0-4ea9-a657-6c6c29123c9a.
41. The Companies Act 2013, ss 328, 329,339,340 &341, Acts of Parliament,2013,(India).
42. The Companies Act 2013, s 447, Acts of Parliament,2013
43. Satapathy S, corporate fraud and criminal liability of Directors, International Journal of Law Management & Humanities, (2022)
44. The Companies Act 2013, s 447.

Moreover, the Tribunal may order an investigation into any misfeasance or breach of trust committed by a promoter, director, manager, company liquidator, or officer of the company, as well as their repayment or contribution to the assets, if they have misapplied, retained, or become liable or accountable for money or property. It establishes criminal penalties for violating this provision.[45] The Act also makes directors and partners who held such positions during the fraudulent transaction liable under the sections.[46] The distinction is regarding the applicability of the offense. In Companies Act[47], the section is applicable only during winding up, and in IBC[48], it is applicable during winding up and CIRP. If there is an ambiguity regarding who has committed the fraud, the penal provision under the Companies Act can be applied as there is an absence of a specific penal provision under IBC. [49]

FRAUDULENT TRANSACTIONS UNDER THE TRANSFER OF PROPERTY ACT, 1882

The necessity of safeguarding creditors interests is recognized by the Transfer of Property Act of 1882.[50] It forbids someone from fending off legitimate claims of their creditors. Any transaction that is not made with good intentions is restricted by it. According to this, a transfer is considered fraudulent if it aims to undermine the interests of the creditor or any subsequent transferee.[51]

For transferred property to fall under the Act's scope, it must be immovable. The transferor is no longer the legal owner of the property; instead, the transfer must be real in order to confer vested ownership in the third party. The primary goal of this section is to safeguard creditors from being taken advantage of by the debtors or undermining their rights by removing their security. Any transaction carried out with the fraudulent intent of preventing the property from being available for the creditor to receive as security will be considered fraudulent. Therefore, in accordance with the Code and the Companies Act of 2013, the transferors purpose must be to defeat or delay the creditors.[52]

The provisions under the Insolvency and Bankruptcy Code, The Companies Act, and the Transfer of Property Act empower the resolution professional to set aside fraudulent transactions.

UNDER U.K LAW

The principles of the UK Insolvency Act 1986 formed the basis for the concepts of fraudulent and wrongful trading that are recognized in India. It was adopted from section 243 of the Insolvency Act. The Government wanted a provision to make the Directors responsible and liable for their acts. Thus, they inserted "fraudulent trading" under Section 213 and "wrongful trading" under Section 214 of the Insolvency Act 1986. The relevant component of fraudulent trading is the dishonest intention to defraud the creditors. While the civil remedy is provided under the Insolvency Act 1986, fraudulent trading was a criminal offense under the Companies Act 2006.

When we look into the provisions of the UK, in the case of Morphitis v. Bernasconi[53], the court

45. The Companies Act 2013, s 341.
46. Insolvency and Bankruptcy Code, 2016, ss 49 & 69
47. The Companies Act 2013, s 339(1).
48. *Id.*
49. The Companies Act 2013, s 447.
50. The Transfer of Property Act 1882, s 53.
51. Brajmohan S, 'Fraudulent Transactions: What to Keep in Mind While Ring Fencing Your Assets', Solomon & Co.,(16 March 2024) https://solomonco.in/fraudulent-transactions-what-to-keep-in-mind-while-ring-fencing-your-assets/.
52. *Id.*
53. Morphitis v. Bernasconi, 2003 EWCA Civ 289

determined that dishonesty is when individuals in control incur business debt knowing that it won't be paid back or that there is a significant and unjustifiable risk of default. Thus, it is necessary to come under the Act. An intention to defraud creditors can be inferred if there was dishonesty against the notion of fair trading. In R v. Grantham[54], It was decided that someone can be found guilty of carrying on the business's affairs "with intent to defraud creditors of the company" if they participate in the management of the company's affairs and obtain credit for the company when they know there is no reason to believe that the funds will become available to pay the debt when it becomes due.'

Transaction defrauding creditors is given under Section 423 of the U.K Insolvency Act 1986 and can relate to transactions entered at an undervalue, which is similar to provisions under IBC and may arise from:

- As gifts to the other person,
- Transactions with another party on terms that provide for him to receive no benefit,
- The transfer for less money or money that is substantially less valuable than the value offered,
- The transaction with the other party in consideration of marriage.[55]

The rationale behind the absence of time can be inferred from the case of Sands v Clitheroe[56], Mr. Clitheroe was a solicitor in practice who gave his wife his share of the family home. He was solvent and a partner in a law firm when he made the gift. But after fifteen years, Mr. Clitheroe filed for bankruptcy as his company went bankrupt. It was established that he had made the transfer to safeguard the family home if the law firm he was a partner in went bankrupt. The Court determined that the transaction aimed to shield assets from creditors' claims. As a result, it was decided that the transaction qualified for section 423, which has no time restriction. Even after considering the fact that at the time of the transaction, Mr. Clitheroe had no outstanding bankruptcy debts.

In addition to bankruptcy trustees, liquidators, and administrators who can seek relief, the victims of the transaction (judgment creditors) can also file applications for relief.[57] The Court has broad power to reverse transactions defrauding creditors, and it can restore the position to protect the interests of the victims of the transaction and require payment of a sum to compensate for the undervalued transaction. However, the Court cannot put a victim in a better position by its decision. Like Indian law, section 423 reviews transactions without regard to a specified period. Despite this, the Courts have adopted a cautious stance.

About the commencement date of a claim under section 423 of the Act, the Limitation Act of 1980 is applied.[58] This means that any money recovered under any statute under section 423 is subject to either a 12-year or a 6-year restriction period.[59] Therefore, a section 423 claim may be subject to the 12-year limitation period. The limitation period runs from (i) the claimant's discovery of its cause of action or (ii)if the claim is made by a trustee in

54. R v. Grantham.,1984 3 All ER 166.
55. 'What Are Transactions Defrauding Creditors?' Oliver Elliot, (20 March 2024) https://www.oliverelliot.co.uk/insolvency-guides-and-information/what-are-transactions-defrauding-creditors/.
56. Sands v. Clitheroe, 2006 BPIR 1000
57. Fiddy M, Moi S and Wood A, 'Transactions Defrauding Creditors: The Use of Corporate Structures to Defeat Creditor Claims: Insights: Mayer Brown', Insights | Mayer Brown, (20 March2024) .https://www.mayerbrown.com/en/insights/publications/2023/09/transactions-defrauding-creditors-the-use-of-corporate-structures-to-defeat-creditor-claims.
58. Rutledge B, 'Piercing the Corporate Veil Series: Transactions Defrauding Creditors', Keidan Harrison Disputes Lawyers, (20 March 2024), https://keidanharrison.com/2022/01/piercing-the-corporate-veil-series-transactions-defrauding-creditors/.
59. *Id.*

bankruptcy, the period begins on the date of the bankruptcy order. [60]

In Arbuthnot Leasing International Ltd v Havelet Leasing Ltd[61], It was discovered that the director of Havelet Leasing Ltd, whose company had become insolvent, had moved certain assets to an affiliated company (which the director controlled) to remove them from the control of Arbuthnot Leasing International Ltd ("Arbuthnot"). Havelet had received financing from Arbuthnot, but when they didn't repay the loan, Arbuthnot named a receiver.It was later found that Havelet had transferred its business, assets, and contractual benefits to Havelet Leasing Finance Ltd. ("Havelet Finance") for a lower value than it had really paid. Since Havelet was given preference over its other creditors, including Arbuthnot, this arrangement was determined to be fraudulent. According to the Court, the transfers were made in order to keep Havelet's assets out of Arbuthnot's hand. Arbuthnot was seeking a reversal of the transaction, and it was successful. The Court decided that Havelet Finance's asset transfers should be returned to Havelet. In totality, under UK law, liability can be incurred only when it is proved that the company conducts fraudulent trading knowingly.

CONCLUSION

Fraudulent transactions occur when the corporate debtor fraudulently prefers a specific creditor or class of creditors over others. To ensure that losses incurred by creditors are reimbursed in the event of liquidation and that the directors responsible for such losses are held personally accountable for such losses, Section 66 ought to be used more frequently. To reduce losses, directors should take prudent actions. Entering the Corporate Insolvency Resolution Process might be the first step. The uncertainty around liability and the challenges associated with proving it may make recovery actions subject to failure. However, the lack of a limitation period and the judgments help uphold the creditors' rights and interests.

60. Hill v. Spread Trustee Company Ltd & Anor, 2006 EWCA Civ 542.

61. Arbuthnot Leasing International Ltd v. Havelet Leasing Ltd,(No 2) 1990 BCC 636.