

INSOLVENCY AND BANKRUPTCY CODE 2016

Akhil Reji Jacob
Research Scholar
Institute of Management in Government,
University of Kerala.

Abstract

Insolvency and Bankruptcy Code 2016 was formulated by Government of India to consolidate existing framework by creating a single law for Insolvency and Bankruptcy. The code was passed by Indian Parliament in May 2016. The code aims to consolidate existing framework by creating a single law for Insolvency and Bankruptcy. An effective legal framework for addressing the problems relating to insolvency and bankruptcy helps in the development of financial markets and encourage entrepreneurship. It would also improve ease of doing business and facilitate more investment leading to higher economic growth and development. The Insolvency and Bankruptcy Code (IBC) envisages minimizing the role of adjudicating authority and replaces hundred year old laws such as The Presidency Town Insolvency Act 1908, Provisional Insolvency Act 1920, and Sick Industrial Companies (special provisions) Repeal Act 2003. The code aims in designating the National Company Law Tribunal (NCLT) and Debt Recovery Tribunal (DRT) as the adjudicating authorities for corporate persons and firms and individuals respectively for resolution of insolvency, liquidation and bankruptcy. By implementing IBC the Government aims to reduce the time involved in insolvency and bankruptcy proceedings and to ensure that the rights of the stakeholders are protected. This article explores the various process and procedures involved Insolvency and Bankruptcy Code 2016 and its implication.

KEYWORDS: Insolvency, bankruptcy, National Company Law Tribunal, Debt Recovery Tribunal

Introduction

The term insolvency means the state of being insolvent, that means a person who is unable to pay his debts. Government of India formulated Insolvency and Bankruptcy code 2016 to consolidate existing framework by creating a single law for Insolvency and Bankruptcy. The aim and objective of the Insolvency and Bankruptcy code 2016 is to merge and modify the laws relating to insolvency resolution of corporate, persons, partnership firms and individuals in a time bound manner. An effective legal framework for timely resolution of insolvency and bankruptcy would support development of credit markets and encourage entrepreneurship. It would also improve ease of doing business and facilitate more investment leading to higher economic growth and development.

The code seeks to provide for designating the National Company Law Tribunal (NCLT) and Debt Recovery Tribunal (DRT) as the adjudicating authorities for corporate persons and firms and individuals respectively for resolution of insolvency, liquidation and bankruptcy. The code also seeks to provide for establishment of Insolvency and Bankruptcy Board of India for the regulation of insolvency professionals, insolvency professional agencies and information utilities. The utmost objective of Insolvency and Bankruptcy code 2016 is to bring the insolvency law in India under a single unified umbrella with the object of speeding up of the insolvency process.

Evolution of Insolvency and Bankruptcy Code

The code was passed by Lok sabha on 5th May, 2016. Before Insolvency and Bankruptcy Code, insolvency procedure consumes large amount of time. A lot of litigations were pending before the various tribunals and courts. Before the code various laws that are related with insolvency are Contract Act, Recovery of Debt due to banks, Securitisation and Reconstruction of Financial Asset and Enforcement of Security Interest (SARFAESI Act, 2002), Financial Institution Act, etc however this laws were not able to achieve desired output. Earlier the stream of insolvency laws can be divided under two heads: Personal Insolvency, which deals with individuals and partnership firms governed by Provisional Insolvency Act, 1920 and Presidency Towns Insolvency Act, 1908. The Insolvency and Bankruptcy Code repeal these Act's i.e., Provisional Insolvency Act, 1920 and Presidency Towns Insolvency Act, 1908. As compared with the earlier Act's the IBC (Insolvency and Bankruptcy Code) is much different, as it shift the responsibility to the creditor to initiate solvency resolution process against corporate debtor. Earlier it was the debtor who primarily initiates the resolution process. Under IBC (Insolvency and Bankruptcy Code) creditor as well as debtor can file for insolvency. During the insolvency resolution the financial creditor will analyze whether there is any scope for revival of the debtor's business. The

resolution process is conducted by Insolvency Professionals. An Insolvency Professional shall be a person who has ten years of experience as Chartered Accountant or Cost accountant or Company secretary or a lawyer. Apart from this he also has to clear Limited Insolvency examination. A person can also become Insolvency Professional by passing the National Insolvency Examination.

Insolvency process in case of Company under Insolvency and Bankruptcy Code 2016:

For a company insolvency process is adjudicated by National Company Law Tribunal. The resolution process will have to be completed within 180 days which can be extended to another 90 days. There is another provision called Fast Tracking Resolution process, where the resolution process will be completed in 90 days, which can be extended up to 45 days. The Ministry of Corporate Affairs has notified the relevant sections 55 to section 58 of the Insolvency and Bankruptcy code 2016, pertain to the fast tracking process. The fast track process shall be applied to following categories of corporate debtors:

1. A small company as defined under clause 85 of Section 2 of the Companies Act 2013 or
2. A start up (other than partnership firm) as defined in the notification dated in 23rd May, 2017 of Ministry of Commerce and Industry or
3. An unlisted company with the total asset as reported in the financial statement of the immediately preceding the financial year not exceeding Rs 1crore.

The NCLT (National Company Law Tribunal) appoints an interim Insolvency Professional. He took over the companies operation and collects the financial information. The adjudicating authority shall appoint an Interim Insolvency professional within the 14 days from the insolvency commencement date. In case of no name of Insolvency professional's are proposed by creditors then the adjudicating authority shall make the reference to the Insolvency and bankruptcy Board for the recommendation of an insolvency professional who may act as an interim Resolution Professional. Within 10 days of the receipt of such reference from the adjudicating authority the board shall recommend the name of the insolvency professional. The term of Insolvency Resolution Professional shall not exceed 30 days from the date of his appointment. The Insolvency Professional constitutes the creditors committee. All financial creditors are part of creditors committee except the one who are related party of the corporate debtor.

In the first meeting the committee of creditors may either resolve to appoint the interim resolution professional as a resolution professional or to replace the interim resolution professional by another resolution professional. Creditor's committee meets within seven days of its formation and decides by 75 percent of votes either to replace or confirm interim Insolvency Professional as resolution professional. After that resolution professional is appointed by NCLT.

During the liquidation the code clearly specifies the order of priority of payment of debts. The order of priority of payment of debts in accordance to Section 178 of Insolvency Bankruptcy Code is given below:

1. Notwithstanding anything to the contrary contained in any law enacted by the Parliament or the State Legislature for the time being in force, in the distribution of the final dividend, the following debts shall be paid in priority to all other debts—
 - a) Firstly, the costs and expenses incurred by the bankruptcy trustee for the bankruptcy process in full;
 - b) Secondly,—
 - The workmen's dues for the period of twenty-four months preceding the bankruptcy commencement date; and
 - Debts owed to secured creditors;
 - c) Thirdly, wages and any unpaid dues owed to employees, other than workmen, of the bankrupt for the period of twelve months preceding the bankruptcy commencement date;
 - d) fourthly, any amount due to the Central Government and the State Government including the amount to be received on account of Consolidated Fund of India and the Consolidated Fund of a State, if any, in respect of the whole or any part of the period of two years preceding the bankruptcy commencement date;
 - e) Lastly, all other debts and dues owed by the bankrupt including unsecured debts.

2. The debts in each class specified in sub-section (1) shall rank in the order mentioned in that sub-section but debts of the same class shall rank equally amongst themselves, and shall be paid in full, unless the estate of the bankrupt is insufficient to meet them, in which case they shall abate in equal proportions between themselves.
3. Where any creditor has given any indemnity or has made any payment of moneys by virtue of which any asset of the bankrupt has been recovered, protected or preserved, the Adjudicating Authority may make such order as it thinks just with respect to the distribution of such asset with a view to giving that creditor an advantage over other creditors in consideration of the risks taken by him in so doing.
4. Unsecured creditors shall rank equally amongst themselves unless contractually agreed to the contrary by such creditors.
5. In the case of partners, the partnership property shall be applicable in the first instance in payment of the partnership debts and the separate property of each partner shall be applicable in the first instance in payment of his separate debts.
6. Where there is a surplus of the separate property of the partners, it shall be dealt with as part of the partnership property; and where there is a surplus of the partnership property, it shall be dealt with as part of the respective separate property in proportion to the rights and interests of each partner in the partnership property.

At present, the High Courts, the Company Law Board (CLB), the Board for Industrial and Financial Reconstruction (BIFR) and Debt Recovery Tribunal (DRT) are having overlapping jurisdiction in the matter of debt recovery and restructuring. This gives rise to systemic delays and complexities in the process. The code intends to overcome these challenges and aims to reduce the burden on the courts as all litigation will be filed under the Code. According to Part II, Chapter VI of the Code, National Company Law Tribunal (NCLT) would be adjudicating authority for insolvency resolution and liquidation of Companies, Limited Liability Partnerships (LLPs), any entity with limited liability under any law and bankruptcy of personal guarantors thereof. An appeal can be preferred from orders of NCLT to National Company Law Appellate Tribunal (NCLAT) within 30 days (15 days' extension if there is sufficient ground). Jurisdiction is territorial based on location of registered office of corporate person. Orders of NCLAT are appealable on a question of law to the Supreme Court within 45 days.

The Central Government has constituted 11 (eleven) Benches of the NCLT in exercise of its powers under sub-section (1) of section 419 of the new Companies Act, 2013. Of the said 11 benches, two shall be situated in New Delhi, and one each at Ahmedabad, Allahabad, Bengaluru, Chandigarh, Chennai, Guwahati, Hyderabad, Kolkata and Mumbai.

Insolvency process in case of Individuals and Partnership firm under Insolvency and Bankruptcy Code 2016:

For the individuals and partnership the code applies in those case where the default is above Rs 1000(may be increased up to Rs 1,00,000 by government by notification). In here IBC provides two distinct processes, they are Automatic fresh start and Insolvency resolution Process.

In Automatic fresh start process, the eligible debtors can apply to Debt Recovery Tribunal (DRT) for discharging from certain debts not exceeding a specified threshold allowing them to start afresh. The fresh start process is only available to individual insolvency and not available for corporate persons. A resolution professional appointed by the DRT examines the application, receives claims from creditors, accepts or rejects the application and submits a report with reasons to the DRT. On the basis of the said report, the DRT accepts or rejects the application. The insolvency resolution process consists of preparation of a repayment plan by the debtor, for approval of creditors. If approved, the DRT passes an order binding the debtor and creditors to the repayment plan. If the plan is rejected or fails, the debtor or creditors may apply for a bankruptcy order.

Under Part III, Chapter VI of the Code, Debt Recovery Tribunal (DRT) would be the adjudicating authority for insolvency resolution and bankruptcy of individuals, unlimited partnerships and partner/s thereof. Jurisdiction would be based on place of residence or works for gain or carries on business. Appeal can be made to Debt Recovery Appellate Tribunal (DRAT) within 30 days (15 days' extension if there is sufficient ground). Further appeal from DRAT would be within 45 days before the Supreme Court only on question of law. It is specifically provided that Civil courts or authority not to have jurisdiction and also cannot grant any injunction.

CONCLUSION

The essential idea of the new Code is that when a corporate person commits default on its debt, control of the corporate will be transferred from the shareholders or promoters to a committee of creditors, who have 180 days (additional 90 days in deserving cases) to evaluate proposals from various parties about reviving the company or taking it into liquidation. When decisions are taken in a time-bound manner, there is a greater chance that the corporate entity can be saved as a going concern and the productive resources of the economy can be put into the best use. The Code contains a provision for including operational creditors (workmen, employees, suppliers) in the Committee of Creditors if their dues are not less than 10% of the debt. They won't be given any voting rights but have a chance to present their views. This will help the resolution professional to keep up the timelines. The Code amends the Sick Industrial Companies (Special Provision) Repeal Act, 2003. Thereby, any proceeding pending before the BIFR under the Sick Industrial Companies Act 1985, immediately before the commencement of this law shall stand abated. Such company, in respect of which such proceeding stands abated, may make a reference to Adjudicating Authority within 180 days from the commencement of this law.

According to the Doing business report published by World Bank, India's rank in resolving insolvency improved from 136 to 103. The Code helps to bring about far-reaching reforms with a thrust on creditor driven insolvency resolution. It aims at early identification of financial failure and maximizing the asset value of insolvent firms. The unified regime helps to create a time-bound process for insolvency resolution and liquidation, which improves the debt recovery rates. With the implementation of Insolvency and Bankruptcy Code we could reduce the time and cost involved in the insolvency process. The code will be able to protect the interests of small investors and make the process of doing business a less complicated one.

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