



# AN OVERVIEW OF THE DEVELOPMENTS OF THE INSOLVENCY AND BANKRUPTCY CODE, 2016

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## **ABSTRACT**

The Insolvency and Bankruptcy Code, 2016 (IBC) is the bankruptcy law of India which seeks to consolidate the existing framework by creating a single law for insolvency and bankruptcy. The legal status of an entity or a person where the debt owed to the creditors cannot be repaid is known as Bankruptcy. A court order imposes bankruptcy in most of the jurisdictions. The IBC, 2016 provides for a time-bound process to resolve insolvency. When a default in repayment occurs, creditors gain control over the debtor's assets and must make decisions to resolve insolvency within 180 days. To ensure an uninterrupted resolution process, the Code also provides immunity to debtors from resolution claims of creditors during this period. The Code also consolidates provisions of the current legislative framework to form a common forum for debtors and creditors of all classes to resolve insolvency.

## **KEYWORDS**

Insolvency & Bankruptcy Code 2016 (IBC), Adjudicating authorities, Insolvency and Bankruptcy Board, NCLT, DRT, CoC (Committee of Creditors).

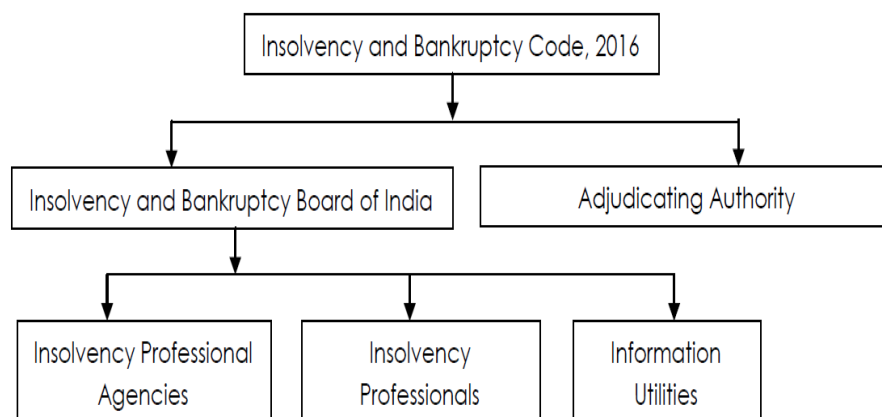
## **INTRODUCTION**

On 28th May, 2016, the Code was published in the official gazette after its passage in Parliament. It has been hailed as a major economic measure, aimed at aligning insolvency laws with international standards. Parliament's previous attempts to ensure recovery of public debt, (through the Recovery of Debts due to Banks or Financial Institutions Act, 1993, hereafter "RDBFI Act") securitization (by the Securitization and Reconstruction and Enforcement of Security Interests Act, 2002 hereafter "SARFESI") deal with certain facets of corporate insolvency. These did not result in the desired consequences. The aim of the Code is to a) promote entrepreneurship and availability of credit; b) ensure the balanced interests of all stakeholders and c) promote time-bound resolution of insolvency in case of corporate persons, partnership firms and individuals.

The Insolvency & Bankruptcy Code 2016 (IBC), enacted to address the troubling shortcomings in existing staggered insolvency laws in India and to bring them under one umbrella, is set up to face a monumental challenge and equally monumental expectations. At present, according to the data available with the World

Bank in 2016, insolvency resolution in India takes around 4.3 years on average, compared with United Kingdom (1 year), USA (1.5 years) and South Africa (2 years). India was ranked 135th/190 countries in the World Bank Ease of Doing Business Index 2015 on the ease of resolving insolvency. Thus, it is apparent that the Code is perhaps one of the most critical legislations introduced in the recent years impacting the ease of doing business in India.

The Insolvency and Bankruptcy Code 2016, has radically changed the process of insolvency resolution in India, is keenly watched by economists and jurists as well as businessmen and investors, for the reason that each aspect of the implementation of law has the potential to critically impact the ease of doing business in India. For this reason, the Code is especially sensitive to interpretation and it is vital that the issues thrown up in its inaugural year of implementation be recognized and the judicial remark on the same be understood. The present article thus traces the emerging jurisprudence of the Code through judgments of the Supreme Court of India and the National Company Law Appellate Tribunal.



The Insolvency and Bankruptcy Code, 2016 (IBC) is facilitated by the following five pillars:

1. **The Insolvency Professionals:** These professionals will administer the resolution process, manage the assets of the debtor, and provide information for creditors to assist them in decision making.
2. **Insolvency Professional Agencies:** insolvency professionals will be registered with insolvency professional agencies. The agencies conduct examinations to certify insolvency professionals and enforce a code of conduct for their performance.
3. **Information Utilities:** Creditors will report financial information of the debt owed to them by the debtor. Such information will include records of debt, liabilities and defaults.
4. **Adjudicating authorities:** The proceedings of the resolution process will be adjudicated by the National Companies Law Tribunal (NCLT), for companies; and the Debt Recovery Tribunal (DRT), for individuals. The duties of the authorities will include approval to initiate the resolution process, appoint the insolvency professional, and approve the final decision of creditors.
5. **Insolvency and Bankruptcy Board:** The Board will regulate insolvency professionals, insolvency professional agencies and information utilities set up under the Code.

The IBC, 2016 proposes the following steps to resolve insolvency:

1. **Initiation:** When a default occurs, the resolution process may be initiated by the debtor or creditor. The decision to resolve insolvency: A committee consisting of the financial creditors will take a decision regarding the future of the outstanding debt owed to them. They may choose to revive the debt owed to them or sell (liquidate) the assets of the debtor to repay the debts owed to them. If a decision is not taken in 180 days, the debtor's assets go into liquidation.
2. **Liquidation:** If the debtor goes into liquidation, an insolvency professional administers the liquidation process. Proceeds from the sale of the debtor's assets are distributed in the already established order of precedence.

## OBJECTIVES & RESEARCH METHODOLOGY

The purpose of the study is to focus on the improvements in the recovery process as has been achieved by repeated amendments to the IBC, 2016. And also, to highlight the loopholes which have existed in the base IBC, 2016. The research paper is purely based on secondary data obtained from various articles, reports and publication of the Government of India in its official Gazette.

## THE INSOLVENCY AND BANKRUPTCY CODE (AMENDMENT) ACT, 2017

1. In section 25 of the principal Act, in sub-section (2), for clause (h), the following clause shall be substituted, namely -

"(h) invite prospective resolution applicants, who fulfil such criteria as may be laid down by him with the approval of committee of creditors, having regard to the complexity and scale of operations of the business of the corporate debtor and such other conditions as may be specified by the Board, to submit a resolution plan or plans."

3. After section 29 of the principal Act, the following section shall be inserted, namely –

"29A. A person shall not be eligible to submit a resolution plan, if such person, or any other person acting jointly or in concert with such person

(a) is an undercharged insolvent;

(b) is a wilful defaulter in accordance with the guidelines of the Reserve Bank of India issued under the Banking Regulation Act, 1949;

(c) has an account, or an account of a corporate debtor under the management or control of such person or of whom such person is a promoter, classified as nonperforming asset in accordance with the guidelines of the Reserve Bank of India issued under the Banking Regulation Act, 1949 and at least a period of one year has lapsed from the date of such classification till the date of commencement of the corporate insolvency resolution process of the corporate debtor;

Provided that the person shall be eligible to submit a resolution plan if such person makes payment of all overdue amounts with interest thereon and charges relating to non-performing asset accounts before submission of resolution plan;

(d) has been convicted for any offence punishable with imprisonment for two years or more;

(e) is disqualified to act as a director under the Companies Act, 2013;

(f) is prohibited by the Securities and Exchange Board of India from trading in securities or accessing the securities markets;

(g) has been a promoter or in the management or control of a corporate debtor in which a preferential transaction, undervalued transaction, extortionate credit transaction or fraudulent transaction has taken place and in respect of which an order has been made by the Adjudicating Authority under this Code;

(h) has executed an enforceable guarantee in favour of a creditor in respect of a corporate debtor against which an application for insolvency resolution made by such creditor has been admitted under this Code;

(i) has been subject to any disability, corresponding to clauses (a) to (h), under any law in a jurisdiction outside India; or

(j) has a connected person not eligible under clauses (a) to (i).

## THE INSOLVENCY AND BANKRUPTCY CODE (AMENDMENT) ORDINANCE, 2018

### The Second Amendment Act

The Ordinance amends the Insolvency and Bankruptcy Code, 2016 to clarify that allottees under a real estate project should be treated as financial creditors. The voting threshold for routine decisions taken by the committee of creditors has been reduced from 75% to 51%. For certain key decisions, this threshold has been reduced to 66%. The Ordinance allows the withdrawal of a resolution application submitted to the NCLT under the Code. This decision can be taken with the approval of 90% of the committee of creditors. The issues with IBC 2016 were missing the deadline, lack of benches and judges, and haircuts which is the extent of write off that banks undertake as part of a resolution plan to get the company back on track. So far financial creditors have got 43 per cent of their claims and 188 per cent of the liquidation value. All these factors are raising concerns that IBC will meet the same fate as DRT and SARFAESI and banks will eventually lose confidence in IBC. The recent Supreme Court order setting aside RBI's decision to send all power companies to the NCLT has also set a wrong precedent. The IBC was amended by the IBC (Second Amendment) Act, 2018 ("Second Amendment Act") introducing the following changes:

- Reduction in the voting threshold of the CoC (Committee of Creditors) from 75% to 66% for certain key decisions such as appointment or replacement of resolution professionals, extension of insolvency resolution process, approval of resolution plan etc.
- Section 12A was introduced, which provides for withdrawal of an application seeking initiation of insolvency resolution after the same is admitted by the NCLT. The applicant can withdraw its application if at least 90% of the CoC (Committee of Creditors) provides its approval.
- It has been clarified that the provisions of the Limitations Act, 1963 have been applicable to all proceedings and appeals made under IBC since the inception of the IBC.
- An explanation to the definition of 'financial debt' was added, whereby any amount raised from allottees under a real estate project (including home buyers) will be considered as a financial debt. This implies that home buyers who were earlier put under the bracket of "other creditors", will now be considered as financial creditors and can now be a part of the Code of Conduct.
- The Second Amendment Act also brought in certain key changes in Section 29A of IBC which discusses the eligibility criteria for resolution applicants. One of the most important changes being the clarification on the timeline for disqualification of those resolution applicants which hold NPA's. The provision now states that a resolution applicant should not hold an NPA at the time of submission of the resolution plan.
- Section 29A (c) of the Insolvency and Bankruptcy Code, 2016. This amendment was brought in to provide prospective resolution applicants the ability to part ways with their NPAs prior to submission of a resolution plan, however, this position has been interpreted narrowly by the Supreme Court in the Essar Steel case.
- The case has been discussed in detail under section IV. The disqualification under sub-section (d) based on conviction of a person for an offense punishable with imprisonment for over two years has now been narrowed down to 25 Acts mentioned under the newly inserted Twelfth Schedule.
- Section 29A (d) of the Insolvency and Bankruptcy Code, 2016. The language in sub-section (i) has been amended to clarify that any disability corresponding to sub-sections (a) to (h) under any law in a jurisdiction outside India must be present and subsisting. This language has been inserted to ensure that a resolution applicant is not held ineligible for any disability suffered in the past and is not subsisting at the time of submission of the resolution plan.
- As per the amendment any financial entity which becomes a related party solely by way of conversion of debt or subscription to equity linked instruments before the insolvency commencement date will not be considered as a related party and will not be disqualified. Further, any entity which has acquired an NPA through the insolvency resolution process under the IBC will not be disqualified from making another acquisition under the IBC for the next three years.



### Third Amendment Act

The IBBI (Insolvency Resolution Process for Corporate Persons) (Third Amendment) Regulations, 2018 (“Third Amendment Act”), provided for the following changes –

- Model timeline to streamline the Corporate Insolvency Resolution Process (“CIRP”) and clarify certain ambiguities and overlapping timelines under the unamended CIRP.
- Procedure and time limit for withdrawal of the CIRP under Section 12A of the IBC.
- Process and format for invitation of Expression of Interest to participate in the CIRP and timeline for submission of the expression of interest. Statutory backing for automatic rejection of expression of interest and resolution plans submitted beyond the prescribed timeline. This deemed rejection of submissions can ensure a fairer process by restricting resolution applicants from revising their plans after analyzing bids submitted by their competitors and also ensure a timely completion of the CIRP.

### Fourth Amendment Act

The IBBI (Insolvency Resolution Process for Corporate Persons) (Fourth Amendment) Regulations, 2018 (“Fourth Amendment Act”) provide that operational creditor would have to be paid on priority over financial creditors under a resolution plan. This pay-out mechanism replaced the previous waterfall which provided for payment of resolution professional costs and liquidation value due to operational creditors and dissenting financial creditors in priority to financial creditors. Therefore, the Fourth Amendment has effectively done away with the requirement to pay the liquidation value due to dissenting financial creditors in priority.

### Liquidation Amendment Act

This Amendment made changes to the Insolvency and Bankruptcy Board of India (Liquidation Process) Regulations, 2016 on October 22, 2018, clarified that assets subject to security interest cannot be sold in liquidation proceedings unless the same have been relinquished to the liquidation estate. Section 52 of the IBC, provides every secured creditor the right to relinquish its security interest over assets and participate in the liquidation proceedings, or realize the secured assets as provided under law. As per the Liquidation Amendment, if a secured creditor does not relinquish its assets, then such assets cannot be sold during the liquidation process. Therefore, it is possible that even a single lender holding a charge over assets might attempt to sell entire verticals of the business or the corporate debtor as a whole.

### Insolvency Law Committee’s Second Report on Cross-Border Insolvency

The Insolvency Law Committee (“ILC”) has submitted its second report to the Government, recommending amendments to the IBC to include provisions on cross border insolvency (“Proposed Amendment”) based on the UNCITRAL Model Law. The Proposed Amendment seeks to incorporate the four major tenets from the UNCITRAL Model Law, namely, (a) direct access to foreign insolvency professionals and foreign creditors to participate in or commence domestic insolvency proceedings against a defaulting debtor; (b) recognition of foreign proceedings & provision of remedies; (c) cooperation between domestic and foreign courts & domestic and foreign insolvency practitioners; and (d) coordination between two or more concurrent insolvency proceedings in different countries. The Proposed Amendment would increase the access of Indian creditors to foreign assets and proceedings and vice versa, thereby strengthening the IBC regime and increasing investor confidence.

### THE INSOLVENCY AND BANKRUPTCY CODE (AMENDMENT) BILL, 2019

Parliament has recently passed the Insolvency and Bankruptcy Code (Amendment) Bill 2019 to resolve a few of the issues. The Code provides a time-bound process for resolving insolvency in companies and among individuals. Insolvency is a situation where individuals or companies are unable to repay their outstanding debt. Under the Code, a financial creditor may file an application before the National Company Law Tribunal (NCLT) for initiating the insolvency resolution process. The NCLT must find the existence of default within 14 days. Thereafter, a Committee of Creditors (CoC) consisting of financial creditors will be constituted for taking decisions regarding insolvency resolution. The CoC may either decide to restructure the debtor’s debt

by preparing a resolution plan or liquidate the debtor's assets. The CoC will appoint a resolution professional who will present a resolution plan to the CoC. The CoC must approve a resolution plan, and the resolution process must be completed within 180 days. This may be extended by a period of up to 90 days if the extension is approved by NCLT. If the resolution plan is rejected by the CoC, the debtor will go into liquidation. The Code provides an order of priority for the distribution of assets in case of liquidation of the debtor. This order places financial creditors ahead of operational creditors (e.g., suppliers). In a 2018 Amendment, homebuyers who paid advances to a developer were to be considered as financial creditors. They would be represented by an insolvency professional appointed by NCLT.

The Bill addresses three issues - First, it strengthens provisions related to time-limits. Second, it specifies the minimum pay-outs to operational creditors in any resolution plan. Third, it specifies the manner in which the representative of a group of financial creditors (such as home-buyers) should vote.

## **INSOLVENCY & BANKRUPTCY CODE (SECOND AMENDMENT) ACT 2020**

Rajya Sabha recently passed an Insolvency & Bankruptcy Code (2nd amendment) Act 2020. The IBC Bill 2020 came into force on June 5th, 2020. After section 10 of the Insolvency and Bankruptcy Code, 2016 the following section shall be inserted –

Section 10 A – Suspension of initiation of the corporate insolvency resolution process. As per Section 10 A, 'Notwithstanding anything contained in sections 7, 9 and 10, no application for initiation of corporate insolvency resolution process of a corporate debtor shall be filed, for any default arising on or after 25th March, 2020 for a period of six months or such further period, not exceeding one year from such date'. Fresh insolvency proceedings will not be initiated for at least six months starting from March 25 amid the COVID-19 pandemic. Default on repayments from March 25, the day when the nationwide lockdown began to curb COVID-19 infections, would not be considered for initiating insolvency proceedings for at least six months.

In Section 66 of the principal Act, after sub-section (2), the following sub-section shall be inserted –

Section 3 – “Notwithstanding anything contained in this section, no application shall be filed by a resolution professional under sub-section (2), in respect of such default against which initiation of the corporate insolvency resolution process is suspended as per section 10A.”

The ordinance suspends Sections 7, 9, and 10 on grounds that the pandemic has created uncertainty and stress for business for reasons beyond their control, the nationwide lockdown has added to disruption of normal business operations in such circumstances it would be difficult to find an adequate number of resolution applicants for a distressed/defaulting business.

## **THE INSOLVENCY AND BANKRUPTCY CODE (AMENDMENT) BILL, 2021**

The Insolvency and Bankruptcy Code (Amendment) Bill, 2021 was introduced in the Lok Sabha to amend the insolvency law and provide for a pre-packaged resolution process for stressed Micro, Small and Medium Enterprises. A pre-pack is an agreement for the resolution of the debt of a distressed company. It is an agreement between secured creditors and investors instead of a public bidding process. The scheme allows only the debtor to trigger its own bankruptcy process with the approval of financial creditors. In general bankruptcy provisions, the proprietors or major shareholders of a small business lose operational control of the enterprise to lenders. In a pre-pack insolvency scheme, the shareholders or proprietors do not lose control over the enterprise. The bill will replace the ordinance that was promulgated on April 4<sup>th</sup> this year. It proposed 'pre-packs as an insolvency resolution mechanism for MSMEs. Under this mechanism, main stakeholders such as creditors and shareholders come together to identify a prospective buyer and negotiate instead of a public bidding process.

### Provisions of the Bill:

- It specifies a minimum threshold of not more than Rs 1 crore for initiating the pre-packaged insolvency resolution process.
- It provides for disposal of simultaneous applications for initiation of the insolvency resolution process and pre-packaged insolvency resolution process, pending against the same corporate debtor.
- Penalty for fraudulent or malicious initiation of pre-packaged insolvency resolution process or with intent to defraud persons, and for fraudulent management of the corporate debtor during the process.
- Punishment for offences related to the pre-packaged insolvency resolution process.

### **CONCLUSION**

A lot many things have been settled through repeated amendments but still, a lot needs to be done. Not only do the new amendments plug loopholes in the Insolvency and Bankruptcy Code (IBC), which some promoters had used to stall resolution of their bankrupt companies, but the changes also seek to ensure time-bound resolution of insolvency cases. There has been a marked improvement in the recovery process which is already leading to billions of dollars being invested in the country due to the protection of creditor rights. Compared to other markets, the pace at which we have achieved this is also noteworthy. The progress in India has been remarkable by global standards.

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