

Insolvency and Bankruptcy Code, 2016:

Its Impact on Corporate Resolution and Recovery of Debt.

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India is one of the youngest republics in the world, with a high concentration of the most dynamic entrepreneurs. Yet these game changers and growth drivers were crippled by an environment that took some of the longest times and highest costs by world standards to resolve any problems that arise while repaying dues on debt.¹ This problem led to grave consequences: India had some of the lowest credit compared to the size of the economy.

It was therefore felt that a comprehensive and consistent treatment of bankruptcy and insolvency for providing resolution mechanism for whole gamut of entities including financial firms, limited liability companies, sole proprietorships, partnerships, limited liability partnerships and individuals, etc. is necessary. It was noted that as regards 'financial firms', Financial Sector Legislative Reforms Commission (FSLRC) headed by Justice (Retd.) Srikrishna, has already recommended establishment of 'Resolution Corporation'² and therefore, the Hon'ble Finance Minister in his budget Speech for 2014-15, announced that an "Entrepreneur friendly legal bankruptcy framework will also be developed for SMEs to enable easy exit."³

Pursuant to the said announcement, the Ministry of Finance (Dept. of Economic Affairs-FSLRC Division) set up a Committee⁴ under the Chairmanship of Shri T. K. Vishwanathan⁵ on 22nd August, 2014 to study the corporate bankruptcy legal framework in India and submit its report along with draft Bankruptcy Code.

The Committee examined the existing bankruptcy framework and found that there was no single law in India that dealt with insolvency and bankruptcy. As per the extant legal framework before 2016, provisions relating to insolvency and bankruptcy for Companies could be found in the Sick Industrial Companies (Special Provisions) Act, 1985 [SICA], the Recovery of Debt Due to Banks and Financial Institutions Act, 1993 [RDDBFI], the Securitization and Reconstructions of Financial Assets and Enforcement of Security Interest Act, 2002 [SARFAESI] and the Companies Act, 2013. Liquidation of Companies was handled by the High Courts. Individual Bankruptcy and Insolvency is dealt with by the respective District Court.

The Committee therefore decided to draft a single unified framework and a modern law dealing with bankruptcy and insolvency of persons other than ‘financial firms’, which is a simple, coherent, time bound and effective answer to the problems under Indian conditions. The Committee was also conscious of the fact that due to multiple Acts and fora, in spite of making lots of efforts in economic developments, India is not able to attract enough foreign investment due to its lower ranking in “ease of doing business” issued by World Bank, every year. The Committee therefore decided to frame an effective statutory framework to deal with insolvency and bankruptcy to facilitate development of credit markets, encouraging entrepreneurship, improving ease of doing business, facilitating investments, creating more employment opportunity leading to higher economic growth and development. Accordingly, the Committee presented its Report along with draft Insolvency and Bankruptcy Code to Government of India on 04th November, 2015.

The Committee took note of the fact that the failure of some business plans is integral to the process of the market economy. When business failure takes place, the best outcome for society is to have a rapid re-negotiation between the financiers, to finance the going concern using a new arrangement of liabilities and with a new management team. If this cannot be done, the best outcome for society is a rapid liquidation. When such arrangements can be put into place, the market process of creative destruction will work smoothly, with greater competitive vigor and transaction costs.⁶

The Draft Bill was introduced in the Lok Sabha on 21st December, 2015. The Bill was then referred to the Joint Committee of Parliament (JCP) having representatives of both the houses of Parliament (20-Lok Sabha; 10-Rajya Sabha). The Committee held 12 sittings in all and sought/invited comments/views and suggestions from all the stakeholders. Based on internal deliberations and suggestions received, the Committee submitted its report along with the modified Draft Bill. The revised Bill was passed by the Lok Sabha on 5th May, 2016 and by the Rajya Sabha on 11th May, 2016. It received President’s ascent on 28th May, 2016 and was Notified as **“The Insolvency and Bankruptcy Code, 2016”** (Act 31 of 2016) on the same day i.e. 28th May, 2016.

Key features

1. Insolvency Resolution: The Code outlines separate insolvency resolution processes for individuals, companies and partnership firms. The process can be initiated by either the debtor or the creditors. A maximum time limit, for completion of the insolvency resolution process, has been set for corporates and individuals. For companies, the process will have to be completed in 180 days,

which may be extended by 90 days. For startups (other than partnership firms), small companies and other companies (with asset less than Rs.1 crore), resolution process would be completed within 90 days of initiation of request which may be extended by 45 days.

Insolvency Regulator: The Code establishes the Insolvency and Bankruptcy Board of India (IBBI), to oversee the insolvency proceedings in the country and regulate the entities registered under it. The Board will have 10 members, including representatives from the Ministries of Finance, Corporate Affairs & Law, and the Reserve Bank of India.

Insolvency Professionals: The insolvency process will be managed by registered professionals. These professionals will also control the assets of the debtor during the insolvency process

Bankruptcy and Insolvency Adjudicator: The Code proposes two separate tribunals to oversee the process of insolvency resolution, for individuals and companies:

- (i) the National Company Law Tribunal for Companies and Limited Liability Partnership firms; and
- (ii) the Debt Recovery Tribunal for individuals and partnerships.

A plea for insolvency is submitted to the Adjudicating Authority (AA-NCLT in case of corporate debtors) by financial or operation creditors or the corporate debtor itself. The maximum time allowed to either accept or reject the plea is 14 days. If the plea is accepted, the AA has to appoint an Interim Resolution Professional (IRP) to draft a resolution plan following which the Corporate Insolvency Resolution process is initiated by appointing a Resolution Professional. During the resolution process, Resolution Professional takes over the management of the Corporate debtor, the board of directors of the company stands suspended and the promoters do not have a say in the management of the company. This is a unique concept and total opposite to the concept prevailing thus far wherein the old management (debtor) used to remain in control of the assets of the debtor company and normally used to siphon off the assets of the debtor company during the process. The Resolution Professional, if required, can seek the support of the company's management for day-to-day operations. If the Corporate Insolvency Resolution Process (CIRP) fails in reviving the company as an ongoing concern, the liquidation process is initiated.

Amendments

Any new system has to be dynamic to address the need that may arise in implementation and be ready to fill the gaps identified in the process to not only make it more effective but also to ensure that the provisions may not be misused by unscrupulous elements to benefit themselves either directly or indirectly. Therefore, based on the experience gained and considering the importance of this legislation in the economic development of the country, the Government has made three Amendments to it so far. The fourth amendment i.e. IBC (Second Amendment) 2019 has also been passed by the Lok Sabha on 12th December, 2019 but is pending in Rajya Sabha.

Following has been the journey of the development of IBC by way of various amendments:

First Amendment to IBC (2017)⁷:

In order to strengthen further the insolvency resolution process, first Amendment to the Code was made within a year of notification of the Code in 2016. These amendments -

- (i). facilitated phased implementation of the provisions of the Code to personal guarantor, corporate debtors, individuals, proprietorship firms and partnership firms;
- (ii). provided clarity as to the persons who can submit a resolution plan in response to an invitation made by the resolution professional.
- (iii). clarified that a resolution applicant can submit the resolution plan individually or jointly with any other person, who is otherwise not disqualified;
- (iv). provided that the committee of creditors should approve a resolution plan after considering its feasibility and viability, and such other requirements as may be specified by the Board;
- (v). provided that in case of liquidation of the debtor, the liquidator shall not sell the property of the debtor to a person who is not eligible to be a resolution applicant.

The main object of these amendments, besides implementation of the Code to other entities [refer (i) above], was to prohibit the promoters of the defaulter, being resolved, and to make them ineligible to submit resolution plan, possibly to prohibit their backdoor entry into the debtor with haircuts.

Second Amendment to IBC (2018)⁸:The Second Amendment-

- (i). Clarified that ineligibility for resolution applicants introduced vide 2017 amendment shall not be applicable to persons applying for resolution of

MSMEs. Meaning thereby, a promotor of a MSME can be a resolution applicant, provided he/she is not otherwise ineligible;

(ii). Clarified that an allottee under a real estate project (home buyers) will be considered a 'financial creditor'. This gave home buyers due representation in the Committee of Creditors (CoC);

(iii). Allowed financial creditors to appoint authorized representatives in certain cases;

(iv). Withdrawal of admitted application for initiation of resolution process was permitted, subject to the approval of 90% vote of CoC;

(v). All decision in the Committee of Creditors to be taken by 51% majority, as against 75% majority envisaged earlier. Further, all major decisions in CoC to be taken by 66% majority as against 75% provided earlier;

(vi). Moratorium not to apply to Guarantors and NCLT to have jurisdiction over the insolvency resolution of the corporate guarantor also.

Third Amendment to IBC (2019)⁹:Third Amendment-

(i). clarified that resolution plan may include provisions for the restructuring of the corporate debtor also including by way of merger, amalgamation and demerger;

(ii). Imposing more discipline to adhere to the strict time lines provided under the Code, a provision has been inserted putting the Adjudicating Authority (AA/NCLT) under obligation to record the reasons if AA delays the admission/rejection of resolution application beyond 15 days, as provided under the Code;

(iii). Making it mandatory to complete the corporate insolvency resolution process within 330 days from the insolvency commencement date [*This provision has however been stuck down in **Essar Steel Case**¹¹ by the Hon'ble Supreme Court terming it to be manifestly arbitrary under Article 14 of the Constitution of India as being unreasonable restriction on litigants' right to carry on business under Article 19(1)(g)*].

(iv). Clarifying that an authorized representative shall cast his vote on behalf of all financial creditors he represents as per the decision taken by a vote of more than 50% of the voting share of the financial creditors he represents;

(v). ensured that operational creditors shall not be paid less than the amount which could have been paid to them had the corporate debtor would have been liquidated or paid if the amount was distributed as per the order of priority as

contained in Section 53 (waterfall), whichever is more. Similarly, financial creditors, who do not vote in favor of the resolution plan, shall also be paid not less than what they could have been paid if the amount was distributed as per the order of priority as per Section 53. This provision has been made to ensure that Committee of Creditors or majority creditors may not discriminate against minority creditors, whether operational or financial.

Fourth Amendment to IBC(2019)¹⁰- [Proposed (Pending in Rajya Sabha)].

The Insolvency and Bankruptcy Code (Second Amendment) Bill, 2019 was introduced in the Lok Sabha on 12 December, 2019. The Statement of objects and reasons of the Bill states that a need was felt to give the highest priority in repayment to last mile funding to corporate debtors to prevent insolvency, in case the company goes into corporate insolvency resolution process or liquidation, to prevent potential abuse of the Code by certain classes of financial creditors, to provide immunity against prosecution of the corporate debtor and action against the property of the corporate debtor and successful resolution applicant subject to fulfilment of certain conditions.

Impact of IBC on recovery of corporate debt, reduction of NPAs and resolution of corporate debtors:

So far, out of 21,136 applications filed, 9,653 cases involving a total amount of approx. Rs.3,74,931.30 Cr have been disposed of at pre-admission stage of IBC. 2838 cases were admitted into Corporate Insolvency Resolution Process (CIRP) out of which 306 cases are closed by appeal/review/withdrawn. In the 161 resolved cases, the realizable amount is Rs. 1,56,814 crore. Further, in the World Bank Doing Business Report 2020 under 'Resolving Insolvency Index', India's ranking has jumped 56 places to 52 in 2019 from 108 in 2018, which was 136 in 2016 and 2017. Recovery rate increased from 26.5% in 2018 to 71.6% in 2019. Time taken in recovery improved from 4.3 years in 2018 to 1.6 years in 2019¹².

From the above, it is clear that by and large, the Code has been able to achieve the objective for which it was enacted. This has turned out to be the most dynamic economic legislation in recent memory in India and not only legislature who has been prompt in amending and inserting new provisions to make it more effective, but also the judiciary has been very prompt in upholding the true object and spirit of the Code, through its various judgments including its constitutional validity¹³.

1. *The Report of the Bankruptcy Law Reforms Committee, 2015 (The Report) [T. K. Vishwnathan Committee].*
2. *Financial Sector Legislative Reforms Commission Report, 2013.*
3. *Para-106 of Budget Speech of the Hon'ble Finance Minister.*
4. *Office Order dated 22.08.2014*
5. *Former Secretary General of 15th Lok Sabha and former LawSecretary.*
6. *Executive Summary- "The Report".*
7. *Insolvency and Bankruptcy Code (Amendment) Act, 2017 [w.e.f.].*
8. *Insolvency and Bankruptcy Code (Amendment) Act, 2018.*
9. *Insolvency and Bankruptcy Code (Amendment) Act, 2019.*
10. *Insolvency and Bankruptcy Code (Amendment) Bill, 2019.*
11. *Committee of Creditors of Essar Steel India Limited Vs. Satish Kumar Gupta & Ors. (Civil Appeal no. 8766-67/2019)*
12. *Year End Review -2019 of Ministry of Corporate Affairs- Posted On: 15 DEC 2019 11:21AM by PIB Delhi*
13. *Swiss Ribbons Pvt. Ltd v Union of India [Writ Petition (Civil) No. 99 of 2018, decided on January 25, 2019 (SC)]*

