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THE MATERIALIZING SPHERE OF CORPORATE INSOLVENCY IN INDIA

-Rohit Jain

ABSTRACT

This article will help you to understand the changing regime of corporate insolvency in India, after the introduction of the Insolvency and Bankruptcy Code of 2016. On the outset, this article will help you to figure out the basic difference between insolvency and bankruptcy. Furthermore, this article discusses reasons which led to the introduction of this code, followed by the procedure, eligibility to file a complaint, the institutional framework, the drawbacks, the path forward and everything which you need to know about this code. Relevant case laws and practical illustrations have also been used throughout this article. It will also help you to understand the impact of this Insolvency and Bankruptcy code on the great Indian Economy. IBC is also said to be the biggest accomplishment of the current Government. The Insolvency and Bankruptcy Code is a huge step towards the ease of doing business in India, and as a result of that India had jumped from 142 (in 2015) to 66 (in 2020) in the ease of doing business Index. This code has the power to solve chronic issues of Insolvency and Bankruptcy in India, thus it is considered as a consolidated Insolvency Scheme. This code was introduced to mend the loopholes in the old insolvency procedure. It is said to be the biggest economic reform in the history of the country. It has made the insolvency procedure fast and economical. This code has benefited the country and helped in solving various cases of insolvency and bankruptcy. It has also repealed the provision of various old laws. The act clearly mentions the classes of people who all can file a complaint. NCLT (National Company Law Tribunal), NCLAT (National Company Law Appellate Tribunal), DRT (Debt Recovery Tribunal) are all part of the adjudicating authorities. It is considered as a consolidated Insolvency Scheme, aimed at giving certainty of time, pace, outcome, and security to the creditors and other participants. It provides a brisk, abrupt and quick solution for resolving insolvencies, which previously was a long process.

1) INTRODUCTION

Insolvency and Bankruptcy Code is said to be the one of the biggest accomplishment of the current Government. The Insolvency and Bankruptcy Code came into force in the year 2016, after decennary of proposals from various different economists and economic organizations from throughout the world, on improving the previous insolvency regime in India. It is considered to be the biggest insolvency transformation in economic past of India. “The code was introduced in Lok Sabha in December 2015 and it was passed by Lok Sabha on 5 May 2016 and by Rajya Sabha on 11 May 2016. The Code received the assent of the President of India on 28 May 2016.”¹ It appears to be the best step in developing the Insolvency Jurisprudence. This code marked numerous changes in the preceding insolvency procedure. It is designed and intended to protect and look after the interest of small investors in India. It provides a brisk, abrupt and quick solution for resolving insolvencies, which previously was a long process. It makes the procedure economically viable. This code is said to be the foremost reason for changing India’s ranking in the World Ease of Doing Business Index. In 2015 India ranked 142 in the ease of doing business index, but after the enactment of IBC this rank has changed to 66 in 2020. This can be said to be a very good accomplishment.

It is considered as a consolidated Insolvency Scheme, aimed at giving certainty of time, pace, outcome, and security to the creditors and other participants. After the establishment of this code the constitutional validity of various different laws has been put for test at the Supreme Court of India. Furthermore in many cases the validity of the provisions of this code itself has also been questioned in the court, and the court had upheld the validity of all of its provision, say, initiation, voting power, distribution on liquidated amount, the procedure, disqualification process, utilities, etc.

The provision of the Insolvency and Bankruptcy Code clearly deals with almost everything relating to Insolvency procedure in India. It also provides for establishment of the Insolvency and Bankruptcy Board of India, which was entrenched by the Government of India on 1st October 2016, which performs the function of regulating the three pillars of the code, i.e the Insolvency Professionals, Insolvency Professional Agencies, Information Utilities.

¹https://en.wikipedia.org/wiki/Insolvency_and_Bankruptcy_Code,_2016

2) MEANING OF INSOLVENCY AND BANKRUPTCY

Insolvency is a term which is used when an individual or an organization is incapable of clearing its debt or arrears. An individual or an organization who fails to clear its debt, is called an insolvent. Being insolvent means a position when an individual or an organization is no longer able to meet its financial obligation. It generally occurs due to increase in expenses and decrease in revenues. Whereas, bankruptcy means the legal proceedings which are followed when a person is declared as an insolvent. It is generally initiated after the debtors file a petition to claim for their money which has become due.

To understand the grey line between insolvency and Bankruptcy, have a look at the following statement. "You can be insolvent without being bankrupt but you cannot be bankrupt without being insolvent."² Many people think of them as the same, but both of them are different in their context. Insolvency is a complication that bankruptcy is constructed to deal with. By insolvency we mean to state that a person's financial position is not such that he can clear all of his arrears. Bankruptcy is a process made to figure out the problem of Insolvency. Bankruptcy can be said to be a financial failure. It means the procedure that is followed when a person is declared as an Insolvent. It is initiated when a debtor files a complaint. Thus, we can say that Insolvency is a problem that bankruptcy is designed to solve.

3) WHY INTRODUCED

There were a number of reasons due to which this new code of Insolvency was introduced. Since a number of lacunas were there in the previous insolvency regime and these lacunas created various chronic problems in the insolvency procedure. And to solve these entire chronic problems this new Code for Insolvency and Bankruptcy was introduced. Here, we will be looking at some of the key reasons which led to the introduction of this Code.

Prior to the introduction of this code we had many laws which dealt with Insolvency in India, Like the Securitization and Reconstruction of Financial Assets, Companies Act, Sick Industries Act, SICA Act, etc. which had certain provision regarding Insolvency. And due to such number

²<http://www.debt.org.com>

of act dealing with the Insolvency and Bankruptcy, Insolvency procedure in India took a very long time. The Insolvency Resolution Process prior to this Code took around 4.3 Years, which is too higher as compared to other nations (Like in UK it is only 1 Year, in USA it is only 1.5 year). These delays were caused due to time taken to resolve cases in courts and confusion due to lack of clarity about the current bankruptcy framework. The purpose of this is to expedite and simplify the process of insolvency ensuring fair negotiation.

This act makes the procedure fast by creating various institution of insolvency like Insolvency Professionals, Professional Agencies, Information Utilities, Adjudicating Authorities etc.. So, the main purpose for introducing this code is to put the insolvency resolution process into fast track. It aims to address around 10 Trillion of nonperforming assets in Indian banks. This act is one of the main reasons for India's jump into ease of doing business report.

Furthermore it is a useful tool for the security of International Creditors and investors, which previously was not provided. Moreover it has a faster debt recovery mechanism, which makes the code a bit more viable economically. One of the important reason for its introduction is that prior to it, for getting the solution of any insolvency related issue, many laws were to be looked at for solution, but this code provides a one step solution to all the insolvency related issues. It also had looked for the employees' welfare after liquidation. Thus the introduction of such code was a vitally required step.

4) THE PAST OF INSOLVENCY AND BANKRUPTCY IN INDIA

Insolvency in India is a matter of English Origin back in 1800. It was firstly included in the Indian laws by the Government of India Act, 1800 under section 23 and 24; this was the first step of Insolvency Resolution in India. After that a specific town Act in the Bombay, Madras and Calcutta presidency was followed. Then The Presidency Town Insolvency Act, 1909 was introduced. Under this act the jurisdiction of adjudicating was with High Courts. In 1920 the Provincial Insolvency Act came into existence, and this was in action prior to the Insolvency and Bankruptcy Code, 2016. With the increasing Globalization there had been an increasing need of the Insolvency procedure in India. And thus it can be said as the need of the time.

5) CONSTITUTIONAL PROVISIONS RELATING TO INSOLVENCY IN INDIA

The insolvency and bankruptcy is a matter of concurrent list, which means that both the centre and state have power to make law. Furthermore there are certain provisions relating to Insolvency and Bankruptcy in both the Union List and the State List. The Union List (List I) under Entry 43, talks about incorporation, winding up, finance, insurance of a company. And Entry 82 of the List II i.e the State List includes all the other matter which are not mentioned under the List I. Due to these powers conferred to the Union under List I the Government of India has formed the Companies Act of 1956. The IBC was introduced after a recommendation of various committees like the Bankruptcy Law Reform Committee, T.Tiwari Committee, JJ. Irani Committee, VB Balkrishna Committee etc.

6) WHO ALL CAN FILE A COMPLAINT

This Insolvency and Bankruptcy Code of 2016 clearly specifies the classes of person who are eligible for filing a complaint regarding insolvency. The person who all can file a complaint are defined under Section 3 (23) of the code: “person includes (a) an individual; (b) a Hindu undivided family; (c) a company; (d) a trust; (e) a partnership; (f) a Limited Liability partnership; (g) any other entity established under a statute, and includes a person resident outside India.”³ Even after specifically mentioning the classes of person eligible to file a complaint, there is one issue on which it is criticized; and i.e. it fails to provide adequate opportunities to the debtors for initiating complaint. It is a bit creditors centric on the matter of initiation of a case, and thus this provision of the IBC need a bit of changes to be added.

7) INSOLVENCY RESOLUTION PROCESS

The Insolvency and Bankruptcy Code of 2016 provides an elaborated procedure for resolving any Insolvency and Bankruptcy matter. This code had introduced a speedy and quick resolution process for solving all the insolvency related issued in a well established manner. The cost for initiating Insolvency Resolution Process is also clearly mentioned u/s 5(3) of the code. It ensures

³Rajendra Kumar commentary on Insolvency and Bankruptcy Code, 2019 Edition, Whytes& Co.

that no extra cost is charged and takes every possible step bar corruption to come in the way of resolving a matter initiated before it. The code provides similar insolvency resolution for both companies and individuals. The steps are as follows:

1. **Commencement of the Resolution Process:-**Section 7,9, and 10 prescribes initiation of a complaint. Whenever any fault occurs the debtor or the creditor may approach to the National Companies law Tribunal or Debt Recovery tribunal. Once the application is approved there, the matter needs to be resolved within 180 days, which may be extended by maximum 90 days on request. During the preceding the debtor enjoys immunity for creditors' claims and lawsuit. Thus by stating the number of days in which the defect is to be settled helps in ensuring speedy resolution of the defect. An Interim Resolution Professional is also appointed at this stage.

2. **Appointment of Interim Insolvency Professional:-** Once the matter is initiated a Insolvency professional will be appointed by the creditors or the tribunal for processing the resolution process a way forward. The Insolvency professional analyzes the Final accounts of the company, helps in making arrangement or liquidating the assets, tries every possible way to bring out a settlement between the debtor and the creditors and have various other functions. Insolvency Professionals main tasks are, to(a) control the debtors assets, (b) collect information of debtor from the information utilities, (c) constitute a creditor committee.

3. **Committee of Creditors (CoC):** The CoC consists of financial creditors of corporate debtors. As per Section 18 of the Insolvency and Bankruptcy Code, it is the duty of IRP (Interim Resolution Professional) to constitute a CoC based on the affirmation received against the Corporate Debtor. A committee will be constituted containing of the creditors who may be secured (backed by some guarantee) or unsecured (not backed by any guarantee). The creditors committee will look after the debtor's property and appoint an Insolvency Professional as mentioned above. All the decisions by the creditors committee will be taken by a majority of 66%. This majority was earlier 75% which now is reduced.

4. **Resolution:-** The creditors committee will decide whether (a) to restructure debtors debt by a proper resolution plan, (b) to liquidate the debtors property. And it is only after such report of the Creditor Committee that the further resolution process takes place. This resolution plan need to be approved by the Creditors Committee, and such approval must be based on the criterion

which will ensure that operational creditors have received as many as they would have received as many as they would have received in the liquidation.

6. **Liquidation**:-If the resolution made by the CoC decides that the debtors property is to be liquidated and gets approved then the process of Liquidation will come into play. The debtor's assets will be sold and the money will be used in paying the outstanding dues. The secured creditors may choose to enforce their securities under any other laws pertaining. The procedure in which the liquidated amount will be paid is specifically prescribed in the code.

8) **INSTITUTIONAL FRAMEWORK**

“The foundation of this code is based on 5 pillars: Adjudicating officers, Insolvency and bankruptcy board, Information Utilities, Insolvency Professionals, and Insolvency Professional Agencies.”⁴

Adjudicating Authorities:-The adjudicating authority includes National Companies Law Tribunal (NCLT), the Debt Recovery Tribunal (DRT) and National Companies Law Appellate Tribunal (NCLAT). Any Individual, organization, Company, Limited liability Partnership, Partnership firm, etc. can file a complaint at DRT or NCLT. Any person can file an application at the NCLT and if not satisfied by its decision can further apply at NCLAT i.e National Companies Law Appellate Tribunal within 30 days. The main objective of the code is to keep all the three adjudicatory authority within the framework of law. As per the precedents the Adjudicating Authorities must provide a right of hearing to the Corporate Debtor as well, on the basis of the principles of Natural Justice. They must issue notice to the corporate debtor, hear them, and then adjudicate the same. The code (u/s 4,6& 7) also provides for withdrawal of complaint due to mutual settlement before its initiation.

Insolvency and Bankruptcy Board of India:-It is the regulatory board under IBC this board was established by government of India on 1st of October 2016. It regulates the 3 pillars i.e. Insolvency Professionals, Insolvency Professional Agencies, Information Utilities, by making rules and regulations for them. It also registers IPA, IP, and IU. The board performs the function

⁴www.ibibi.gov.in

of collecting and making records relating to insolvency and bankruptcy. It also aims at promoting transparency. The new code helps the board in speeding its decision. It also handles the cases using adjudicating authorities mentioned above.

Insolvency Professional Agencies:-It's a not for profit company which enroll, educate, monitor, regulate and guide the insolvency professionals. Currently there are 3 IPA's registered with IBBI:Indian Institute of Insolvency Professionals of ICAI, ICSI Institute of Insolvency Professionals, Insolvency Professional Agency of Institute of Cost Accountants of India. This agency performs various functions such as monitoring IP's, educate, safeguards the rights, train, lays standards, provides redressal mechanism.

Insolvency Professionals:- A person who has passed the limited insolvency examination and has a experience of 10 years as a chartered accountant, company secretary, advocate or any other graduate and must have at least 15 years of management experience is eligible to become a Insolvency Professional. He is the one who can deal with both corporate and individuals. The insolvency professionals are subjected or answerable to the Insolvency and Bankruptcy Board of India.

Information Utilities:- Information utilities are professional organizations registered with Insolvency and Bankruptcy board u/s 210 of the Insolvency and Bankruptcy Code, they collect high grade and verified details about the debt and provides such information to the creditors for formation of a resolution plan.It can be said as a central source of information regarding individual or organizations economic capacity.

9) **ISSUES**

1. Removal of some old laws is yet another challenge after the enactment of IBC. The Acts such as The Presidency Town Act which had certain provisions relating to insolvency needs to be dispensed off.
2. The difference made between Operational and Financial creditors is not based on intelligible differentia, and therefore liable to be slashed down, thus there is a challenge of bias in the code. Furthermore the operational creditors votes in the creditors committee who are not willing,are forced.

3. Quick and Fast resolution with wealth maximization was the main objective of the Insolvency and Bankruptcy Code, but as we can see in the landmark Essar Steel case that neither of them seems to be achieved in reality.
4. There are 27 NCLT benches in India which handles around 16000 cases in total. The biggest challenge is the huge amount of litigation and thus there is a need to increase the bench capacity by developing the infrastructures of the Tribunals.
5. The code provides for insolvency and bankruptcy fund; however no proper guidelines have been given for the use of such funds. It discusses everything related to the fund like the source of funds, power of central government in rule making, but it fails to talk about how these funds are to be appropriated.
6. The code provides power to non-judicial authorities, i.e to the Insolvency Professionals which is violating the basic aspect of dispensation of Justice and access to justice.
7. The process of initiation of corporate insolvency resolution process does not provide adequate opportunities to corporate debtors.
8. The priorities of distribution of debtors liquidated assets are unclear like secured creditors who will get complete amount rather than equilateral security value.
9. The code provides for presence of multiple information utilities, such presence may scatter the information gathered.

Even after these many issues the government had amended the code three times till 2019 and had passed another amendment bill in March 2020, by doing so the government is trying its best to remove the loopholes; suppress the mischief and advancing the remedies. Thus on a brighter side we can see a more viable and fluent insolvency process in the coming time.

10) IMPACT OF INSOLVENCY AND BANKRUPTCY CODE IN INDIAN ECONOMY:-

The Insolvency and Bankruptcy code is proved to be one of the biggest accomplishmentsof the current Government. It had anextensive and momentous impact on the Indian Economy. The speed in which the Government had acted and brought the reform is unprecedented and commendable, as it generally takes time in country like India to take such bold steps. This code

had changed the loan recovery landscape in the country. It is also the key reason due to which India jumped in the ease of doing business index ranking.

Before the introduction of this code the debt recovering or the insolvency time in India was 4.3 years and the cost of recovering was 9% of the total assets of the Debtor. Both of these data/stats has changed after the introduction of this code. This code has helped in resolving 88 corporate loan defaults cases involving around 2.09 lakh crorenon performing assets. Various big cases like Bhushan Steel, Alok Industries, Essar Steel, have been solved; and all this had happened with the same adjudicating infrastructure without any addition.

This code will change the imparting of money i.e. lending and financing culture and bring some positive impact in the economy, and will help in addressing the non-performing assets problem. Earlier loan recovery legislations like Sick industries act, Securitization and Reconstruction of Financial Assets Act (SARFAESI act) have been replaced. RBI has also played significant role in ensuring large number of cases are resolved through IBC. This code is continuously evolving, which is one of the most important benefits of it. An effective insolvency procedure was important for economic development and wealth creation and ensuring financial stability. It may also help in enhancing and attracting the global investment in the great Indian Economy.

As every coin has two sides, this code also has certain drawback. The loss making companies under the IBC are continuing their business and thus are further loosing lenders money. The rich promoters are yet continuing living a luxurious life but the creditors are dying of worries. The rising Non Profit Assets are raising the amount of debts, but this code had overcome it by setting up a time framework. Another issue is the lack of infrastructure in the field of Adjudicating Authority. There are already around 16000 cases pending, and the number of benches is just 27 and thus there is an immediate needs that the adjudicating infrastructure for making the procedure fast and economically viable.

11) **DIFFERENCE IN BETWEEN THE COMPANY LAW AND IBC**

Earlier the winding up was only done by the old companies law of 1956 and 2013, u/s 230-231 and 271-365. But now the winding up of a company is done u/s 33-54 and sec 59 of the

Insolvency and Bankruptcy Code. The old companies law provided for 3 modes of winding up a company:- 1. Compulsory winding up i.e winding up by court, 2.Voluntary winding up,3.Winding up subject to supervision of court. But now IBC have introduced Compulsory Insolvency Resolution Process, which removes the mode of insolvency prescribed under the old company's law.

The major and the best change that have been brought in IBC is the Time prescription. The companies law did not provided any specific time for the procedure of insolvency but the IBC has focused on such time. IBC now provides specific time within which a step of insolvency must be taken. Thus it can be said that this code of insolvency is far a step ahead from the insolvency procedure given under the old Companies Law.

12) ANALYSIS

- A) The best advantage of this code is its time lines. The code provides timeline for everything like the decision for rejection and admission has to be taken by the NCLT within 15 days of application. This time limitation makes the procedure more economical and fast.
- B) Concept of operational and financial creditors is yet a bit controversial in my view. This concept is not based on intelligible differentia. Therefore it is liable to be struck down. Various questions in this regards have been raised in the SC as well.
- C) Application for hearing under this code had to be made to the respective adjudicating authority. No action can rise without an application to the NCLT or DRT.
- D) Provision of Mutual Settlement is also provided under this code. Rule 8 of the code deals with it, an application can be withdrawn before it is admitted, but there is no provision for withdrawal of application once it is admitted.
- E) The code had also provided in for a new procedure for winding up, this procedure is different from the procedure provided in the Companies Act.
- F) Repugnancy of state laws, it means that there is an inconsistency between state law and the central law.
- G) Constitutionality of various provision s of this code had been challenged on various grounds like initiation, liquidation etc.

CONCLUSION

This code is said to be one of the biggest accomplishment of current Government in the field of economics. The code is a huge step toward the ease of doing business in India and has the potential of solving chronic issues relating to insolvency and bankruptcy of corporate and individuals. It provides resolution of these problems in a time bound manner. It not only divides the authority and jurisdiction of NCLT and DRT between individuals and companies thereby ensuring speedy disposal of cases with a list of cases with priorities which shall be given preference for settlement of such debt at the time of liquidation of assets of the company.

Like every coin have two sides, even the bankruptcy and the insolvency have some advantages and disadvantages, as we looked at the advantages, we now must look at the disadvantages as well. The code had failed to differentiate or clarify on the matter of Operational and Financial Creditors. This code had neither provided a proper sequence of distribution of the liquidated amount. The code provides for multiple utilities, which may disguise the main information, and may lead to difficulty in framing resolution plan, Furthermore there is a lack of infrastructure in the Adjudicating Authority, there is an urgent need to enhance this problem as quickly as possible.

The code accepts that the business and individuals may fail in repaying their debts and allows them to make a new start. While facilitating failed firms to wind up endlessly and bankrupt individuals to come out of their debt trap, the code can pave the way to resurrection also.

It makes the insolvency procedure fast and economical. This code provides six important pillars (Adjudicating Authorities, Insolvency and Bankruptcy Board of India, Information Utilities, Insolvency Professional Agencies, Insolvency Professionals) that will help in solving the insolvency problems in India. The code has prescribed a proper sequential process (from initiation to liquidation) for liquidation of a firm in India.

So, we can conclude that even if this code have some issues, but yet it is the biggest economic reform till date for resolution of insolvency and bankruptcy problems in India.