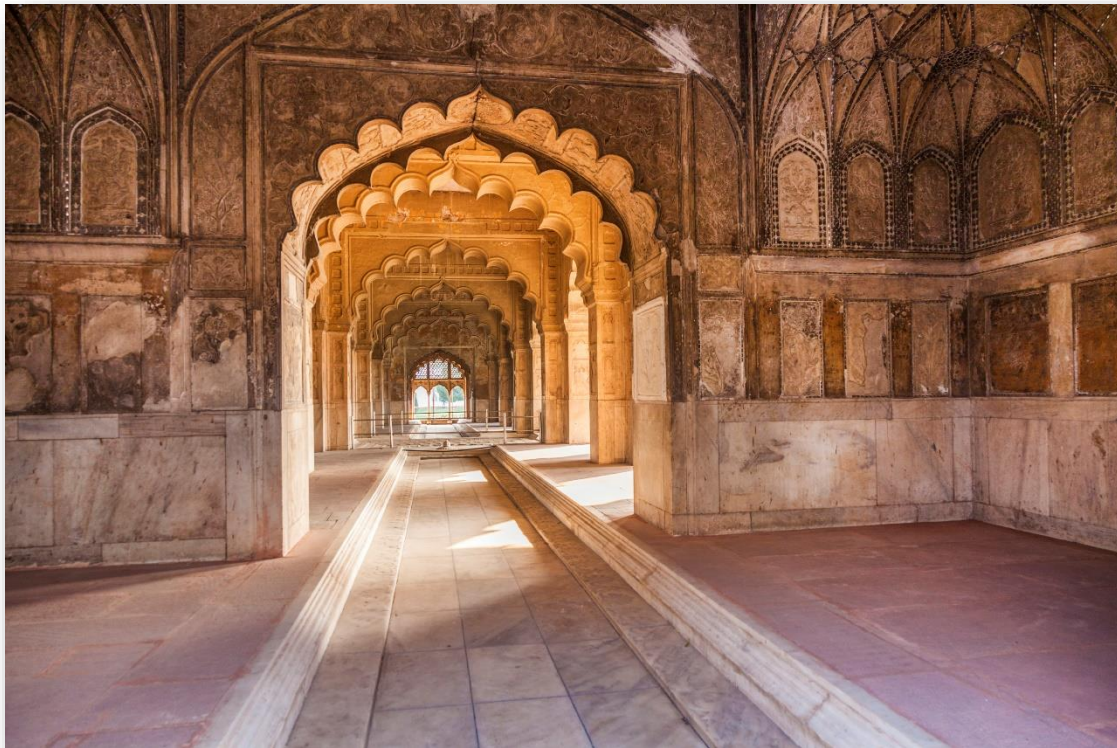




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Bankruptcy, Insolvency & Rehabilitation Proceedings in India

ILN RESTRUCTURING & INSOLVENCY GROUP



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KEY FACTS OF BANKRUPTCY, INSOLVENCY & REHABILITATION PROCEEDINGS UNDER INDIAN LAW

The Code:

Introduction of a comprehensive insolvency and bankruptcy law in India is a recent event, with introduction of the Insolvency and Bankruptcy Code, 2016 (“**the Code**”) in the year 2016. The Code is oriented to be the umbrella legislation in India for laws relating to insolvency and bankruptcy. At present the Code only governs rehabilitation and liquidation of companies and extends to guarantors. However, its scope would eventually include individuals and others forms of legal entities as well.

The Code is administered through the newly formed National Company Law Tribunals (“**NCLT**”) across India, with an appellate tribunal based in New Delhi, and the Supreme Court of India having the final jurisdiction.

The Code seeks to introduce many fresh legal concepts as also modify the pre-existing ones. Upon admission of a case against a company under the Code, it prescribes for a mandatory Corporate Insolvency Resolution Process (“**CIRP**”) for such company (corporate debtor) within which period all efforts are to be made to revive/rehabilitate the corporate debtor. If the revival efforts fail, the corporate debtor can be put into liquidation, where the available assets are distributed against liability claims, as per the priority specified by the Code, with payments being effected to the Insolvency Resolution Professional (“**IRP**”), the secured and unsecured creditors, workmen, Government, shareholders, etc.

The CIRP can be commenced by the NCLT, upon admission by it of any application presented by any applicant (financial or operational creditor) or the corporate debtor itself with evidence of default by the corporate debtor in relation to a debt of INR 10,000,000 (USD 132,000) or above. In addition:

- if an operational creditor approaches the NCLT – it must have already served a 10-day demand notice onto the corporate debtor and the corporate debtor must have failed to either pay the amount or to disclose a pre-existing bona-fide dispute; or
- if a corporate debtor itself approaches the NCLT – its shareholders must have passed a resolution in such regard with 75% majority.

THE CIRP AND LIQUIDATION

Once the NCLT is satisfied that a financial default has been committed by the corporate debtor, it directs commencement therewith of the CIRP, i.e., a 180 days’ resolution window for revival of the corporate debtor while confirming appointment of an IRP. Within this 180 days’ window (extendable by 90 days), the creditors may either with 66% majority decide to revive the company, as per the resolution plan to be subsequently approved by the NCLT or decide to liquidate the corporate debtor. Failure of the creditors to take a decision also leads to liquidation of the corporate debtor.

With commencement of the CIRP, the powers of management of affairs of the corporate debtor moves to the hands of the IRP, who reports to the committee of creditors, and is also entitled to take all steps to ensure that the business of the corporate debtor continues as a going concern. The Code also contains provisions governing penalties and punishments for extortionate and improper transactions, both prior to and during the insolvency process and proceedings.

In the process of liquidation, the timelines would depend upon facts and circumstances of each case such as complexity in sale of assets of the company, finalization of liabilities and any disputes related to rejection of any party’s claims by the liquidator, any pending legal



proceedings, tax disputes, appeals, realization of receivables, etc.

PROTECTION GRANTED TO THE DEBTOR:

The foremost protection that the Code accords to the corporate debtors is the “moratorium” which commences with commencement of the CIRP. The NCLT, while admitting an application of a creditor against a company or an application by the company itself, declares “moratorium.”

The “moratorium” continues through the CIRP and puts an embargo on institution or continuation of suits including execution of any judgment, decree, or order of any court of law, arbitration panel or any other authority. In addition to this, the moratorium also restricts the transfer, alienation, or disposal of any assets or legal right or beneficial interest of the corporate debtor. Also, no action can be taken during the moratorium period to foreclose, recover or enforce any security interest created by the corporate debtor.

The moratorium seeks to provide an atmosphere for revival of the corporate debtor.

The protection under moratorium is granted only qua the property, rights, and obligations of the corporate debtor. Irrespective of the moratorium, fresh criminal prosecutions can be lodged, and those lodged earlier can continue, against the corporate debtor as also against its directors/promoters, etc., for any criminal offences.

The benefit of moratorium under the Code is also not available to the guarantors and sureties of the corporate debtor. After the initial conflicts in interpretation, and subsequent observations by the Supreme Court of India, the Code was amended in June 2018 to clarify that no moratorium would apply to the legal actions of recovery against the surety and guarantors of a corporate debtor.

Moratorium also does not apply to the writs as also on the constitutional powers of the Supreme Court and the High Courts. The IRP is expected to appear in, and contest in the best interest of the corporate debtor, all matters which do not fall under moratorium, as also to ensure compliance with all the applicable laws during the CIRP period.

End to Suspension Period Imposed by the Indian Government due to the Coronavirus:

The COVID – 19 pandemic had a severe impact on the various industries and different economies around the world. In 2020, the Indian Government after rounds of discussion and deliberations, assessed the adversity that may be caused due to the Coronavirus on Indian economy. Thereafter the Indian Government considered and imposed a suspension on the IBC proceedings to curtail the devastating impact of the Coronavirus and increased the threshold limit of a default to drag a defaulting company to the insolvency tribunal to INR 10 million, from the earlier threshold of INR 0.1 million.

The aforesaid suspension for initiation of IBC cases finally came to an end on March 24, 2021, vide an Ordinance dated April 24, 2021, but the increased threshold is unlikely to be reduced to the original limits.

Pre-Packaged Insolvency Resolution Process (PPIRCP):

The Insolvency and Bankruptcy (Amendment) Ordinance, 2021 has introduced a new concept of PPRICP. PPRICP is a framework provided for resolution of stress of corporate MSMEs (as covered under MSME Act, 2006). Unlike Corporate Insolvency Resolution Process, PPRICP is available to defaults where the default is at least INR 1 million arising between March 25, 2020, to March 24, 2021.

The PRICP is a hybrid process, where pre-initiation phase is largely informal and post-initiation stage is formal. The informality at pre-



initiation stage offers flexibility for the corporate debtors and its creditors to swiftly explore and negotiate the best possible outcome to resolve stress in the business, while the post-initiation is focused on maximization of value and bestows the resolution plan with the statutory protection.

Conclusion: The Code has arguably tilted the debtor-creditor balance in favour of the creditor, as one of the consequences of admission of proceedings under the Code is that the erstwhile management of the company is ousted, even if the company is rehabilitated. In cases of small and medium enterprises, the promoters can still lay reclaim the ownership and control of their company, provided they are not declared willful defaulters by the financial institution(s). The pre-packaged insolvency may provide the much-needed respite to the genuine promoters.

Within a short span since its implementation, and despite Coronavirus given business adversities, the Code is proving to be a more effective tool for rehabilitation and liquidation as compared to the winding up provisions of the (Indian) Companies Act and the Sick Industrial Companies Act, 1985, it repealed and replaced.