

Penny for a Thought? The IBC Perspective of Personal Guarantor Insolvency
written by Siddartha Karnani | December 21, 2019



Hell hath no
fury like the targeted Personal Guarantors; with the 15th November
2019 notification^[1] that
was brought into force on 1st December 2019 by the Central
Government of India under the Insolvency and Bankruptcy Code 2016 (“IBC”).
With the effectuation of this notification, personal guarantors will be
forced
to face the wrath and impending doom if their companies are unable to repay
their debts. This means lenders can drag these guarantors to the tribunals
alongside their companies if the companies are incapable of paying their
debts.
The new rules and regulations have proved to be a boon for creditors as now
they can saunter their way not only against the principal borrower i.e. the
company but also the personal guarantor before the National Company Law
Tribunals (“NCLT”).
The litigation
maze of the “Essar Steel Case” and the initiated changes under the
IBC has supposedly sought itself, to no derailing by bringing a ginormous
sigh
of relief to banks in specificity. The resolution process will now back
secured
lenders and ensure big returns in their favor. This case has been capering
its
way through the High Court, NCLT, National Company Law Appellate Tribunal
(“NCLAT”)
and the Supreme Court of India. Procedurally and holistically, the recovery
process is going to be a blessing in disguise for lenders. One of the main
reasons for the change being that the IBC allows 180 days for insolvency
proceedings inclusive of just one 90day extension but the concerned case has
already crossed 600 days.
Penny Wise
Pound Foolish
Analyzing the status
of a guarantor under the ambit of the IBC, one standpoint of understanding
can be

whether the creditor owns the power to sell the assets of the personal guarantor during the insolvency regimen. The Bombay High Court in a landmark judgment[2]

analyzed the base rooting of Section 14 of the IBC and cratered the factual base of the benefit of moratorium

not being available to the personal guarantors of the corporate vultures (debtors). The NCLAT also opined on akin lines in another such case.[3]

The crux of these judgments boiled down to the fact that personal guarantors' assets can be disposed of to assuage a debt.

Another point of consideration would be as to which

jurisdictional house gets to determine the liability of a personal guarantor? The NCLT or the DRT? It has come to be that the NCLT has an upper hand and the

same has been reiterated in a writ petition decided by the Allahabad High Court.[4] The scarring consequence of this would loop

the personal guarantor alongside the borrower, thereby, helping the spiteful creditor to take lead and secure his debt spontaneously. Section 60(2) of the IBC runs in the negative for a creditor but stands in equilibria to institutionalize a corporate insolvency process against a personal guarantor. Insolvency proceedings against personal guarantors can be initiated on a meagre

amount of default of Rs.1000 in terms of the guarantee.

The Chronicles of the phased maze: Supreme Court on the Essar Steel Case

The Essar Steel's promoter, Prashant Ruia was put to chase for the failure towards the personal guarantee for payment on the loan he had given for Essar. Now, Essar, having failed on their part to pay off the debts,

had the banks get after Ruia. The resolution plan made Ruia's right of subrogation ineffective; to an extent such that banks had drawn utter dismay from NCLAT's ruling.

The 'Right of Subrogation' takes its base understanding as rooted in the Contract Act 1872 which allows a guarantor to make the move happen by stepping into the shoes of the lenders. This levy is because it allows the guarantor to be able to recover the amount, he paid towards the debt

clearance. This, in clear terms, meant that the NCLAT's ruling had Ruia covered

under the safe haven of negative consequential bearings.

However, the recent purview of the Supreme Court in the Essar

case in totality was a banter that allowed these very lenders to get after the

personal guarantors. The new charter allows us to carry on the recovery process

with the creditors even on the closure of the Corporate Insolvency Resolution Process

("CIRP").

Concluding in the parallel universe

Where the new rules have protracted the scope of the IBC, it is opined that there would be a need to ensure certain amendments, with at least bringing some favour for personal guarantors. Experts feel that creditors will be able

to extract a huge sum of money from these guarantors in a short span of time. As a matter of fact, till now IBC was limited to working around corporate insolvency and corporate vultures. Where the new amendments hold in favour for creditors it would be rather appalling for the guarantors. Further, bearings will be observed in due course of time. Though we see that the new amendments have forced their way through, banks are now not living on the edge and technically have juxtaposed the company and the personal guarantor of their fate and fault. These new changes have fermented long doings and buried the fears of no speedy and effectual resolutions to the matters which were/are tainted by loan defaults, completely guarded by personal guarantors. Looking at the possible obstructions, the government is indeed going to have to take lead in terms of the teething issues that crop up in the resolution process. All in all, banks (lenders) have found themselves in a safe situation with a futuristic bearing.

- [1] <https://ibbi.gov.in/uploads/legalframework/1fb8c2b785f35a5126c58a2e567be921.pdf>
- [2] *Alpha & Omega Diagnostics (India) Ltd. v. Asset Reconstruction Company of India Ltd. & Ors.*; (AT) (Insol.) No. 116 of 2017
- [3] *Schweitzer Systemtek India Pvt. Ltd. v. Phoenix ARC Pvt. Ltd. & Ors*; Company Appeal (AT) (Insolvency) No. 129 of 2017.
- [4] *Sanjeev Shriya v. State Bank of India*; Writ - C No. - 30285 of 2017
Contributed By - Siddartha Karnani
Designation - Partner
King Stubb & Kasiva,
Advocates & Attorneys
[Click Here to Get in Touch](#)
[New Delhi](#) | [Mumbai](#) | [Bangalore](#) | [Chennai](#) | [Hyderabad](#) | [Kochi](#)
Tel: [+91 11 41032969](tel:+911141032969) | Email: info@ksandk.com