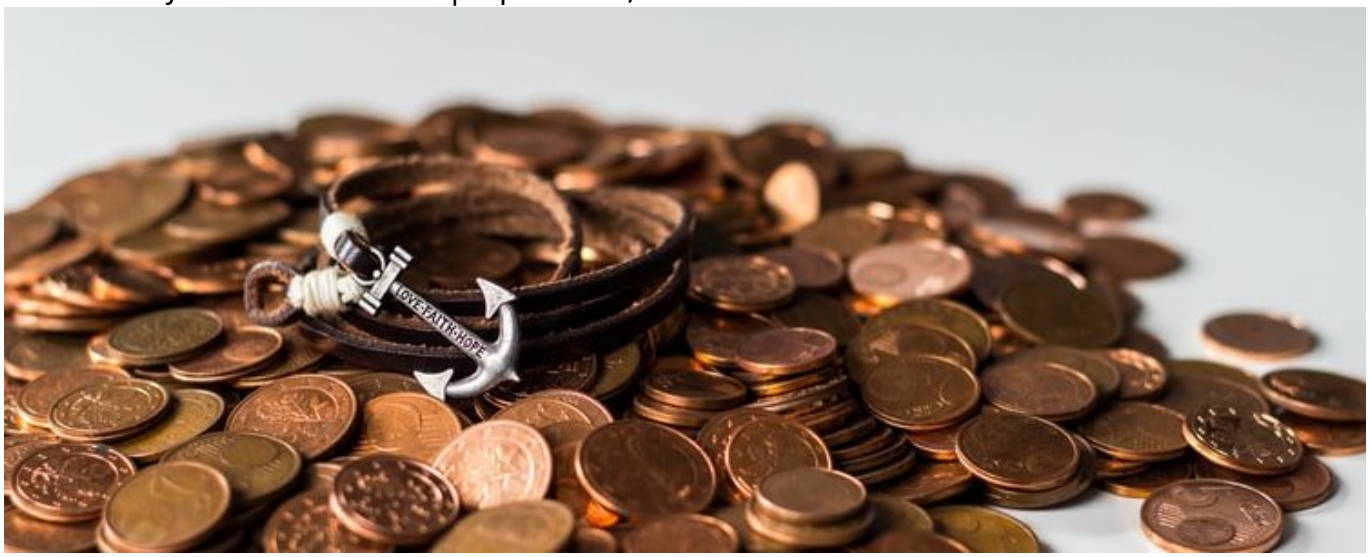
"A Rip Roaring Spectacular Journey of IBC"
written by Simran Tandon | April 20, 2020



The Tenor Astounding IBC Amendment Act 2020

Notification Raising the Threshold Limit for Triggering the Insolvency

In a time as tough as today, when the whole world is under the impact of Covid-19 which has forced the country to be under lockdown, the notification dated March 24, 2020,[1] wherein the Ministry of Finance announced several important relief measures on the statutory and regulatory compliance matters related to several sectors has provided a sigh of relief to everyone. The government by exercising its powers under Section 4 of the Insolvency and Bankruptcy Code, 2016 ("Code"), has raised the threshold limit triggering the insolvency from rupees one lakh y hundred times to rupees one crore as the minimum amount of default.

It is pertinent to note here that the Central Government has raised the minimum default threshold to its maximum capacity as rupees one crore is the maximum threshold that the Central Government can prescribe under Section 4. This is a big step for the benefit of the MSME sector companies struggling due to the lockdown.

Insolvency and Bankruptcy Code (Amendment) Act, 2020

"The said amendments are in sync with the time and also adhere to a Supreme Court order in letter and spirit." This was replied by the Finance Minister, Nirmala Sitharaman in a debate carried on a bill before the house of the Parliament. The bill was passed by Lok Sabha on March 6, 2020, and by Rajya Sabha on March 12, 2020. It received the Presidential assent and was published in the Official Gazette on March 13, 2020.[2]

The Insolvency and Bankruptcy Code (Amendment) Act, 2020 ("Act") seeks to remove bottlenecks and streamline the corporate insolvency resolution process.

Highlights of the Amendment Act of 2020 and its analysis

- Insolvency commencement date
  - The Act deletes the proviso to Section 5(12) of the Code and brought in a change that the insolvency commencement date is the date of admission of an application for initiating the Corporate Insolvency Resolution Process (CIRP). Presently under the Code, the insolvency resolution process used to commence when the Insolvency Resolution Professional (IRP) was appointed by the adjudicating authority.
  - This also brought in a change to Section 16(1) of the Code which mandates the

adjudicating authority to appoint the IRP on the insolvency commencement date which at present was within 14 days from the insolvency commencement date. Thus, this has removed the earlier gap of 14 days between the date of initiation of CIRP and the appointment of IRP, and now the CIRP will only be initiated on the appointment of IRP. This reduces the uncertainty which used to prevail earlier as the stressed companies had the time of 14 days to go under in a delicate situation.

- The threshold for initiating the resolution process by Financial Creditor
  - The Act has raised the minimum threshold for certain classes of financial creditors for initiating CIRP by adding an additional requirement that an application under Section 7 (1) of the Code should be filed jointly by not less than 100 of such creditors in the same class or not less than 10% of the total number of such creditors in the same class whichever is less. These classes include real estate allottees and security or deposit holders represented by a trustee or an agent.
  - The Act also added a proviso that clarifies that where an application for initiating the CIRP against the corporate debtor has been filed but not admitted by the adjudicating authority before the commencement of the Act, such an application shall be modified to comply with the abovementioned requirements within 30 days of the commencement of the Act failing which it shall be deemed to be withdrawn before its admission.

    The Act raises the question of whether is it a reasonable classification or not of increasing the threshold for certain creditors for initiating the insolvency proceedings, particularly for the homebuyers. With this wherein, one of the financial creditors can initiate the insolvency proceedings easily but the homebuyers who have been accorded the status of the financial creditors by the Second Amendment Act, 2018 are left with no liberty to initiate the proceedings if they are not complying with the requirement as laid down in the Act.

    Although the legislature has tried to bring this provision in order to minimize or avoid the frivolous complaints it does not deal with the practical problem of the homebuyers as they are not aware of how many units have been sold and to whom in order to determine the 10% of the total number of the units or who other 99 buyers are in order to initiate the insolvency proceedings.
- Corporate debtors entitled to make an application
  - An explanation to Section 11 of the Code has been inserted which stipulates that a corporate debtor should not be prevented from filing an application for initiation of the corporate insolvency resolution process against other corporate debtors.

    This will enhance the maximization of the value of a corporate debtor as the Resolution Professional will have the power to recover the outstanding debts of a corporate debtor against whom CIRP is already in progress in order to manage the affairs of the financially stressed companies.
- Licenses and permits are not to be terminated due to Insolvency
  - The explanation to Section 14(1) of the Code has been inserted by the Act which states that a license, permit, registration, quota, concession, clearance, or a similar grant or right will now not be terminated or suspended during the moratorium period. But such a condition will be applicable as long as the debtor does not default in the payment of current dues arising for the use or continuation of such licenses or permits.

Thus, this is a very important change as it enables the Corporate Debtor as a going concern and will also maximize the value of assets.

- The Act inserts Section 2A under Section 14 of the Code which states that the IRP or RP will have to consider the supply of goods and services which are critical to protect and preserve the value of the Corporate Debtor and to manage the operations of such Corporate Debtor as a going concern.
  - The Act amended Section 14(3)(a) of the Code which now protects not only the transactions from moratorium but also agreements or other arrangements notified by the Central Government.
  - The Act also added the new clause (ia) to Section 240 of the Code under which IBBI is empowered to make regulations to provide for circumstances in which the supply of critical goods or services may be terminated, suspended, or interrupted during the period of moratorium under Section 14 (2A) of the Code.

  Thus, the insertion of Section 2A under Section 14 of the Code is also a controversial point as on one hand, it is for the benefit of the continuity of the company undergoing the insolvency proceedings in order to preserve and manage the operations of the corporate debtor as a going concern but on the other hand, there is a casualty which will be faced by the MSME sector companies that are now being mandated by law to continue the supply of critical and essential goods and services to the companies undergoing the insolvency proceedings.

  With this amendment, the risk of the MSMEs becoming sick has increased as major cash-flow problems faced by MSMEs are due to the delayed payments made by the big companies only. Also, it interferes with the contractual relationships between the suppliers i.e., the MSME and the corporate debtors and it is not made clear whether any additional contract has to be signed during the moratorium period between IRP or RP, the corporate debtor & the company.
- Management of Operations of the Corporate Debtor
  - The proviso under Section 23 (1) of the Code is substituted which states that RP shall continue to manage the operations of the corporate debtor after the expiry of the CIRP period until an order of the resolution plan under Section 31(1) or appointing a liquidator under Section 34 is passed by the adjudicating authority.

  This will help the RP to function properly and not seek directions by filing an application to run the management of the company.
- Liabilities for Prior Offences
  - The Act inserted Section 32 A in the Code which provides a safeguard for the successful bidders of insolvent companies from the risk of criminal proceedings for offenses committed by the previous promoters of the corporate debtors. This also protects the prospective resolution applicant’s property from the threat of the criminal proceedings.
  - Further, the Act provides a shield to the company from attachment, seizure, retention, or confiscation of their property in relation to such offenses.

  Thus, now the prospective resolution applicant or the new promoter will be safeguarded from the legal complications in which the past promoters are embroiled and now the new prospective bidder will not be burdened with the legacy issues faced by the past promoters. However, this provision will be applicable only when the new promoter was nowhere in the management or control of the corporate debtor or was not a related party of such a person.

Thus, this will encourage the new promoters to come forward to revive the companies which are into insolvency proceedings to save them from being liquidated.

- Positive Impact of IBC so far:
  - The 2018-2019 report of RBI on the trend and progress of banking in India tells that the gross NPA of all the Schedule Commercial Banks has come down to 11.2% to 9.1% and IBC has played an important role in this.
  - Also, to judge the efficacy of the Code, it is important to see not only the figures of how many cases have been resolved through this law but also the number of cases that are settled between the creditors and the debtors even without bringing the case to the tribunal as the law has made people aware of the implications which will be faced by them if their case is brought to the tribunal.
- Limitations of the IBC:
  - The insolvency and bankruptcy law has resulted in the recovery of just 10% of defaulted loans in the case of companies other than the seven big cases referred for resolution.
  - Of the 970 cases referred to IBC, 780 have been liquidated, indicating a mortality rate of 80%.
  - Experts opine that only 43% of the loans have been recovered, implying that banks took a haircut of 57% on their loans.

Conclusion

Code, being the transformational piece of legislation has undergone 4 amendments in a short span of 4 years but it can be seen as the responsiveness of the government in order to balance out the business with the economics and make the Code efficacious in the line of ease of doing business in India and making the objective of the Code to improve the recovery rate. We have come a long way but the recovery rate as seen from the ground reality is far less than the expected rate and the government should bring in the changes by increasing the number of benches of NCLT so that the cases can be resolved quickly.

An increase in the threshold limit to file the insolvency against the companies is a good change brought in by the government under the relief package but still, the safeguards are required to be provided to the MSME companies as they are the backbone of the Indian economy and the interest of the homebuyers should also be protected, keeping a balance between the real estate companies and the homebuyers. It furthermore needs scrutiny to iron out the shortcomings and make the resolution process much more efficient and creditor friendly.

- [1]https://ibbi.gov.in//uploads/legalframwork/48bf32150f5d6b30477b74f652964edc.pdf
- [2]https://ibbi.gov.in//uploads/legalframwork/d36301a7973451881e00492419012542.pdf

Contributed By - Simran Tandon
Designation - Associate
King Stubb & Kasiva,
Advocates & Attorneys
Click Here to Get in Touch
New Delhi | Mumbai | Bangalore | Chennai | Hyderabad | Kochi
Tel: +91 11 41032969 | Email: info@ksandk.com