

PROPOSED AMENDMENTS TO THE INSOLVENCY AND BANKRUPTCY CODE, 2016

1. INTRODUCTION

1.1 Among many reforms aimed at increasing ease of doing business, introduction of the Insolvency and Bankruptcy Code, 2016 (Code) is a bold step. This code consolidates and repeals previous laws on corporate and individual insolvency. Only those provisions of the Code have been enforced which relates to the insolvency and liquidation of corporate debtors or companies. The Code establishes a Board and an Adjudicating Authority to deal with insolvency-related matters and establishes a timeline for doing so.

1.2 This Code allows a creditor (financial or operational) to file an application for insolvency against a corporate debtor. A resolution professional is appointed to oversee the implementation of the provisions of the Code and to take care of claims submitted by various creditors. This ensures that the corporate debtor exists as a going concern and all stakeholders are able to get a certain share of their claims. There is a provision for liquidation of the corporate debtor, however, this is to be used only in case of failure of the insolvency proceedings.

1.3 In three years of its introduction, many issues were raised by various stakeholders. However, most of them were resolved due to the timely intervention of the legislature and the judiciary. The recent amendments to the Code approved by the Union Cabinet and introduced in the Lok Sabha (House of the People) are aimed at encouraging the revitalization of stressed companies and motivating investors to go for the bidding of these companies.

2. SIGNIFICANT AMENDMENTS PROPOSED TO THE ACT

2.1. Power to include last-mile funding under interim finance - The appropriate authority under the Code can now specify what kind of debts are part of interim finance. This empowers Insolvency and Bankruptcy Board of India to specify additional debts which can be included within the scope of interim finance and hence would be included in insolvency resolution process costs. This amendment has been passed to ensure that list mile funding given to a corporate debtor to prevent them from going into insolvency is paid first as per the waterfall mechanism of the IBC. Under the waterfall mechanism, all interim finance has to be paid first before the liabilities of other stakeholders are discharged. Thus, stressed asset companies, nonbanking financial creditors and private investors which seek to provide last mile funding can be at ease as their claim would be paid first in case the company goes into insolvency. However, the appropriate authority must specify such funding to be within the scope of the interim finance.

2.2. A minimum number of applicants required under certain cases - The amendment seeks to specify a minimum number of applicants (for certain class of applicants) required to file an application for initiating corporate insolvency resolution process before the Adjudicating Authority. If allottees of a real estate project are seeking to initiate IBC proceedings against their developer,

then it has to be filed jointly by at least one hundred allottees or not less than ten per cent of allottees (whichever is less) of a particular real estate project. The real estate developers made several representations to the government fearing that even a single allottee can hold an entire project to ransom affecting the rights of other allottees who might want to wait for the competition of the project. One such case was witnessed wherein a major real estate company faced insolvency proceedings due to the application filed by a single allottee. The amendment seeks to prevent such misuse of the provisions of the Code.

- 2.3. Corporate debtor allowed to initiate proceedings against other corporate debtors - A corporate debtor can initiate proceedings under the Code against other corporate debtors, provided other party is not undergoing or has completed corporate insolvency resolution process. This provision merely seeks to clarify what was already there in the code. As debt funding and operational credit is common in corporate financing, discharge of debt by one company is dependent on the settlement of debt by other companies. Thus, this amendment seeks to ensure that the remedy under the Code is available to maximum stakeholders.
- 2.4. Licenses, permissions and other governmental permissions to continue - All governmental permissions including but not restricted to license, permit and registration of the corporate debtor can't be suspended or terminated merely on the grounds of proceedings under the Code. However, the resolution professional managing the corporate debtor during the moratorium period must ensure that there are no dues for the continuation

of use of governmental permissions during the moratorium period. All governmental fees related to licenses and governmental permissions must be paid during the moratorium period.

- 2.5. Supply of vital goods and services cannot be terminated - All goods or services which are essential to ensure that the corporate debtor continues as a going concern shall not be discontinued during the moratorium period. However, there is an obligation on part of the corporate debtor to pay dues arising from the supply of such goods or services during the moratorium period. The appropriate authority can also specify other circumstances under which the supply of such goods or services can be terminated.
- 2.6. Extension of tenure of corporate resolution professionals - The amendment also seek to extend the tenure of insolvency resolution professionals to ensure that he is involved from the start of the corporate resolution insolvency process. It is mandatory to appoint a resolution professional on the date on which the proceedings under the Code are initiated. They shall continue to exercise authority even after the expiry of the period of the moratorium period until an order is passed by the Adjudicating Authority approving the resolution plan.
- 2.7. Cessation of proceedings against corporate debtors with respect to previous offences - The most significant amendment is the cessation of liability of the corporate debtor for offences committed prior to the commencement of the corporate proceedings. It is only applicable to those corporate debtors whose management or control has undergone

change due to the proceedings under the Code. However, previous management would continue to face action under the appropriate laws for offences committed by the corporate debtor prior to the initiation of the proceedings under the Code. The amendment also extends to the property of the corporate debtor which are placed under the resolution plan by the Adjudicating Authority. Thus, there can be no seizure or attachment of such property by any authority in respect of the offences committed by the corporate debtor prior to the initiation of the proceedings. With a spike in cases where properties of companies undergoing corporate insolvency resolution process were being attached by Enforcement Directorate and Income Tax Authorities, there was a fear that new management might have to suffer because of the offences committed by previous management or promoters. This could have defeated the whole objective of the Code as it seeks to give a fresh slate to companies facing bankruptcy due to the actions of promoters and previous management.

3. IMPACT ANALYSIS

3.1 The object and purpose of IBC are to provide for a timebound resolution of stressed companies while ensuring that maximum value is derived for stakeholders. Time and again, the government have stressed that the IBC was enacted to prevent companies from getting shut down instead of sending them to insolvency or liquidation. The extension of the definition of interim finance allows the appropriate authority to include last-mile financing within its scope. However, the question remains what sort of debts should be included. While

last-mile financing can come from various sources including erstwhile promoters, these can cause heartburn among secured creditors who were safe because of the recent judgment in Essar Steel case. If promoters are allowed to get their share first, then creditors put pressure of erstwhile promoters to forego shares. This could easily raise various disputes and further clog the list of existing cases at National Company Law Tribunals. The appropriate authority should be careful while including other debts within the scope of interim finance.

3.2 The IBC was enacted to threaten promoters or management into giving up their positions. Time and again, the judiciary has emphasized that the Code should be used only in exceptional circumstances. These amendments would ensure that a certain number of applicants file an application (especially for real estate projects) before the Adjudicating Authority admits it. The relators can relax now but they must ensure that they are complying with other laws like RERA and Consumer Protection Act, 1986.

3.3 While an investor may be willing to put in financial resources, he needs a guarantee that his investment would be safe and the corporate debtor would continue as a going concern.

3.4 The judiciary had to interfere in certain cases where governmental permissions were withdrawn merely on the grounds of insolvency. The amendments would ensure that all governmental permissions available to the previous management of a corporate debtor are also available to the new one after the implementation of the resolution plan. However, the resolution professional needs to ensure that necessary fees (if any) are paid to

the authorities. This makes the role of insolvency resolution professionals more vital. Therefore, Insolvency and Bankruptcy Board of India needs to ensure that they are acting professionals and not sabotaging the corporate insolvency resolution process at the behest of the previous owners.

4. CONCLUSION

These proposed amendments are in the right direction as it would resolve many issues that were being faced by various stakeholders especially the new management of corporate debtors while trying to revive the stressed company. Although there are some lacunas with these proposed amendments, the intention of the legislature to provide a clean slate to new management must be appreciated. The implementation of the Code shows that new issues can arise anytime and with foreign stressed funds seeking to make a beeline, we should be seeing more companies going into insolvency.

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