

*De Jure*

*June 13, 2016*

**THE INSOLVENCY AND BANKRUPTCY CODE,  
2016- A STEP TOWARDS ACHHE DIN**



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## INTRODUCTION

Indian government's move to enact the Insolvency and Bankruptcy Code, 2016 ("**Code**") will help in streamlining and consolidating all the laws/legislations regulating insolvency to make the process simpler. The Code has now received President's assent on May 28, 2016. It will provide an easy exit option for insolvent and sick firms. The enactment of Code is an innovative plan awaiting correct execution. The Code creates a unified framework for resolving insolvency and bankruptcy matters and is a key element in the government's strategy to rid the financial sector of its bad debt problem.

The Code will enable quick and prompt action to be taken in the early stages of debt default by a firm, maximising the recovery amount and will extend to individuals, companies, limited liability partnerships and partnership firms in a time-bound manner.

## BACKGROUND

The need for an insolvency law in India was first articulated in the three Presidency-towns of Calcutta, Mumbai (then known as Bombay) and Chennai (then known as Madras). The Presidency Towns Insolvency Act of 1909 covering Kolkata, Chennai and Mumbai and the Provincial Insolvency Act, 1920 for the rest of India, were enacted to regulate the insolvency law. The Acts applied to individuals and partnerships but it exempted corporations from its ambit. After the independence, bankruptcy and insolvency were specified in Entry 9 of the Concurrent List of the Seventh Schedule, under Article 246 of the Constitution.

Today, bankruptcy proceedings in India are governed by multiple laws some of which are the Companies Act, 'Sick Industrial Companies (Special Provisions) Act, 1985 ("**SICA**"), the Recovery of Debts due to Banks and Financial Institutions Act, 1993 ("**RDDB Act**") and the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 ("**SARFAESI**"). Also, some of these laws have not yielded good results due to inefficient enforcement and court delays. The functioning of these legislations has not been found to be satisfactory as many issues were identified during its implementation. A key problem of the present environment is the presence of multiple frameworks such as DRT, CDR, etc. The bankruptcy process has become drawn out and involves battling it out through many steps. RBI's Scheme' adds one more layer of complexity into an already complex system.

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The Code is, therefore, a complete compilation of laws and rules pertaining to the subject of bankruptcy law in India. The Code repeals the Presidency Towns Insolvency Act, 1909 and Provincial Insolvency Act, 1920 and further seeks to amend various laws, including the Companies Act, 2013, RDDB Act and SICA, amongst others. The Code introduces a time limit on the bankruptcy process. In the case of a default, the time-limit is 180 days, within which the resolution has to be completed. This can be extended by another 90 days by the adjudicator, depending on the process.

## **HIGHLIGHTS OF THE CODE ARE SUMMARISED BELOW:**

### ➤ **ADJUDICATING AUTHORITIES**

The Code provides for two adjudicating authorities to deal with insolvency viz. The National Company Law Tribunal ("**NCLT**") and the Debt Recovery Tribunal ("**DRT**"). NCLT will adjudicate cases for companies and limited liability partnerships.

### ➤ **THE INSOLVENCY AND BANKRUPTCY BOARD OF INDIA**

The Code provides for the establishment of a body corporate by the name of the Insolvency and Bankruptcy Board of India. The Board shall consist of the members appointed by the Central Government for a term of five years or till they attain the age of sixty five years whichever is earlier. The Board will frame and implement various regulations and guidelines on matters relating to insolvency and bankruptcy as may be required. The Board will exercise regulatory oversight over insolvency professionals, insolvency professional agencies and informational utilities.

The Code ousts the jurisdiction of any civil court to entertain any suit or proceedings in respect of any matter on which NCLT or the National Company Law Appellate Tribunal has jurisdiction under this Code.

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➤ **INSOLVENCY PROFESSIONAL AGENCY ("IPA"):**

Every person (which includes an individual, a Hindu undivided Family, a company, a trust, a partnership, a limited liability partnership, any other entity established under a statute and a resident outside India) can act as an IPA. Such IPA would be required to obtain certificate of registration issued by the Insolvency and Bankruptcy Board of India in accordance with the principles governing registration of IPA. The agencies shall conduct examinations to certify the insolvency professionals and enforce a code of conduct for their performance. Every IPA is required to perform such functions as prescribed in the Code



➤ **INSOLVENCY PROFESSIONALS ("IP")**

The Code creates a specialised team of licensed professionals. Every person to act as IP is required to obtain a membership of an insolvency professional agency. After obtaining the same, every IP is required to register itself with the Board within such time, in such manner and on payment of such fee, as may be specified by regulations. IP will administer the resolution process, manage the assets of the debtor and provide information for creditors to assist them in decision making.

➤ **INFORMATION UTILITIES:**

The Code provides for establishment of information utilities. Their duty is to collect, collate, authenticate and disseminate financial information from listed companies and financial and operational creditors of companies. Insolvency Information Utilities will require registration with the Board.

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➤ **INSOLVENCY REGULATOR**

The Insolvency and Bankruptcy Board of India will be established as a regulator to oversee functioning of IPs, insolvency professional agencies and information utilities. The Board will have 10 members, including representatives from the central government and the Reserve Bank of India.

➤ **BANKRUPTCY AND INSOLVENCY PROCESS FOR COMPANIES AND OTHER LIMITED LIABILITY ENTITIES**

The Insolvency Code provides a speedy process for insolvency resolution and liquidation for companies and other limited liability entities.

➤ **INSOLVENCY RESOLUTION PROCESS**

- This shall be conducted by the resolution professional;
  - It may be initiated by a financial creditor, an operational creditor or by the debtor itself by making an application to the Adjudicating Authority;
  - The entire process will have to be completed within 180 days and may be extended by order for further period of 90 days in certain circumstances;
  - Upon admission of application, the Adjudicating Authority will declare moratorium which prohibiting institution or continuation of any kind of litigation in any court of law, tribunal, arbitration panel or other authority against the corporate debtor;
  - During this process, the management of the debtor and custody of the assets of the corporate debtor will be vested with the resolution professional to ensure protection of the assets of the debtor.
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### How the Liquidation Process Works

#### ➤ Liquidation Process

- This can be initiated against a corporate debtor if the resolution plan has not been approved by the Adjudicating Authority, or it does not receive a resolution plan within the prescribed time period
- The Adjudicating Authority will pass an order for liquidation of the debtor.
- The insolvency resolution professional will act as liquidator for liquidation of the debtor.
- The assets of the corporate debtor, in case of liquidation will be distributed in the order as prescribed by the Code.
- Once the liquidation order is passed, no legal proceedings can be commenced or continued against the debtor

#### ➤ BANKRUPTCY AND INSOLVENCY PROCESS FOR INDIVIDUALS AND PARTNERSHIP FIRMS

##### • Fresh Start Process

This process may be initiated either by a debtor himself or through a resolution professional by making an application to the Adjudicating Authority for a discharge from their 'qualifying debts'. A period of interim –moratorium is to commence upon filing the said application in relation to all debts and the same is to cease to have effect on the date of admission or rejection of such application.

##### • Insolvency Resolution Process:

An insolvency resolution process may be initiated by the creditor or the debtor. The negotiations will take place between the creditors and the debtor to arrive at an agreeable repayment plan for composition of the debts and affairs of the debtor, supervised by a resolution professional. The repayment plan will approval of a three-fourth majority of creditors in value. The repayment plan may authorise or require the resolution professional to: (a) carry on the debtor's business or trade on his behalf or in his name;

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b) realize the assets of the debtor; or (c) administer or dispose of any funds of the debtor. The repayment plan will be implemented in supervision of the insolvency professional.

- **Bankruptcy Process**

This can be initiated only after the failure of the resolution process or non-implementation of repayment plan. The bankruptcy trustee is responsible for administration of the estate of the bankrupt and for distribution of the proceeds on the basis of the priority.

- **INSOLVENCY AND BANKRUPTCY FUND**

The Code creates an Insolvency and Bankruptcy Fund for the purposes of insolvency resolution, liquidation and bankruptcy of persons under the Code. The Fund will receive voluntary contributions from any person. In case of insolvency proceedings being initiated against the contributor, he will be allowed to withdraw his contribution for making payments to workmen, protecting his assets, etc.

➤ **AGREEMENTS WITH FOREIGN COUNTRIES**

The Central Government may enter into an agreement with the Government of any country outside India to enforce the provisions of the Code in relation to the assets or property of corporate debtor or debtor, including personal guarantor of a corporate debtor, situated in a country outside India.

➤ **OFFENCES AND PENALTIES**

The Code provides for the punishment in terms of imprisonment as well as fine for provision of false information by a debtor or a creditor in insolvency resolution process. The Code also provides for punishment for deliberate contravention of the provisions of the Code by an Insolvency Professional. The Code further specifies the punishment for providing false information or concealment by bankrupt.

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## CONCLUSION / OUR VIEWS

The Code is one of the most forward-looking and modern-day legislations in recent times. This Code is a welcome initiative for creditors, investors and debtors alike. The streamlining of procedures, simplification of the insolvency process and fast-tracking of recovery are hallmarks of the Code which is likely to result in a positive effect on India's lending climate.

This will definitely improve India's position in the World Bank's index on the ease of resolving insolvencies and doing business. India's weak insolvency regime was one of the reasons for the state of credit markets in India. The Code promises to bring about far-reaching reforms with focus on a creditor insolvency resolution. The Code aims at early identification of financial failure and maximising the asset value of insolvent firms. In our view, the provisions in the Code to address cross border insolvency through bilateral agreements and reciprocal arrangements with other countries is a good step forward specially in light of big defaulters taking shelter under the loopholes. The Code should significantly improve debt recovery rates. The Government is also considering to bring a new insolvency law for banks and financial institutions to vest with depositors the first right over assets of a defunct entity.

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This update only contains a summary/ limited description of the topic dealt with hereinabove for general information purposes and should not be construed as a legal opinion or be relied upon in absence of specific legal advice. For further information or legal advice please feel free to contact us.

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