# *De Jure*

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## IBC (Amendment) Ordinance: The Cat is Out of the Bag!


Rajani Associates
simple solutions

In order to prevent companies to be dragged into insolvency under the Insolvency and Bankruptcy Code, 2016 ("***Code***") due to the present pandemic, certain announcements were made by the Government under the Code. In this article, we have analysed the effect of these announcements on possible scenarios that the creditors or corporate debtors may be faced with. Before proceeding with our analysis, it may be worthwhile to have a brief recap on the announcements by the Government.


- March 24, 2020 - The Union Finance Minister announced that the threshold for invoking insolvency proceedings was raised from Rs. 1 lakh to Rs. 1 crore, which was subsequently notified on same date. In the same announcement, it was mentioned that the Government may consider suspension of Sections 7, 9 and 10 of the Code.

- May 17, 2020 – The Union Finance Minister announced: (i) Special insolvency resolution framework for MSMEs under the proposed Section 240A of the Code; (ii) Suspension of fresh initiation of insolvency proceedings upto 1 year depending upon COVID-19 situation and (iii) Empowering the Central Government to exclude COVID-19 related debts from the definition of "default" under the Code for the purpose of triggering insolvency proceedings.

Keeping in mind the aforesaid announcements and various insolvency measures adopted by countries like U.S.A[1], United Kingdom.[2], Australia[3] etc., the Central Government has now introduced an ordinance dated June 5, 2020 ("***Ordinance***") to suspend initiation of corporate insolvency resolution process of a corporate debtor under Sections 7, 9 and 10 of the Code for any default arising on or after March 25, 2020 for a period of six months, or such further period not exceeding 1 year ("***suspension period***"), as may be notified in this regard.

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[1] Section 1113 of The Coronavirus Aid, Relief and Economic Security Act or the "CARES Act" - https://www.congress.gov/116/bills/hr748/BILLS-116hr748enr.pdf (accessed on June 7, 2020)

[2] Measures announced on March 28, 2020 by the Hon. Alok Sharma, M.P. (Secretary of State for Business, Energy and Industrial Strategy - https://www.gov.uk/government/news/regulations-temporarily-suspended-to-fast-track-supplies-of-ppe-to-nhs-staff-and-protect-companies-hit-by-covid-19 (accessed on June 7, 2020)

[3] Part 1 of Schedule 12 of The Coronavirus Economic Response Package Omnibus Act, 2020 - https://www.legislation.gov.au/Details/C2020A00022 (accessed on June 7, 2020)

The Ordinance also suspends filing of an application by the resolution professional under Section 66(2) of the Code against directors or partners of corporate debtors in respect of such default against which initiation of corporate insolvency resolution process would be suspended by virtue of the Ordinance.

## Newly inserted Section 10A and its proviso: Different treatments for the same subject matter?

The newly inserted Section 10A by which the suspension is given effect reads as follows:

*"**Section 10A: Suspension of initiation of corporate insolvency resolution process***

*10A. Notwithstanding anything contained in Sections 7, 9 and 10, no application for initiation of corporate insolvency resolution process of a corporate debtor shall be filed for any default arising on or after 25th March, 2020 for a period of six months or such further period, not exceeding one year from such date, as may be notified in this behalf.*

*Provided that no application shall ever be filed for initiation of corporate insolvency resolution process of a corporate debtor for the said default occurring during the said period.*

*Explanation: For removal of doubts, it is hereby clarified that the provisions of this section shall not apply to any default committed under the sections before 25th March, 2020."*

- It is apparent from the above reading of Section 10A that the operative part of the section as well as its proviso deal with the same subject matter i.e. *default arising on or after March 25, 2020.* While the operative part of the section provides for a temporary suspension on initiating corporate insolvency for any default arising on or after March 25, 2020, it appears that the proviso seeks to give permanent immunity to such defaults from the Code.

- Does the immunity mean that the creditors will never ever be able to proceed against the corporate debtor for such default under the Code? - As the Ordinance reads now, it seems that the Ordinance, literally, debars the creditors from proceeding under the Code

in relation to defaults occurring during the suspension period. However, one plausible view could be that 'default', as defined under the Code, continues to remain a 'default', until it is paid in full, or as agreed. So, a default that has occurred during the suspension period, may continue even beyond the suspension period.

**Tabular clarification of possible scenarios for creditors or corporate debtors who wish to avail the available mechanism under the Code post the Ordinance**

| Scenario No. | Date of default | | Amount of default | | Date of issuing demand notice (not applicable to financial creditors and corporate applicant under Sec. 10 of the Code) | | Date of filing Application with NCLT under the Code | | Whether Application filed under the Code will be maintainable after the Ordinance? |
|---|---|---|---|---|---|---|---|---|---|
| | Before March 25, 2020 | On or after March 25, 2020 | > Rs.1 lakh | > Rs.1 crore | Before March 25, 2020 | On or after March 25, 2020 | Before March 25, 2020 | On or after March 25, 2020 | |
| I. | Yes | -- | Yes | -- | Yes | -- | Yes | -- | Yes |
| II. | Yes | -- | Yes | -- | Yes | -- | -- | Yes | No |
| III. | Yes | -- | Yes | -- | -- | Yes | -- | Yes | No |
| IV. | Yes | -- | -- | Yes | -- | Yes | -- | Yes | Yes |
| V. | -- | Yes | -- | Yes | --- | Yes | --- | Yes | No |

## Our views on the Ordinance

- The proviso to section 10A attempts to widen the scope of the operative/enacting part of the section in so far as it protects any default occurring during the suspension period even beyond the expiry of such suspension period. It is a settled principle of interpretation of statutes that the ambit and the scope of the enacting section cannot be widened or curtailed by the proviso when the enacting part is not susceptible to several possible meanings. One can hope that ambiguity arising under the Ordinance may be clarified when the Ordinance becomes an amendment act or by judicial review.

- The underlying rationale of the newly inserted sub-section 3 to Section 66 of the Code, via the Ordinance, is to boost the confidence of the directors or partners of companies to use their best endeavours to continue trading during this unprecedented market situation, without the threat of personal liability, if at all the company goes into insolvency.

- Pending applications i.e. those applications which are already filed with the NCLT, but are yet to come up for hearing or applications which have come up for hearing(s) but are pending admission or rejection, will remain unaffected. The NCLT, Kolkata Bench in the matter of ***Foseco India Ltd. vs. Om Boseco Railproducts Ltd.***[4] has held that the increased threshold limit of Rs.1 crore under the Code does not apply retrospectively. This order proceeds on the well-settled law that a statute is presumed to be prospective, unless it is held retrospective, either expressly or by necessary implication. Even NCLT, Chennai Bench has concurred with this view in the matter of ***M/s. Arrowline Organic Products Pvt. Ltd. vs. M/s. Rockwell Industries Ltd.***[5]

[4] Order dated May 20, 2020 in C.P. (IB) No. 1735/KB/2019

[5] Order dated June 2, 2020 in C.P. in I.A./341/2020 in IBA/1031/2019

- The Ordinance is in consonance with the aggregate moratorium of 6 months on payment of instalments in term loans as well as exclusion of the period for classification of an asset as NPA under the RBI's COVID-19 Regulatory Package. Thus, majority of the financial creditors may not be moved by the Ordinance. However, the Ordinance is likely to be detrimental to the interests of operational creditors. Be that as it may, it will be interesting to see what treatment is accorded to MSMEs, vis-a-vis special framework for MSMEs under the proposed Section 240A.

- The Ordinance could have provided clarity on the possible issues that may arise due to COVID-19 with regard to various stages specific to a resolution plan viz. where resolution proposal is submitted to the CoC, but not approved by the CoC; where resolution application is approved by the CoC, but pending approval of the NCLT and where the resolution plan is approved by the NCLT, but remains to be implemented.

- The Government could consider bringing into force the fresh start process chapter and also have a statutory amendment qua pre-package insolvency regime under the Code.

**Now that the cat is out of the bag, what could be the way forward?**

- Financial creditors may pursue (i) restructuring / re-arrangement schemes like one-time settlement (OTS); (ii) scheme under Section 230 of the Companies Act, 2013; (iii) inter-creditor agreement (ICA) in accordance with the RBI's circular dated June 7, 2019 on 'Prudential Framework for Resolution of Stressed Assets'; (iv) filing an application against the debtor before the DRT under the SARFAESI Act, 2002, (v) proceeding against the 'personal guarantor' of the corporate debtor under the Code.

- Corporate debtors whose rights are being taken away by the Ordinance for initiation of insolvency process

under the Code may avail other remedies like voluntary liquidation under the Code and the winding up mechanism for specified companies defined under the Companies Act, 2013 read with the Companies (Winding up) Rules, 2020 which have come into force from April 1, 2020.

- Operational Creditors could opt for debt recover mechanisms such as filing Summary Suits under Order XXXVII of the Code of Civil Procedure, 1908; regular recovery civil suits under the Commercial Courts Act, 2015 before the civil courts; remedies under the MSME Act, 2006 and arbitration proceedings under Arbitration & Conciliation Act, 1996 subject to the existence of arbitration agreement/clause etc.

## Contributed By:

**Devesh Juvekar, Partner:** devesh@rajaniassociates.net

**Dikshat Mehra, Principal Associate:** dmehra@rajaniassociates.net

**Chintan Gandhi, Associate**: cgandhi@rajaniassociates.net

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## CONTACT US

# Rajani Associates

simple solutions


| | |
|---|---|
| **Address:** | Krishna Chambers<br>59 New Marine Lines<br>Churchgate<br>Mumbai 400020<br>Maharashtra, India |
| **Telephone:** | (+91-22) 40961000 |
| **Facsimile:** | (+91-22) 40961010 |
| **Email**: | dejure@rajaniassociates.net |
| **Website:** | www.rajaniassociates.net |