Insolvency & Bankruptcy (Amendment) Act, 2018: A Game Changer

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Abstract:

The Indian economy has been plagued with bad debts for many years. The Insolvency and Bankruptcy Code, 2016 ("**Code**") is one of the most landmark reforms introduced by the Modi Government as a respite to the frailing economy. The Code remains under constant scrutiny and progress and has witnessed several amendments over the last two years. One of the most iconic amendments to the Code is the Insolvency and Bankruptcy (Amendment) Act, 2018 ("**Amendment Act**") which was enacted with the primary objective of streamlining the corporate insolvency resolution process prescribed under the Code. In this paper, the author has made an attempt to shed some light on the key changes introduced by the Amendment Act and critically analyze their impact on the ever-evolving Indian insolvency and bankruptcy regime.

I. INTRODUCTION

Until late 2016, the insolvency and bankruptcy regime in India was governed by multiple legislations. In the event of a default by a corporate debtor, the promoters usually took the driving seat and the creditors and external financers would be left with limited command and influence. Conflict between the interests of the creditors on one hand, and the promoters on the other, made debt recovery in India an extremely complicated and lengthy process. Moreover, lack of clarity due to multiplicity of legislations gave room to the stakeholders to manipulate situations and stall progress. This necessitated the need for a comprehensive mechanism to deal with insolvency and bankruptcy in India.

The Code was enacted with the intent to amend and consolidate the extant myriad insolvency and bankruptcy laws under a robust legal framework. The Code seeks to achieve time-bound reorganization and insolvency resolution of corporate persons, partnership firms and individuals, while at the same time, balancing the interests of all stakeholders.

II. CORPORATE INSOLVENCY RESOLUTION REGIME UNDER THE CODE

The Code postulates the existence of two types of creditors, a financial creditor and an operational creditor. Broadly, financial creditors are those whose relationship with the entity is a pure financial contract, such as a loan or a debt security. Operational creditors, on the other hand, are those whose liability from the entity comes from a transaction on operations.[1] If a corporate debtor commits a default of INR 1,00,000 (Rupees One lakh) towards a financial creditor or an operational creditor, then such creditor or even the corporate

[1] Vol. 1, The Report of the Bankruptcy Law Reforms Committee, Rationale and Design, 2015 (77)

debtor itself may initiate the corporate insolvency resolution process of the corporate debtor under the Code by making an application before the adjudicating authority. The National Company Law Tribunal ("**Tribunal**") has been appointed as the adjudicating authority in relation to the insolvency resolution and liquidation process under the Code.

Once the application is admitted by the Tribunal, the corporate insolvency resolution process of the corporate debtor is deemed to have been initiated. The initiation of the corporate insolvency resolution process is marked by:

(a) The onset of a statutory moratorium of a maximum of 180 (One hundred and eighty) days from the date of admission of the application, against any recovery, action, enforcement of security or the institution or continuation of suits / proceedings against the corporate debtor. The objective of the moratorium is to prevent the economic value of the corporate debtor from being further eroded; and

(b) The appointment of a resolution professional to take over the management and operations of the corporate debtor and conduct the corporate insolvency resolution process. The role of the resolution professional is to preserve the value of the property of the corporate debtor and manage its operations as a going concern.

The resolution professional is required to constitute a committee of creditors consisting of financial creditors of the corporate debtor. Prospective applicants are invited to submit resolution plans for the revival of the corporate debtor as a going concern, which are placed before the committee of creditors for its approval. If a resolution plan is approved by at least 75 % (Seventy five percent) of voting shares of financial creditors, it is submitted to the Tribunal for its sanction. The corporate insolvency resolution process is required to be completed within a period of 180 (One hundred eighty) days from the date of admission of the application by the Tribunal with a one-time extension of another 90 (Ninety) days, upon failure of which, the Tribunal may order for the liquidation of the corporate debtor.

III. Insolvency and Bankruptcy (Amendment) Act, 2018

Since its inception, the legislators have reached out to various market participants to seek their suggestions on the Code. In the last two years, the Code had witnessed several amendments. One such key amendment is the Insolvency and Bankruptcy Code (Amendment) Bill, 2017, which was passed by both the houses of the parliament and thereafter received the President's assent on January 18, 2018 to become the Amendment Act. The Amendment Act seeks to keep the sanctity of the Code intact by placing adequate safeguards to prevent persons of questionable antecedents from misusing or vitiating the provisions of the Code.

IV. Key Provisions of the Amendment Act- A Brief Analysis

- **Applicability of the Code**

Prior to the introduction of the Amendment Act, the applicability of the provisions of the Code was restricted to (a) companies; (b) limited liability partnerships; (c) partnerships firms; (d) such bodies as may be notified by the Central Government; and (d) individuals. The Amendment Act extends the applicability of the Code to (a) personal guarantors of the corporate debtor; and (b) proprietorship firms, both of which were earlier excluded from the ambit of the Code.

The Hon'ble High Court of Judicature at Allahabad, in a recent judgement[2], had analyzed the much debated question of initiation of insolvency resolution proceedings against personal guarantors of the corporate debtor. Inclusion of personal guarantors within the ambit of the Code, has finally put this issue to rest. Further, even though most of the Indian small and medium enterprises function on a proprietorship-based model, until now, there is no legislation governing the functioning of such firms. By including proprietorship firms under the insolvency regime, the legislators have tried to hardcode the mechanism for insolvency and bankruptcy of such firms.

- **Eligibility criteria for the resolution applicants**

Under the erstwhile Code, the resolution professional had the right to invite any prospective lender, investor and any other person to put forward a resolution plan for the insolvency resolution of the corporate debtor. The Code did not prescribe any qualification or eligibility criteria required to be fulfilled by the resolution applicants for submitting a resolution plan.

The Amendment Act casts upon the resolution professional the obligation to lay down certain eligibility criteria and invite only such resolution applicants for presenting the resolution plan who fulfill the eligibility criteria as determined by the resolution professional with the approval of the committee of creditors. While determining the eligibility criteria, the resolution professional is required to factor in the complexity and scale of business operations of the corporate debtor and such other conditions as may be prescribed by the Insolvency and Bankruptcy Board of India. The Amendment Act has ensured that only persons/ entities with sufficient and relevant financial, legal and technical competency submit the resolution plan.

Further, by way of introduction of Section 29A in the Code, the Amendment Act prescribes a list of persons who are not eligible to submit a resolution plan. As per Section 29A of the Code, a person is barred from submitting a resolution plan if such person or any other person acting jointly or in concert with such person (a) is an undischarged insolvent; (b) is a willful defaulter as per the guidelines prescribed by the Reserve Bank of India; (c) has an account or an account of a corporate debtor under the management or control of such person which has been classified as non performing asset and a period of one year has lapsed since such classification; (d) is convicted of any offence punishable with imprisonment for two years or more; (e)

[2] Sanjeev Shriya v. State Bank of India and Ors. Writ C No. 30285 of 2017

is disqualified to act as a director under the Companies Act, 2013; (f) is prohibited by the Securities Exchange Board of India from trading in securities or accessing the capital markets; (g) has been a promotor or in the management or control of a corporate debtor in which a preferential or undervalued or extortionate credit or fraudulent transaction has taken place in respect of which an order has been made by the Tribunal; (h) has executed an enforceable guarantee in favour of a creditor, in respect of a corporate debtor undergoing insolvency proceedings; or (i) has been subject to any disability, corresponding to clauses (a) to (h) above, under any law in a jurisdiction outside India.

In addition to the ineligibility criteria laid out above, the Amendment Act prohibits a person or any other person acting jointly or in concert with such person who has a 'çonnected person' suffering from any of the disqualifying factors mentioned in (a) to (i) above from presenting a resolution plan. The term 'connected person' has been defined under the Amendment Act to mean any person (i) who is the promotor or in management or control of the resolution applicant; or (ii) who will be the promotor or in management or control of the business of the corporate debtor undergoing an insolvency proceeding; or (iii) the holding company, subsidiary company, associate company or related party of a person referred to in clauses (i) and (ii) above. A connected person, however, does not include a scheduled bank, an asset reconstruction company and an alternative investment fund.

The aforesaid amendments appear to have been introduced in view of the recent discussions around credibility of resolution applicants. By imposing such stringent restrictions, the Amendment Act seeks to ensure that persons who do not meet the requisite legal and financial credibility for submitting a resolution plan are refrained from doing so.

- **Approval of resolution plan by the committee of creditors**

Under the erstwhile Code, the vote of atleast 75 % (Seventy five percent) of voting shares of financial creditors was required to approve the resolution plan. The Amendment Act further casts upon the committee of creditors the onus to approve the resolution plan only after considering the viability and feasibility of such resolution plan. However, the committee of creditors is not allowed to approve any resolution plan submitted before the commandment of the Insolvency and Bankruptcy Code (Amendment) Ordinance, 2017 i.e., before November 23, 2017, by resolution applicants who are ineligible Section 29A of the Amendment Act and if no other resolution plan is available with the creditors committee then it may invite fresh resolution plans.

- **Punishment where no specific punishment or penalty is provided**

The Amendment Act introduces an encompassing provision to prescribe punishment for contraventions where no specific penalty or punishment is provided under the Code. Any contravention of the provisions of the Code or rules and regulations made thereunder for which no punishment is prescribed for will be

punishable with a fine of not less than INR 1,00,000 (Rupees One Lakh) extending upto INR 2,00,00,000 (Rupees Two crore).

V. CONCLUSION

The Amendment Act has been designed with the primary objective of strengthening and streamlining the insolvency resolution process and bar certain ineligible persons from participating in the resolution process. The enactment of the Amendment Act is definitely a welcome move and the changes brought about by the Amendment Act are a testimony towards its objectives. However, its success will primarily depend on how genuine resolution applicants who are debarred from submitting a resolution plan on account of reasons beyond their control choose to react. Only time will tell if the Amendment Act opens gates to litigation in the near future.

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