

INSOLVENCY AND BANKRUPTCY CODE, 2016

By:

Karishma Jaiswal

Associate

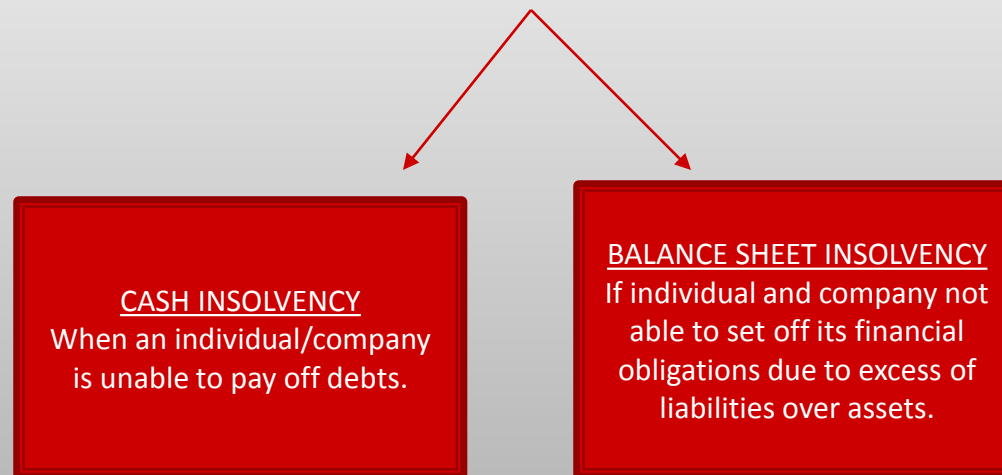
Maheshwari & Co.

Advocates & Legal Consultants

INTRODUCTION

- **INSOLVENCY:** Insolvency is a situation which arises due to the inability to pay off the outstanding debt to the creditors because the assets are not enough to meet the liabilities. It means that an entity's liability exceeds its assets. A state of insolvency can lead to bankruptcy.
- **BANKRUPTCY:** Bankruptcy is a legal declaration where an individual/organization sends an application to the court to declare himself as insolvent due to his inability to pay off debts and expenses and thereby seeking to be declared bankrupt. It is a legal status of a person or other entity that cannot repay the debts it owes to creditors.

INSOLVENCY IS OF 2 TYPES



Tighten the financial
reforms in India

Need of a unified code

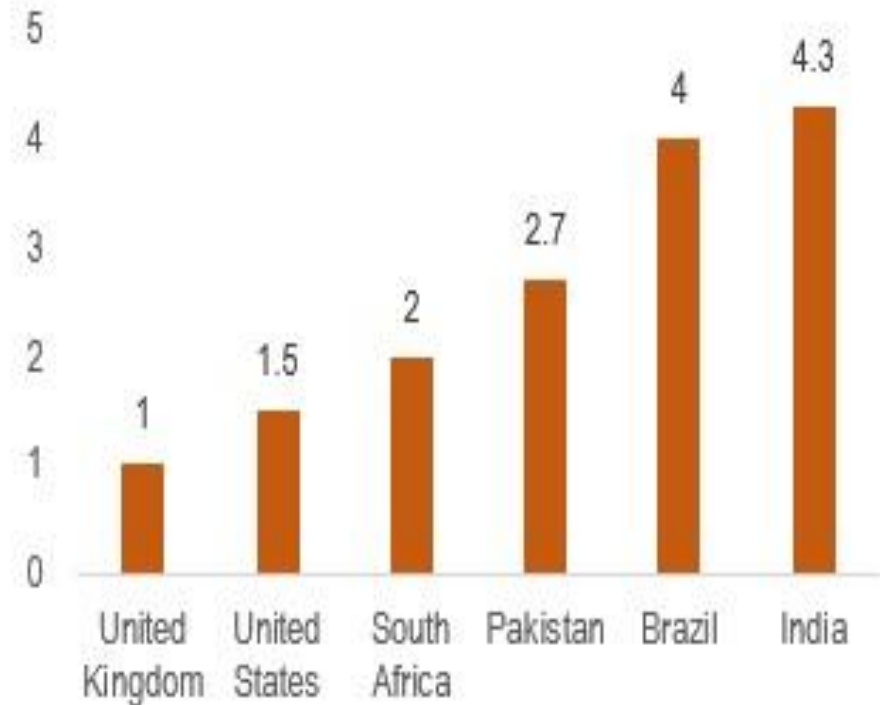
Provide ease of doing
business

Consolidation of existing
legal framework

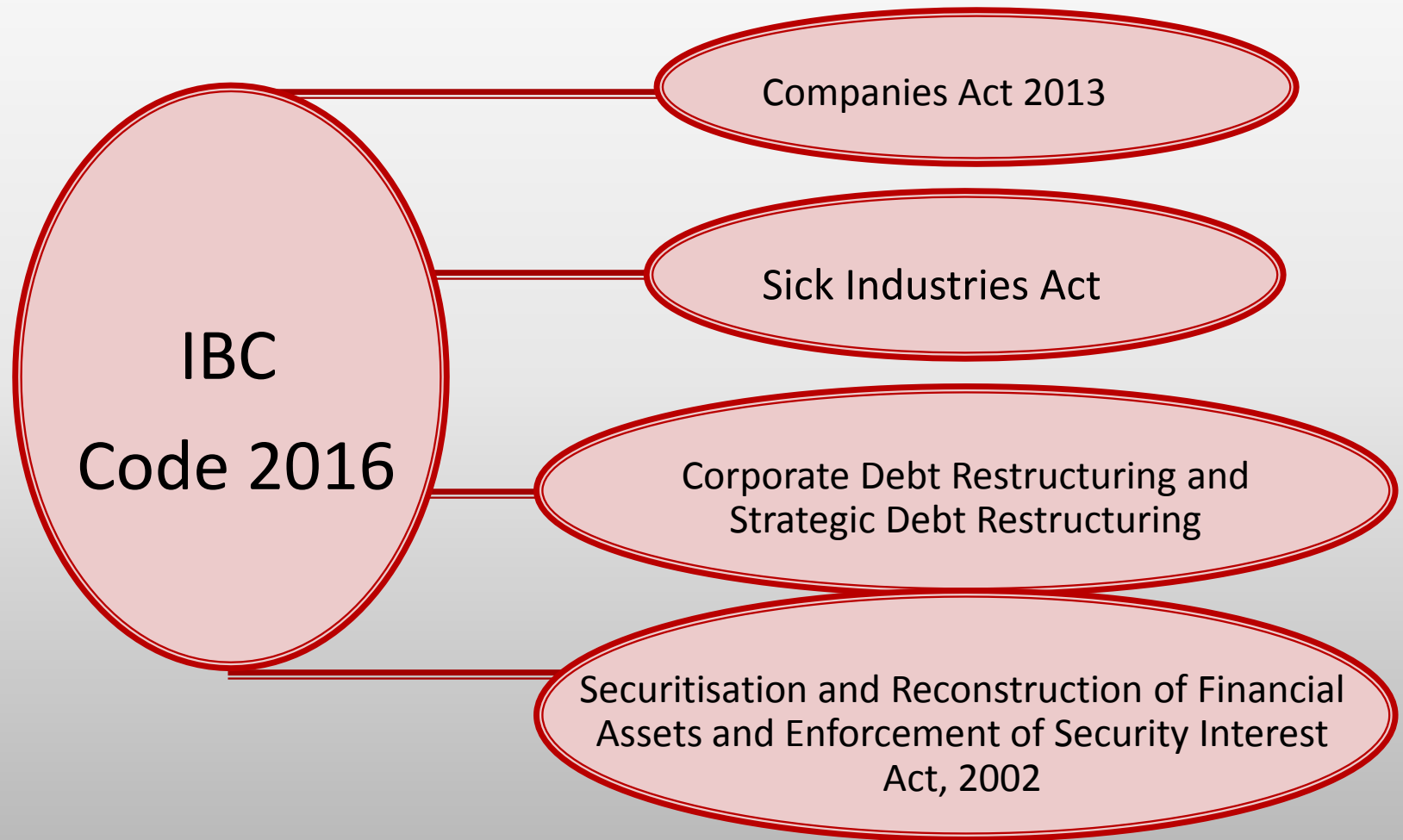
Repair the framework
dealing with insolvency
of corporates,
individuals and
partnerships

- As of 2015, insolvency resolution in India took 4.3 years on average. This is higher when compared to other countries such as United Kingdom (1 year) and United States of America (1.5 years). These delays are caused due to time taken to resolve cases in courts, and confusion due to lack of clarity about the current bankruptcy framework.
- As per the Doing business index 2016 released by World Bank, India continues to fare the worst amongst the BRICS nation at 136.
- At recovery rate of 25.7 cents per dollar, India is ahead only of Brazil amongst BRICS nation
- At present creditors are aware of the fact that they have weak rights resulting in low recovery rate, and have strong feeling of opposition to lending specially unsecured loans.
- Delay in insolvency process causes value destruction.

Figure 1: Time to resolve insolvency (years)



Source: "Time to resolve insolvency", World Bank, 2015.



- a) Any company incorporated under the companies act, 2013 or under any previous company law;
- b) Any other company governed by any special Act;
- c) Any Limited Liability Partnership incorporated under Limited Liability Partnership Act, 2008;
- d) Such other body incorporated under any law for the time being in force, as the Central Government may specify
- e) Partnership firms and individuals.

In relation to their insolvency, liquidation, voluntary liquidation or bankruptcy as the case be.

****** Part III of the code pertaining to insolvency of individuals and firms does not apply to State Of Jammu & Kashmir.

****** The code is not applicable to financial service providers as per sub-section 7 of section 3 read with subsection 17.

ACTS MODIFIED / AMENDED

- Amendments to Companies Act, 2013
- Amendments to Indian Partnership Act, 1932 *(Not yet Notified)*
- Amendments to the Central Excise Act, 1944
- Amendments to the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (SARFAESI)
- Amendments to the Sick Industrial Companies (Special Provisions) Repeal Act, 2003
- Amendments to the Income Tax Act, 1961
- Amendments to the Customs Act, 1962
- Amendments to the Recovery of Debts Due to Banks and Financial Institutions Act, 1993 *(Not yet Notified)*
- Amendments to the Payment and Settlement Systems Act, 2007
- Amendments to the Limited Liability Partnership Act, 2008
- Amendments to the Finance Act, 1994

ACTS REPEALED

- **The Presidency –Towns Insolvency Act, 1909** *(Not yet Notified)*
- **The Provincial Insolvency Act,1920** *(Not yet Notified)*



- Resolution before Liquidation: If possible, the business should be revived before liquidation
- Time bound process: Unlike previous practice, now the entire insolvency resolution process shall complete in at max 270 days.
- Information Utilities have been formed under the Code to provide timely dissemination of information to the concerned.
- Automatic liquidation if revival process does not complete within 180 or 270 days as the case may be.
- Creditors Voluntary winding up done away with.

IMPORTANT DEFINITIONS UNDER THE CODE

Section	Term	Definition
2 (7)	Corporate person	<ul style="list-style-type: none"> • Company as defined in CA, 2013 • An LLP [As per LLP Act, 2008] • Any other person incorporated with limited liability under any law for the time being in force • Excludes - Financial service provider
2(8)	Corporate Debtor	<ul style="list-style-type: none"> • A corporate Person who owes a debt to any person
2(10)	Creditor	<ul style="list-style-type: none"> • Any person to whom debt is owed • Financial or operational Creditor / Decree holder
2(11)	Default	<ul style="list-style-type: none"> • Non-payment of debt – whole/part/installment
4(14)	Insolvency resolution process period	Period of 180 days beginning from the insolvency commencement date and ending on 180th day
4(6)	Dispute	<ul style="list-style-type: none"> • Includes a suit or arbitration proceedings relating to— • the existence of the amount of debt; • the quality of goods or service; or • the breach of a representation or warranty;
4(13)	Insolvency commencement date	<ul style="list-style-type: none"> • Date of admission of application for Corporate Insolvency Resolution process by NCLT

(PART-I) INSOLVENCY RESOLUTION AND LIQUIDATION FOR CORPORATE PERSONS

Application:

This Part shall apply to matter relating to the insolvency and liquidation of corporate debtors where the minimum amount of the default is one lakh rupees,

Provided that the Central Government may, by notification, provide for higher minimum amount not beyond Rs. One crore.

Corporate Insolvency Resolution Process: Where any corporate debtor commits a default, a financial creditor, an operational creditor or the corporate debtor itself may initiate corporate insolvency resolution process in respect of such corporate debtor. It provides for collective mechanism to the lenders to deal with the distressed situation of a corporate debtor.

It is little different from that of the existing legal framework as the burden or responsibility to initiate a re-organisation process lies with the debtor and the lenders may pursue distinct actions for recovery, security enforcement and debt restructuring. The moment a default occurs a financial creditor or the operational creditor or the corporate applicant may approach the adjudicating authority with an application to initiate the IRP.

STEPS TO BE FOLLOWED IN CORPORATE INSOLVENCY RESOLUTION PROCESS

STEP 1-

COMMENCEMENT OF IRP :- The Corporate Insolvency Resolution Process shall commence from the date of admission of the application filed by a financial creditor for a financial debt, an operational creditor for an unpaid operational debt against a corporate debtor or by a corporate applicant itself at the NCLT (National Company Law Tribunal).

STEP 2-

MORATORIUM PERIOD & PUBLIC ANNOUNCEMENT :- The Adjudicating Authority, after admission of the application, shall, by an order

- (a) declare a moratorium for the purpose referred to in section 14;
- (b) cause a public announcement of the initiation of corporate insolvency resolution process and call for the submission of claims under 15; and
- (c) appoint an interim resolution professional in the manner as laid down in section 16.

Moratorium means suspension of activity for a particular period of time. Here in this case Moratorium is stipulated by the NCLT for the limited IRP period to prevent any type of suits, proceedings, recovery/ enforcement action against the corporate debtor . It generally refers to as a “calm period”.

STEP 3-

APPOINTMENT OF INTERIM RESOLUTION PROFESSIONAL :- The Adjudicating Authority shall appoint an interim resolution professional within fourteen days from the insolvency commencement date.

The term of the interim resolution professional shall not exceed thirty days from date of his appointment.

STEP 4-

COMMITTEE OF CREDITORS :-The interim resolution professional shall after collation of all claims received against the corporate debtor and determination of the financial position of the corporate debtor, constitute a committee of creditors. The committee of creditors shall comprises the financial creditors of the corporate debtors as the decision makers and are responsible for deciding all the important affairs of the company. operational creditors or their representatives if the amount of their aggregate dues is not less than ten per cent of the debt are eligible to attend the meeting but they cannot have the power to vote.

STEP 5-

APPOINTMENT OF RESOLUTION PROFESSIONAL:- The committee of creditors may, in the first meeting, by majority vote of not less than seventy-five percent of the voting share of the financial

creditors, either resolve to appoint the interim resolution professional as a resolution professional or to replace the interim resolution professional by resolution professional.

STEP 6-

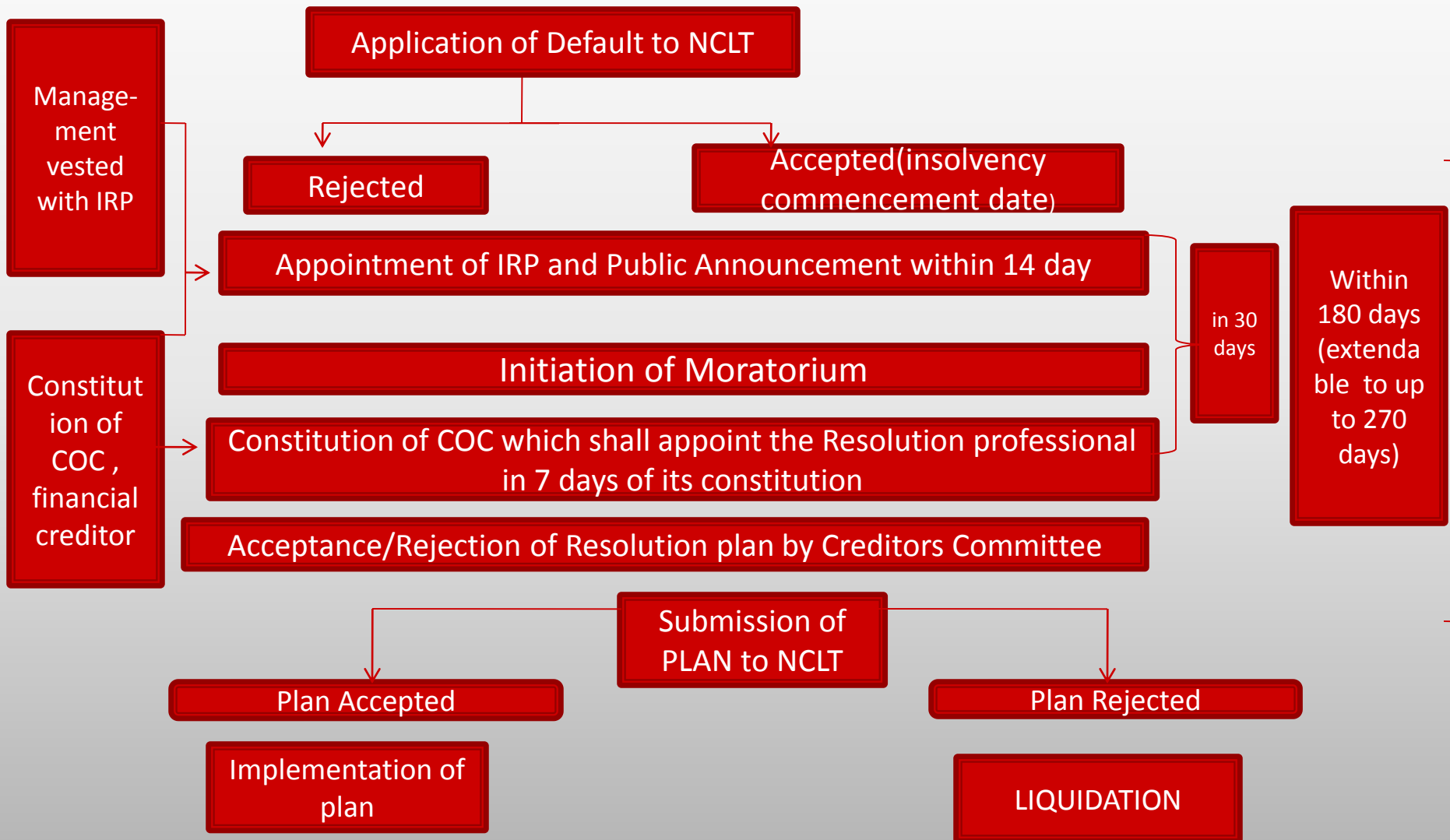
INFORMATION MEMORANDUM:- The resolution professional shall prepare an information memorandum in such form and manner containing such relevant information as may be specified by the Board for formulating a resolution plan.

“**resolution plan**” means a plan proposed by any person for insolvency resolution of the corporate debtor as a going concern.

STEP 7-

RESOLUTION PLAN :- A resolution applicant may submit a resolution plan to the resolution professional prepared on the basis of the information memorandum.

“**resolution applicant**” means any person who submits a resolution plan to the resolution professional. The resolution professional shall present to the committee of creditors for its approval. The committee may approve a resolution plan by a vote of not less seventy five per cent of voting share of the financial creditors.



INITIATION OF LIQUIDATION

- The creditors committee decides to liquidate the company;
- The creditors committee cannot agree on a workable resolution plan within the specified IRP period i.e. 180 days or the extended period;
- The NCLT rejects the resolution plan
- The corporate debtor contravenes provisions of the resolution plan.

THE NCLT SHALL DO THE FOLLOWING WORK :-

- a) Pass an order requiring liquidation of corporate debtor
- b) Make a public announcement of corporate debtor entering liquidation.
- c) Require a liquidation order to be sent to the registering authority of the corporate debtor like for example Registrar of Companies in case of companies incorporated under Companies Act)

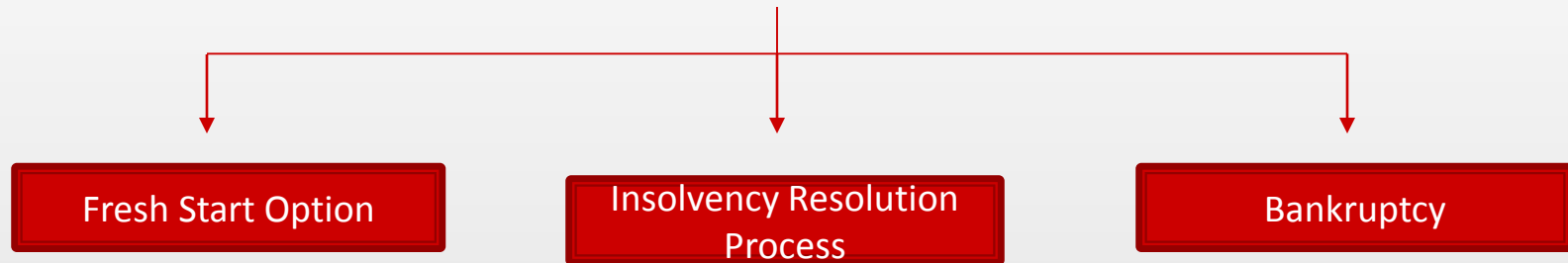
ORDER OF PRIORITY FOR DISTRIBUTION OF ASSETS {WATERFALL MECHANISM}

- Insolvency Resolution and Liquidation Cost
- Secured Creditors and workmen's dues for a period of 24 months preceding the liquidation commencement date
- Wages and unpaid dues to employees
- Unsecured Creditors
- Government Dues up to 2 years
- Any remaining debt and dues and dues of preference shareholders if any; and equity shareholders or partners



- Application for insolvency can be made by financial creditor or operational creditor, but decision making is in the hands of Financial Creditor;
- Financial creditors are voting at par;
- Government dues take a backseat;
- Shareholders have no say during the process of revival as well as resolution.
- Operational creditors with more than 10 percent aggregate exposure have mere "observer status" during the Committee of Creditors meetings and no voting Right.

Insolvency of Individuals and Firms involves a 3 way process



1) FRESH START – A debtor may apply, either personally or through a resolution professional, for a fresh start in respect of his qualifying debts. This option is available for defaults where amount involves is quite less.

- WHO CAN APPLY ? Defaulting Debtor whose -
 - (i) Gross annual income not exceeding Rs.60,000
 - (ii) Aggregate value of assets not exceeding Rs.20,000
 - (iii) Aggregate value of qualifying debt of such individual /partnership firm not exceeding Rs.35,000.
 - (iv) No dwelling house
 - (v) He should not be an undischarged bankrupt and there is no previous fresh start process/insolvency resolution process existing against him.
- WHOM TO APPLY : Adjudicating Authority of DRT

- **MORATORIUM** - An interim moratorium commences on the date of filing of application of fresh start till the date of admission or rejection of application during which no legal action can be taken against or initiated in respect of the debtor. It however imposes certain restrictions on the debtor such as he cannot act as the director of any company or remain involved in promotion or management of any company. He is also not allowed to dispose off his assets or travel abroad without the permission of adjudicating authority.
- 2). **INSOLVENCY RESOLUTION PROCESS** - The IRP process can be initiated by either the debtor personally or through an insolvency resolution professional or by the creditor either personally or with other creditors jointly through an insolvency professional. But in case of partnership firm it cannot be filed unless a joint application is filed by majority of the partners of the partnership firm
- **REPAYMENT PLAN** :- In the insolvency resolution process the creditors and debtors are required to arrive at a common resolution repayment plan in order to restructure the debts and affairs of the debtor, which is supervised by an Resolution Professional. The plan will require an approval of a 3/4th majority of financial creditors .It may require the Resolution Professional to :-
 - Carry on debtor's business or trade on his behalf in his name.
 - Realize the assets of the debtor.
 - Administer or dispose of any funds of the debtor.

APPLICATION FOR BANKRUPTCY

- The Bankruptcy of an individual can be initiated only after the failure of resolution process or non-implementation of repayment plan.
- It can be initiated by the debtor , the creditors or by the partners of a partnership firm
- The bankruptcy trustee is entrusted with the responsibility for managing and settling of the estate of the bankrupt and thereafter distributing the profit /gain as per the priority.

NCLT- Adjudicating authority in relation to insolvency resolution/ liquidation for corporate persons/corporate debtors including personal guarantors thereof

- Appeal against the order approving resolution plan could be filed on the ground of contravention of laws, material irregularity, non-compliance with the statute etc
- Appeal lies before the NCLAT followed by the Supreme Court for orders issued by NCLT
- Penalties (Sec68-77) prescribed for:
 - Concealment of property
 - Undertaking transactions defrauding creditors
 - Misconduct in course of corporate resolution insolvency process
 - Falsification of Books of corporate debtor
 - False representation to creditors
 - Imprisonment for a term of 1 – 5 years + Monetary penalty in the range of INR 100,000 - 10,000,000
- Insolvency Professional contravening the provision of this Code liable for imprisonment up to 6 months and monetary penalty in the range of INR 100,000 – 5,00,000

DRT - Adjudicating authority in relation to insolvency resolution/ Bankruptcy for Individual / Partnership firm

- Appeal lies before the DRAT followed by the Supreme Court for orders issued by DRT.



Thank
You