A PARADIGM SHIFT OF IBC CONSEQUENT TO COVID 19: AN ANALYSIS

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ABSTRACT

The IBC, 2016 is a landmark development in the dynamic world of resolution of stressed assets laws in our country. The Insolvency and Bankruptcy Code, 2016, is India's bankruptcy law that seeks to consolidate the existing framework by establishing a single law for insolvency and bankruptcy. The research paper analyses the principles and legal framework of the code in relation to the COVID-19 pandemic. Because of the widespread economic impact of COVID-19, the Central Government issued the IBC Amendment Ordinance, 2020.

The goal of this paper is to look at how the COVID-19 pandemic has affected the Insolvency and Bankruptcy Code. This paper also demonstrates how the IBC Amendment Ordinance, 2020, is extremely useful in improving India's image on a global scale. In line with that, the paper examines the implementation of the 2020 ordinance in India in light of the current state of the Indian economy. The research paper will also reaffirm the validity of the aforementioned amendment in the eyes of stakeholders. A concerted effort will be made to assess the various challenges encountered, as well as the numerous benefits of emendation in India. In addition, a study is being conducted on some International Jurisdictions to demonstrate their progress in reforming their respective statutes in the midst of COVID-19. Finally, in the final section, an attempt will be made to provide some suggestions for improvement in IBC during COVID-19.

Keywords: Insolvency, Bankruptcy, COVID 19, IBC Amendment Ordinance, 2020, International Jurisdictions

INTRODUCTION

- ***Legal position prior to IBC for resolving the defaults:***

The Insolvency and Bankruptcy Code, 2016, enacted comprehensive bankruptcy and insolvency laws in India. Notably, the aforementioned code is one of the most important economic laws in our country, influencing the ease with which we conduct business. According to World Bank data from 2016, it took nearly 4.3 years to develop the aforementioned legislation. Before the establishment of the IBC, India had a very intricate insolvency regime governed by numerous laws such as the Sick Industrial Companies Act, 1985, the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002, the Recovery of Debt Due to Banks and Financial Institutions Act, 1993, and the Companies Act, 2013, none of which could provide a complete solution to the problems that were being faced. Because there was no comprehensive code for dealing with business failure, it amended 11 laws and brought them under one umbrella.

The terms insolvency and bankruptcy are synonymous. Insolvency can occur without bankruptcy, but bankruptcy cannot occur without insolvency. Insolvency refers to a person's or corporation's inability to pay their bills when they become due and payable. And bankruptcy occurs when a person is declared unable to pay their bills on time. Prior to IBC, there was a bad loan recovery mechanism. The economy was booming in the early 2000s, prompting public sector banks to lend heavily to corporations. The economy slowed, and businesses were unable to repay their debts, which is the primary cause of the increase in NPA in India. This reduced the requirement for the new code, the Insolvency and Bankruptcy Code of 2016.

- ***Implementation of IBC:***

The code went into effect on December 1, 2016. Previously, creditors had little power to act during a default, and promoters retained control of the company even during a default. This code was created to maximise asset value, credit availability, and achieve balance in the best interests of all stakeholders. The IBC facilitated the transition from a debtor-controlled model to a creditor-driven process.

The longer the insolvency proceeding is delayed, the more difficult it will be to realise the assets because they can suffer from a high rate of value destruction. The need for a speedy trial

of the insolvency proceeding arises as a result, leading to the establishment of IBBI, the apex governing body of IBC.

The Corporate Insolvency Resolution Process (CIRP) is a process outlined in the code for reviving a company from insolvency. It may be initiated based on an application filed with the NCLT for the purpose of initiating CIRP by the company's financial creditor or operational creditor based on the fact of default established from the information utility's records. Following the acceptance of the application, the committee of creditors is formed, which appoints a professional who manages and presents a resolution plan. Following that, a timeline of 180 days is provided, which can be extended by another 90 days to complete the resolution process.

The most important aspect of the IBC code is its discussion of moratorium applicability. It refers to a stay or "calm period," which is the period during which no creditor can take recovery action against the corporate debtor, implying that creditors' actions will remain halted, and the IBC court will consider the possibility of rehabilitation. The mandatory moratorium is 180 days throughout the entire resolution process, with a one-time extension of up to 90 days.

The code also includes a Fast Track Resolution Process, which allows the process to be completed in 90 days rather than the usual 180 days. It is applicable in the case of corporate debtors of a specific class or having the income level prescribed by the Central Government, with a general focus on small businesses.

COVID-19 IMPACT

The global spread of coronavirus compelled the Government of India (GOI) to declare a nationwide lockdown due to a public health crisis. The government has taken various initiatives under the "Atmanirbhar Bharat Yojana." This Pandemic has not only afflicted humans physically and mentally, but it has also afflicted the global financial markets. This has significantly disrupted regular business activities, resulting in a decrease in income and an increase in unemployment. The most evocative victims of this lockdown, however, have been Micro, Small, and Medium Enterprises (MSME). Thereupon, A desperate need to maintain the status quo was so compelling that a series of resolutions concerning contractual obligations,

corporate debtors, and new insolvency proceedings were passed. To address an extremely troubling market situation and prevent corporate organisations from going bankrupt, the Indian government has implemented a variety of credit exposures, economic relief packages, and legal and regulatory measures by amending the Insolvency and Bankruptcy Code, 2016.

The Insolvency and Bankruptcy Code (Amendment) Ordinance, 2020 (Ordinance) was promulgated by the President on 5 June 2020, with immediate effect. The Ordinance's goal is to "protect corporate entities that have experienced a sudden halt in operations and have thus defaulted on their repayment obligations from being dragged into insolvency."[i]

The Ordinance amends the IBC, 2016, by adding Section 10A, which suspends the application of

i. Section 7[ii] (insolvency application by a financial creditor).

ii. Section 9[iii] (insolvency application by an operational creditor).

iii. Section 10[iv] (voluntary insolvency application by the corporate debtor).

iv. Insertion of sub section (3) under section 66[v] thus in respect to forbidding a Resolution Professional ("RP") from applying under section 66 (2) which primarily contend with the wrongful trading or any fraudulent act by the director or the partner of the corporate debtor.

This applies to the six-month period following payment defaults that occur on or after March 25, 2020. (Suspension Period). In addition, the Ordinance provides that the Suspension Period may be extended by Government notification for a maximum of one year. As a result, the government has made an effort to promote some measures with the goal of reducing the burden on companies and providing them with the possibility of revival.

THE INSOLVENCY AND BANKRUPTCY CODE AMENDMENT (ORDINANCE), 2020

- ***With the limited suspension, will the Indian Government be able to save the nation?***

The code has been amended three times since its inception. The Lok Sabha and Rajya Sabha both approved the Insolvency and Bankruptcy Code (Amendment) Bill, 2020. The bill was passed in order to break the stalemate in the corporate insolvency resolution process. The ordinance's goal was to protect new owners of a loan defaulter company from prosecution due to the misdeeds of previous owners. The Bill was amended and passed as an ordinance. President Ramnath Kovind published the modification through the Insolvency and Bankruptcy Code Ordinance, 2020, altering several parts of the code, and it took immediate effect on June 5, 2020, suspending the activities of Sections 7, 9, and 10[vi] and the Ordinance added additional sections 10A and 66(3) to the Insolvency and Bankruptcy Code, 2016. It was enacted to protect corporate entities from financial hardship as a result of the exceptional circumstances during the COVID-19 era.

- ***Changes made through the ordinance:***

IBC Amendments clause Section 10A[vii] does not bar bankruptcy proceedings in the cases where the default has arisen before March 25, 2020. Cases where the 180-day deadline expired in January will still be heard in bankruptcy court. There is no escape when the default is not tied to COVID-19. The primary concern now is that defaulters will be given a blanket exemption from Insolvency procedures because no corporate actions would be initiated for the next 6 months, which can be extended to a year starting on March 25. The sole viable remedy is if the default persists until it is paid in full or as negotiated between the parties. A default that happens during the suspension period will persist even after the suspension period has ended.

This legislation was enacted to assist corporate debtors who have been directly impacted by the COVID-19 pandemic's significant interruption of commercial activities across the country. In the meantime, the operational creditor, to whom an operational debt is owed and includes any person to whom such debt has been legally assigned or transferred, can recover their debt by filing a civil suit, or the Corporate Debtors can avail of the Voluntary Liquidation under the

winding-up mechanism of the Companies Act, 2013 read with the Companies (Winding up) Rules, 2020, which became effective on April 1, 2020.

In the event of an operational creditor, the operational creditor is required to send a demand notice on the corporate debtor. If the operational creditor has submitted the demand notice under section 8 before the date of notification, which is March 25, 2020, then the operational creditor may file an application under section 9 of the IBC, 2016. The only difference is that the default sum should be more than one crore. Previously, the amount of default was 1 lakh, however the Amendment Ordinance, 2020 raised the minimum threshold of default. The increase in the threshold limit was first implemented to safeguard small businesses and MSMEs from the impact of the lockdown enforced to prevent the spread of COVID-19. However, if the demand notice is delivered after March 25, 2020, the filing of the section 9 application would be barred.

Section 66[viii] deals with fraudulent trading or wrongful trading, i.e., transactions which were committed to defraud the creditors of the corporate debtors, and to identify and hold liable such persons who were responsible for such fraudulent transactions. Clause 2 of the section makes the director or partner liable to contribute to the debtor's asset on an application initiated by the Resolution professional if they are carrying out business activities with the intent to defraud creditors or are not exercising due diligence prior to the start of CIRP. When the CIRP is suspended under Section 10A, the insertion of clause 3 protects the directors or partners from any such default responsibility.[ix]

The objective for inserting section 66 clause 31 is to allow the directors or partners of the firms to continue operating in the market in the event of a pandemic, without fear of personal culpability if the company goes bankrupt. Individual and corporate economic growth are also vital in reviving the country's economic growth.

The question that arises is that whether the ordinance that has been passed is going to have retrospective effect or prospective effect? As per the precedent over the years the SC has laid down that, S.L. Srinivasa Jute Twine Mills v. Union of India[x], Unless specifically stated differently, a legislation is presumed to be applied prospectively. However, the raised threshold limit's application is still being construed as a result of court intervention because it was only issued by notification, not by the amendment itself. Furthermore, the RBI, in a notification

dated May 23, 2020, extended the EMI moratorium on term loans for another three months, and the suspension of Section 7 does not have much significance because it offers financial creditors a total moratorium of six months. The regulation, however, disadvantages operational creditors because financial creditors already have a moratorium under the RBI.

The NCLT's Kolkata and Chennai Benches, in their Orders dated 20 March, 2020 in M/s. Foseco India Limited v M/s. Om Boseco Rail Products Limited and 02 June, 2020 in M/s. Arrowline Organic Products (P) Ltd v M/s Rockwell Industries Limited, respectively, have provided some clarification on this matter. After careful consideration, the Hon'ble Adjudicating Authorities concluded that the statute did not expressly grant the delegate the authority to make the challenged notification with retroactive effect.It was determined that the notification dated March 24, 2020 is only prospective in nature, allowing pending cases before various Adjudicating Authorities across the country to reach a decision on the maintainability on the basis of the minimum threshold limit of default being questioned, as of date.[xi]

The objective behind IBC is to safeguard the firms by providing them a second chance even after default financially or operationally. Section 10[xii] provides the locus standi to the corporate debtors to voluntarily apply for the CIRP petition against itself and start the proceedings while maximizing the assets in the interest of all the stakeholders.

The substantial policy revisions implemented by the Finance Minister in the IBC in 2016 raised a number of confusing concerns in the current insolvency and bankruptcy procedure. The key difference is in the definitions of "default" and "wrongful trade."

- ***Further Revamping:***

In September 2020, the Reserve Bank of India issued another circular with the goal of rescheduling loan payback timelines. According to the circular, residual loan repayment can be deferred for up to two years in payments made from March 1 to August 31. Borrowers will now benefit from the following action. The economy is suffering greatly as a result of the epidemic, and there is a substantial possibility of skipping an EMI in this scenario. The authorities in charge of the recovery procedure may adopt punitive measures that harm an individual's credit score. Without a question, a solid credit score is required for an individual to take out loans. A poor credit score also reduces the likelihood of obtaining a loan. As a result, the Reserve Bank of India provides further relief to borrowers by extending the 2-year loan

payback period. The case of Embassy Property Development Pvt. Ltd. vs. the State of Karnataka might be used to analyse this circumstance,[xiii] wherein the matter has been judged an extension of the government's lease The Supreme Court determined that Section 14 of the IBC only bans the right to be evicted but not the right to extend the lease. A moratorium's objective is to conserve the status quo rather than to create a new right.

- ***Implementation as a challenge:***

During the crisis, the ordinance was created with the goal of protecting stressed enterprises who are unable to survive in this tough period of time since they will not be able to function realistically in an indebted state. And the insertion of Section 10 A[xiv] has made it plain that defaults that happened solely during the suspension period of 6 months, extendable to 1 year, will be covered by the same blanket; but, defaulters who were in default before to March 25, 2020 will not be able to protect themselves under this suspension period. A new alternative policy framework would be presented to cater to credit availability in the event of default during the suspension period, and for that reason, an unique Insolvency Resolution framework for MSME will be developed under Section 240A[xv] of the IBC, 2016. Even if the threshold limit is breached, MSMEs cannot claim the default amount, raising the possibility of deliberate default by corporate creditors. Furthermore, while the raised threshold was intended to provide assistance to MSMEs, the position of stressed MSME enterprises has exacerbated as a result of the suspension of CIRPs.

The ordinance's negative consequence is that debtors will unfairly benefit from the law's protection, and they will always be able to use the escape to pay for their mistakes. Creditors will be unable to recover debts even after the crisis has passed, leading borrowers to default as much as possible during the short time of suspension of certain laws, defeating the aim of the foundation of IBC.

The ordinance makes no mention of the insolvency resolution process for personal guarantors, whose obligation for the debt is joint and several with that of the corporate debtor. As a result, procedures against personal guarantors can still be commenced, causing a stumbling block in attaining the ordinance's goal and adding to the uncertainty.

CONCLUSION

The IBC, 2016, has generally presented as a tool for protecting the interests of business investors. The extreme necessity to safeguard the COVID-19 situation was so pressing that a series of decisions were made. Because of the changing character of the business world, it is necessary to change the law with the goal of re-organization and insolvency resolution in a time-bound way for asset maximisation. The Insolvency and Bankruptcy Code is one of the support mechanisms in place to keep businesses from going bankrupt. Despite the noble intent of the adjustments, many of them are short-sighted and will cause issues for stakeholders in the long term. The relaxations must accommodate everyone and not just one or more groups, which necessitates a study of the proposed adjustments. It is expected that the legislature will now seem as the best option to balance the government's pre-packaged framework. The paragraph would have been difficult to write, but with a few changes, it would have resulted in the easy application of the pre-pack regime in the Code.

ENDNOTES

[i] India: Insolvency And Bankruptcy Code Amended To Suspend Initiation Of Insolvency Proceedings For Six Months, mondaq connecting knowledge and people, https://www.mondaq.com/india/insolvencybankruptcy/962218/insolvency-and-bankruptcy-code-amended-tosuspend-initiation-of-insolvency-proceedings-for-six-months.

[ii] The Insolvency and Bankruptcy Code, 2016, no. 31, Acts of Parliament, 2016 (India).

[iii] Ibid

[iv] Ibid

[v] The Insolvency and Bankruptcy Code (Amendment) act, 2020, NO. 1, Act of Parliament,

2020 (India).

[vi] The Insolvency and Bankruptcy Code, 2016, no. 31, Acts of Parliament, 2016 (India).

[vii] Ibid

[viii] Ibid

[ix] Ibid

[x] 5S.L. Srinivasa Jute Twine Mills v. Union of India, (2006) 2 SCC 740.

[xi]Anant Merathia and Poornima Devi, IBC Amendment Ordinance 2020: No fresh insolvency for default after lockdown declaration, The New Indian Express, https://www.newindianexpress.com/business/2020/jun/08/ibc-amendment-ordinance-2020-no-fresh-insolvencyfor-default-after-lockdown-declaration-2153907.html.

[xii] Ibid

[xiii] Embassy Property Development Pvt. Ltd. vs. State of Karnataka, Civil Appeal No. 9170 0f 2019.

[xiv] Ibid

[xv] Ibid