IBC - THE JOURNEY SO FAR

The Government, as the prime mover of the economic and financial system of the Country, has time and again taken support of law as a tool to given direction to the eco system and to make it more responsive to the changing needs. Right from 1965 Government has tried to address the requirement of the developing economic system by effecting changes in the applicable law. Changes in Company Law, Depository Laws, SEBI, Competition Act, FEMA and so on, has propelled the commercial activities in the Country. This was followed by liberalization of the economy during 1990s. While such changes gave a boost to the economic development but the burden of fulfilling the financing needs of such booming economy largely remained with public sector banks. This acted both as boon and bane for the Banking System. As, failure is part and parcel of any business activity, Banking System did not remain aloof when such failures happened in commercial world, and this lead to rise of NPAs with the Banks.

BACKGROUND: To address the issue the Government initiated structured efforts based on the Narasimham Committee Report[i] by strengthening prudential norms, setting up specialized courts (Debt Recovery Tribunals). This was followed-up by another drastic legislation in the form of SARFAESI Act. RBI too came out with various schemes from time to time to provide solution to ever increasing problem including CDR mechanism. Board for Industrial and Financial Reconstruction (BIFR) under SICA[ii] which was set up for specific purpose to check the industrial sickness, miserably failed to address the issue due to inherent lacunas which were mostly used by defaulters to escape recovery action by banks/lenders. The Supreme Court commenting upon the object of the Code and inadequacy of the system under SICA, observed that:

> *"The object of the law is clear. A radical departure was contemplated from the erstwhile regime, which was essentially contained in The Sick Industrial Companies (Special Provisions) Act, 1985, and which manifested a deep malaise, which impacted the economy itself. To put it shortly, the procedures involved under the Act, simply meant procrastination in matters, where speed and dynamic decisions were the crying need of the hour. The value of the assets of the Company in*

distress, was wasted away both by the inexorable and swift passage of time and tardy rate at which the forums responded to the problem of financial distress. The Code was an imperative need for the nation to try and catch up with the rest of the world, be it in the matter of ease of doing business, elevating the rate of recovery of loans, maximization of the assets of ailing concerns and also, the balancing the interests of all stakeholders. The Code purports to achieve the object of maximization of the assets of corporate bodies, inter alia, which have slipped into insolvency[iii]."

The provisions of the Companies Act dealing with compromise and arrangements were very scantly used by stakeholders. Thus, the system needed a mechanism which could address both the issues and provide solution.

NEW LAW & REGIME UNDER IBC: At this stage, the new law governing insolvency in commercial world was brought out in the form of **Insolvency and Bankruptcy Code, 2016** (IBC/Code) based on the report submitted by the Bankruptcy Law Reforms Committee headed by Dr T K Vishawanathan[iv]. While the law was new, but it was mostly built upon the principles of the then existing mechanism under the Companies Act, 1956 and BIFR and practices followed in other jurisdiction such as UK and USA and UNCITAL Guide on Insolvency Law. Since the law was devised out of experience under SICA/BIFR, it provided in built checks to plug-in the loopholes under the previous regime.

THE CHANGES: The foremost change that was brought in the system was **limiting the jurisdiction of Courts to deal with commercial matters** as it was considered that such matters need to be left to experts. Lenders (**Committee of Creditors**) who were not only equal stakeholders in the fate of the enterprise but also competent to assess its viability, cause of sickness and also suggest and finalize viable options, were entrusted with the job. This later on got to be developed into the concept of "**Commercial Wisdom of the CoC**". In K. Sashidhar v. Indian Overseas Bank & Ors[v], the Supreme Court, inter alia, held that the National Company Law Tribunal ("**NCLT**") and the National Company Law Appellate Tribunal ("**NCLAT**") have no jurisdiction and authority to analyse or evaluate the commercial decisions taken by the committee of creditors ("**CoC**").

The Court laid down that "….. the commercial wisdom of the CoC has been given paramount status without any judicial intervention, for ensuring completion of the stated process within the timelines prescribed by the I & B Code. There is an intrinsic assumption that financial creditors are fuly informed about viability of the corporate debtor and feasibility of the proposed resolution plan. They act on the basis of thorough examination of the proposed resolution plan and assessment made by their team of experts. The opinion on the subject matter expressed by them after due deliberation in the CoC meeting through voting, as per voting shares, is collective business decision. The legislature, consciously, has not provided any ground to challenge the "commercial wisdom" of the individual financial creditors for their collective decision before the adjudicating authority. This is made nonjusticiable."

The new regime ushered in a new concept of "**Creditor in Control**" (as against "debtor in control" regime under BIFR) by divesting the promoters of the control of the enterprise and vesting it with the Resolution Professional with approving power on certain critical issue to CoC.

The law also separated the function of managing the insolvency process from court officials and vested it with Insolvency Resolution Professionals (IRPs/RPs).

Another significant change was limiting the timeline for completion of various actions connected with insolvency process.

To deal with the delays happening in proving the case of default, the system envisaged setting up of **information utility company** which will house all information about sanction, disbursement and default of Bank cases and whose certificate will be treated as final proof and evidence of default[vi].

The system also envisaged time bound admission and disposal of application by the judicial authority namely National Company Law Tribunals (NCLTs). Overall, the new system promised a robust and much needed specialized avenue for both the banking sector as well as for the industry.

THE BEGINNING: As the system was untested, it took some time and some impetus from the Government and Reserve Bank[vii] to accelerate the process of filing cases with the Tribunals under the provisions of IBC. The journey which started with the case of **Innoventive Technology Ltd**, has since completed more than four years. Since

inception of the Code in December 2016, 4,117 applications have been admitted as on December 31, 2020. Nearly 23 per cent of the cases admitted were settled or withdrawn after the commencement of Corporate Insolvency Resolution Process (**CIRP**[viii]). Out of the 1420 cases for which the CIRP process has been completed, liquidation has happened nearly 3.6 times the resolution as at this stage 73 per cent (799 cases) of cases undergoing liquidation and 33 per cent of cases (101 cases) undergoing resolution had been brought in from earlier regime under BIFR where most of the cases were practically dead. Having been able to revive 101 of such cases is an achievement. The CIRP for non-BIFR legacy has yielded 195 resolutions and 288 liquidations till December 2020. This also means that the resolution rate for non-BIFR legacy cases is more than three times higher at 40 per cent when compared to BIFR cases[ix].

Resolution Under IBC & Recovery for Banks: As per the statistic under the Economic Survey 2020-2021 Report, the Code has rescued 308 CDs (which owed Rs 4.99 lakh crore to creditors) as on December 2020 through resolution plans. The creditors recovered Rs 1.99 lakh crore, which is more than 193 per cent of the realisable value of such CDs. The recovery for financial creditors (FCs), as compared to their claims, was found to be more than 43 per cent. RBI data indicates that as a percentage of claims, scheduled commercial banks (SCBs) have been able to recover 45.5 per cent of the amount involved through IBC for the financial year 2019-20, (the amount recovered by SCBs under IBC was Rs 1.73 lakh crores) which is the highest as compared to recovery under other modes and legislations[x]. The recovery though not as expected but has yielded satisfactory results for the Banking Sector in the absence of any other effective alternative timebound mechanism.

COVID-19 pandemic has halted this process as the Government came out with the Insolvency and Bankruptcy (Amendment) Ordinance, 2020 on June 5, 2020 which

suspended initiation of the CIRP of a corporate debtor (CD) under section 7 though, personal insolvency remained outside this restriction.

TIME-LINE UNDER IBC & AREAS OF CONCERN: The IBC offered very promising and optimistic timeline for culmination of the CIRP within 180 days with only one extension of 90 days being allowed[xi]. The Code also prescribed time limit of 14[xii] days for admission of the application by Tribunals. This was very optimistic given the fact that under the previous regime of insolvency resolution took 4.3 years on an average. However, so far this time limit has remained a distant dream to be achieved. As per the Study by IBBI[xiii], the average number of days taken for admission of applications under CIRP is 133 days. As regards CIRP, the result in 308 CIRP cases which have yielded resolution plans by the end of December 2020, it took on average 441 days for the conclusion of the process. Similarly, the 1112 CIRPs, which ended up in orders for liquidation, took on average 328 days for the conclusion. Further, 181 liquidation processes, which have closed by submission of final reports till December 31, 2020, took on average 380 days for closure but most of such cases pertained to BIFR regime and the time taken liquidation process extends to almost two years as against the time of one year allowed under the Regulations. Thus, the actual timeline in cases both at admission and approval stage, remain a cause of concern and IBBI has been mulling various options to address this including bringing out an amendment in IBC and use of the word "mandatory completed[xiv]" but it has not yielded desired outcome so far. Not only delay at admission is a cause of concern but repeated challenges of such proceedings also affect the entire process. For example, in the case of *Reliance Communications Limited* the application was admitted on May 15, 2018, this order of NCLT was however, stayed in appeal by the National Company Law Appellate Tribunal (NCLAT) by its order dated May 30, 2018. The stay came to be vacated after 11 months on April 30, 2019. IBBI Research on delays under IBC note

that reducing the ***delay at stage of admission as one of the most important factors for securing success of IBC***.

Delay at approval stage (approval of resolution plan after it is recommended by CoC) has also impacted timely resolution and recovery for the Banks. IBBI study also note that 27.4% of the total delay is caused in taking approvals of the resolution plan from CoC. IBBI Study also point out that ***litigation is taking maximum time and there is an urgent need to develop the capacity of NCLT to reduce delay at two main stages i.e., admission & approval of resolution plan. A separate study needs to be done to evaluate whether the delay is due to a smaller number of judges at NCLT or whether the productivity of judges is not up to mark. The latter signifies the need for appropriate training as well as need for providing conducive environment and support in form of backend administrative functions which are vital for efficient performance of judicial function***.

BEHAVIOURIAL IMPACT: The single most achievement of IBC, if we may say so, apart from resolutions facilitated, is the fact that the Code has brought about significant and much needed behavioral changes among the creditors and debtors thereby redefining debtor-creditor relationship. Threat of losing control of the enterprise under CIRP has led to perceptible change in the manner the eco system looks at default. It was noticed that in the absence of a potent legal regime, defaulting to banks was not perceived as a threat by promoters as litigations before DRT or otherwise action under SARFAESI seldom posed threat of losing control of the enterprise. However, the Code delinked 'default' with lenders and thus paved way for initiation of CIRP even when the company is not in default to that lender. Threat of action under the Code has forced debtors to address and settle default expeditiously with the creditor, preferably outside the Code. It is very much visible from the fact that since the enactment of the Code in 2016, 18,892 applications that were dealt with, as many as 14,884 cases involving defaults of Rs 5.15 lakh crore were withdrawn

by September 2020 before admission and 897 processes were closed mid-way by December 2020. These figures indicate that almost 83 per cent of the CDs are getting resolved on the way, before the official commencement of CIRP under the Code on account of behavioral change among the defaulting debtors[xv].

Experience of cases under the Code has also forced the lenders to revisit the credit appraisal modules and mechanisms and built-in better risk mitigations.

ON THE LEGAL FRONT: The factors which could be said to be key for rapid and successful stabilization of the legal positions, have been timely initiatives by the Government by introducing timely amendment in the Code wherever needed and some landmark judgments by the Supreme Court which helped in accelerating the process and cutting short the time. In a short span of four years there were as many as four major amendments in the Code.

The first major amendment was introduced on 23rd day of November 2017 which, beside introducing other small amendments which were more of clarificatory nature, inserted section 29A in the Code which lead to exclusion of promoters and their related parties from CIRP. This provision eventually led to exclusion of promoter and its group entities in Essar case. The provisions are also applicable at the stage of liquidation.

The **second major amendment came by way of Ordinance of June 06, 2018**, this amendment, inter alia, defined the term 'related party', 'relative' in the context of provisions of section 29A. It also introduced **section 12A enabling withdrawal of application and paved way for settlement between parties at any stage before approval of resolution plan**. Section 14 was also amended to clarify the position that moratorium under section 14 of the Code will not include action against guarantors, thereby clearing deck for action against guarantors even while borrower is undergoing CIRP. It strengthened the position of the lenders. It also reduced the voting requirement for approval of resolution plan from original percentage of 75%

to 66%. This ordinance also brought in some important changes to clarify position of creditors who become shareholder of CD under a restructuring plan and excluded them from the definition of related party for the purpose of section 29A. This amendment also excluded Resolution Applicants under IBC from the exclusion under section 29A, where account of corporate debtor acquired by it continued to remain NPA or where avoidable transaction[xvi] were reported before approval of resolution plan. This amendment also introduced requirement of an affidavit by a resolution applicant to the effect that it is eligible to submit the plan as per the provisions of section 29A.

The amendment also resolved another major issue related to compliances with the provisions of the Companies Act, 2013 as regards various resolutions/ approval required on account of change in management and shareholding of corporate debtor by inserting an Explanation in section 30 of the Code to the effect[xvii]. Another important amendment related to application of Limitation Act to IBC. This was done by insertion of new section 238A[xviii]. Section 240A[xix] excluded MSMEs from application of clauses (c) and (h) of section 29A.

The **third amendment was introduced vide notification and amendment dated 06th August, 2019** which, inter alia, prescribed and inserted provisions relating to widening of scope of resolution plan to include merger, amalgamation and demerger (section 5(26) definition of resolution plan).

It also introduced the requirement under section 7 of the Code, requiring NCLT to record reasons if application is not admitted within the period of 14 days. It, as also discussed earlier, prescribed maximum time allowed for CIRP and limited it to 330 days including time spent in litigation.

From the lenders perspective it laid down requirement of minimum payment of their share of liquidation value to financial creditor who do not vote in favour of the resolution plan. **Another critical amendment related to recognition of inter-se**

priority of charge among the lenders which was an issue of intense debate till then. It inserted a new clause (4) in section 30 of the Code by laying down that *The committee of creditors may approve a resolution plan by a vote of not less than [sixty-six per cent. of voting share of the financial creditors, after considering its feasibility and viability, the manner of distribution proposed, which may take into account* ***the order of priority amongst creditors as laid down in sub-section (1) of section 53****, including the priority and value of the security interest of a secured creditor.*

Section 31 of the Code was also amended to clarify the legal position that on approval a resolution shall be binding on the corporate debtor and its employees, members, creditors, **including the Central Government, any State Government, or any local authority to whom a debt in respect of the payment of dues arising under any law for the time being in force, such as authorities to whom statutory dues are owed**, guarantors and other stakeholders involved in the resolution plan. This was in view of the experience that such statutory bodies and tax authorities were initiating action against CD even after approval of plan which extinguished such liabilities of CDs.

During 2020 the Code was amended twice by way of Amendment Act of March 2020 and then by way of Ordinance of June 05, 2020 which was later on replaced by Amendment Act of 2020 w.e.f. September 23, 2020. In between there was notification of March 18, 2020, which extended provisions of the Code to the reconstituted States and UT of Jammu and Kashmir.

March 2020 amendments mainly related to prescribing new requirements for filing of applications by home buyers and such other entities. From the resolution point of view, it introduced two critical provisions in section 14 of the Code, by clarifying that that a ***licence, permit, registration, quota, concession, clearance or a similar grant or right given by the Central Government, State Government, local authority, sectoral regulator or any other authority constituted under any other law for the time being in force, shall not be suspended or terminated on the grounds of***

insolvency, subject to the condition that there is no default in payment of current dues arising for the use or continuation of the license or a similar grant or right during moratorium period.

It also empowered a resolution profession of CD to considers and decided which of the services were critical for survival of CD and which would come under moratorium of section 14 of the Code.

It also introduced another critical and much needed provision in the form of new section 32A in the Code, which facilitated a ***'clean slate transfer'*** of corporate debtor to new resolution applicant after approval of resolution plan. It provided immunity to the Corporate Debtor and it new management from any liability or prosecution for offence committed prior to the commencement of CIRP. Such provisions are also available for sale of assets at liquidation stage.

The **Ordinance of June 05, 2020**, introduced a new section 10A to deal with the default caused on account of Covid-19 situation, by laying down that no application under section 7, 9 and 10 of the Code 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. It is noteworthy that such default is perpetually out of IBC ambit as no application can ever be filed for such default. The amendment has also excluded such COVID-19 period from filing any application on the ground of fraudulent transactions thereby providing leverage to the management to overcome difficulties faced on account of COVID-19 situation. By way of notification dated 22nd December 2020 provisions of section 10A have been extended for further period of three months from the 25th December, 2020.

JUIRISPRUDENCIAL HISTROY: If we look at jurisprudential history of IBC regime, Supreme Court has passed some of the landmark judgments which have helped further evolution and strengthening of IBC regime. The jurisprudence under IBC started with the case **of *Innoventive Industries Ltd v. ICICI Bank and Anr***, where the

Supreme Court upheld overriding effect of provisions of IBC over other enactments. While IBC did not lay down requirement of hearing a corporate debtor before admission of the application under IBC, but such requirement was built in by way of judgement of the Hon'ble Supreme Court which laid down '***where the statute is silent on the right of hearing, and it does not in express terms, oust the principles of natural justice, the same can and should be read into it'***.

As regards constitutional validity of the Code, the Hon'ble Supreme Court in the case of ***Swiss Ribbons Pvt. Ltd. & Anr. v. Union of India & Ors***, upheld the constitutional validity of the Code in its entirety.

In ***Arcelor Mittal India Pvt. Ltd. v. Satish Kumar Gupta*** case, the Court dealt with the issue of person acting jointly or in concert with other persons and referred to this as a ***'see-through provision'*** where each case would have to be examined on merits to determine whether, in the facts of a particular case, the disqualification would be applicable and whether certain persons were acting together or whether such persons shared an objective or purpose.

Constitutional validity of section 12A was upheld in the matter of Swiss Ribbons prior to this the view was that once the CIRP is initiated by admitting the application, it cannot be withdrawn nor can it be set aside 'except for illegality to be shown or if it is without jurisdiction or for some other valid reason'.

As regards the timeline, the Hon'ble Supreme Court in the case of ***Arcelor Mittal India Pvt. Ltd. v. Satish Kumar Gupta*** case, has laid emphasis on the need for adherence to strict timelines, however, it allowed exclusion of time taken in legal proceedings from the maximum period of 330 prescribed under the Code.

In the case ***of K Sashidhar v. Indian Overseas Bank***[xx] the Supreme Court again settled another important issue dealing with power of CoC and re-established the scheme of the Code by laying down that the ***role of Adjudicating Authority is limited to being***

satisfied that the plan, as approved by the CoC, meets with the requirements of section 30(2). Nothing beyond. AA has no jurisdiction or authority to analyse or evaluate the commercial wisdom of the CoC.

State Bank Of India Vs V. Ramakrishnan & Anr[xxi] the Apex court clarified that the moratorium under section 14 the Code will not apply to a personal guarantor to a corporate debtor. The case of ***B.K. Educational Services Private Limited Vs Parag Gupta And Associates***[xxii] clarified that application under IBC has to be initiated within the limitation period as prescribed under Article 137 of the Limitation Act. Supreme Court in its judgment in the case of ***Mobilox Innovations Private Limited vs. Kirusa Software Private Limited***[xxiii] has categorically laid down that IBC is not intended to be substitute to a recovery forum. NCLT can also reject the application if the notice of dispute has been received by the operational creditor or there is a record of dispute in the information and this view was reiterated in the case of ***Transmission Corporation Vs Equipment Conductors***[xxiv].

In a recent judgement[xxv] in the Supreme Court, to the much relief of former directors of companies undergoing CIRP, has clarified that proceeding under Section 138/141 of the Negotiable Instruments Act cannot be initiated or continued during the moratorium.

NCLAT in the case of ***Gulabchand Jain Vs. Mr. Ramchandra D. Choudhary*** clarified that CoC is empowered to take a decision to liquidate a CD even after an application has been filed by the Resolution Professional placing the Resolution Plan approved by the COC before the Adjudicating Authority for approval. NCLAT in the case of ***Bharat Aluminium Co. Ltd Vs. M/S J.P. Engineers Pvt Ltd***, clarified that the bank guarantee is not an asset of Corporate Debtor and Bank guarantee can be invoked even during moratorium under section 14 of the IBC in view of the amended provision under Section 14(3)(b) of the IBC.

However, despite introduction of section 32A, the issue of immunity of CD remain to the decided by the Supreme Court. While NCLAT, in the case of in ***JSW Steel Limited v. Mahender K. Khandelwal and others***, has held that the PMLA proceedings ought to be quashed against CD under the new management, however, an appeal against the judgment of the NCLAT is pending before the Supreme Court. In a separate case, Delhi High in the case of in ***Tata Steel BSL Limited and another v. Union of India*** , discharged the accused in proceedings filed against them before the trial court for alleged offences under the Companies Act, 2013, Companies Act, 1956 and the Indian Penal Code, 1860 consequent to approval of Tata Steel Limited's resolution plan for revival of the Bhushan Steel Limited under the IBC process. More recently, in ***Manish Kumar v. Union of India*** the Supreme Court dismissed a writ petition challenging the constitutional validity of Section 32A of the IBC while observing that ***the legislature ought be given freedom to experiment with economic laws and recognizing the imperative need for the IBC in the Indian context. The Court also*** held that the "extinguishment of criminal liability of the corporate debtor is apparently important to the new management to make a clean break with the past and start on a clean slate".

As regards the timeline, we notice a perceptible change at NCLAT level as number of judgements have come from the appellate authority laying down that Adjudicating Authority is statutorily bound to pass an order of admission or rejection on being satisfied in respect of debt, default and completeness of the application within 14 days from the date of filing of such application – ***Aditya Birla Finance Ltd. Vs. Sintex Prefab and Infra Ltd*****. However, at ground level a lot is desired to be done as admission of application (which is supposed to be done within 14 days time) is taking on an average more than 200 days.**

As regards the issue of admissibility of application under section 7 of the Code based on acknowledgement of debt, the position largely remained inconclusive on account

of divergent view taken by different Benches of NCLAT, however, the things appears to be clearing with the judgement of NCLAT in the case of **M M Ramachandran Vs. South Indian Bank Ltd. & Ors.** Decided on 22.01.2020, where NCLAT allowed admission of section 7 application of the Bank and extension of time of limitation on the basis of email under which the borrower had acknowledge its liability. Appeal filed against this judgement before the Supreme Court was also dismissed so by way of doctrine of merger NCLAT judgement got merged with the order of the Supreme Court. The Supreme Court in its judgement dated 26th March 2021, in the case of ***Laxmi Pat Surana Vs Union of India***[xxvi] has set the issue to rest.

EMERGING LEGAL ISSUES CLOGGING RESOLUTION: There are few major emerging issues which could impact resolutions under IBC (especially in large cases), one of course is ***shrinking market for resolution***. CD attracts proposals if it has inherent value and technology used by it is not changed (which is very unlikely) and it is viable in its market space. Since, there are few takers, the value offered hovers around liquidation value and in many cases substantially below liquidation value. This puts CoC in dilemma whether to approve such proposals or take the Company into liquidation. **The second issue which impact resolution in such cases is the role of dissenting creditors** who see opportunity to maximize their recovery (at least liquidation value) by dissenting. This position is getting stronger as now they have to be paid in cash that too in priority to assenting creditors in view of judgement of the Supreme Court in the case of ***Jaypee Kensington Boulevard Apartments Welfare Association*** [xxvii]. Thus, one group which see benefit in dissenting to a proposal is getting enriched at the cost of the other which is striving for a resolution and thus made to pay cost. This is happening in cases where resolution amount hover around liquidation value. In such cases if one dissent he is guaranteed minimum of his share of liquidation value as compared to the assenting group gets lesser amount as proposed in the Plan. It has created a situation where few FCs get incentivized by

dissenting to even a viable plan thereby putting assenting FCs to a disadvantageous position as usually the additional amount to be paid to dissenting FC (on account of their share of liquidation value) is taken out of the total amount proposed by a resolution applicant to Financial Creditors.

The third issue which could have wider ramification than mere resolution is "***inter se priority of charge holder***" during CIRP and at liquidation stage. Lending in India largely derive comfort from the security obtained from the Borrower. It not only work as a risk mitigant but also a critical factor influencing cost of funding. Inter-se priority of charge holder is well established and accepted norm not only in banking parlance but also in law. Section 48 of the Transfer of Property Act, 1882 lay down the principle governing the priority which is well recognized under section 30 and 53 of the Code. Supreme Court in its numerous judgements has recognized this principle while deciding the issue of priority in insolvency matters (**ICICI Bank Ltd vs Sidco Leathers Ltd. & Ors**[xxviii]**)**. Prior to this the legal position was settled by way of judgement of of Karnataka High Court in **State Bank of Mysore v. Official Liquidator & Ors**[xxix]. 1985 (58) Company Cases 609, wherein it was held that ". …. *In the result, the bank is entitled to realize that amount on a preferential basis as a secured creditor notwithstanding the fact that it filed the affidavit indicating that it stands within liquidation but subject to the reservation of its security being continued*."

However, due to few decisions which have been recently passed, courts have taken a divergent view which have the effect of nullifying this preference and position of a secured creditor in liquidation or CIR Process. This issue could have serious implication both on flow of credit and on resolution if the established and well recognized position of law is not restored.

The concept was well accepted and recognized by the Supreme Court in the case of **Committee of Creditors of Essar Steel India Limited Versus Satish Kumar Gupta &**

Ors[xxx]. The Supreme Court in its judgement had also explained the rationale behind obtaining security by lenders by with the following quote:

Rationale of security - The main purposes and policies of security are: protection of creditors on insolvency; the limitation of cascade or domino insolvencies; security encourages capital, e.g. enterprise finance; security reduces the cost of credit, e.g. margin collateral in markets; he who pays for the asset should have the right to the asset; security encourages the private rescue since the bank feels safer; security is defensive control, especially in the case of project finance; security is a fair exchange for the credit.

With a view to settle the issue the Section 30 of the Code was also amended, by inserting requirement for CoC to, inter alia, take into account the order of priority amongst creditors u/s 53 (1) **including the priority and value of the security interest of a secured creditor**, while approving a resolution plan.

Insolvency Law Committee Report of 2020 The issue was also considered by the Insolvency Law Committee Report of 2020, while dealing with the issue of relinquishment of the security under the Code and its effect on inter-se priority among the charge holder, the Committee had observed that ***this provision could not have been intended to provide secured creditors who relinquish their security interest, priority of repayment over their entire debt regardless of the extent of their security interest, as it would tantamount to respecting a right that has never existed. Further, if the "debts owed to a secured creditor" is not restricted to the extent of the security, there would be broad scope for misuse of the priority granted under Section 52(1)(b), as even creditors who are not secured to the full extent of their debt would rely on the mere fact of holding any form of security, to recover the entire amount of their unpaid dues in priority to all other stakeholders. The Committee had thus recommended that***:

7.4. On the basis of the above discussion, the Committee agreed that the priority for recovery to secured creditors under Section 53(1)(b)(ii) should be applicable only to the extent of the value of the security interest that is relinquished by the secured **creditor.** (unquote)

The sanctity of priority of charge has also been recognized in various other reports:

World Bank Report of 2015 Titled Principles for Effective Insolvency and Creditor/Debtor Regimes states:

"Claims and Claims Resolution Procedures Treatment of Stakeholder Rights and Priorities C12.1 The rights of creditors and the priorities of claims established prior to insolvency proceedings under commercial or other applicable laws should be upheld in an insolvency proceeding to preserve the legitimate expectations of creditors and encourage greater predictability in commercial relationships. Deviations from this general rule should occur only where necessary to promote other compelling policies, such as the policy supporting reorganization, or to maximize the insolvency estate's value. Rules of priority should enable creditors to manage credit efficiently, consistent with the following additional principles:

C12.2 **The priority of secured creditors in their collateral should be upheld and, absent the secured creditor's consent, its interest in the collateral should not be subordinated to other priorities granted in the course of the insolvency proceeding. Distributions to secured creditors should be made as promptly as possible.**

C12.3 Following distributions to secured creditors from their collateral and the payment of claims related to the costs and expenses of administration, proceeds available for distribution should be distributed pari passu to the remaining general unsecured creditors, unless there are compelling reasons to justify giving priority status to a particular class of claims. Public interests generally should not be given precedence over private rights. The number of priority classes should be kept to a minimum.

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"4. Ensuring equitable treatment of similarly situated creditors.

The objective of equitable treatment is based on the notion that, in collective proceedings, creditors with similar legal rights should be treated fairly, receiving a distribution on their claim in accordance with their relative ranking and interests. This key objective recognizes that all creditors do not need to be treated identically, but in a manner that reflects the different bargains they have struck with the debtor.." (unquote)

Therefore, the important issue would need to be settled to ensure smooth CIR Process under the Code.

PRE-PACKED INSOLVENCY: In view of delay happening under the CIRP under the Code, the system needed a more effective tool to address insolvency in cost effect and timely mechanism. Thus, demand for pre-pack was growing. The Government put in place this mechanism for MSMEs by way of Ordinance dated 04.04.2021 by which

section 54A TO 54P were introduced putting in placed mechanism for Pre-Pack for MSMEs. However, due to additional stages being introduced (approval by unrelated FC on the base plan and appointment of RP, filing of application, Order on Admission, Insolvency Process, approval of the plan and so on) and inherent constraint and limitation under base plan (which drastically limit scope of base plan), the Pre-Pack for MSME does not offer any better option to MSME as compared to normal CIRP (where MSME are eligible to submit plan (unless disqualited under section 29A and there is no limitation on haircuts to FC/OC or to any statutory body).

CONCLUSION: Thus, while there are challenges mainly on account of delay and hair cut,s but the legal position is slowly but surely getting clearer. However, a lot is required to be done to ensure timely admission and approval of plans. Delay at these stages is practically defeating the whole object of the Code as delay (at whatever stage) not only diminishes value of the enterprise but also reduces changes of resolution as it is seen that resolution applicants have moved applications to exit the process wherever there are inordinate delays in approval of plans.

On Personal insolvency front while the Supreme Court has cleared the way by way of judgement in the case of **Lalit Kumar Jain vs Union of India**[xxxi], however, still not much progress is noticed on admission front. Personal insolvency is an opportunity for guarantors as well as lenders to settle the dues within a limited time frame. Of late Banks have starting using provisions of section 95 against guarantors as it offers final and conclusive culmination of the process of recovery as against guarantors.

Two areas which remain wanting under the insolvency regime are **group insolvency and cross border insolvency**. It is experienced that when a parent company under a group default it affects the entire group and led to insolvency of all connected concerns within the group. Business structure of group is usually such that it works as single entity and thus needs a common resolution. But so far there are no express provision to deal with such matters an NCLTs/NCLAT have tried to find out solution

by clubbing the proceedings, the case under reference being Videocon Industries, however, in the absence of clear provisions it remain at the discretion of the Adjudicating Authority.

In a complex business mechanism where entity might have assets and business operation spread across many countries and jurisdiction, no single court can resolve the issue unless there is co-ordination and co-operation amongst the courts in different jurisdiction which could facilitate smooth conduct of process and its seamless implementation.

Overall, while there remain certain areas of concern, but as discussed earlier, the new regime has tried to address the real issues impacting resolution and default. It has successfully sent a message that one cannot survive if issue of financial constraints are not address within time. There is clear message to debtors and to creditors (as they suffered substantial haircuts under resolution plans) that there has to be serious efforts before planning a project and finance for it. Learning out of almost five years of experience under IBC will lead to strengthening of financial system in the Country in a long run.

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[i] Committee on the Financial System; M. Narasimham (1992). Narasimham Committee report on the financial system, 1991

[ii] Sick Industrial Companies (Special Provisions) Act, 1985

[iii] CIVIL APPEAL NO.10355 OF 2018 P. MOHANRAJ & ORS. … APPELLANTS VERSUS M/S. SHAH BROTHERS ISPAT PVT. LTD.

[iv] https://ibbi.gov.in/uploads/resources/BLRCReportVol1_04112015.pdf

[v] Civil Appeal No. 10673 of 2018

[vi] National E-Governance Services Limited is the only information utility so far set up under IBC which is functional and issuing such record of default to lenders.

[vii] Twelve large accounts were referred to NCLT under IBC, as directed by RBI in June 2017. Together they had an outstanding claim of Rs 3.45 lakh crore as against liquidation value of Rs. 73,220 crores.

[viii] CIRP is the name given to the process which gets triggered with admission of application against a corporate debtor. It puts in place a moratorium which protects the enterprise from any enforcement or legal actions. Board of Director are suspended, and RP takes control of the operation of the Company and invite resolution plans from interested parties which are considered by CoC. If proposal is found viable and approved by 66% vote of CoC it is filed with NCLT for approval and no plan is received or no plan is found viable, the company then goes into liquidation process based on order of NCLT.

[ix] Source: Economic Survey of India 2020-21

[xx] Source: Economic Survey of India 2020-21

[xi] Section 12 of the Code

[xii] Section 9 of the Code

[xiii] Assessment of Corporate Insolvency and Resolution Timeline

[xiv] Code was amended by the Insolvency and Bankruptcy Code (Amendment) Act, 2019 inserted a proviso to sub-Section 3 of Section 12 to the effect that the CIRP shall mandatorily be completed within a period of 330 days from the ICD, including any extension of the period of CIRP and the time taken in legal proceedings in relation to such CIRP.

[xv] Source: Economic Survey of India 2020-21

[xvi] These are preferential transactions (section 43), undervalued transactions (section 44), transaction defrauding creditors (section 49), extortionate transactions (section 50). Section 29A debars any application from proposing a plan if such party was responsible and or has been promoter or in the management or control of a corporate debtor in which such transactions has taken place and in respect of which an order has been made by the Adjudicating Authority under the Code.

[xvii] that if any approval of shareholders is required under the Companies Act, 2013(18 of 2013) or any other law for the time being in force for the implementation of actions under the resolution plan, such approval shall be deemed to have been given and it shall not be a contravention of that Act or law"

[xviii] Limitation. – The provisions of the Limitation Act, 1963 (36 of 1963) shall, as far as may be, apply to the proceedings or appeals before the Adjudicating Authority, the National Company Law Appellate Tribunal, the Debt Recovery Tribunal or the Debt Recovery Appellate Tribunal, as the case may be.

[xix] 240A. Application of this Code to micro, small and medium enterprises. –(1) Notwithstanding anything to the contrary contained in this Code, the provisions of clauses (c) and (h) of section 29A shall not apply to the resolution applicant in respect of corporate insolvency resolution process of any micro, small and medium enterprises.

[xx] (2019) 12 SCC 150

[xxi] Judgment dt. 14.08.2018

[xxii] Judgment dt. 11.10.2018

[xxiii] CIVIL APPEAL NO. 9405 OF 2017 dated 21.09.2017

[xxiv] CIVIL APPEAL NO. 9597 OF 2018 dated 23.10.2018

xxv Mohanraj & Ors. Vs. M/S. Shah Brothers Ispat Pvt. Ltd. – Supreme Court

[xxvi] Civil Appeal No. 2734 pf 2020 decided on 26.03.2021

[xxvii] JAYPEE KENSINGTON BOULEVARD APARTMENTS WELFARE ASSOCIATION & ORS..... APPELLANT(S) VERSUS NBCC (INDIA) LTD. & ORS. CIVIL APPEAL NO. 3395 OF 2020 decided on 24.03.2021

[xxviii] Appeal (civil) 2332 of 2006 dated 28.4.2006

xxix 1985 (58) Company Cases 609

xxx CIVIL APPEAL NO. 8766-67 OF 2019

[xxxi] TRANSFERRED CASE (CIVIL) NO. 245/2020 decided on 21.05.2021