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Avinash Kumar

Avinash Kumar has completed his Ph.D. in International Investment Law from the Dept. of Law & Governance, Central University of South Bihar. His research work is on "International Investment Agreement and State's right to regulate Foreign Investment." He qualified UGC-NET and has been selected for the prestigious ICSSR Doctoral Fellowship.He is an alumnus of the Faculty of Law, University of Delhi. Formerly he has been elected as Students Union President of Law Centre-1, University of Delhi.Moreover, he completed his LL.M. from the University of Delhi (2014-16), dissertation on "Cross-border Merger & Acquisition"; LL.B. from the University of Delhi (2011-14), and B.A. (Hons.) from Maharaja Agrasen College, University of Delhi. He has also obtained P.G. Diploma in IPR from the Indian Society of International Law, New Delhi.He has qualified UGC – NET examination and has been awarded ICSSR – Doctoral Fellowship. He has published six-plus articles and presented 9 plus papers in national and international seminars/conferences. He participated in several workshops on research methodology and teaching and learning.

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Corporate Insolvency Resolution Process In India: A Comparative Study

Authored By- Kamya Sharma

Abstract

The Insolvency and bankruptcy code, 2016 is the bankruptcy law of India which seeks to consolidate the existing framework by creating a single law for insolvency and bankruptcy in the past insolvency regulation process included operations of simultaneous acts . In this it was changed and several insolvency laws were consolidate which creating a single law. These include the Sick Industrial Companies Act, 1985. The recovery of debt due to banks and financial Institutions Act, 1993, the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 and the Companies Act, 2013. This code provides a genuine rehabilitation and restructuring of the company. The IBC process gives substantial power to financial creditors, both domestic and foreign.

Keywords: Insolvency and bankruptcy code, 2016, Sick Industrial Companies Act, 1985,Recovery of Debt due to Banks and Financial Institutions Act, 1993, the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002&Companies Act, 2013.

1. Introduction

This code is a reflection of radical thinking, It enables creditors to restructure bad debt by a process of CIRP where It includes various steps to raise fresh funds or look for a new buyer to sell the company that is included in the resolution plan which if accepted may revive the company and if rejected by the committee, the company shall go into liquidation subject to the order of the tribunal.

2. Object Of Insolvency Law

The main object of this law is to provide the help and benefit to the innocent debtor who is not able to pay his outstanding debts due to the unforeseen conditions and the another object is to fulfill the claims of the eligible creditors by distributing the assets of the debtor equally among them by the procedure established by the law.

In the case of YenamullaMalludora vs P.Seetharatna[1], Supreme Court of India observed, The object of the law of insolvency is to seize the property of an insolvent before he can squander it and to distribute it amongst his creditors. It is however not every debtor who has borrowed beyond his assets or even one whose property is attached in execution of his debts, who can be subjected to such control. The jurisdiction of the Court commences when certain acts take place which are known as acts of insolvency and which give a right to his creditor to apply to the Court for his adjudication as an investment.

3. Historical Development Of The Insolvency And Bankruptcy

Insolvency laws were originates from the English laws. According to the section 23 and 24, Government of India Act, 1800, the Supreme Court was having the jurisdiction for dealing the cases related to the insolvency. After that Indian Insolvency Act, 1848, came into force, but the provisions of the act were not helpful to meet the requirements of the growing economy. After that the Presidency Town Insolvency Act, 1909, came into force and along with that another legislation named, Provincial Insolvency Act, 1920 was enacted. Both these legislations were helpful to resolve theindividual insolvency and insolvency related to the sole proprietorship, and partnership even their formal content was same but there is a difference in the jurisdiction. Presidency Town Insolvency Act, 1909 applied only on the presidency towns like madras, Bombay, Kolkata etc. but Provincial Insolvency act applied on other towns. After that Companies Act, 1956 came into force

[1] AIR 1966 SC 918.

to resolve and reorganization of insolvent corporate entity through the procedure of winding up[2]. Part VII of section 42 to 56 of the companies act 1956 makes provisions deals with mode of winding up cases in which the company may be wound up the court.[3]After that Sick Industrial Companies Act, 1985 was enacted which introduced the provisions for restructuring and reorganization of the corporate entity.

Constitution of India give powers to the legislatures to make laws on the subject of Insolvency and Bankruptcy under entry 9 list III. To make the strict regulations related to the insolvency various committees were set up by the government to give their recommendations. In the Budget speech of the 2014-2015, the government of India announced to develop a framework for the insolvency resolution and reorganization of corporate and individual entity. And for the development of framework a committee was established which was headed by Shri T.K. Viswanathan.

4. Stages Of CIRP

1. DEFAULT: Section 4 talks about the application of part 2 of the code to the corporate persons. It says that it applies where the minimum amount of the default is at least 1 lakh, however, there is a provision that states that the central government has the power to increase the limit to 1 crore which has been done recently by the central government on 23rd of march 2020.

2. INITIATION OF CIRP: Following persons can initiate the CIRP;

- *Financial creditor*: those people whose relationship with the corporate debtor is based on a financial contract. Under section 7 they can initiate CIRP by proposing the name of the IRP and also they must prove the existence of a default on the part of the corporate debtor by facilitating any records.
- *Operational creditors*: are the creditors that have their credit due to their day to day operations of the business .it is given in section 5 (20). Their liabilities come from the operations of the business. Section 8&9 talks about the filing of an application by operational creditors. So, besides the requirements of that is needed by the financial creditor to be fulfilled there are 3 more steps to be fulfilled that are firstly operational creditor has to give notice to the corporate debtor demanding the payment of the unpaid operational debt

[2] Section 2 (94A) of the Companies Act, 2013.
[3]Mevorach, I., 2009. Insolvency Goals in Legal Systems. In Insolvency within Multinational Enterprise Groups. pp. 105–126.

- after waiting for the reply for 10 days to such notice by proving there was an existence of a dispute and that is why the corporate debtor has not paid the amount or else it will pay back the operational creditor. So if nothing of this happens in such 10 days then the operational creditor can begin to apply to section 9 of the code. Under this section operational creditor, they shall furnish a copy of the invoice that demanded payment from the corporate debtor and affidavit that there is no notice given by the corporate debtor as to the existence of a dispute.
- *Corporate debtor*: Under section 10 of the IBC they shall with the application furnish a special resolution that has been passed by the shareholders of the corporate debtors or the resolution passed by the 3/4th of the members of the corporate debtor in case it was a firm. It will also have to propose the name of the interim resolution professional and like the other two, they will also have to prove the existence of the default.

3. ADMISSION OR REJECTION BY THE ADJUDICATING AUTHORITY: Here the adjudicating authority is National Company Law Tribunal. When an application is filed in the NCLT it should see it as a whole. It shall see whether the application is complete in the aspects of filing of forms and other various documents that are necessary under the sections. It shall also check the evidence of default and the records and necessary documents corroborating it. The authority also has to check with the IBC Board of India that the proposed interim resolution professional does not have any disciplinary proceedings pending against him. Apart from these 3 aspects if an application is submitted by operation creditor it shall also have to submit an affidavit saying there was a dispute between him and the corporate debtor.

4. COMMITTEE OF CREDITORS: The day of the admission of the application in NCLT is known as the insolvency commencement day. Now the adjudicating authority appoints an interim resolution professional and on this day itself, there will be a declaration of a moratorium. By day 3 a public announcement is made in form A which invites claims from people who may have some claims due to the corporate debtor. It shall be published in an English newspaper as well as in the vernacular paper. The people may submit their claims by day 14 of the process. By day 21 the claims submitted shall be verified, they will start the verification within 7 days from the last submission of the claim by the IRP and after the verification, he will constitute a committee of creditors report the constitution to NCLT. Till day 30 the first meeting of the committee should be done. The primary matter they discuss is whether to continue with the same IRP or change him.

The interim resolution professional is granted 180 days to find a resolution that can be extended by 90 days and it should be mandatorily completed by 330 days. "If the IRP fails to find a resolution by then, the company is liquidated and is directed to pay the creditors. Appeals can be filed in NCLAT. In Quantum Limited v. Indus Finance Corporation, the application seeking an extension of the CIRP was filed after the expiry of 180 days. The NCLT rejected the application as it was not filed before the expiry of 180 days. An appeal was filed and while allowing the appeal, the NCLAT held that the provisions of the Code do not require the applicationto be filed before the expiry of the 180 days. Further, the NCLAT excluded the period between the 181st day and the passing of the order."[4]

5. Comparative Analysis Of Insolvency Laws

One of the usual questions that arises in our minds is how is the Indian IBC 2016 compared to other Insolvency Codes practiced internationally. Since Internationally Insolvency and bankruptcy laws have been in place for a long time, have dealt several cases a look into their laws may give some more insight. As we know, IBC 2016 was enacted in May 2016 and is therefore, young and evolving. It should be really appreciated how proactively and speedily the regulator (IBBI) is reacting to each and every emerging situation by bringing rules and regulations to deal with various situations appropriately.

1.UNITED KINGDOM: A vast majority of legal systems in the most countries are founded as English Common law. Hence, it is not a surprise that the Code closely mirrors the UK Insolvency Regime. Although the Indian Insolvency and Bankruptcy Code, 2016 is based on the UK structure, India has identified key aspects of the legislation that might not work in an Indian scenario, and therefore appropriately customized it for India.

2. UNITED STATES: Chapter 11 of US Bankruptcy Code focuses on preserving reorganisation or going concern value over liquidation value. As a corollary, Chapter 11 assumes that the most efficacious way to achieve that result is to retain management and enable multiple outcomes either through a plan of reorganization, series of going concern sales and even a liquidation plan. Chapter 11 enables a wide range of proposals to be put into a reorganization plan, including having the company and its management survive the process. Chapter 11 cases fall into two general

[4]Computation Of Time Period Of Corporate Insolvency Resolution Process - Insolvency/Bankruptcy - India (mondaq.com)

categories: the "freefall" case or a pre-packed to pre-negotiated case. In the former, relief is sought under Chapter 11 of the Bankruptcy Code without having an agreed strategy among the company and at least a critical mass or core group of creditors.

3. AUSTRALIA: There are separate insolvency regimes in Australia for insolvent corporations. The insolvency regime in Australia in primarily governed by the Corporations Act, 2001 ("the Corporations Act") and its associated regulation, which provides the legislative framework for corporate insolvencies, and the Bankruptcy Act 1966 ("the Bankruptcy Act") and its associated regulations, which provides a statutory regime for insolvent individuals. The position in Australia is that the key test of solvency is the 'cash flow' test, rather than the 'balance sheet' test.

The Insolvency and Bankruptcy regime in Australia in constantly evolving through chances and reforms brought into the law. One such major overhaul of Insolvency regime in Australia is the introduction of the Insolvency Law Reform Act, 2016 (ILRA) which has amended different legislations like the Bankruptcy Act, 1996, the Corporations Act, 2001 and the Australian Securities and Investment Commission Act, 2001.

4. GERMANY:The purpose of German insolvency proceeding is to jointly satisfy the creditors by utilizing the assets and distributing the proceeds, or by deviating from an insolvency plan, in particular to preserve the company. The honest debtor is given the opportunity to free himself from his remaining liabilities. The German Insolvency regime is regulated by the Germany Insolvency remaining liabilities. The German Insolvency regime is regulated by the Germany Insolvency Code ("InSO"). It is centralized on federal level. Thus, the 16 single states of Germany do not have their own applicable insolvency law. Insolvencies in Germany are mainly governed by the Insolvency Code ("**Code**") which was enacted on 5th October 1994 which applies to all regardless of which industry a debtor is in.

5. SINGAPORE: Singapore's system of Insolvency laws comprises procedure for liquidation as well as rehabilitative debt restructuring procedures. The main types of proceedings within the latter category are judicial management and schemes of arrangement. The key statue governing insolvency and corporate rescue mechanisms in Singapore is Chapter 50 of the Companies Act, 1967. Parliament passed significant amendments to various insolvency and debt restructuring provisions in the companies Act in 2017 and those have come into force with effect from 23 May 2017.

6. Conclusion

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The objective of our paper is to analyze the corporate insolvency resolution process of India, and some other countries. The underlying motivation of this exercise is to highlight the similarities as well as differences across the laws and procedures of these three countries and to learn important lessons for India, in context of the formation of a new committee in 2014 to reform the country's corporate bankruptcy law. The fragmentation of the existing legal framework and the delays in enforcement in India have created incentives for rent seeking by various participants in the insolvency process. If a robust market for credit is to develop in India, the corporate insolvency process must give clarity to all debtors as well as all classes of creditors about the procedures and rules to deal with in an event of insolvency. Only then will a credit market without concentration of any one class of debtors or creditors can develop.

Another key element of an effective insolvency resolution framework is to create a strong and well-defined liquidation law, which can act as a viable threat forcing parties into reorganization. While the reorganization procedures themselves need to be effective and well designed, a timely and well-enforced liquidation mechanism will create substantial incentive for the parties involved to push for reorganization. Finally, the insolvency resolution law should be such that at various points in the entire process there should be clear predictability of outcomes, well written rules under the laws clarifying procedures, as well as specific and clearly defined timelines, so as to design a resolution framework that will minimize the probability of default and maximize the loss given default. Furthermore, mechanisms need to be built at every stage of the law to create sufficient disincentives for strategic behaviour by the parties involved. Likewise, the IP system must also be a strong one such that their objectives are aligned with those of the insolvency resolution system. While the corporate insolvency resolution law can lay out clear and well-defined provisions governing the procedures at each stage, effective and timely resolution of an insolvency case will depend to a large extent on the efficiency with which those provisions and rules are enforced. Hence the success of the new law proposed by a committee in any country including India will depend critically on the extent to which good institutions can be created and adequate State capacity can be built.