E-mail - indianjournaloflawandci@gmail.com

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THE INSOLVENCY AND BAKRUPTCY CODE (AMENDMENT) ORDINANCE 2020- A STEP TOWARS PROTECTING BUSINESSES AGAINST THE PANDEMIC

Author-

Divya Raj

Student

RMLNLU, LUCKNOW

ABSTRACT

In the present paper, the author has analysed the The Insolvency and Bakruptcy Code (Amendment) Ordinance 2020 as a regulatory method of the government to help the businesses and the MSMEs to get through the pandemic and the nationwide lockdown which was imposed in India. The government made a few announcements in march-april 2020 and on 5th June 2020 the ordinance was passed. At first the minimum threshold for initiating Corporate Insolvency Resolution Process was raised from INR 1 lakh to INR 1 crore and then the Ordinance was introduced. The ordinance puts a bar on the initiation of insolvency proceedings against a corporate debtor by the financial creditors, the operational creditors, the debtor himself and the resolution professional for defaults arising on or after 25th March, 2020. It also has retrospective affect starting from 25th march 2020 for a period of six months or for a period not exceeding one year as may be notified by the government. The new minimum threshold would be applied prospectively and it does not even have a time limit of operation. In the paper the researcher has reiterated the pros and cons of the ordinance.

KEYWORDS- Insolvency, Bankruptcy, Amendment, Ordinance, Default, Maintainability of application, NCLT.

INTRODUCTION

COVID-19 is nothing short of a catastrophe straight out of Pandora's box. It is a pandemic which is defining the global health crisis of the present time. It is not just a health crisis but also a socio-economic quandary. With the unprecedented spread of the coronavirus to most of the world, country after country retorted to measures of applying lockdown in an attempt to stop the spread of the disease. India went into a nationwide lockdown for 21 days which had adverse effects on the economy. People lost their jobs and source of income with absolutely no knowledge of when things would return to the status quo. It also affected various businesses in varied sectors. In an attempt to save the distressed businesses from being pushed towards insolvency because of the upheavals caused by COVID-19, the government of India introduced various regulatory measures. One of the latest measures is the amendment to the Insolvency and Bankruptcy Code, 2016.

On 5 June 2020, the President promulgated the Insolvency and Bankruptcy Code (Amendment) Ordinance, 2020 with immediate effect. The *raison d'être* for the ordinance as suggested by its preamble is, amongst others, to:

1. prevent companies, which are experiencing distress on account of the COVID-19 pandemic, from being pushed into insolvency proceedings, and
2. exclude defaults arising on account of the COVID-19 pandemic for the purpose of insolvency process under the Insolvency and Bankruptcy Code, 2016. [1]

The Ordinance has inserted section 10A which states that no application shall be filed under section 7, 9, and 10 of the Insolvency and Bankruptcy Code for the initiation of the corporate insolvency resolution process against a corporate debtor for any default arising on or after 25th March 2020 for a period of 6 months or for a period not exceeding one year ('Suspension Period') as may be notified by the government at a later time.

Further, the ordinance also amends section 66 of the Code by barring a resolution professional from filing an application against the director or partner of the corporate debtor with respect to defaults arising within the Suspension Period even if the default is because of the malpractices and fraudulent activities of the people.

Earlier, in view of the economic distress caused by COVID-19, the Reserve Bank of India, vide circulars issued on 27th March 2020[2] and 23rd May 2020[3], permitted lending institutions (including commercial banks and non-banking financial companies) to allow a moratorium of 6 months on payment of instalments in respect of all term loans outstanding as on 1st March, 2020. Further, in respect of working capital facilities, the lending institutions were permitted to defer recovery of interest for a period of 6 months. The Ordinance appears to align the suspension of insolvency process with the moratorium/deferment permitted by the RBI.

[1] The Insolvency and Bakruptcy Code (Amendment) Ordinance, 2020.
[2] https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11835&Mode=0
[3] https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11835&Mode=0

SECTION 10A AND ITS PROVISO

Section 10A of the Insolvency and Bankruptcy Code states that:

"Section 10A: Suspension of initiation of corporate insolvency resolution process

10A. Notwithstanding anything contained in Sections 7, 9 and 10, no application for initiation of corporate insolvency resolution process of a corporate debtor 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.

Provided that no application shall ever be filed for initiation of corporate insolvency resolution process of a corporate debtor for the said default occurring during the said period.

Explanation: For removal of doubts, it is hereby clarified that the provisions of this section shall not apply to any default committed under the sections before 25th March, 2020."[4]

On a plain reading of the Section it transpires that the operative part of the section as well as the proviso to the section both deal with the same subject matter i.e., the default arising on or after 25th March, 2020. The enacting part seems to give a temporary relief to the corporate debtors by prohibiting the initiation of a corporate insolvency resolution process under Section 7,9, and 10 of the Code for '*a period of six months or such further period, not exceeding one year from such date*'[5] but the rider to the section seems to provide a blanket immunity to the same. The proviso provides that "no application shall ever be filed"[6] with respect to the default arising during the Suspension Period. The ordinance does not provide any clarification as to why there is a permanent immunity to such defaults. At its heart, the ordinance is supposed to help the businesses from going bankrupt but it leaves the creditors high and dry. Even in cases of continuing defaults, i.e., the default that began in the suspension period and have not been taken care of after the aforesaid period, the creditors will not be able to procure a remedy under the Code unless a fresh fault occurs after the suspension period. The creditors will have to pursue other forms of recovery as the ordinance does not affect remedies provided under other statutes such as the restructuring schemes, schemes under the Companies Act, 2013, filing an application against the debtor before the DRT under the SARFAESI Act, 2002, proceeding against the corporate guarantor of the principal debtor etc. Operational creditors on the other hand do not have so many options to procure a remedy as is enjoyed by the financial creditors. The most that the operational creditors, especially the MSME's could do is file a suit under the commercial court or civil court, or file for remedies under the MSME act, 2006, or proceed under the Arbitration & Conciliation Act, 1996 subject to the existence of arbitration agreement

In furtherance of the blanket prohibition, the ordinance has also prohibited voluntary initiation of the corporate insolvency resolution process under Section 10 of the code. The objective of the same is not limpid as it only takes away the recourse of the corporate debtor who is willing

[4] The Insolvency and Bakruptcy Code (Amendment) Ordinance, 2020.
[5] The Insolvency and Bakruptcy Code (Amendment) Ordinance, 2020.
[6] The Insolvency and Bakruptcy Code (Amendment) Ordinance, 2020.

to subject himself to the insolvency procedure. Since an application cannot be filed by the resolution professional under Section 66(2) of the code as well, an application under Section 10 should have been permitted to be filed so as to provide flexibility to the corporate debtor, who notwithstanding covid-19 and its impacts and after careful scrutiny makes an informed assessment that it is unable to continue as a going concern. It would have also helped to maintain the efficiency of the market. The corporate debtor may look forward to other remedies such as voluntary liquidation under the Code and the winding up mechanism for specified companies defined under the Companies Act, 2013 read with the Companies (Winding up) Rules, 2020.

THE MINIMUM DEFAULT UNDER THE CODE

The Ministry of Corporate Affairs vide notification dated 24.03.2020, amended the Insolvency and Bankruptcy Code to raise the minimum amount of default to INR 1 crore from the previous amount of INR 1 lakh. This was done with a view to prevent the banks from filing an application under insolvency regime for an insignificant loan amount and to protect the businesses from any hardship and abuse that they might face because of the pandemic. By raising the minimum threshold for filing an application under the code, the creditors will now have to retort to methods outside of the Insolvency and Bankruptcy Code which would in turn help to unclog the judicial system that is currently overcrowded with bogus applications. This raise will also benefit the micro, small and medium enterprises. In the case of *Pankaj Aggarwal v. Union of India and Ors*[7], the NCLT observed that the purpose behind this increase was to benefit the MSMEs so that they "were not inflicted with sudden insolvency proceedings as they may have faced set-backs during the lockdown period."[8] The notification does not prescribe a time limit to this increase i.e., it is nowhere stated that this increase in the minimum amount is only for the period of the pandemic. The NCLT clarified the position of the notification in the case of *Foseco India Limited* vs *Om Boseco Rail Products Limited* (NCLT, Kolkata)[9], and *Arrowline Organic Products Pvt. Ltd.* vs. *Rockwell Industries Limited* (NCLT, Chennai)[10], and held that the amended threshold would apply prospectively.

THE DETERMINATION OF DATE OF DEFAULT

The Ordinance revolves around the same subject matter i.e., default arising on or after 25th March, 2020. It has become of utmost importance for the Adjudicating Authority to determine the date of default. Creditors have to take care that the default they are filing against is either from before the suspension period or after it because the proviso to Section 10A puts a

[7] Pankaj Aggarwal v. Union of India and Ors.
[8] Pankaj Aggarwal v. Union of India and Ors.
[9] Foseco India Limited vs Om Boseco Rail Products Limited (NCLT, Kolkata)
[10] Arrowline Organic Products Pvt. Ltd. vs. Rockwell Industries Limited (NCLT, Chennai)

prohibition on the filing of any corporate insolvency resolution process for the default arising during the suspension period.

Now the question arises that whether the amendment would be applicable on the cases already pending before National Company Law Tribunal on 5th June, 2020 which are pertaining to the default which took place on or after 25th March, 2020. The National Company Law Tribunal, Chennai Branch held in the case of *Siemens Gamesa Renewable Pvt Ltd vs Ramesh Kymal* that the provisions of section 10A would apply retrospectively even in case of the defaults arising on or after 25 March 2020 but prior to 5th June, 2020. For a better understanding of the same, here are a few scenarios as to when the application filed under IBC would be maintainable or not:

- If the date of default is before 25th March, 2020 and the date of application with NCLT is also before 25th March, 2020, then the application will be maintainable even after the Ordinance.
- If the date of default is after 25th March, 2020 and the date of application with NCLT is also after 25th March, 2020, then the application will not be maintainable after the Ordinance.
- If the date of default is before 25th March, 2020 for an amount which is less that INR 1 crore and the date of application with NCLT is after 25th March, 2020, then the application will not be maintainable after the Ordinance.
- If the date of default is before 25th March, 2020 for an amount which is more that INR 1 crore and the date of application with NCLT is after 25th March, 2020, then the application will be maintainable after the Ordinance.

In the above scenarios it is seen that the maintainability of the application after the ordinance comes to effect is dependent of the date of the default, the date of making the application to the NCLT and the default amount against which the application is being filed. Further in an order[11] issued by the NCLT, the period of lockdown was excluded from the statutory period in respect of the pending corporate insolvency resolution process. It did not amend or increase the statutory period of 180 days or 270 days required for the process but excluded the period of lockdown from the timeline.

AMENDMENT TO SECTION 66 OF THE CODE

Section 66 of the Insolvency and Bankruptcy code, 2016 talks about the fraudulent trading or wrongful trading of the directors/partners of the corporate debtor. Under Section 66(2) of the Insolvency Code, during the CIRP of a corporate debtor and upon an application filed by the resolution professional with the relevant National Company Law Tribunal, the directors or

[11] https://nclat.nic.in/Useradmin/upload/5186278465e81baf8ac471.pdf

partners of the corporate debtor can be ordered to personally contribute to the corporate debtor's assets if the director or partner knew or ought to have known that there was no reasonable prospect of avoiding CIRP and did not exercise due diligence to minimize potential losses to creditors. The Insolvency Ordinance now inserts sub-section (3) to Section 66 of the Insolvency Code, which states that:

"(3) Notwithstanding anything contained in this section, no application shall be filed by a resolution professional under sub- section (2), in respect of such default against which initiation of corporate insolvency resolution process is suspended as per section 10A"[12]

This change has been brought upon to help the directors and partners act more confidently and efficiently towards the betterment of the company without any threat of personal liability but the same can be misused by some people as it provides unwarranted protection to them. They can carry their malpractices without any fear of prosecution for the same.

[12] The Insolvency and Bakruptcy Code (Amendment) Ordinance, 2020.

CONCLUSION

COVID-19 has turned the world upside down. People and businesses faced so distress both health-wise and economically. In order to help the businesses in such difficult times the government introduced various regulatory measures. One of the measures was the amendment to the Insolvency and Bankruptcy Code, 2016. The Insolence and Bankruptcy (Ordinance) 2020 introduced Section 10A which prohibited the initiation of the Corporate Insolvency Resolution Process under section 7,9, and 10 of the code for defaults arising on or after 25th March 2020 and Section 66(3) prohibits a resolution professional from filing an application against the corporate debtor. The ordinance was passed bonafide to help the businesses and the MSMEs from being grabbed by the clutches of insolvency in the pandemic period but the amendments made are capable of being misused and are very rigid. There is no recourse given to a corporate debtor that wants to subject itself to the insolvency proceeding notwithstanding the impact of covid-19 on itself. Further it would be misused by the management of a company for malpractices as they are provided with immunity under section 66(3). No doubt the amendments will help many firms to stay in the market and successfully go through the pandemic without any harassment from the creditors as the minimum threshold has also been increased to INR 1 crore and the lockdown period has been excluded from the pending CIRP but there still needs a lot of work done towards smoother functioning of the system as certain unintended consequences also flow from it. People might abuse the provisions as there is no distinction made between defaults arising on account of covid-19 and those which are completely independent of the upheavals caused by covid-19. Further, there should be more emphasis on the out of court settlement regime as after the ordinance the creditors will be left with remedies available outside the code.

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