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Code Correction

The Insolvency Resolution Process (IRP) is one such mechanism under the IBC where the NCLT initiates a Corporate Insolvency Resolution Process (CIRP) when a company defaults on making payments to creditors

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Not Long Ago, if a company that had lent money to another company went to court to recover the amount, it would on average take a crushing 4.3 years for the dispute to be resolved. Today, it takes roughly one-fourth the time, or 394 days on average to settle such matters. We have the Insolvency and Bankruptcy Code, 2016 (IBC) to thank for this. Still, IBC needs to do better than this and bring the average time taken for resolution down to 330 days, the timeline prescribed in the code.

Similarly, under IBC, if a resolution plan is not approved by the committee of creditors within the stipulated 270 days, the NCLT or the National Company Law Tribunal can order the liquidation of the defaulting company. But somehow matters have tended to drag on for longer durations.

Four years after the code came into being, it is yet to achieve the timelines it set for itself for resolution of corporate disputes. According to experts, there are issues galore that have prevented IBC's optimal functioning.

Says Senior Advocate U.K. Chaudhary, "For more than six months now, there is no president of the National Company Law Tribunal and no chairperson of National Company Law Appellate Tribunal (NCLAT). Both institutions are headed by Acting President and Acting Chairperson, respectively. This in itself reflects the apathy of the Central government towards tribunals. It is baffling as to why the Central government cannot treat the tribunals seriously and take timely measures to ensure the smooth working of such important tribunals dealing with high stake matters of trade and industry under the Companies Act and the Insolvency and Bankruptcy Code."

'Under Construction'

The Insolvency and Bankruptcy Board of India (IBBI) concedes that the IBC has been a 'road under construction' for good reasons. It may have started as a plain vanilla process but underwent 'course correction' in order to serve its inherent purpose. And what is its purpose? The three main orders of IBC, amongst others, are 'resolution', 'maximisation of value' of assets of firms, and then promoting entrepreneurship, ensuring availability of credit, and balancing the interests of the stakeholders.

In keeping with its purpose, IBC has witnessed five legislative interventions since its enactment. The purpose of each one was to strengthen the processes and to further its objectives in line with the emerging market realities.

The Insolvency Resolution Process (IRP) is one such mechanism under the IBC where the NCLT initiates a Corporate Insolvency Resolution Process (CIRP) when a company defaults on making payments to creditors. Arijit Basu, Managing Director, Commercial Clients Group, SBI says, "Earlier, banks only had a 'loan structuring' option which used to take five to six years. Now, the IBC has provided equal opportunity to the corporate sector and banks. It has changed the relationship between borrowers and creditors and provided a mechanism of insolvency."

Atul Kumar Gupta, President, Institute of Chartered Accountants of India (ICAI) highlights the role chartered accountants are playing in the IBC ecosystem as Insolvency Professionals (IPs). "Almost 62 per cent of IPs are CAs. Besides, IBC has opened several new opportunities for CAs in the form of valuers, liquidators, technical experts in the NCLT, the NCLAT, high courts, and also the Supreme Court, and also various kinds of advisory services," he says.

Support to MSMEs/SMEs

The government has been very conscious of the needs of the SME/ MSME sector all this while. Take, for instance, the amendments brought by the government to deal with the exigencies caused by the pandemic. The minimum threshold to initiate insolvency proceedings has now been raised to Rs 1 crore from Rs 1 lakh. The step largely insulates SMEs/ MSMEs from sudden insolvency proceedings, as their businesses may have suffered a setback during the lockdown period.

“The biggest positive of the IBC is the re-orientation in the mind-set that it has achieved,” says Shardul S. Shroff, Executive Chairman and National Practice Head - Insolvency and Bankruptcy, Shardul Amarchand Mangaldas & Co. “The IBC recognises the importance of separating commercial decision making from judicial decision making and vested commercial decision making in the hands of creditors. Equally importantly, the IBC recognises that the control of the company is not a divine right of promoters, and has created a mechanism through which third parties can also propose plans for the company,” he adds.

Agrees Faisal Sherwani, Partner, L&L Partners, “The code effectively provides a one-stop shop for insolvency resolution, which is something to celebrate. Also to be appreciated is the endeavour of the code to ensure maximisation of value of the corporate debtor’s (CD) assets. As per an IBBI publication this year, the Code has rescued a total of 250 corporate debtors till June 2020, through resolution plans.”

Then, there is the need to cut short the time taken in insolvency proceedings, particularly in litigation. Also, there is an urgent need to develop the pre-IBC framework (including through introduction of pre-packs) better so that the costs of ‘formal insolvency proceedings’ are not borne by companies. On the issue of whether IBC is aligned with the inter national best practices, legal experts give a big thumbs up. Says Shroff: “That the IBC’s framework incorporates international best practices can be seen clearly also from the way it performs on the World Bank’s ‘Strength of Insolvency Framework’ index in the Ease of Doing Business ranking. It has provisions that allow for continuation of essential supplies in insolvency, for effective management of the debtor’s estate in insolvency, and it puts in place minimum requirements for resolution plans and protects the rights of dissenting creditors and operational creditors. Where it deviates from prescribed international best practices, it does so to deal with ‘peculiar’ Indian problems.”

Challenges & Bottlenecks

In the last couple of years, legal experts have noticed a lot of inconsistent views taken by different NCLT benches and ultimately the Supreme Court or the NCLAT had to step in to settle the law. “There is an urgent need to appoint commercially minded members (who understand commercial transactions) with prior experience in dealing with complicated questions of commercial law in the NCLT,” says Alipak Banerjee, Leader, International Dispute Resolution, Nishith Desai Associates.

“One may consider ad-hoc appointments for a tenure of 3-5 years, and this may bring a lot of interest within the practitioners to take up the role of a sitting NCLT member,” says Banerjee. He points to the example from the United Kingdom. “In jurisdictions like the UK, it is not uncommon for a practitioner to be appointed as a judge for couple of years and return back to practice,” Banerjee adds.

Lack of capacity with regard to NCLT is also a pressing concern, say experts. Lakshmi Prakash, Partner, Cyril Amarchand Mangaldas says there are three bottlenecks that need immediate attention. “The infrastructure of the NCLT/NCLAT and DRTs (specifically for individual insolvency cases) needs attention; more capacity building among the insolvency professionals; and provision of efficient, almost single-window for obtaining the relevant approvals,” says Prakash. In live

cases, experts say they see a lot of time being spent in litigation before the NCLT. These delays shake investor confidence, and the litigationrelated delays should reduce going forward.

Sherwani of L&L Partners points to Section 12 of the IBC that prescribes a total of 330 days for conclusion. “However, once the period of litigation is excluded, we find that the effective time period for completion is far in excess of 330 days. According to the World Bank’s 2020 report, it takes at least 1.6 years on average for a CIRP to be completed. This is in contrast to countries like the US, UK and Australia, where the time taken is just around a year. Clearly, we must realise that we are lacking in this aspect,” he adds.

How can the situation improve? In a discussion paper shared with BW Businessworld, Rajeev Vidhani and Ashwin Bishnoi, Khaitan & Co offer key suggestions. For example, a pre-packaged insolvency regime – inspired by various other jurisdictions, would aid the timelines for resolution presently contemplated under the IBC. The timelines, although stipulated to be binding, are often exceeded on account of various litigations (which has been addressed by an amendment to the law) or other challenges – making the Corporate Resolution Process longer and risking value erosion, they said.

Legal experts suggest that additional benches is the need of the hour. But Sherwani of L&L Partners points to the fact that the IBC is a ‘rather young legislation’. “It may be too early in the day to start handing out report cards to the tribunals. Nonetheless, some amount of acclamation is due. Statistically speaking, creditors have managed to recover about Rs 1.96 lakh crore before the global lockdown due to the pandemic,” he says. Critics also point to the high pendency of cases before the NCLT. The age-old issues of lack of benches and poor administrative support has started to catch up with the NCLT too. “In a matter that I have attended to personally, the final order was pronounced after the lapse of six months from the date on which it was reserved. This isn’t ideal by any stretch of imagination,” says Sherwani.

Then there are some specific instances which need to be rectified. Aashit Shah, Partner, J Sagar & Associates points to the recent stand of the RBI prohibiting asset reconstruction companies from bidding for companies under the CIRP. Shah says this move “must be withdrawn” as it will significantly impede the ability of creditors to maximise their value. “Lastly, the perpetual suspension of initiating corporate insolvency resolution proceedings against companies for defaults that take place during the suspension period from March 24 to December 23, 2020 needs to be revisited. The government can consider providing some additional time period for curing such defaults. However, a perpetual suspension will leave several creditors with inapt remedies to resolve such defaults,” says Shah.

The IBC also requires certain actions to be taken only with the prior approval of the creditor committee, which according to Parveen Mahtani, Chief Legal Officer, Mahindra Life Space Developers, “may be impractical and could risk slowing down the restructuring process”. “Also, there may be no difference in rights between overseas and domestic creditors. Essentially, the IBC should plug the loopholes to prevent opportunistic creditors from initiating proceedings,” says Mahtani.

Vatsala Rai, Counsel at AZB Partners points to the conflict amongst government departments that should be resolved. “The objective to ensure discipline amongst creditors has been lost sight of by the government itself where different departments have taken different and conflicting stands,

despite the clear mandate of the law doing away with the concept of priority of crown debts in favour of financial creditors (largely banks and financial institutions or FIs), thereby ensuring re-circulation of public monies lent by banks and FIs that is assisting credit growth. Examples: Department of Telecom and the Directorate of Enforcement," says Rai.

The departments have sought to assert the old position of priority such as the tax departments for their tax claims, the Directorate of Enforcement for ostensible proceeds of crime (at times chasing the very banks on whose complaint the money laundering proceedings came about) or the Department of Telecom (despite agreeing to the fact that lenders can lend to telecom service providers against the license). "This has added to uncertainty in resolution process resulting in diminishing of value. Further, this has caused endless litigation and involved court time, not just within the machinery of IBC but also the High Courts, specialised tribunals and the Supreme Court," says Rai.

Let's hope right steps are taken quickly to bolster the IBC and those of the tribunals who continue to do good work despite headwinds.