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# THE INSOLVENCY AND BANKRUPTCY CODE, 2016:A STEP TOWARDS “ACHE DIN”

Authored By-Arshita Agarwal

## Abstract

In India, the legal and institutional machinery for dealing with defaults in debts has not been in line with the accepted global standards.<sup>1</sup> The recovery action by creditors, either through the Contract Act or through special laws such as the Recovery of Debts Due to Banks and Financial Institutions Act, 1993 (RDDBI) and the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (SARFAESI) has not had desired outcomes. Business failures in a market-focused economic system cannot be avoided but however, they need to be handled in such a way that causes the least amount of disturbance to the affected stakeholders. And so the robust, efficient and effective insolvency laws are needed. Although being an essential element for a well-functioning economy, India lacked such robust insolvency regime until 2016. The enactment of the [Insolvency and Bankruptcy Code, 2016 \(IBC\)](#), was a new dawn for India's legal system it is drafted by a specially constituted “Bankruptcy Law Reforms Committee” (BLRC) under the Ministry of Finance. The code has been acted as a game changer in the way, the Indian promoters and companies function and their approach towards borrowings and debt.

The main aim of the Code, is protecting the interests of all stakeholders. The objective of the Code as provided- *‘An Act to consolidate and amend the laws relating to reorganisation and insolvency resolution of corporate persons, partnership firms and individuals in a time bound manner for maximisation of value of assets of such persons, to promote entrepreneurship, availability of credit and balance the interests of all the stakeholders including alteration in the order of priority of payment of Government dues and to establish an Insolvency and Bankruptcy Board of India, and for matters connected therewith or incidental thereto.’*<sup>2</sup> This research aims to study the formation and evolution of IBC, 2016 as an act of excellence by the government, understanding the concept of insolvency and bankruptcy along with its history and impact on Indian economy.

**Keywords:** Code, IBC2016, Insolvency, bankruptcy, liquidation.

1. Available at <https://pib.gov.in/newsite/printrelease.aspx?relid=145286> (accessed on 30<sup>th</sup> Apr. 2022)

2. Long title of the Insolvency and Bankruptcy Code, 2016 <https://www.mca.gov.in/Ministry/pdf/TheInsolvencyandBankruptcyofIndia.pdf>

## INTRODUCTION:

On 28th May, 2016, the Code was published in the official gazette after its passage in the Lok Sabha on 21 December 2015 and was subsequently referred to a Joint Committee of Parliament. The Committee submitted its recommendations and the modified Code, was passed by Lok Sabha on 5 May 2016 and by Rajya Sabha on 11 May 2016.

It has been addressed as a major economic measure, aimed at bring into line insolvency laws with the international standards. Government's previous efforts for ensuring the recovery of public debt, through the Recovery of Debts due to Banks or Financial Institutions Act, 1993, ("RDDBFI Act") by the Securitization and Reconstruction and Enforcement of Security Interests Act, 2002 ("SARFESI") deal with certain aspects of corporate insolvency which does not result in the desired consequences.

The Insolvency & Bankruptcy Code, 2016 was enacted to address the deficiencies and weakness in existing insolvency laws in India, which was also fragmented and scattered. To bring those fragmented and scattered law under one umbrella was also the objective of the code. According to the data available with the World Bank for the year 2016, insolvency in India takes around 4.3 years for resolution on average, which compared with United Kingdom is only 1 year, with USA 1.5 years and with South Africa 2 years.<sup>3</sup> India was ranked 135th/190 countries in the World Bank Ease of Doing Business Index 2015 on the ease of resolving insolvency<sup>4</sup>. Thus it is apparent from the above that the Code is undoubtedly one of the most critical legislations introduced in the recent years impacting the ease of doing business in India.

The objects clause of the Code enacted under the Act provides that it is an Act which is enacted to consolidate and amend the laws relating to reorganization and resolving the insolvency matters of corporate persons, including partnership firms and individuals in a time bound manner<sup>5a</sup>.

3. Available at <https://www.slideshare.net/ShawnMenon/note-on-the-insolvency-and-bankruptcy-code-2016> (accessed on 30<sup>th</sup> Apr. 2022)

4. Available at <https://documents1.worldbank.org/curated/en/688761571934946384/pdf/Doing-Business-2020-Comparing-Business-Regulation-in-190-Economies.pdf> (accessed on 30<sup>th</sup> Apr. 2022)

5. <https://www.indiacode.nic.in/handle/123456789/1362/simplesearch?query=Commencement%20of%20Sections%20under%20Chapter%20VII%20of%20Part%20IV%20and%20sections%20under%20Part%20V%20of%20the%20Code&searchradio=notification> (accessed on 30<sup>th</sup> Apr. 2022)

5a. long title, *supra* note, 2

By analyzing the objective clause of the Code it lays down the following key objectives:

1. To consolidate and amend the laws relating to re-organization and insolvency resolution of corporate persons, partnership firms and individuals to provide for a time bound insolvency resolution mechanism.
2. To ensure maximization of value of assets,
3. To promote entrepreneurship,
4. To increase availability of credit,
5. To balance the interests of all the stakeholders, and
6. To establish an Insolvency and Bankruptcy Board of India as a regulatory body,
7. To provide procedure for connected and incidental matters.

## **The Concept Of Insolvency And Bankruptcy**

The words “Insolvency” and “Bankruptcy” are generally used interchangeably in common dialect but there is distinction between the two. Insolvency and bankruptcy are not synonymous. The term “insolvency” denotes the state of any person whose assets are not sufficient to pay back all his liabilities; or in other words his inability to pay his debts as they become due in the ordinary course of business. Whereas the word “bankruptcy” denotes the situation of being in insolvency, it is a legal status of a person or any entity who cannot repay debts. The word “bankruptcy” is derived from an Italian phrase “bancarotta”-“banca” means bench and “rotta” means broken. . The main role of the law, in a bankruptcy process, is to lay down the rules and procedure for which the conflict is channeled, and which finally results in a settled solution. A sound legal framework provides procedural certainty about the process of negotiation, in such a way as to reduce problems of common property and reduce information asymmetry for all economic participants<sup>6</sup>. The term insolvency is used for both, individuals as well as organizations or corporates. The ultimate result for, if insolvency not resolved, is bankruptcy in case of individuals and liquidation in case of corporates. Liquidation, on the other hand, denotes to closing or winding up of corporation through a legal process for reason of its inability to meet its obligations of paying off its debts. In order to clear the indebtedness, the assets are sold at the most reasonable rates by a competent liquidator or appointed in this regard.

Therefore, in nutshell now it can be said that insolvency is the situation of inability of debtor(s) to pay back their debts, on the other hand the bankruptcy, is a formal or legal declaration of insolvency in accordance with the law.

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6. Available at [https://ibbi.gov.in/BLRCReportVol1\\_04112015.pdf](https://ibbi.gov.in/BLRCReportVol1_04112015.pdf) (accessed on 30<sup>th</sup> Apr. 2022)

Insolvency defines a situation where the debtor is unable to meet his/her obligations of paying back his/her debts while bankruptcy happens when a court of law defines a person as insolvent, and provides a legal order for it to be resolved and so, the insolvency is a state and bankruptcy is the result or the conclusion. In case of insolvency, one cannot pay off the debts, whereas in the case of bankruptcy, a court order states as how an insolvent person or business has to pay off their debts-by way of selling their assets or erasing the debt that cannot be paid

## History Of Insolvency Before The Code:

The Indian insolvency law takes its origin from the English law. In India, the first ever Act for insolvency was laid down for the Presidency Towns. The provisions relating to insolvency matters for the Presidency Towns can be drawn from sections 23 and 24 of the **Government of India Act, 1800**. These two sections provides the jurisdiction of insolvency only to the Supreme Court at Fort Williams (Calcutta), Madras and Recorder's Court at Bombay as the need for an insolvency law was first felt in Presidency Towns of Calcutta, Bombay and Madras where the Britishers majorly carried on their trade and business. These Courts were authorized to make rules and grant relief to insolvent debtors. Later the insolvency courts were established in these Presidency-Towns when **Statute 9 was passed in 1828**. The Act of 1828 definitely marks the beginning of special insolvency legislation in India<sup>7</sup>.

Next the **Presidency Towns Insolvency Act, 1909** was enacted to cover the insolvency of individuals, partnership firms and association of individuals in three presidency towns of Chennai, Kolkata and Mumbai. And to cover the insolvency of areas other than the aforesaid Presidency Towns the **Provincial Insolvency Act, 1920** was there. These two Acts were applicable on both, individuals and partnership firms as well.

The laws covering matters relating to corporate insolvency were the **Companies Act, 1956 and Companies Act, 2013** for winding-up and strike-off of companies; **Sick Industrial Companies Act, 1985** (SICA) that focused solely on restructuring of sick industrial companies; **Recovery of Debts and Bankruptcy Act, 1993** (RDBFI); **Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002** (SARFAESI Act). These laws did not yield the desired results due to inefficient enforcement and court delays and turned out to be completely ineffective. The functioning of these legislations was unsatisfactory as many issues were identified during its implementation.

7. Available at <https://www.icsi.edu/media/webmodules/Insolvency%20law%20and%20practice.pdf> (accessed on 30<sup>th</sup> Apr. 2022)

One of the major problem before the coming of IBC was the presence of multiple overlapping laws and adjudicating forums such as Debt Recovery Tribunal (DRT), Corporate Debt Restructuring, etc. and cause of which the bankruptcy process was drawn out and involved battling through many steps, creating moral issues in industrial, banking and political areas which necessitated the new legal framework for insolvency in the form of the IBC which is adequate, effective and resulted in speedy resolution of the matters.

## **IBC A promising Code:**

It can be rightly said that before the enactment of the Insolvency and Bankruptcy Code, 2016 there was not a single law in the country to deal with insolvency and bankruptcy matters effectively and efficiently. The creation of the Code as a single unified legislature to resolve the insolvency matters of companies, limited liability partnerships, partnership firms and individuals and thereby balancing the interest of debtors, secured creditors and other stakeholders was a game changer indeed. The very first impressive thing about this code is that it is very much organized; it consists of a total of 255 sections categorized in five Parts. Part I deals with preliminary, Part II deals with insolvency resolution and liquidation for corporate persons whereas Part III lays down procedure for insolvency resolution and bankruptcy for individuals and partnership firms. Part IV of the Code provides for the provisions for regulation of Insolvency Professionals, Agencies and Information Utilities and Part V includes provisions for miscellaneous matters the Code also has eleven Schedules which amends various statutes.

The second impressive thing about the code is that it is regulated by the Insolvency and Bankruptcy Board of India (IBBI) which was established on 1st October, 2016 under the Code. It is a key pillar of the ecosystem, whose main responsibility is for proper implementation of the Code. The IBBI has regulatory oversight over professionals and related institutions<sup>8</sup> - Insolvency Professionals (IPs), Insolvency Professional Agencies (IPAs), Insolvency Professional Entities (IPEs) and Information Utilities (IUs) - in the insolvency space. It has the responsibility to make regulations and guidelines on matters relating to insolvency processes - corporate insolvency resolution process (CIRP), pre-packaged insolvency resolution process (PPIRP), corporate liquidation process, voluntary liquidation process, fresh start process (FSP), individual insolvency resolution process and individual bankruptcy process - under the Code. For the time being, it also acts as the authority for valuation profession.

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8. Available at <https://www.ibbi.gov.in/about> (accessed on 1st May, 2022)

The objective of the Code is to promote entrepreneurship, availability of credit, and balance the interests of all stakeholders by consolidating and amending the laws relating to reorganization and insolvency resolution of corporate persons, partnership firms and individuals in a time bound manner and for maximization of value of assets of such persons and matters connected therewith or incidental thereto. Under the code section 12 (1) provides completion of corporate insolvency resolution process within 180 days from the **date of admission of the application** to initiate such process.

## Impact Of The Code On Indian Economy

The Code has significantly helped the banking sector in recovery the recovered amount is around Rs 5.5 lakh crores of the total bad debts. Out of this, amount close to Rs 1 lakh crores was recovered from accounts that were written off<sup>9</sup>. Although Code is not at all a recovery mechanism, but has resulted in mean recovery of 44% for financial creditors which in comparison is double to from Debt Recovery Tribunals (DRT) (which was 24%), SARFAESI Act and Lok Adalats combined, for the financial years 2018-2020. As from the data available, till 31 July 2020, total 19,844 cases were pending before NCLT of which 12,438 pertained to IBC<sup>10</sup>. Approximately, 3,000 cases have undergone resolution and liquidation<sup>11</sup>. It is positive to note that debtors and creditors are using the provisions of the Code, which can be proved through figures, till December 31, 2021, a total of 457 companies have been resolved under the code so far said by Rao Inderjit Singh, Minister of State in the Ministry of Corporate Affairs (MCA)<sup>12</sup>, Post implementation of the Insolvency and Bankruptcy Code (IBC), the overall recovery rate for lenders till Q4FY21 improved to 39.3 per cent<sup>13</sup>. The Economic Survey of 2020-21 states that till December 2020, IBC has rescued 308 Corporate Debtors through resolution plans. These Corporate Debtors owed Rs. 4.99 lakh crores to creditors<sup>14</sup>.

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9. Available at <https://www.businesstoday.in/latest/economy/story/rs-55-lakh-cr-of-bad-debt-recovered-through-reforms-such-as-ibc-govt-302364-2021-07-26> (accessed on 1<sup>st</sup> May, 2022)

10. Available at <https://economictimes.indiatimes.com/news/economy/policy/insolvency-resolution-the-ibc-story-so-far-and-the-way-forward/articleshow/80399160.cms?from=mdr> (accessed on 1<sup>st</sup> May, 2022)

11. Kuldeep Sharma, **2021 IBC and its Impact on the Indian Economy - An Overview** available at <http://www.lawstreetindia.com/experts/column?sid=633> (accessed on 1<sup>st</sup> May, 2022)

12. Available at [https://www.business-standard.com/article/companies/financial-creditors-recovered-only-one-third-of-amount-from-ibc-cases-122020900396\\_1.html](https://www.business-standard.com/article/companies/financial-creditors-recovered-only-one-third-of-amount-from-ibc-cases-122020900396_1.html) (accessed on 1<sup>st</sup> May, 2022)

13. Available at <https://www.thehindubusinessline.com/money-and-banking/overall-recovery-rate-under-ibc-improved-till-march-end-2021/article38026431.ece> (accessed on 1<sup>st</sup> May, 2022)

14. Kuldeep Sharma, *supra* note 11

Under the Code, the creditors recovered Rs. 1.99 lakh crores, which is more than 193 per cent of the realizable value of these corporate debtors<sup>15</sup>. The recovery for financial creditors, as compared to the claims made by them, was found to be more than 43% for all the years since the commencement of the Code<sup>16</sup>. The Code has facilitated the recovery of non-performing assets by banks; RBI data indicates that as a percentage of claims, scheduled commercial banks have been able to recover 45.5 % of the amount involved through IBC for the financial year 2019-20, which is the highest as compared to recovery under other modes and legislations<sup>17</sup>. Further, the amount recovered by scheduled commercial banks under the Code was Rs. 1.73 lakh crores which is more than all the amount recovered by all other alternative mechanisms for 2019-20.<sup>18</sup>

## The Fast Settling Jurisprudence

Under the Code, the insolvency system shifted away from the traditionally debtors-in-possession system to the modern creditors-in-control system. The modern concept of creditor-in-control model rules the hand of control to the creditors over the debtor and relies upon the managerial skills of a newly appointed management to take over the sick or an ailing company and ensure that business continues to run. The Supreme Court in **Swiss Ribbons v. Union of India**<sup>19</sup> has held that the core objective of the Code is to ensure revival and continuation of the corporate debtor. Thus, the Code has a larger concern to play public-welfare. The apex court in the first case of the Code, **Innoventive Industries Limited v. ICICI Bank Limited**<sup>20</sup> decided on the matter related to the operation and functioning Code i.e., regarding the concept of default and how it must be ascertained, the court held that concept of default under the Code is very wide in nature, it is simpliciter a non-payment of debt when the same becomes due and includes non-payment of even a part thereof.<sup>21</sup>

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15. Available at <https://timesofindia.indiatimes.com/ibc-redefines-debtor-creditor-relationship-says-economic-survey/articleshow/80586303.cms> (accessed on 1<sup>st</sup> May, 2022)

16. Available at [https://www.indiabudget.gov.in/economicsurvey/ebook\\_es2021/files/basic-html/page526.html](https://www.indiabudget.gov.in/economicsurvey/ebook_es2021/files/basic-html/page526.html) (accessed on 1<sup>st</sup> May, 2022)

17. Available at [https://www.indiabudget.gov.in/economicsurvey/ebook\\_es2021/files/basic-html/page526.html](https://www.indiabudget.gov.in/economicsurvey/ebook_es2021/files/basic-html/page526.html)

18. Available at <https://www.indiabudget.gov.in/economicsurvey/> (accessed on 1<sup>st</sup> May, 2022)

19. **2019 SCC OnLine SC 73**, decided on January 25, 2019. Available at <https://www.mondaq.com/india/insolvencybankruptcy/781154/swiss-ribbons-and-its-implications--the-supreme-court-on-the-constitutionality-and-key-provisions-of-the-insolvency-bankruptcy-code> (accessed on 1<sup>st</sup> May, 2022)

20. L. Viswanathan and Indranil Deshmukh (2017), *Innoventive Industries Limited v. ICICI Bank Limited: Paradigm Shift in Insolvency Law in India*, Available at <https://corporate.cyrilamarchandblogs.com/2017/09/innoventive-industries-limited-v-icici-bank-limited-paradigm-shift-insolvency-law-india/> (accessed on 1<sup>st</sup> May, 2022)

21. *Ibid.*

Further the Code provides majorly three classes of persons who can file application to start the corporate insolvency resolution process or the CIRP against the debtor, i.e., the financial creditors, operational creditors and the corporate applicant.

For the operational debtor, the Apex Court in **Mobilox Innovations v. Kirusa Software**<sup>22</sup> observed that the operational debt<sup>23</sup> should be free from any pre-existing dispute which cannot be dealt with summarily in insolvency proceedings. The clarification for the term liability of a guarantor was done by the apex court through the judgment in **Lalit Kumar Jain v. Union of India**<sup>24</sup>, where the Supreme Court clarified that the liability of a guarantor was co-extensive with that of the principal debtor which directly means that proceedings could be initiated against the guarantors as well.

Although the most important element of this Code is the timeliness of the timeline of insolvency resolution process. As per Section 12 sub-section (1) of the Code, the insolvency resolution process of corporate entity (CIRP) shall be completed within a period of 180 days from the date of admission of the application. It is seen that there can be situation or cases, where the resolution process can be completed before the set maximum time period, concerning these situation the NCLT (Mumbai bench) in the judgment of **SBI v. Jet Airways (India) Limited**<sup>25</sup> held that the IBC provision provides for 180 days for completion of the CIRP, but every effort should be made by the Interim Resolution Professional / Resolution Professional (IRP/RP), and members of Committee of Creditors (CoC) to expedite the matter and try to finalise the resolution plan on the fast track mode and they should not preferably wait for the completion of the statutory period of 180/270 days timeline permissible under IBC<sup>26</sup>.



22. (2018) 1 SCC 353, decided on September 21, 2017. Available on <https://ibbi.gov.in/webadmin/pdf/order/2017/Sep/21st%20Sept%202017%20in%20the%20matter%20of%20Mobilox%20Innovations%20Private%20Limited%20Vs.%20Kirusa%20Software%20Private%20Limited%20CA%20No.%209405-2017-2017-09-22%2013:36:08.pdf> (accessed on 2<sup>nd</sup> May, 2022)

23. "Section 2 clause (21) of the Code defines the term operational debt. It means a claim with respect to the provisions of goods or services including employment or a debt which is due under any law and payable to the Government, Available on <https://singhania.in/blog/status-of-statutory-dues-under-ibc-operational-or-financial-creditors-who-decides->

24. MANU/SC/0352/2021 available on <https://www.legalbites.in/lalit-kumar-jain-v-union-of-india/> (accessed on 2<sup>nd</sup> May, 2022)

25. 2019 SCC OnLine NCLAT 385, decided on 12-07-2019 available on <https://www.sconline.com/blog/post/2019/07/15/nclat-jet-airways-nclt-order-declaring-insolvency-proceedings-in-netherlands-as-not-maintainable-stayed/> (accessed on 5<sup>th</sup> May, 2022)

26. Available at <https://ibclaw.in/analysis-on-time-limit-under-section-12-of-the-code-for-completion-of-cirp/> (accessed on 5<sup>th</sup> May, 2022)

The Supreme Court in **Kridhan Infrastructure v. Venketesan Sankaranarayan**<sup>27</sup> ruled that the insolvency resolution should not suffer from an indefinite delay in complete disobedience of the timelines fixed under the Code. Further, in **Prowess International Pvt. Ltd. v. Parker Hannifin India Pvt. Ltd**<sup>28</sup> NCLAT, ruled that - thereafter, in case(s) where all creditors have been satisfied and there is no default with any other creditor, the formality of submission of resolution plan under section 30 or its approval under section 31 is required to be expedited on the basis of plan if prepared.<sup>29</sup>

## Conclusion

Undoubtedly the Code has rephrased the Indian insolvency laws on a great magnitude. It has greatly added to development of disciplined borrowing amongst companies. In a very short span of time, this Code has made great developments in providing a predictable framework whose main aim is to provide timely, efficient and impartial resolution of businesses and a transparent liquidation process, which also recognizes the creditor's rights and respects the priority of claims too. The Code is a landmark reform among various 'Ease of Doing Business' initiatives undertaken by the Government of India, mainly because it consolidated all past provisions to institutionalize a common legislation for insolvency resolution in a time bound manner. Its results have proved that it was rightly hailed as a progressive and dynamic economic legislation. It is the true example of time bound justice oriented system, providing the much needed 'freedom to exit' to failing businesses. It is a new India's legislature which shift from the erstwhile insolvency provisions in all terms be it in terms design and architecture, professionalization of insolvency services and skillfully balancing the interest of all stakeholders. Like everything else, this new, effective and efficient system of insolvency, too, should keep growing which is the only thing that is, embracing the future. The Code has, till now, evolved and at-tuned to every emerging market requirement and will continue to do the same to remain germane for all times to come.

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27. 2021 (225) CompCas 694: 2021 (2) BC 117: AIR 2021 SC 2578: (2021) 6 SCC 94 available on <https://indiankanoon.org/doc/111851421/> (accessed on 5<sup>th</sup> May, 2022)

28. [2017] ibclaw.in 18 NCLT.

29. *Supra* note, 26