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REVERSE CORPORATE INSOLVENCY RESOLUTION PROCEDURE: AN ANALYSIS

By: Anjali Sharma BBA LLB (Semester VII)

INTRODUCTION:

The Real estate sector of India is a growing sector, and has a huge influence on the economy of the country. The Real estate sector of India is regulated by RERA (Real Estate Regulatory Authority) and also has its own legislation known as Real Estate (Regulations and Development) Act, 2016. Before the appearance of RERA into the picture, there were several irregularities taking place in between the Real Estate sector for the homebuyers and the builders. The homebuyers were specifically very much exploited due to those irregularities before this Act came into force. The problems that were mainly faced by the home buyers were like delay in the completion of the project, biased contract in the favour of the builders or developers, no specific date mentioned for the completion of the project, no proper disclosure of the plan that is to be sanctioned and other various problems that caused a havoc for the home buyers of the country.

Also, there lacked complete transparency and accountability in the Real estate sector before this Act came into force. Hence, to protect the interest and the rights of the home buyers and to bring transparency in the Real estate sector, the Government of India introduced the Real Estate (Regulations and Development) Act, 2016. The period before RERA introduced itself in the picture, if any home buyer had any difficulties or problems regarding their Real estate with the builders or developers, they would have to go to the Consumer Court to file a complaint regarding any fraud or wrongdoing by the builder and would have to wait for a long period of time to get proper justice, but post RERA, the home buyers can approach the RERA tribunal or authority and can get justice in a short period of time. The Rules and Regulations of RERA are stricter and harder so that no builder or developer cannot have the scope to exploit the home buyer.

Now, talking about IBC (Insolvency and Bankruptcy Code) which was introduced in 2016 is a bankruptcy law of India which integrates or merges the existing framework by creating a single law for insolvency and bankruptcy. The aim of IBC is to save the corporate debtor, debt resolution in fixed time period, revival of companies, and maximization of asset value of the corporate debtor, also give availability of credit.

The concept of 'Reverse Insolvency' is very much alien and new to the Insolvency and Bankruptcy Code, 2016. It is a well acknowledged fact that since the Code first came into force, it has undergone several amendments along the way. And one of the most prominent amendment being that inclusion of homebuyers as the financial creditors. But the corporate insolvency resolution process of Real estate Company was not that uncomplicated. The process created a major hurdle in terms of the rigorousness that could prejudice the rights of the home buyers. The reverse corporate insolvency resolution process was brainchild of National Company Law Appellate Tribunal. It may altogether project a totally different idea. However, it is just a supplementary mechanism providing for debt resolution and maximization of asset value.

In this paper, we would talk about the concept of Reverse Insolvency and how it was introduced into the Insolvency and Bankruptcy Code, 2016. We would further talk about the benefits of it to the homebuyers and how it has changed the issues related to the Real Estate that were causing loop in the law and violating the rights of the home buyers.

SCOPE:

The scope of this research paper is to get to know the new concept of Reverse Insolvency and see how and when it was introduced into the law. We would also get to know what was the need of such concept and what is the impact of it on the Real Estate sector. This paper would introduce us to this alien concept and would give us a wide view regarding how major amendments are being introduced into the Insolvency and Bankruptcy Code, 2016 and how they are being applied.

METHODOLOGY:

The researcher has followed the non-doctrinal method for research design. The researcher has used both primary and secondary sources of extracting required information. Primary Sources being the Insolvency and Bankruptcy Code, 2016 and any other acts mentioned in the paper and the secondary sources being the various case laws and articles referred to complete this research paper.

LITERATURE REVIEW:**1. India: Orders Under Insolvency and Bankruptcy Code W.R.T. Corporate Persons, Manoj K Singh, Daizy Chawla:**

This article talks about the various amendments that was made under the Insolvency and Bankruptcy Code recently and one of them being that the home buyers were given the space under the definition of financial creditors. It briefly talks about how it was made and what was the effect of that. The author has studied in detailed and has explained the topics in very nice way. The article uses a simple but legal language and hence it might be a little difficult to understand but not too much, rather it shows that how much the writer wanted to the legal aspect of it and not just any casual article.

2. Reverse Corporate Insolvency Resolution Procedure [Reverse CIRP]: A Novel Experiment Conducted by the NCLAT, Nikunj Mehta:

This article talks about Reverse Corporate Insolvency Resolution Procedure and how it came into the picture in the first place. He starts by talking about the flat buyers' case that first time ruled that home buyers can be considered as financial creditors and gave them a space in the IBC Code. Then this article talks about the effects of the case and how it led to amend the IBC Code and considered making the judgment as a legal provision for the home buyers to file a complaint in the IBC Code and get a more efficient resolution under it and hence this article was an important read. The author has kept the article simple and hence making it a nice read.

Research Questions:

- 1. What is the concept of Reverse Insolvency in the Insolvency and Bankruptcy Code, 2016?**
- 2. What is the impact of the concept of Reverse Insolvency and how is it beneficial for the homebuyers in the Real Estate sector?**

Hypothesis:

As per IBC Laws, if any corporate company defaults in debts exceeding prescribed amount, then

the such creditor can file petition under the applicable section of IBC, before Hon'ble NCLT to initiate the Corporate Insolvency Resolution Process. On admission of such petition, an IRP is appointed by NCLT to find the resolution of said company as per the details IBC laws. This is a remedy available to buyers and builder to construct the pending delayed and stalled projects where the construction of the project can be done in time bound manner.

INSOLVENCY RESOLUTION PROCESS UNDER THE IBC

An application for the initiation of CIRP is processed by the operational or financial creditor on the incidence of default by any Corporate Debtor (CD). While this whole process is completed, a moratorium under Section 13(1)(a) is issued by the NCLT, which averts all judicial proceedings for recovery, enforcement of security interest, sale or transfer of assets, or termination of essential contracts to be instituted or continued against the Corporate Debtor. After the application made by the financial creditor is accepted, an Interim Resolution Professional (IRP) is appointed to take charge of the corporate debtor. The IRP is accountable for the constitution of the Committee of Creditors (COC), and appointment of the Resolution Professional (RP).

Subsequently, a resolution plan (a bid document), constituting the terms of the proposal (including payment structure to various lenders, business plan along with its assumptions, transaction structure, etc), is proposed before the Committee of Creditors. On acceptance with the requisite majority provided under the IBC, a plan would be passed or the CD would have to go through liquidation.

Home Buyers as Financial Creditors Under the IBC:

After the second amendment of the IBC dated August 2018, the home buyers of a Real Estate and Infrastructure Project were declared 'financial creditors' under Section 5(8) of the IBC. This amendment provided the home buyers with the right to approach the adjudications authorities on the occurrence of any default in delivery of possession or delay in completion of the project by a real estate developer.

CONCEPT OF REVERSE CORPORATE INSOLVENCY PROCESS:

The concept of Reverse Corporate Insolvency was introduced by the Hon'ble National Company Law Appellate Tribunal (NCLAT) in Flat Buyers Association Winter Hills-77, Gurgaon vs Umang Realtech Private Limited through IRP & Ors¹, which means that during the Corporate Insolvency Resolution Process, the resolution (end result) is reached without approval of the third-party resolution plan.

In this case Mr. Ajay Singh and Mrs. Rachna Singh who were allottees or Financial Creditors (according to IBC) moved an application under section 7 of IBC, 2016 to NCLT, Principal Bench, New Delhi to start Corporate Insolvency Resolution Process and without endorsement of any plan of a third party (Resolution applicant) against 'M/s Umang Realtech Pvt. Ltd.', which is a real-estate company (here referred as 'Corporate Debtor'). The Authority acknowledged the application and appointed an Interim Resolution Professional (IRP) and directed the financial creditors to deposit Rs. Two lakhs with the IRP to perform further functions given to him.

Now, the problem is that in IBC when an IPR is appointed the duty of IPR is to keep the company in running process and in case of real-estate infrastructure company the duty of IRP is to build the remaining infrastructure to keep company in running process. In this case, it is not possible for the IRP to complete the project within Rs. Two lakhs which were ordered by the Authority to Financial Creditors to deposit it with IRP to keep the company in going concern. Now, in this case one of the Promoter 'Uppal Housing Pvt. Ltd.' came out and agreed to remain out of the Corporate Insolvency Resolution Process and intended to play a role of Financial Creditor by infusing case flow. This leads to making sure that the CIRP completes, and the construction of the remaining project is also completed. The completion of the project enables the allottees to take possession of the flats in the project without any third-party intervention. The NCLAT approved this experiment with the ongoing process of CIRP so that rights of promoters are not compromised. The aim of Reverse CIRP is to get twin benefits: the first one is to save promoters from insolvency and the

¹ *Flat Buyers Association Winter Hills-77, Gurgaon vs Umang Realtech Private Limited through IRP & Ors [CA(AT)(Insolvency) No. 926 of 2019]*

second one is to give possession to the allottees in the project.

The intention behind the introduction of the concept of reverse insolvency was to protect the interests of all the stakeholders including allottees, financial institutions, etc and the Real Estate company keeps functioning as going concern with the help of promoter working along with the Resolution Professional. The Hon'ble NCLAT also issued various directions with respect to CIRP against a real estate infrastructure and same are enumerated as follows:²

- a. In CIRP against a real estate, if allottees (financial creditors) or financial institutions/Banks (Other Financial Creditors) or Operational Creditors of one project initiated CIRP against the Company then the allottees or financial institutions/Banks or operational creditors of the other project cannot file its claim before the Resolution Professional. Further, the CIRP will be confined to such a project of the Company.
- b. A secured creditor such as financial institutions/banks cannot be provided with the asset (flat/apartment) by preference over the allottees (Unsecured Financial Creditors) to whom the project has been approved. Their claims are to be satisfied by providing the flat/apartment.
- c. As an alternative to achieve the object of maximization of the asset, an allottee may agree to opt for another flat/apartment or one tower or another tower if not allotted to any other.
- d. Prayer for refund cannot be allowed by the Adjudicating Authority or by the NCLAT.

Analysis:

In circumstances like these, where the shareholders have decided altogether and come up with a viable option to resolve the financial stress of the CD, adopting measures such as reverse CIRP is a probably step of recognising and ensuring the rights of the home buyers.

Through this judgment, the NCLAT wants to show how the steps has been taken towards the “equality for all” approach. This approach, however, is in direct contradiction to the current

² India: Orders Under Insolvency and Bankruptcy Code W.R.T. Corporate Persons, Manoj K Singh, Daizy Chawla, 25th March 2020, <https://www.mondaq.com/india/insolvencybankruptcy/905776/orders-under-insolvency-and-bankruptcy-code-wrt-corporate-persons>.

law of distribution declared by the Supreme Court in the landmark Essar Steel case³. This practical step, against the status quo Law, is termed by the tribunal as an ‘experiment’ which was required for the effective implementation of the IBC’s object of maximising the assets of the CD. Quoting from the judgement, the tribunal stated that Investment of the Home-buyers, termed as a ‘financial debt’ demands quick delivery of the plot’s ownership as its only effective fruit. This view follows from the SC’s judgement in the Pioneer Infrastructure case⁴, where it has stated that a refund, or any other financial compensation is not a plausible option of repaying the dues of home buyers.

BENEFITS OF REVERSE CIRP FOR HOME BUYERS AND DEVELOPERS:

1. Settlement of Claims amongst secured and unsecured creditors:

As there being a huge distress in the business of the CD, even when the resolution plan has been passed, it still becomes difficult to pay off entire debts of all classes of the creditors, while keeping the CD a going concern. Hence, making the equitable and effective distribution of amounts to different classes of creditors as essential need.

The tribunal noticed and pointed out that differentiating amongst the ‘secured’ and ‘unsecured’ creditors, and by denying the whole concept of the ‘Equality for all’ principle, the Supreme Court (SC) in the Committee of Creditors of Essar Steel v. Satish Kumar⁵ mentioned that neither the IBC, nor any regulation enacted under it, provided for an equal percentage-wise distribution of the same amount of proceeds under a resolution plan amongst all classes of creditors. In the present case the tribunal said that where the defaulting real estate developer is on the verge of finishing the project, the principle of giving preferential treatment to the ‘secured creditors’ should not be applied. The tribunal, towards the end of the judgement

³ Committee of Creditors of Essar Steel India Limited Through Authorised Signatory v Satish Kumar Gupta and ors, Civil appeal No. 6409, 2019

⁴ Pioneer Urban Land and Infrastructure Limited & Anr. V Union of India & Ors, W.P 43 of 2019.

⁵ *supra* n 3

concluded that since the flats or the plots of an infrastructure company are contractually approved for allottees of those projects, giving any preference to the secured creditors of such company is unjust.⁶

While talking about the decision of the Hon'ble SC in Pioneer Urban Land and Infrastructure Co Ltd. v. Union of India⁷, the tribunal pointed out in the judgment that since there is no other mode (refund) of repaying the dues of the home buyers, allotment of flats and plots of the project remains the only way of repayment. Hence, secured creditors such as banks and financial institutions cannot be allotted with asset (flat/apartment) by preference over the allottees (Unsecured Financial Creditors) for whom they were approved initially.

2. Supply of Essential Goods and Services:

According to the tribunal, the amount of Rs. 2 Lakhs was minimal to ensure the supply of essential goods and services, and to ensure the going concern status of the CD. The requirement of immediate resources to finish the common amenities like swimming pool, club house etc as promised to the allottees cannot be fulfilled as all of these do not fall under the list of essential goods mentioned under the Regulation 36 of the CIRP, the NCLAT did not take those amenities into consideration while they determined the amount to run the expenses.

The NCLAT, stated this as another limitation of the CIRP, as it prevents the maximization of the value of the CD's assets. It mentioned that these provisions affecting to the process put both the homebuyers and project developers under distress.⁸

3. Applicability of a Resolution Plan to other projects:

Another feature of the decision, in which the court later set an unprecedented case for a ruling

⁶ Reverse Corporate Insolvency Resolution Procedure [Reverse CIRP]: A Novel Experiment Conducted By The NCLAT, Nikunj Mehta, April 8 2020, <https://libertatem.in/articles/reverse-corporate-insolvency-resolution-procedure-or-reverse-cirp/>

⁷ *supra* n 4

⁸ *supra* n 6

on a similar issue, was the applicability of the Settlement Plan. According to NCLAT, the proposed solution plan approved by the project's COC should not affect other projects of the same real estate company (CD) elsewhere. The reasons given by NCLAT behind such proceedings were different lands, different allottees owning plots on that land, and different financial institutions funding those projects. Therefore, you should not maximize the assets of CDs that belong to completely different projects.⁹

4. Restrictions on filing petitions on occurrence of defaults:

The petition for this proceeding was filed by two homebuyers from a group of a total of 624 allottees. The applicant has filed a petition to initiate CIRP, contrary to the consensus of the other creditors. While adjudicating, NCLAT gave the precedence to the mutual solution achieved by the joint will of all recipients, including immediate delivery of assets to recipients, in exchange for the recipient's promise from the allottees to repay the outstanding amount consideration towards their plots to the CD.¹⁰

LEGISLATIVE AMENDMENTS POST THE JUDGMENT:

Following NCLAT's decision, parliament implemented the 2020 Bankruptcy and Bankruptcy Act (Amendment) Act. The following were amendments led by NCLAT's decision.

Restrictions on filing bankruptcy Resolution processes by certain financial creditors

A minimum threshold for initiating CIRP is set to avoid cases where a small number of successful bidder applications are submitted without the permission or will of the other successful bidders. According to the amendment, IBC u / s 7 (1) homebuyer applications must be jointly filed by at least 100 of these creditors, or 10% of the total. It also explains that if such requests have already been submitted before the start of the 2020 amendment, those requests must be amended within 30 days of the start of the law.

⁹ Supra n 6

¹⁰ supra n 6

Providing essential products and services

The amendment inserted a subsection (2A) in Article 14 of the IBC. This amendment stipulates that RP/IRP maintain the supply of "important goods and services". This broadens the scope of the term "essential goods and services" as set out in Rule 36 of the 2016 IBC Regulations (CIRP). It also gives the IRP / RP the autonomy to determine the value of the cost to cover the cost of the CD, and keep it a going concern. This amendment ensures that the IRP specified in CIRP has sufficient autonomy to obtain the correct amount to cover the CD cost.¹¹

CONCLUSION:

The theoretical analysis of the reverse business insolvency process certainly looks quite promising. Additionally, an important aspect of the reverse CIRP is the option to claim reimbursement of the full amount that was not made available to the successful allottees. However, after offering allotment, an allottee can ask the Interim Resolution Professional/Promoter, who is in charge, to find out the third party to buy said flat / apartment and recover the money or the allottee can find a buyer in the market and may request the resolution professional or successful resolution applicant to acknowledge the transfer in the records of the Corporate Debtor. In addition, it specifies the claim of allottee on the claim of other financial creditors such as "financial institutions / banks".

These financial creditors will not receive the asset (flat / apartment) in preference to the allottees for whom the project was approved. Allottees' claims must first be satisfied by handing over possession to them.

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