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Critical Analysis of the Insolvency and Bankruptcy Code, 2016 under the light of emerging trends in Mergers & Acquisitions

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ABSTRACT

Since the advent of the Insolvency and Bankruptcy Code in 2016, India has witnessed constant efforts aimed towards strengthening its credit ecosystem. It has been more than two years the code was enacted, with the promise of being the biggest post-independence reform in the economic sphere. The Code is considered as a monumental reform to improve 'Ease of doing Business' in India. It amalgamated all previous provisions to institutionalize in a time-bound manner a common law for the resolution of insolvency and reformation of corporate entities and partnership firms. It has incredibly reinforced the juridical foundation pertaining to the liquidation, reformation and revival of feeble corporate entities, which will ultimately go a long way in improving India's ranking on the Ease of Doing Business Index.

This article sheds light on the evident and emerging impacts of the growing insolvency code phenomena on the mergers and acquisition deals. Further this article seeks to highlight the changes introduced by the government in the code since its inception and how these changes made the IBC even more potent, making the ground even more fertile for M&A activity. Many of the lingering issues around the code have been tackled by the judiciary's positive explication and the efficacious changes brought about by the parliament which have been analysed in the paper. Thus the article seeks to examine the landmark judicial interpretations in the litigation involving some of the most high profile corporations like Bhushan Steel, Essar Steel, and Jaypee Infratech.

Eventually this article seeks to shed light on the reasons as to why the Insolvency & Bankruptcy Code has not been able to perform near its full potential and the changes that can be brought so that it meets its lofty goals specifically in the light of mergers and acquisitions.

Keywords: *Financial creditors, Operational creditors, corporate insolvency restructuring process, amalgamation, takeover*

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I. INTRODUCTION

India has regularly been rebuked for having fallen behind as far as the advancement of its corporate economy is concerned by neglecting to recognize the worldwide patterns. In accordance with the vision of India's premiere executive Narendra Modi, different policy changes have been envisioned in order to improve the global picture of India's corporate economy by enacting trailblazing laws that will go far in clearing the way for financial development and advancement of the nation. The Insolvency and Bankruptcy Code (hereinafter referred to as "**IBC**") provides an amalgamated system for settling corporate insolvency in India. It seeks to inculcate efficiency within the insolvency and bankruptcy law regime by separating the commercial and judicial aspects of the insolvency process. IBC relies on four columns: Insolvency and Bankruptcy Board of India (IBBI, the regulator), the National Company Law Tribunal and the National Company Law Appellate Tribunal (the unified adjudicatory authority), insolvency professionals and information utilities. IBC has beefed up the previous apparatus of debt resolution to be more potent and viable. In a significant move, the Code strikes a stark contrast from the earlier approach of "debtor in possession" to "creditor in possession"[2].

Among its many lofty goals, one was to resolve India's ubiquitous non-performing asset crisis. At first pundits thought that IBC would not be able to make significant impact. But after three years and some hits and misses, IBC has proved its mettle for the Indian economy by hanging a target on the distressed assets.

Distressed Mergers and Acquisition (hereinafter referred to as "**M&A**") activity comprised a significant 12% of total M&A value, led by deals involving Bhushan Steel (Rs. 5474 crores), Reliance Communications (Rs. 2516 crores) and Fortis Healthcare (Rs. 8880.2 crores).[3] According to the Kroll Spotlight Asia report, close to Rs. 7400 crores of these deals have been closed in 2018 alone. Since May 2016, some 900 companies have been referred to the National Company Law Tribunal (NCLT) and the list of companies going through the restructuring and insolvency process – starting with the notorious "dirty dozen"– continues to grow[4]. As distressed assets continue to mushroom in the market both quantitatively and qualitatively, the probability of conception of a merger or acquisition increases many times

[2] Thomas E. Plank, *The Creditor in Possession Under the Bankruptcy Code: History, Text, and Policy*, 59 MARYLAND LAW REVIEW 253, 263 (2000).
[3] PTI, *More distressed Merger & Acquisition deals in pipeline: Report*, ECONOMIC TIMES (Jan. 23, 2020, 10:14 PM), https://economictimes.indiatimes.com/news/company/corporate-trends/more-distressed-merger-acquisition-deals-in-pipeline-report/articleshow/66443665.cms?from=mdr.
4 Tarun Bhatia, *Spotlight Asia: Distressed M&A in India: A risk worth taking*, KROLL (Jan. 26, 2020, 12:56 PM), https://www.kroll.com/en/insights/publications/apac/spotlight-asia-kroll-ma-october-2018.

over.

The following sections of the paper will focus upon the two essential questions revolving around the economic impact – that is how the law is being applied as well as questions regarding the judicial process – as to how the courts are functioning under the law.

II. CONSTITUTIONAL VALIDITY OF IBC AND ITS MANDATE

The Indian Constitution enumerates the manner in which insolvency and bankruptcy proceedings shall be undertaken. The insolvency and bankruptcy aspect of corporate law has been listed in the Concurrent List, entry 9, given under Schedule VII and also under Article 246 of the Constitution, which gives both central government and the states the power to make laws and rules on the subject.[5] Since India is a quasi-federal, there exists a separation of power between the Centre and state governments with flexibility. However, if any state law is found to be in contradiction to any law made by Central Government, the Supreme Court can strike down that particular provision from the statute book by applying the 'Test of Repugnancy'[6]. The constitutional validity of the Code was discussed at length by the Supreme Court of India in the celebrated case of Innoventive Industries Limited,[7] where it was observed that the Code, being the central law, prevailed over all existing laws pertaining to insolvency and bankruptcy.

The IBC is explicitly different from the existing legal framework and practices in many aspects[8]. The law does not lay out the form of the resolution outcomes, but designs the form of the process leading to the resolution. For instance, it adds new institutions to the ecosystem – the Insolvency Professionals (IPs), the Insolvency Professional Agencies (IPAs) and the Information Utilities (IUs), all of which ensure efficient and timely resolution of distress, with a statutory bankruptcy regulator to regulate the industries as well as the resolution processes. The law establishes a framework for combined action by creditors to iron out the financial stress of the debtor, another first in India. The process shifts away from a debtor-in-possession model to a model where creditors decide on the resolution while an impartial

[5] 1 M.P. JAIN, INDIAN CONSTITUTIONAL LAW (Lexis Nexis 2018).
[6] REPUGNANCY - An inconsistency, opposition, or contrariety between two or more clauses of the same deed, contract, or statute, or between two or more material allegations of the same pleading, or any two writings. Lehman v. U. S., C.C. A.N.Y., 127 F. 45, 61 C.C.A. 577; Swan v. U. S., 9 P. 931, 3 Wyo. 151; Hansen v. Bacher, Tex.Com. App., 299 S.W. 225, 226, HENRY CAMPBELL BLACK, BLACK'S LAW DICTIONARY 1467 (4 ed. WEST PUBLISHING CO. 1968).
[7] Innoventive Industries Limited v. ICICI Bank & Anr., Civil Appeal Nos. 8337-8338 (2017).
[8] Rajeshwari Sengupta et al., *Evolution of the insolvency framework for non-financial firms in India*, Tech. rep. IGIDR (2016).

professional runs the operations of the debtor as a going concern.[9]

Additionally, the legislation empowers the National Company Legislation Tribunal (NCLT) as the adjudicating authority, which does not interfere in the resolution process, but solely adjudicates the fairness of the procedure and compliance with the corporate insolvency law. The National Company Law Appellate Tribunal (NCLAT) is designated as the appellate forum by the law. It is worth mentioning again that the Code sought to improve the ease of doing business in India and to set up better and faster debt recovery mechanisms.[10]

The main hurdles for the earlier mechanism for solving insolvency and bankruptcy issues were multiplicity of laws, overlapping jurisdictions and limited links between the existing statutes. A delay often leads to loss to the economy in terms of resources, production, employment and development of the industry concerned, leading to poor growth and development.[11] A trust deficit is also created among the creditors, who in order to create a firewall around them, lend selectively and become wary of investing in entrepreneurial initiatives like start-ups and small scale industries.

In the past creditors received very few rights and little legal protection when it came to the recovery of dues in the event of a default, as the delinquent promoters and management would more often than not remain in absolute control of company assets.[12] That creditors have often been handed a raw deal is indicated by the fact that they were willing to take huge haircuts even after the introduction of the Code, as was indicated in the case of ***Synergies Dooray Automated Ltd v. Edelweiss Asset Reconstruction Company Limited and Ors.***[13]**.** In this case, the creditors took a 94 % haircut, under the code; that is, they realized INR 54 crores. Synergies Dooray applied to the tribunal under Section 10[14] for initiating a resolution process, pursuant to which an interim resolution professional was appointed and a public notice issued. The total debt of the company amounted to Rs. 972.15 crores. The plan by Synergies Casting Ltd received 90.16 % of the vote out of the four resolution plans that were received and it was decided that debt would be sold for INR 5408.21 lakhs (amounting to

[9] IBBI, *The report of the Bankruptcy Law Reforms Committee Volume I: Rationale and* Design (2015). Bankruptcy Law Reforms Committee 2015 noted that, "...Control of a company is not divine right. When a firm defaults on its debt, control of the company should shift to the creditors. In the absence of swift and decisive mechanisms for achieving this, management teams and shareholders retain control after default. Bankruptcy law must address this."

[10] Aayushi Mehra et al., *A study of Insolvency and Bankruptcy Code and its Impact on Macro Environment of India*, 7 IJEDR 28, 29 (2019).

[11] Kenneth Ayotte et al., *Bankruptcy or Bailouts?*, 35 Journal of Corporate Law 469, 498 (2010).

[12] Jongho Kim, *Bankruptcy Law Dilemma: Appraisal of Corporate Value and Its Distribution in Corporate Reorganization Proceedings*, 29 Northwestern Journal of International Law & Business 119, 194 (2009).

[13] Civil Appeal No. 57 (2017).

[14] Insolvency and Bankruptcy Code 2016, s. 10.

about 54 crores). This case reflects the reality that creditors have generally had to struggle to realize their dues and were therefore suspicious of the entire settlement process under the Code as well. Going by their experiences of the past, they decided to accept the miniscule amount in lieu of the total debt in the hope of at least realizing some portion of the credit advanced by them.

III. THE CODE'S EFFICIENCY IN TACKLING ECONOMY & BUSINESS FAILURES

As per the Bankruptcy Law Reforms Committee report,[15] lenders are able to realize only 20 % of their dues. It is pertinent to note that credit is the backbone of an economy and no economy can prosper without it. A constant supply of credit is thus essential for a successful corporate growth. For various reasons, a company that freely enters the competitive corporate sector may fail to deliver as planned. The reasons may be not necessarily being economic, they can be policy driven, social or because of bad faith among market participants. In any case, the failure of one creditor to realize his credit advanced should not dampen the spirit of lending. The Indian economy has suffered in a number of ways due to the absence of a potent mechanism for addressing this default.

One of the major setbacks suffered by the economy is a poorly developed credit market, as lenders are unwilling to lend because they fear a loss of investment and therefore lower funds at their disposal, which in turn will limit their ability to lend again.[16] In fact, poor or delayed recovery raises credit rates, leading to expensive projects that are actually not unviable. In a cash-strapped economy, the lack of adequate credit availability has further stifled corporate growth. Most labour-intensive businesses took a beating after being starved of credit facilities. The Code therefore tackles business failures either by rescuing faltering businesses or by channelling resources from failed businesses back into the economy, thereby promoting corporate growth and providing a fertile ground for entrepreneurship.[17] Through provisions for resolution and liquidation, the Code empowers lenders to recover funds from future earnings, after resolution or after the sale of liquidation assets. They can now distinguish price and credit risks across risk categories and offer differentiated and customized credit products across the value chain.[18] The management and promoters of the corporate debtor are kept in check from committing a defaults they know the inevitable consequence of a resolution process, thereby minimizing the occurrence of defaults. The supply of credit is

[15] *Supra* note 9.
[16] Roman Tomasic, *Creditor Participation in Insolvency Proceedings – Towards the Adoption of International Standards*, 14 Insolvency Law Journal 173, 187 (2006).
[17] M.S. Sahoo, *Message to the Readers*, 1 ICSI IPA Insolvency and Bankruptcy Journal (2017).
[18] *Id.*

hence increased, reducing the cost of funds and developing a debt market. The Code thus addresses default, promotes debt servicing and enhances the availability of credit for a business.

A significant improvement has been seen in credit realization, with a sudden burst of debt clearances by corporate debtors: 2,100 companies settled INR 83,000 crores worth of dues immediately after the implementation of the Code.[19] Therefore the Code seems to be a breath of fresh air for an economy getting suffocated, as it aims at the settlement of debt in a timely manner with the intention of safeguarding the interests of all stakeholders. A point worth emphasising is that the Code acts as a catalyst for better utilization of resources while preserving the value of an enterprise.[20] It provides a fertile ground for the optimum utilization of resources by restricting the use of resources below the optimum level, ensuring that resources are absorbed efficiently within the firm through the resolution of insolvency and by releasing unutilized or underutilized resources so they can be used efficiently through closure of the firm. The Code thus tackles the inefficiency of resource utilization and thereby maximizes the value of assets. It is believed that "if resources that are currently unutilized or underutilized for whatever reason can be put to more efficient use the growth rate may well go up by a few percentage points, other things being equal, particularly when this is accompanied by the availability of credit and entrepreneurship".[21]

IV. FINANCIAL CREDITOR VERSUS OPERATIONAL CREDITOR

New and distinct concepts of "*Financial Creditor"* and "*Operational Creditor"* have been introduced by the IBC, as opposed to the Companies Act, 2013 which only introduced the term "creditor", without any classification thereof. The corporate insolvency resolution process (hereinafter the "**CIRP**") is the backbone of the Insolvency and Bankruptcy Code, 2016. To analyse the CIRP, it is important to understand the distinct concepts of Financial and Operational Creditor.

An applicant first has to satisfy the Tribunal that it falls either within the definition of "*Financial Creditor"* or "*Operational Creditor"* under the IBC, if he wants his application for initiating corporate insolvency resolution process to be maintainable. An order which is especially relevant to the concept of "*Financial Creditor"* and "*Operational Creditor*" is the

[19]Sidhartha, Owners settle Rs.83,000 crore bank dues, TOI (Jan. 28, 2020, 10:40 AM), https://timesofindia.indiatimes.com/business/india-business/owners-settle-rs-83k-crore-bank-dues/articleshow/64279946.cms.

[20] Nilesh Sharma, *Corporate Insolvency Resolution Process, Under the Insolvency and Bankruptcy Code, 2016 – An Analysis*, 9 Chartered Secretary 56 (2017).

[21] *Supra* note 12.

order dated 20th February 2017 passed by the Hon'ble National Company Law Tribunal, Principal Bench, New Delhi in ***Col. Vinod Awasthy v. AMR Infrastructure Limited***[22] in which the definition of "*Operational Creditor"* under the IBC to ascertain the applicability of the same to a flat purchaser has been interpreted by the Hon'ble Tribunal. In most cases, suppliers, contractors and customers are classified as operational creditors. Additionally the operational creditors are mostly unsecured. Banks and lenders usually come under the category of financial creditors and they can be secured or unsecured. Secured financial creditors and unsecured operational creditors differ in the priority of payments given to them upon liquidation. Therefore without any ambiguity it can be said that the law makers have chalked out distinct definitions of "financial creditor" and "operational creditor" and that they are not to be interpreted as mutually inclusive or exclusive of each other.

In ***Col. Vinod Awasthy v. AMR Infrastructure Limited***[23], the Hon'ble Tribunal dismissed the Petition instituted under Section 9 of the Insolvency and Bankruptcy Code, 2016 at the stage of admission itself. The tribunal decided the issue of whether; a *flat purchaser* would fall within the definition of an "*Operational Creditor*" as defined under Section 5(20) of the IBC to whom an "*Operational Debt"* as defined under Section 5(21) of the IBC is owed[24]. It was observed by the Hon'ble Tribunal that the architects of the IBC had not intended to include within the expression of an "operational debt" a debt other than a financial debt. The operational debt would therefore be limited to only four categories as defined in IBC Section 5(21) such as goods, services, and employment and government duties. The Tribunal held that "the debt owed to the claimant (in this case a purchaser) did not arise from any goods, services, jobs or duties payable to the Central / State or local authorities under any statute". The refund sought to be recovered by the petitioner was linked with the possession of immovable property.

The Hon'ble Tribunal while deciding the question of whether a flat purchaser could be considered an operation creditor considered the observations of the Bankruptcy Law Reforms Committee in paragraph no. 5.2.1 of the Final Report[25]:

"Operational Creditors are those whose liability from the entity comes from a transaction on operations. Thus, the wholesale vendor of spare parts whose spark plugs are kept in inventory by car mechanics and who get paid only after the spark plugs are sold is a

[22] Civil Petition No. (IB) 10 PB (2017).
[23] *Supra* note 2.
[24] Aarohee Gursale, *Financial Creditor And Operational Creditor Under The Insolvency And Bankruptcy Code, 2016,* MONDAQ (Jan.30, 2020, 8:09 PM), https://www.mondaq.com/india/InsolvencyBankruptcyRe-structuring/607738/Financial-Creditor-And-Operational-Creditor-Under-The-Insolvency-And-Bankruptcy-Code-2016.
[25] *Supra* note 9.

Operational creditor. Similarly, the lessor that the entity rents out space from is an operational creditor to whom the entity owes monthly rent on a three-year lease."

It was held by the Hon'ble Tribunal that, "the Petitioner had neither supplied goods nor had rendered any services to acquire the status of an Operational Creditor". Additionally it was held that the wide construction of Section 9 read with Section 5(20) and Section 5(21) of the IBC was not possible so as to include within its scope, cases where dues were on account of advance made to purchase a flat or a commercial site from a construction company or a builder like the Respondent, especially when the Petitioner had other remedies available under the Consumer Protection Act and the General Law of the land.

In conclusion it can be said that in order to succeed in kick-starting the corporate insolvency resolution process against a debtor, it is indispensable to prove that the creditor falls within the ambit and scope of the definition of either[26] "*Financial Creditor"* under Section 5(7) or "*Operational Creditor*" under Section 5(20) of the IBC. It is evident from the case law discussed above, that the Tribunals are very strict in their interpretation of the definition of "Operational Creditor" under the IBC and are generally refraining from hearing applications wherein the applicants are not strictly falling within the scope of the IBC and have alternate effective remedies available.

It is pertinent to note that the NCLAT's interpretation in the Essar Steel case by trying to create parity between secured creditors and operational creditors was defeating the very purpose and the spirit of the Insolvency Code. If rights of different classes of creditors are recognised equally, then in many cases, secured financial creditors will be incentivised to vote for liquidation rather than resolution, as they would have better rights if the corporate debtor was to be liquidated rather than a resolution plan being approved. This would defeat the entire objective of the Code which is to first ensure that resolution of distressed assets takes place and only if the same is not possible should liquidation follow.

If there was any ambiguity left, it has been removed by the recent judgement of the Supreme Court in the long pending Essar steel case[27] wherein the Supreme Court upheld the primacy of secured financial creditors over the operational creditors in the distribution of funds received under the corporate insolvency scheme. The Supreme Court also noted that the committee of creditors will have the final say in the resolution plans under the Insolvency and Bankruptcy Code, and that the NCLT and the NCLAT cannot interfere with the commercial

[26] Divyata Badiani, *India: Are Receivers Of Goods And Services, Operational Creditors?*, MONDAQ (Feb. 4, 2020, 7:35 PM), https://www.mondaq.com/india/InsolvencyBankruptcyRe-structuring/818044/Are-Receivers-Of-Goods-And-Services-Operational-Creditors.

[27] Committee of Creditors of Essar Steel India Limited v. Satish Kumar Gupta, SCC OnLine SC 1478 (2019).

decisions taken by the Committee of Creditors.

V. A STATISTICAL ANALYSIS OF CORPORATE INSOLVENCY RESOLUTION PROCESS

In the last decade a new phrase has found place in the narrative related to the national economy, Crony capitalism[28]. The Asian Financial Crisis as well as the subsequent economic disasters in Greece, Russia, Cyprus, and the Iberian Peninsula is said to be in part because of crony capitalism. Indian economy hasn't been immune to this nexus either. India's record bad-loan pile has been attributed, in part, to crony capitalism. In the last months of 2016, the Government of India sought to eliminate crony capitalism, and liberated about Rs. 7400 crores stuck in debt in diverse industries such as cement, steel, infrastructure, financing, housing and jewellery[29]. Hence the Insolvency and Bankruptcy Code (IBC) was a well-intentioned and the most ambitious piece of economic legislation in the country till date. But its record has been mixed since it was conceived in May 2016.

Due to Lengthy litigation, vested interests and periodic reinterpretations of the law, the IBC mechanism has been sluggish in extricating the stuck capital in unviable ventures. The **Essar Steel insolvency** is the most prominent example of the journey of IBC which can be termed as chequered at best. This case will be analysed in detail in the coming sections. It's been more than 600 days since this case valued at Rs 50,000 crore entered the IBC. Initially considered a shining example for the success of the new mechanism, this resolution programme has come to characterize the delays in what was a long-awaited judicial reform. According to details released by the Insolvency and Bankruptcy Board of India (IBBI), out of the 1,484 cases admitted for the corporate insolvency resolution process (CIRP), 586 have been closed till December 2018. That marks a hit rate of about 40%.[30]

As of March 2019, out of the 1858 admitted cases in CIRP, 152 have been closed. 91 cases have been closed by withdrawal under Section 12A. 94 cases have been closed by Resolution and 378 by Liquidation. In a massive 1143 cases, CIRP is still ongoing. This can be attributed to narrow interpretations by the courts of the insolvency law. Applications are to be admitted within 14 days, according to the Code. The courts have held a "position that these 14 days

[28] NARESH KHATRI, CRONY CAPITALISM IN INDIA 5 (Springer 2017). In crony capitalism, power and favors are wielded, exchanged, and acquired via an intricate system of personal contacts, favouritism, and championing of interests. Holcombe (2012) characterizes it as a system in which the profitability of a business depends on political connections.

[29] Bloomberg, *India's crony capitalism claims another victim*, ECONOMIC TIMES (Feb. 13, 2020, 4:30 PM), https://economictimes.indiatimes.com/industry/banking/finance/banking/view-indias-crony-capitalism-claims-another-victim/articleshow/68699683.cms?from=mdr.

[30] Joel Rebello, *With IBC about to be 3, a look at the hits & misses and the road ahead*, ECONOMIC TIMES (Feb. 17, 2020, 4:56 PM), https://economictimes.indiatimes.com/industry/banking/finance/banking/changes-challenges-and-interpretation-of-bankruptcy-law/articleshow/69017429.cms?from=mdr.

will be directory and not mandatory". Interpretation in this way allowed for filing of replies by corporate debtors and endless legal arguments. Subsequently, pending cases have not been admitted for more than a year. The most revered advantage of IBC was said to be timely resolution which is not true in absolute terms but in relative terms to Debt Recovery Tribunal or winding up under Companies Act, 2013[31]. However, the fear of IBC has worked in favour of banks where more and more defaulting borrowers are paying loans to avoid IBC proceedings. According to the World Bank, before IBC, the time taken to resolve stressed loans was 4.3 years and recovery rate was 26% for financial creditors. The recovery rate has improved to 48% recovery after two years of IBC. The time period is now about 1-1.5 years through the IBC[32].

VI. MERGERS & ACQUISITIONS UNDER THE LIGHT OF INSOLVENCY AND BANKRUPTCY CODE, 2016

A decline in M&A activity was observed in the first quarter of 2019, but nevertheless it is encouraging to see a steady pipeline of deals from 2015 to 2018. 2018 in particular, was a blockbuster year for M&A. Enabled through the corporate insolvency resolution process under the Insolvency and Bankruptcy Code, about 70% of the growth in M&A activity in 2018 was led by distressed deals. Mergers and acquisitions (M&A) activity in India has remained buoyant from 2015 well into 2019 with more than 3,600 M&A deals with an aggregate value of more than Rs. 2294 crores.[33] Several developments led to an unprecedented re-organisation of asset ownership in India. The present landscape provides a tremendous opportunity for well-managed business with strong foundations, looking for new avenues of growth and improving profitability.

Looking at the deals from January 2015 to April 2019, it can be seen that the profile of M&A in India has shifted significantly with more emphasis on making the M&A a success across the deal cycle. About 60 largest transactions by investors in India during this period, each valued at more than Rs. 1850 crores - are referred to as "large deals".

This can be attributed to the passage of the Insolvency and Bankruptcy Code (IBC) in 2016, which enabled bidding for several distressed assets in 2018. Deal volume has been robust across sectors, with industrial goods, energy, and telecom & media representing more than 60% of deals by volume and value. The largest deals took place in the energy and technology sectors. Notable examples include Walmart's acquisition of Flipkart (2018), the acquisition

[31] IBBI, *Discussion Paper on Corporate Liquidation Process along with Draft Regulations* (2019).
[32] *Supra* note 29.
[33] Harsh Pais et al., *2019 M&A Report: India*, International Financial Law Review (2019).

of Essar Oil by a Rosneft-led Russian consortium (2017), and Adani Transmission's acquisition of Reliance Infrastructure's integrated Mumbai power distribution business (2018). Thus the Insolvency and Bankruptcy Code, 2016 (IBC) has been widely considered a landmark legislation that has brought about a paradigm shift in the recovery and resolution process.

However, every coin has two sides and similarly there are many hurdles that have been posed by the Code. Entrusting multiple stakeholders with structuring the resolution plan was one issue that caused process delays[34]. Although the committee of creditors prepare the first draft, with varying recovery rates allocated to different types of creditors, this often gets challenged, resulting in further delays. IBC also did not clearly designate the preference order for financial secured, financial unsecured and operational creditors. Amendments released by the government in August 2019 address the lack of clarity on the priority-order of creditors. It also sets the process deadline to 330 days. With these amendments, it can be expected that the cases under IBC will get resolved more quickly and subsequently the slowdown seen in the M&A activity in 2019 probably will be short-lived.

VII. EXISTING PROBLEMS IN THE IBC REGIME AND WAY AHEAD

During the implementation of the IBC over the past two years and eight months, several challenges have emerged, including:

1. The Supreme Court recognises the paramount importance of following model timelines under Regulation 40A of the Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons), 2016 (CIRP Regulations) to ensure timely completion of CIRP[35]. However, adherence to the timelines (completion of corporate insolvency resolution process (CIRP) within 180 or 270 days), especially on account of intervening legal proceedings, has been almost impossible. The time spent in any legal proceedings that hinders the CIRP was excluded by the tribunals[36];

2. On account of judicial pronouncements[37] by the Hon'ble National Company Law Appellate Tribunal (NCLAT), including the recent one in ***Standard Chartered Bank vs. Satish Kumar Gupta, R.P. of Essar Steel Ltd. and Others***[38], the following position had emerged:

[34] MCA, *Report of the Insolvency Law Committee* (2018).
[35] Arcelor Mittal India Private Limited v. Satish Kumar Gupta and Others, SCC OnLine SC 1733 (2018).
[36] *Id.*
[37] CA (AT) Insolvency No. 289 of 2017 (NCLAT).
[38] **Standard Chartered Bank v. Satish Kumar Gupta, R. P. of Essar Steel Ltd. & Ors., Company Appeal**

(a) Financial and operational creditors must be given similar treatment; and

(b) discrimination amongst financial creditors on the basis of existing priorities or security interest is not permitted in a resolution plan;

3. There were serious ambiguities introduced by the NCLAT order[39], in the Essar Steel's insolvency resolution. NCLAT took the position that there cannot be any difference between an operational creditor and a financial creditor with regards to the priority given to the repayment of debt and that therefore, both should be treated equally under a resolution plan[40]. This equal treatment of financial and operational treatment can weaken the very foundations of the Insolvency Code;

4. The NCLAT has also taken the position, that the committee of creditors has no role to play in determining the manner of distribution of proceeds of a resolution plan amongst the financial or operational creditors, since the financial creditors comprising the Committee of Creditors are interested parties and there will be a conflict of interest if they are permitted to decide on the manner of distribution[41];

5. Applications to initiate CIRP have taken significantly more time than the prescribed 14 days in several cases. This is despite the requirement that the Adjudicating Authority has to ascertain the existence of a default from the records of an information utility or on the basis of other evidence provided by the financial creditor within 14 days of the receipt of an application by such financial creditor, as the timelines have been held to be directory and not mandatory[42];

6. It has been observed that a large volume of litigation is initiated by tax authorities against successful resolution applicants for recovery of pre-CIRP tax dues, even after approval of a resolution plan by the Adjudicating Authority[43];

Way Ahead

a) Clarity on allowing comprehensive corporate restructuring schemes such as mergers, demergers, amalgamations and so on as part of the resolution plan;

(AT) No. 242 (2019).

[39] ***Id.***

[40] Padmanabhan Venkatesh v. Shri V. Venkatachalam & Ors., Company Appeal (AT) (Insolvency) No. 128 (2019), I.A. No. 675 (2019).

[41] Id.

[42] Surendra Trading Company v. Juggilal Kamlapat Jute Mills Company Limited and Others, 16 SCC 143 (2017).

[43] Edelweiss Asset Reconstruction Co. Ltd. v. Euro Pallets Pvt. Ltd., MA 168 (2019).

b) Greater emphasis must be given on the need for time bound disposal at application stage;

c) A deadline for completion of CIRP within an overall limit of 330 days needs to be set including litigation and other judicial processes;

d) Votes of all financial creditors covered under section 21(6A) of the Code must be cast in accordance with the decision approved by the highest voting share (more than 50%) of financial creditors on present and voting basis[44];

e) A specific provision which states that the financial creditors who have not voted in favour of the resolution plan and operational creditors shall receive at least the amount that would have been received by them if the amount to be distributed under the resolution plan had been distributed in accordance with section 53 of the Code or the amount that would have been received if the liquidation value of the corporate debtor had been distributed in accordance with section 53 of the Code, whichever is higher. This will have retrospective effect where the resolution plan has not attained finality or has been appealed against[45];

f) Inclusion of commercial consideration in the manner of distribution proposed in resolution plan, within the powers of the Committee of Creditors;

g) A clarity must be there that the plan shall be binding on the all stakeholders including the Central Government, any State Government or local authority to whom a debt in respect of the payment of the dues may be owed;

The changes are expected to lead to timely admission of applications and timely completion of the Corporate Insolvency Resolution Process, greater clarity on permissibility of corporate restructuring schemes, manner of distribution of amounts amongst financial and operational creditors, clarity on rights and duties of authorized representatives of voters and applicability of the resolution plan on all statutory authorities[46]. The amendments are expected to address the issue of sanctity of timelines for completion of the entire corporate insolvency resolution process and also maximize the outcomes envisioned in the Code. The proposal is in line with the overall objective of the government to achieve the outcomes envisioned in the Insolvency and Bankruptcy Code and seeks to ensure speedier resolution of cases involving corporate debtors.

[44] *Rajya Sabha passes he Insolvency and Bankruptcy Code (Amendment) Bill 2019;Critical Gaps in corporate insolvency framework covered*, SCC ONLINE (Feb. 12, 2020, 5:16 PM), https://www.scconline.com/blog/post/tag/insolvency-and-bankruptcy-code-amendment-bill-2019/.
[45] Insolvency and Bankruptcy Code (Amendment) Act 2019.
[46] PTI, *Govt. clears 7 amendments to insolvency law*, PRESS TRUST OF INDIA (Feb. 28, 2020, 5:45 PM), http://www.ptinews.com/news/10713868_Govt-clears-7-amendments-to-insolvency-law.html.

VIII. ANALYSIS OF THE LATEST AMENDMENTS TO THE CODE

Going forward the government's biggest challenge will arise from the very amendments the government introduced to give more teeth to IBC. The amendments enacted so far have been inspired by various on-going and past cases but some of these amendments have led to ambiguity. Thus, it is important to analyse the upcoming cases of CIRP and Liquidation in a much more practical approach in line with the current business dynamics rather than just being regimental. Notwithstanding the four amendments effected to IBC, ambiguity and legal challenges still remain in the resolution process.

Given the importance that IBC has attained in the last two years and its potential impact, one cannot afford to be complacent about the relevant iterations and changes that needs to be brought about to improve its effectiveness:

a) For example, it is not clear whether the Resolution Professional is liable to conduct an independent scrutiny of the eligibility of the Resolution Applicant under Section 29 (A) of the IBC or he can rely on the affidavit submitted under Section 30(1);

b) The definition of related party under Section 29 (A) is stretched too far thus excluding potential bidders who do not have a shared interest with the promoters;

c) The period for which a potential bidder / promoter is ineligible to comeback as a stakeholder in the same company needs to be clarified;

d) The creditor's status did not fully address the problems of Home buyers as they stand fourth in the order of priority in the Waterfall Mechanism provided under Section 53 of the IBC;

e) The priority given to the payment of Operational Creditors (OCs) as per the fourth amendment over and above the Financial Creditors needs to be further refined and articulated;

f) Given the exponential addition in the number of cases expected to be referred to NCLT under IBC it is imperative to create additional benches to minimize the delay in the resolution process;

As per the IBC, the insolvency procedure can be initiated by a creditor with a default of an amount as low as Rs 1 lakh, which opens up the NCLT to a lot of additional burden with cases filed by operational creditors as part of the recovery effort. Recent government initiatives which empower the Registrar of Companies to handle minor violations of the

Companies Act eliminated the need to approach NCLT[47]. This would help in reducing the work load on NCLT while providing faster process for minor issues. New initiatives such as *Samadhan* and *Sashakt* which aim to encourage Pre-NCLT resolution for stressed companies may also lead to reducing the burden and effective utilization of the NCLT benches and avoid value diminishing due to delay in the resolution process at NCLT. However these alternatives have so far panned out to be only of theoretical significance since the mood with senior Bankers[48] seems to suggest that when it comes to taking haircut they prefer decision making through NCLT rather than sticking out their neck to endorse a resolution plan outside court process. This is ironical since Bankers are fully aware that Pre-NCLT solutions may clearly workout better in terms of overall recovery.

Empowering decision making based on merit with Banks and Financial institutions to take such bold calls without the fear of being questioned by Investigative Authorities is one of the most significant takeaways and can go a long way in terms of de-clogging the NCLT ecosystem. Training and support to Insolvency professionals is required to ensure that a high level of competence and professionalism is maintained in the resolution process.

In the author's opinion it may not be a bad idea to assess the suitability of resolution professional based on his sectoral expertise and exposure of dealing with similar cases rather just banking on historical empanelment with Committee of Creditors. Delays are also caused by procedural inefficiencies such as following the conventional internal processes for obtaining internal approvals for the resolution plan within each of the constituents of the Committee of Creditors. This needs to be streamlined within each of the Banks respectively according a Fasttrack approval and decision making process for IBC cases and also ensuring the decision makers to be a part of the Committee of Creditor's meetings when the resolution plan is being deliberated/ negotiated with the Resolution Applicant. Further legal hurdles are also contributing to the delays since stakeholders in several cases have moved to NCLAT and Supreme Court delaying the resolution process. In order to avoid inordinate delays there should be a hard stop on the review process and timelines, which unfortunately has lost essence in the current scenario given that more than half of the outstanding cases are expected to cross the prescribed deadline.

It would be better to have a more realistic timeline, even if it is as long as one year to ensure consistency in the resolution process across cases and maximize the recovery value. As per

[47] ISMT Limited v. Asmi Metal Products Private Limited, CP No. 3806 MB (2018).
[48] Dheeraj Tiwari, *PSBs can find resolution under Project Sashakt now*, ECONOMIC TIMES (Feb. 29, 2020, 6:34 PM), https://economictimes.indiatimes.com/markets/stocks/news/psbs-can-find-resolution-under-project-sashakt-now/articleshow/68698005.cms?from=mdr.

the provisions of IBC, in case of non-completion of the CIRP in 270 days, the adjudicating authority is required to pass an order to liquidate the corporate debtor. However, in most cases, the tribunal has further slowed down the process and extended the time period in the larger the interest of efficient resolution. Although the extensions are being granted with the right intention and aimed towards maximization of value, they are setting a bad precedent. Apart from the legal standpoint, with the stretched timelines the companies can lose sight of running business on a going concern basis leading to further value erosion. In liquidation scenario with extended timelines the recovery value diminishes at a rapid pace and hence such a process needs to be executed in a robust and timely manner.

IX. CONCLUSION

Experience across the world indicates that effective bankruptcy laws can help deepen the bond market. In countries such as Brazil, Russia, United Kingdom and China, the corporate bond market as a percentage of GDP has significantly increased after implementing bankruptcy reforms. The development of the nascent Indian bond market which is only about 17% of the GDP depends critically on the effective implementation of the IBC. To achieve the larger goals of the IBC to promote entrepreneurship and availability of credit and to improve ease of doing business in India and attract investment, it is imperative to swiftly address some of the above mentioned teething problems. However it is fair to conclude that irrespective of the time it takes for the process to stabilise the long term impact of the IBC initiative would certainly result in redeeming the Banking industry and infuse the much needed booster to the investor community and the Indian economy.

All said and done, the truth is that we have to measure the success or failure of the IBC relative to the previous system. It would be pertinent to say that there has been a marked improvement in the recovery process which is already leading to billions of dollars being invested in the country due to the protection of creditor rights. Compared to other markets, the pace at which we have achieved this is also noteworthy. In the US, for example, it took 10 years (from 1978) for the bankruptcy law to attain some stability. At one point, they were even considering repealing it. The progress in India has been remarkable by global standards. According per IBBI, approximately Rs. 2 lakh crores of debt pertaining to 4452 cases were disposed of even before admission into the IBC as the borrowers made good the amounts in default to their creditors. In the author's view this particular statistical data, which is often ignored, reflects the most significant achievement of IBC.

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