

COVID- 19 AND THE SUSPENSION OF IBC- A STEP BACK

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INTRODUCTION

The entry of a black swan event, i.e. COVID-19, has significantly affected the lives of people. The effects of this pandemic have been looming mainly on the economy. To overcome the unprecedented shock to the economy, Nirmala Sitharaman has recently announced a significant relief to cash-starved firms in the form of a suspension of Insolvency proceedings for six months which may extend up to one year. The Government of India in its move to amend the Insolvency and Bankruptcy Code (IBC) by introducing Section 10A in the code which suspends the Section 7, 9 and 10 of the IBC. In short, the creditors/lenders during these six months cannot file any fresh case for bankruptcy². However, the amendment is waiting for the President's approval³.

IMPACT OF INTRODUCTION OF SECTION 10A

Essentially, the intention of the government behind introducing Section 10A is to give some sigh of relief to companies. The Section 10A puts an embargo on Section 7, 9 and 10 of IBC. Section 7 lays down a provision under which the financial creditors can file an application for insolvency proceeding, Section 9 lays down a provision under which operational creditors can file an application for insolvency proceedings and under Section 10 the corporate debtor can itself file an application for initiating insolvency proceedings⁴. Although the suspension of these sections acts as a breather for those companies who have a fear of being dragged into NCLT, these changes will serve as a dark phase for the creditors. These changes will bleed the balance sheet

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² Timsy Jaipuria, *Government to suspend insolvency proceedings for six months- amends IBC*, CNBC TV 18, available at <https://www.cnbctv18.com/legal/govt-allows-temporary-relief-from-insolvency-proceedings-for-firms-5758061.htm>, last seen on 24/04/2020.

³ Arnav Sinha, *Case against Suspension of the Insolvency and Bankruptcy Code amidst COVID-19*, The Indian Review of Corporate and Commercial Laws, available at <https://www.irccl.in/single-post/2020/05/22/Case-against-Suspension-of-the-Insolvency-and-Bankruptcy-Code-amidst-COVID-19-Lockdown>, last seen on 24/05/2020.

⁴ Anjali Bhatia, *No Fresh Insolvency cases for a year- A narrow escape for companies*, IBC Laws, available at <https://ibclaw.in/no-fresh-insolvency-cases-for-a-year-a-narrow-escape-for-companies-by-advocate-kajal-bhatia/>.

of creditors. Here, the question arises that does the amendment of blanket suspension will serve the legislative intent of government? Is there a need to give a closer look to the amendment? Will there be unintended consequences that still need to be evaluated? Are we going back to Pre-IBC period?

ANALYSIS

Does the suspension of IBC serve the purpose of code? It does not serve the purpose of IBC. There is no doubt that the IBC is one of the finest reforms in India which acted as a ray of hope for ease of doing business. In Bankruptcy Law Reforms Committee report, the committee stated that the objective of bankruptcy reforms is to avoid problems in extreme downturns in the business cycle¹. But the blanket suspension of IBC has thwarted the way for better insolvency outcomes.

The powers given to the creditors under Section 7 and 9 for applying to insolvency proceedings will be taken away. This has triggered the creditor in control regime of IBC, which played a significant role in its success. These recent changes will do exactly opposite, and we will be again reverted to debtor-in control regime. This will force the creditors to accept the unfair demands of corporate debtors, and it will also put them in an unreasonable position.

Even if we consider the intention of government behind the suspension of Section 7 and 9, the decision makes sense but the suspension of Section 10 will not serve the purpose. It closes all the doors for the corporate debtor to go for voluntary insolvency. This can also be used as a tool by wilful defaulters to escape from the legal proceedings. It won't be too far-fetched to say that it is a double-edged sword which can be used by corporate debtors.

However, it is pertinent to note that the insolvency proceedings against personal guarantors have not been suspended. If the promoters of a company have provided personal guarantees to lenders, the companies may still be dragged into courts under Part III of IBC.

¹ Ministry of Finance, Government of India, *The Report of the Bankruptcy Law Reforms Committee Volume 1: Rationale and Design November 2015*, available at https://ibbi.gov.in/BLRCReportVol1_04112015.pdf.

The attention has to be drawn towards the limited alternative remedies that will be available to the creditor to get their claims back. After the suspension of IBC, the creditors will have to go for extensive litigation which will lead to undue delays. The creditors can file a summary suit under Order XXXVII of CPC or file a commercial suit under Commercial Courts Act, 2015. The lenders can also take over the management of a company under SARFAESI ACT, 2002 if they hold a mortgage over the immovable properties of a debtor.

No doubt, the suspension of IBC along with the operation of other recovery laws, will not achieve the objective of its suspension, but it will surely deprive both creditors and debtors of the benefits under IBC¹.

SUGGESTIONS

The ominous cloud of recession or at least a hitherto inexperienced economic slowdown requires a robust framework for rehabilitation more than ever before². But a blanket suspension of the IBC is an incomplete solution to keep the wheel of an economy moving. It could result in further delays in the already overburdened system and result in other unintended consequences³. Various channels are available to the government to make the insolvency regime better in the situation of global crisis other than a blanket suspension of IBC.

The introduction of Pre-Pack deals will also act as a blessing in disguise⁴. Although Section 29A is a significant hindrance to introducing Pre-Pack deals, it can be added as an exception under IBC. However, there are various criticisms regarding the introduction of Pre-Pack schemes in India. Therefore, India needs a new-devised Pre-Pack policy where operational creditors can also

¹ Hemant Kothari, *Suspension of IBC- A Half Baked solution to ease financial stress*, Money Control, available at <https://www.moneycontrol.com/news/economy/policy/suspension-of-ibc-its-a-half-baked-solution-to-ease-financial-stress-5285481.html>, last seen on 19/05/2020.

²Krishnava Dutt, *Is IBC suspension antithetical to pandemic protection*, The New Indian Express, available at <https://www.newindianexpress.com/opinions/2020/may/26/is-ibc-suspension-antithetical-to-pandemic-protection-2147967.html>, last seen on 26/05/2020.

³Aditi Deshpande, *Fresh Insolvency to be suspended for Six months under the IBC*, available at <https://www.outlookindia.com/outlookmoney/talking-money/fresh-insolvency-to-be-suspended-for-six-months-under-the-ibc-4638>, last seen on 15/04/2020.

⁴ Anandaday Mishra, *Pre-Packaged Deals in IBC*, Tax Guru, available at <https://taxguru.in/corporate-law/pre-packaged-deals-ibc.html>, last seen on 8/05/2020.

be a part of the decision-making process. The increase in the moratorium period under IBC is another change that could have been brought in by the government.

The attention has to be drawn towards the case of *Union of India v. Infrastructure Leasing and Financial Services Limited & Others*¹, in which NCLAT had granted a moratorium relief over the loans taken by the IL & FS and its 348 subsidiaries². The relief had been granted under Section 241 and 242 of the Companies Act, 2013. The NCLAT had passed this order under the principle of equity, keeping in mind the economic interest of the nation and IL & FS. Similarly, in the case of *Bhupinder Singh v Unitech Limited*³, the Supreme Court also granted two months moratorium relief to Unitech from any legal proceedings against the company's management⁴.

Courts can also take the approach adopted by the courts in these two cases, in the recent scenario where moratorium relief can be granted to corporate debtors depending upon various factors such as the nature of the default, economic interest of company and public. Another amendment of the government to exclude 'COVID-19' related debt from the definition of default and increase in threshold limit from Rs. 1 lakh to 1 crore already serves the purpose of government to protect MSMEs and Corporate Debtors from insolvency proceedings. But these amendments seem redundant in the light of the blanket suspension of IBC.

Various countries like the United Kingdom, Singapore, Belgium and Germany etc. across the globe have changed the procedural aspects of Insolvency and Bankruptcy laws. Still, no country has put a blanket suspension of Insolvency and Bankruptcy Code. Thus, the effects of the blanket suspension of insolvency proceedings call for an urgent need to revisit the decision, and the government has to devise a policy by balancing the interest of both creditors and debtors.

¹ Union of India v Infrastructure Leasing & Financial Services Limited and Others, Company Appeal (AT) No. 346 of 2018 (NCLAT New Delhi, 12/10/2018).

² Shashank Pandey, *Explainer- The IL & FS Insolvency case*, Bar and Bench, available at <https://www.barandbench.com/columns/ilfs-insolvency-the-journey-so-far>, last seen on 21/07/2019.

³ Bhupinder Singh v Unitech Limited, Civil Appeal No. 10856/2016 (Supreme Court, 20/01/2020).

⁴ *Government to take management control of Unitech- Supreme Court agrees*, Live mint, available at <https://www.livemint.com/companies/news/govt-to-take-over-management-control-of-unitech-supreme-court-agrees-11579517982836.html>, last seen on 20/01/2020.