

STUDENTS' ECONOMIC FORUM

A monthly publication from South Indian Bank

*To kindle interest in economic affairs...
To empower the student community...*



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Student's corner

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Insolvency & Bankruptcy Code, 2016



WHY

WHO

WHEN

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HOW

May 2017

Theme 306

**INSOLVENCY AND BANKRUPTCY CODE, 2016 – PART II
(INSOLVENCY RESOLUTION PROCESS FOR CORPORATES)**

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Theme No: 306: Insolvency and Bankruptcy Code, 2016 – Part II
(Insolvency Resolution Process for Corporates)

A well informed customer will make the policy makers as well as organizations which produce goods and render services more responsive to the customer needs. This will also result in healthy competition among organizations and improve the quality of its products.

The “SIB Students’ Economic forum” is designed to kindle interest in the minds of younger generation. We highlight one theme in every monthly meeting of the “Forum”. This month, we will discuss “Insolvency and Bankruptcy Code, 2016 – Part II (Insolvency Resolution Process for Corporates)”.

Business failure affects all the stakeholders of an organization including its lenders, shareholders, creditors, suppliers, customers, workers and central / state governments, very adversely. It is, therefore, essential that the valuable resources including capital, manpower, machinery and management, are pulled out of the failed / unviable businesses at the earliest and are deployed in other profitable ventures. The viable businesses are however, required to be re-organized at the earliest.

If the stakeholders can make rational and quick decisions to deal with corporate insolvency i.e. the decision about continuation of business, its re-organization or its closure, a law to deal with the insolvency and the related intervention of the courts may not be required. However, it has been observed that the stakeholders fail to take such decisions to deal with the situation of insolvency and therefore the need for a corporate insolvency law.

1. What is the difference between Insolvency & Bankruptcy?

Insolvency is when an individual or organization is unable to meet its outstanding financial debt due towards its lender. Insolvency can be resolved by way of changing the repayment plan of the loans or writing off a part thereof. If it cannot be resolved, then a legal action may be pursued against the insolvent and his / her assets will be sold to pay off the outstanding debts. Generally, an official assignee/liquidator appointed by the Government of India, realizes the assets and allocates it among the creditors of the insolvent.

Bankruptcy is a concept slightly different from insolvency, in that it is rather amicable. Bankruptcy is when a person voluntarily declares himself as an insolvent and goes to the court. On declaring him/her as ‘bankrupt’, the court liquidates the personal property of the insolvent debtor and hands it out to the creditors. It provides

a fresh lease of life to the insolvent. Thus Insolvency is a situation where a debtor is unable to meet his / her obligations and Bankruptcy is a legal process by which an insolvent debtor seeks relief.

2. Who can initiate corporate insolvency resolution process?

When any corporate debtor commits a default, a financial creditor / an operational creditor itself may initiate corporate insolvency resolution process in respect of such corporate debtor.

A financial creditor either by itself or jointly with other financial creditors may file an application for initiating corporate insolvency resolution process against a corporate debtor before the Adjudicating Authority when a default has occurred.

An operational creditor may on the occurrence of a default deliver a demand notice for the unpaid amount or copy of an invoice demanding the payment of the amount involved in the default to the corporate debtor. The corporate debtor shall, within a period of ten days of the receipt of the demand notice or copy of the invoice, bring to the notice of the operational creditor any existence of a dispute. If the operational creditor does not receive payment from the corporate debtor or notice of the dispute within 10 days of the receipt of the demand notice, the operational creditor may file an application before the Adjudicating Authority for initiating a corporate insolvency resolution process.

3. What is the Time-limit for completion of Corporate insolvency resolution process?

The corporate insolvency resolution process shall be completed within a period of one hundred and eighty days from the date of admission of the application to initiate the insolvency process. The resolution professional shall file an application to the Adjudicating Authority to extend the period of the corporate insolvency resolution process beyond one hundred and eighty days. A resolution is passed at a meeting of the committee of creditors by a majority of seventy-five per cent of the votes. If the Adjudicating Authority is satisfied that the corporate insolvency resolution process cannot be completed within a period of one hundred and eighty days, it is extended for a further period but not exceeding ninety days.

4. Briefly describe the Corporate Insolvency Resolution Process (IRP)?

The IRP provides a collective mechanism to lenders to deal with the overall distressed position of a corporate debtor. This is a significant departure from the existing legal framework under which the primary onus to initiate a reorganisation process lies with the debtor, and lenders may pursue distinct actions for recovery, security enforcement and debt restructuring.

The Code envisages the following steps in the IRP:

- i. A financial creditor (for a defaulted financial debt) or an operational creditor (for an unpaid operational debt) can initiate an IRP against a corporate debtor at the National Company Law Tribunal (NCLT). The defaulting corporate debtor, its shareholders or employees, may also initiate voluntary insolvency proceedings.

- ii. Corporate insolvency process shall be completed within 180 days of admission of application by NCLT. Upon admission of application by NCLT, Creditors' claims will be frozen for 180 days, during that time NCLT will hear proposals for revival and decide on the future course of action. No coercive proceedings can be launched against the corporate debtor in any other forum or under any other law, until approval of resolution plan or until initiation of liquidation process.
- iii. NCLT appoints an interim Insolvency Professional (IP) upon confirmation by the Insolvency and Bankruptcy Board within 14 days of acceptance of application. Interim (Insolvency Professional) IP holds office for 30 days only. Interim IP takes control of the debtor's assets, company's operations and collects financial information of the debtor from information utilities.
- iv. NCLT causes public announcement to be made of the initiation of corporate insolvency process and calls for submission of claims by any other creditors.
- v. After receiving claims pursuant to public announcement, interim IP constitutes the creditors' committee. All financial creditors shall be part of creditors' committee and if any financial creditor is a related party of the corporate debtor, then such financial creditor will not have any right of representation, participation or voting. Operational creditors should be part of Creditors' Committee if their aggregate dues are not less than 10% of the debt.
- vi. Creditors' committee shall meet first within seven days of its constitution and decide by 75% of votes either to replace or confirm interim IP as Resolution Professional. Thereupon, Resolution Professional is appointed by the NCLT upon confirmation by the Board. The creditors' committee, with a majority of 75% votes, can change Resolution Professional any time.
- vii. The creditors' committee has to then take decisions regarding insolvency resolution by a 75% majority voting.
- viii. If three-fourths of the financial creditors consider the case as complex and require extension of time beyond 180 days, the NCLT can grant a one-time extension up to 90 days.
- ix. Resolution Professional to conduct entire corporate insolvency resolution process and manage the corporate debtor during the period.
- x. Resolution Professional shall prepare information memorandum for the purpose of enabling resolution applicant to prepare resolution plan. A resolution applicant means any person who submits resolution plan to the resolution professional. On receipt of resolution plans, Resolution Professional shall place it before the creditors' committee for its approval.
- xi. Once a resolution is passed, the creditors' committee has to decide on the restructuring process that could either be a revised repayment plan for the company or liquidation of the assets of the company. If no decision is made during the resolution process, the debtor's assets will be liquidated to repay the debt.
- xii. The resolution plan will be sent to NCLT for final approval, and implemented once approved.

5. Under which circumstance is the corporate debtor put into liquidation?

A corporate debtor is put into liquidation in the following scenarios.

- (i) A 75% majority of the creditor's committee resolves to liquidate the corporate debtor at any time during the insolvency resolution process.
- (ii) The creditor's committee does not approve a resolution plan within 180 days (or within the extended 90 days).
- (iii) The NCLT rejects the resolution plan submitted to it on technical grounds.
- (iv) The debtor contravenes the agreed resolution plan and an affected person makes an application to the NCLT to liquidate the corporate debtor.

Once the NCLT passes an order of liquidation, a moratorium is imposed on the pending legal proceedings against the corporate debtor, and the assets of the debtor (including the proceeds of liquidation) vest in the liquidation estate.

6. What is the order of priority for distribution of assets in case of liquidation?

- i. Insolvency related cost
- ii. Secured creditors and workmen dues upto 24 months
- iii. Other employees' Salaries/dues upto 12 months
- iv. Financial debts (unsecured creditors)
- v. Government dues (upto 2 years)
- vi. Any remaining debts and dues
- vii. Equity

7. Briefly explain the manner in which fast track corporate insolvency resolution process is initiated.

An application for fast track corporate insolvency resolution process may be filed by a creditor or corporate debtor along with the:

- (a) The proof of the existence of default as evidenced by records available an information utility or such other means as may be specified by the Board.
- (b) Any other information as may be specified by the Board to establish that the corporate debtor is eligible for fast track corporate insolvency resolution process.

8. What is the time frame for completing the fast track corporate insolvency resolution process?

The fast track corporate insolvency resolution process shall be completed within a period of ninety days from the insolvency commencement date. The Adjudicating Authority can give an extension in time period not exceeding forty five days if the insolvency resolution process is not completed within the stipulated period.

9. Briefly explain the Voluntary Liquidation of Corporate person?

The Code provides for voluntary liquidation proceedings by a corporate person who intends to liquidate it and has not committed any default and can pay off its debts fully from proceeds of liquidation of its assets. The law requires a declaration to that effect from majority of directors of the company stating that the company is not being liquidated to defraud any person. A resolution passed to this effect shall be approved by creditors representing two-thirds value of the company's debts.



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