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Yearly Rewind 2023

INSOLVENCY & RESTRUCTURING

INDEX

INSOLVENCY AND RESTRUCTURING

In this section, we detail the path that the Code has taken in terms of its evolution and emerging jurisprudence; the continual improvements during the past one-year, key judgments and amendments, the impact that the law has had on stakeholders, and lastly, what lies ahead (hopefully).

The number game – how the Code fared in 2023

While the overarching objective of the Code, as articulated in its preamble, is the timely reorganization and resolution of corporate insolvency, aiming to maximize asset value, the quarterly newsletters from the Insolvency and Bankruptcy Board of India (**IBBI**) for July-September 2023 *(read the report **here**)* paints an interesting picture.

Insolvency Proceedings – better recovery, but delayed timelines

As of September 2023, a whopping 7,058 Corporate Insolvency Resolution Processes (**CIRPs**) have kicked off, and 2,001 are still ongoing. However, 808 of these 7,058 CIRPs have culminated in successful resolution plans for the corporate debtors (**CD** / **CDs**) while 2,249 have been pushed into liquidation. Further, the successful CIRPs have yielded the creditors INR 2.92 trillion (~USD 35.19bn) against their claims of INR 9.23 trillion (~USD 111.23bn), resulting in a realization of 31.62%. Financial creditors secured 33.8% of their claims, while operational creditors recovered 18.3%.

Table No. 1
Outcome of CIRPs
(No. of CIRP)

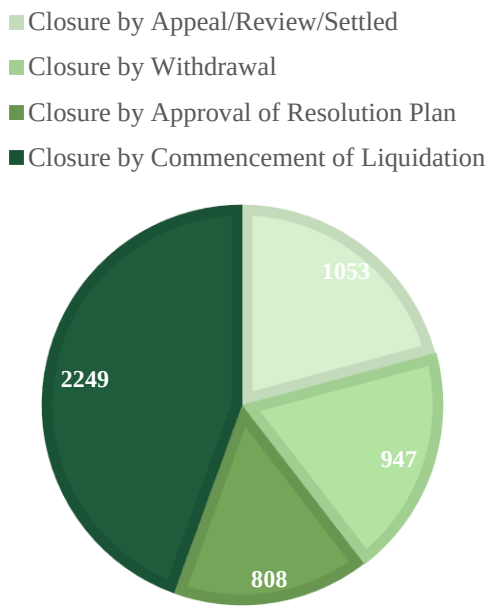
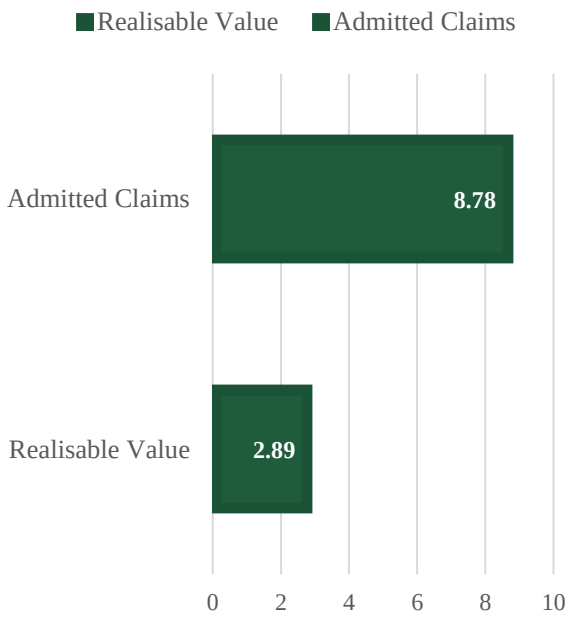


Table No. 2
Realisation of claims
(amt. in INR trillions)



The average duration for the resolution of successful CIRPs was 653 days, posing a challenge in meeting the mandatory 330-day timeline stipulated in the Code. Another issue in this regard is the extended duration for admitting insolvency cases, typically taking upwards of 12 months. For example, the application for CIRP of

Reliance Naval & Engineering Ltd. took about 16 months for admission highlighting the gap between the letter of law and ground realities.

Media reports claim that the Central Government is planning to establish dedicated benches within the National Company Law Tribunal (**NCLT**) which will focus solely on the admission or rejection of insolvency petitions. This initiative aims to streamline the process, ensuring decisions are made within the 14-day timeframe stipulated in the Code. The data shows that the present infrastructure is inadequate for completing CIRP within the prescribed 330 days. Accordingly, it is expected that these specialized benches will facilitate timely adjudication of applications for admission of the CDs into CIRP.

Liquidation process – liquidation is the norm

As of September 2023 (*see Table Nos. 1 and 2)*, out of the 7,058 admitted CIRPs, 2,249 cases have been admitted to liquidation, constituting 31.8% of all admitted CIRPs. Interestingly, only 808 CIRPs have been successful, representing merely 11% of the total admitted cases. The recent ruling in *Gayatri Polyrub Pvt. Ltd. v. Anil Kohli & Anr.* by the National Company Law Appellate Tribunal (**NCLAT**) reiterated the Code's primary objective of reviving the CD, emphasizing that liquidation should be the last resort.

However, despite this intent of the Code, the trend seems to be moving more towards liquidation than resolution. It is possible that banks and financial institutions, facing delays in the resolution process and asset value depreciation, may prefer timely liquidation over prolonged resolution, with concerns about inadequate recovery and extended timelines.

Illustrative cases include the insolvency of Lavasa Corporation Limited, lasting almost 5 years and concluding in July 2023, where the recovery amounted to 24% of the total claim of INR 66.42 billion (~USD 800.4mn). Similarly, Indu Projects Limited, admitted to insolvency in February 2019, saw a resolution plan approved in July 2023, offering INR 3.9 billion (~USD 47mn) against an admitted debt of INR 39 billion (~USD 470mn), reflecting a significant haircut of almost 90%!

Fate of pre-packs

The introduction of the Pre-packaged Insolvency Resolution Process (**PPIRP**) during the pandemic aimed to safeguard Micro, Small, and Medium Enterprises (**MSMEs**), vital to the Indian economy, from insolvency. Unlike regular CIRPs, PPIRP follows a debtor-in-possession model, preserving the board of directors without transferring management to the resolution professional. Despite its distinct structure, as of September 2023, only 6 applications have been admitted, with 1 withdrawal and 3 approved resolution plans for Amrit India Limited (18.79% recovery), Sudal Industries Limited (33.2% recovery), and Shree Rajasthan Syntex Limited (37.55% recovery). 2 PPIRP cases are still pending.

The Institute of Cost Accountants of India's Insolvency Professional Agency suggests that the limited response may stem from the hesitancy shown by financial institutions to invoke PPIRP *(read more **here**)*. Notably, in PPIRP, creditors have early insight into the potential haircut, whereas in CIRP, the extent of the haircut becomes clear at a later stage, and possibly, the creditors anticipate a relatively favourable resolution plan.

Use of technology in insolvency space

To address the issue of delays in admission of insolvency applications, the Code now recognizes the Record of Default (**RoD**) from an Information Utility (**IU**) as evidence of debt and default, aiding the NCLT in deciding on insolvency proceedings. The Code mandates the submission of RoD as evidence of default in CIRP initiation applications. The National E-Governance Services Ltd. (**NeSL**), the sole IU, has issued approximately 112,017 RoDs to support the insolvency ecosystem by the end of September 2023.

Effectiveness of the Code vis-à-vis earlier legislations

According to a November 2023 report by CRISIL *(read more **here**),* the recovery rates under the Code surpass those of other mechanisms, averaging between 5-20%. This highlights the Code as the most effective avenue for lenders to recuperate their dues. 720 CIRPs have been withdrawn due to settlement between CD and the creditors. Further, 26,000 applications having underlying default of INR 9.33 trillion (~USD 112.42bn) have been withdrawn before their admission.

Major judgments and amendments

Improving outcomes in real estate cases

As of September 2023, the real estate sector accounted for 21% of all admitted CIRPs, totalling 1,482 cases. However, only 121 of these cases have seen successful resolution plans, while 404 have been admitted into liquidation. Despite the significant presence of the real estate sector in the Code, it is observed that insolvency resolution of CDs in this sector have posed a major challenge due to the peculiarities of this sector.

Though the Code has clarified the status of the allottees in a real estate project as financial creditors and made them a core part of the Committee of Creditors (**CoC**), at times, their divergent interests do not align with the scheme of the CIRP. Unlike banks and financial institutions, these real estate allottees typically favour obtaining possession of the property over partial refunds through the insolvency process. To protect the interests of allottees, several judicial experiments have been conducted to adapt CIRPs to the nature of the real estate sector, such as 'reverse CIRP' *(read our article **here**)* and 'conjoined CIRP' *(read our article **here**)*.

In a significant decision in *Mist Avenue Pvt. Ltd. v. Nitin Batra & Ors.*, the NCLAT has ruled on the maintainability of a joint petition under the Code to seek conjoined CIRP of three corporate entities linked to a common real estate project. The NCLAT upheld the joint petition, emphasizing the interconnectedness of the three entities and the necessity for their inclusion in the CIRP to ensure project resolution and prevent losses to allottees. This decision showcases the commitment of the insolvency courts to find pragmatic solutions for complex issues arising out of real estate projects.

The Supreme Court of India, in the case of *Vishal Chelani & Ors. v. Debashis Nanda*, has clarified the status of home buyers in insolvency proceedings under the Code. The Supreme Court ruled that all home buyers, irrespective of their recovery decree under the Real Estate (Regulation and Development) Act, 2016 (**RERA**), should be treated as financial creditors in insolvency proceedings and they cannot be treated differently. This landmark judgment ensures fairness and equity in dealing with the financial claims of home buyers and sets a significant precedent for the treatment of such cases in India.

Supreme Court clears the path for personal guarantor insolvency

Following the enactment of the Insolvency and Bankruptcy Code (Second Amendment) Act, 2018, and subsequent notification No. S.O. 4126 dated 15 November 2019, insolvency proceedings may be initiated by creditors against personal guarantors even where no proceedings are initiated against the CD *(read our article **here**)*.

As of September 2023, a total of 2,289 applications have been submitted to initiate the Personal Guarantors Insolvency Resolution Process (**PGIRP**), with 282 admissions. Out of these admitted PGIRPs, 90 cases have been successfully concluded, 21 with approved repayment plans. In these resolved cases, creditors have recovered INR 912.7 million (~USD 11mn), constituting 5.22% of their admitted claims.

A landmark ruling by the Supreme Court in *Surendra B. Jiwrajika v. Omkara Assets Reconstruction Pvt. Ltd.* has upheld the constitutionality of the Code's provisions related to PGIRP (sections 95 to 100). This decision dismissed 384 petitions challenging the legal validity of these provisions, where the petitioners argued that personal guarantors were not afforded an opportunity to present their case prior to the initiation of the insolvency resolution process. The Supreme Court, however, ruled that these provisions cannot be deemed unconstitutional for not providing a hearing opportunity to personal guarantors before the insolvency petition is admitted.

Effect of breach of settlement agreement under the Code

The issue of reviving a CIRP after withdrawal due to a breach of settlement terms has sparked conflicting judgments in various NCLTs. The question at hand is whether the CIRP is automatically revived in case of breach of a settlement agreement or whether the creditor must file a fresh application under the Code. The recent NCLAT judgment in *IDBI Trusteeship Services Ltd. v. Nirmal Lifestyle Ltd.* settles the controversy, ruling that an insolvency petition may be revived upon a breach of settlement terms if the terms allow for such revival *(read our article **here**)*.

Leased oil assets outside moratorium

On 14 June 2023, the Ministry of Corporate Affairs (**MCA**) issued a notification which will impact CDs involved in transactions, arrangements, or agreements governed by the Oilfields (Regulation and Development) Act, 1948. In essence, petroleum assets leased by a company undergoing CIRP will no longer enjoy the protective shield of the moratorium provided by the Code. The rationale behind this move seems to ensure that crucial national assets in the petroleum sector do not remain inactive during CIRP. This move highlights the economic importance of the oil sector and aims to facilitate the seamless continuation of projects critical for various economic activities *(read our update **here**)*.

Big relief to aircraft lessors in airline insolvencies

On 03 October 2023, the MCA issued a notification exempting arrangements involving aircraft, aircraft engines, airframes, and helicopters from the moratorium imposed by the Code. This decision was likely prompted by the global aviation community's strong critique of Go Airlines (India) Ltd. (**Go First**) CIRP *(read our update **here**)*.

In the Go First CIRP, aircraft lessors raised concerns about the Code's moratorium conflicting with their rights under the Cape Town Convention on International Interests in Mobile Equipment. The disparity lies in the rights of creditors/lessors to reclaim leased aircraft during the lessee/debtor's insolvency. While the Code's moratorium prohibits asset repossession during the CIRP, the Cape Town Convention requires the debtor to return the aircraft to the lessor within 60 days of an insolvency-related event. This discrepancy posed challenges for foreign lessors of Go First, hindering their ability to reclaim aircraft. The MCA notification signals India's commitment to align with the Cape Town Convention obligations.

Avoidance Application – major ambiguities resolved

Under the Code, the resolution professional/liquidator is mandated to identify and reverse avoidable transactions (preferential, undervalued, defrauding creditors, and extortionate transactions) by filing avoidance applications before the NCLT. Previously, a Delhi High Court single bench ruled that NCLT lacks jurisdiction post-approval of a resolution plan to decide such applications. However, the Division Bench, in *TATA Steel BSL Ltd. v. Venus Recruiter Pvt. Ltd.,* has now ruled that avoidance applications can continue even after CIRP approval, emphasizing the need to uncover dubious transactions and prevent wrongful benefits to promoters and other parties *(read our article **here**)*.

In the case of *Arvind Garg, Liquidator of Carnation Auto India Pvt. Ltd. v. Jagdish Khattar & Ors.,* an interesting issue arose on whether the legal representatives of a deceased director of the CD can be impleaded in the proceedings concerning avoidable transactions. The NCLAT allowed the impleadment of the director's widow as his legal representative, considering her possession of the late director's estate and her status as a legal heir. This decision sets an important precedent, aiding insolvency professionals in recovering misappropriated assets and returning funds to the CD *(read our article **here**)*.

The Code provides a 'look back period' for investigating avoidance transactions by a CD. This period is two years for transactions with related parties and one year for others. However, fraudulent transactions don't have a specified look back period in the Code. Typically, if a limitation period isn't defined, the action can be taken within three years under the Limitation Act, 1963. In *Mr. Thomas George v. K. Easwara Pillai and Others*, the NCLAT ruled that the three-year limitation doesn't apply to fraudulent transactions under the Code. This means

insolvency professionals can investigate beyond the period of three years from the initiation of CIRP for fraudulent transactions *(read our article **here**)*.

Speaking of fraudulent transactions, Section 65 of the Code addresses potential misuse of insolvency applications by imposing penalties of up to INR 10 million on those fraudulently initiating CIRP. The key issue was whether Section 65 applied when an application for initiation of CIRP was pending admission before the NCLT. In *Ashmeet Singh Bhatia v. Sundrm Consultants Pvt. Ltd. and Anr.*, the NCLAT clarified that Section 65 is applicable even when the CIRP application is pending admission before the NCLT and fraudulent initiation of CIRP can be challenged even before 'admission' *(read our article **here**)*.

Supreme Courts emphasis on time bound processes under the Code

In the recent case of *RPS Infrastructure Ltd. v. Mukul Kumar & Anr.,* the Supreme Court emphasized that claims filed after the approval of a resolution plan by the CoC cannot be entertained, as allowing such claims could potentially jeopardise the resolution plan that had already received the CoC's approval and this will disrupt the time bound insolvency resolution process. This ruling reinforces the Code's objectives of a creditor-driven, time-bound resolution process.

The Supreme Court decision in *Eva Agro Feeds Pvt. Ltd. v. Punjab National Bank* has significant implications for the powers and responsibilities of Liquidators under the Code. This case involved the cancellation of an auction during the liquidation process of the CD, raising questions about the discretion of the liquidator and the rights of the highest bidder. The Court ruled that the liquidator cannot cancel auctions without providing reasons, emphasizing the importance of a thoughtful decision-making process. It highlighted that mere expectation of a higher price is an insufficient ground for cancelling a valid auction, as such actions could incur unnecessary expenses and undermine the credibility of the auction process. The judgment reinforces the idea that the liquidator must operate within a legal framework, performing duties for the benefit of all stakeholders while upholding the law.

Power to "recall" judgments

In *Union Bank of India v. T. Venkatasubramanian and Others,* a five-member bench of the NCLAT clarified the authority of insolvency tribunals i.e., NCLT and NCLAT to recall their earlier orders. The ruling establishes that insolvency tribunals, similar to judicial bodies, possess inherent power to recall orders based on the violation of principles of natural justice. This decision brings clarity to the ongoing confusion and conflicting opinions on whether insolvency tribunals have the jurisdiction to recall their previous rulings *(read our article **here**)*. The Supreme Court in *Union Bank of India v, Financial Creditors of M/s Amtek Auto Limited & Ors.* upheld the view taken by NCLAT.

Amendment to the CIRP process

The IBBI introduced the IBBI (Insolvency Resolution Process for Corporate Persons) (Second Amendment) Regulations, 2023 on 18 September 2023. The amendments include:

1. Detailed information required from creditors in CIRP initiation applications.
2. Procedures for the resolution professional's control of assets and records.
3. Extended timelines for claim filing by creditors.
4. Enhanced roles and fees for authorized representatives.
5. Committee-approved audits of the CD.
6. Synchronized procedural timelines.
7. Changes in the invitation for expression of interest.
8. Inclusion of CoC minutes in compliance certificates to be filed by the resolution professional.

9. Prompt disclosure of debt assignment details by creditors. *(read our update **here**)*

Supreme Court clarifies law on MSME registration during CIRP

MSMEs have played an indispensable role in the Indian economy for decades, particularly fostering entrepreneurship in semi-urban and rural regions. The insertion of Section 29A into the Code in 2017 outlined the criteria for individuals who are ineligible to submit resolution plans for CDs, including promoters of the CD. Subsequently, Section 240A was introduced in the Code in 2018, exempting MSME CDs from certain restrictions imposed by Section 29A. Consequently, the promoter of a MSME CD is eligible to submit a resolution plan for the same.

However, a 2021 ruling by the NCLAT in *Digamber Anand Rao Pingle v. Shrikant Madanlal Zawar & Ors.* had established that former promoters/directors of CDs cannot bypass their ineligibility under Section 29A by obtaining MSME registration during CIRP.

This position has now been reversed by the Supreme Court of India by its 2023 judgment in *Hari Babu Thota*, affirming that promoters of MSME CDs are eligible to submit resolution plans, even when the MSME registration was obtained during CIRP *(read our update **here**)*.

Wish list for 2024

Insolvency petition – To Admit or not to Admit

The Code allows financial creditors to initiate insolvency against a debtor for non-repayment of debt. In 2022, the Supreme Court, in *Vidarbha Industries Power Ltd. v. Axis Bank Ltd.*, introduced discretion for NCLT to reject a creditor's application based on a CD's financial health *(read our article **here**)*.

However, in the 2023 judgment of *M. Suresh Kumar Reddy v. Canara Bank and Others*, the Supreme Court has distinguished the *Vidarbha Industries Power Ltd. v. Axis Bank Ltd.* judgment and held that the non-payment of the debt when it becomes due and payable, will amount to default on the part of the CD and initiation of insolvency proceedings under the Code must follow. These judgments of coordinate two-judge benches raise uncertainties, and a conclusive resolution by a larger Supreme Court bench is recommended to clarify and settle the controversy on the criteria for admitting insolvency applications *(read our article **here**)*.

Statutory claims on par with secured creditors?

The Supreme Court in *State Tax Officer v. Rainbow Papers Ltd.* (**Rainbow Papers**) ruled that by virtue of a 'security interest' created in favour of the Government for tax claims arising under Gujarat Value Added Tax Act, 2003 (**GVAT Act**), the tax authorities i.e., the Government is a 'secured creditor' under the Code. The Court held that if a resolution plan excludes statutory dues payable to the Government, it cannot be said to be in conformity to the provisions of the Code and, as such, will be non-binding on the Government *(read our article **here**)*. Recently, the Supreme Court in *Sanjay Agarwal v. State Tax Officer* dismissed the review petition against Rainbow Papers.

However, in *Paschimanchal Vidyut Vitran Nigam Ltd. v. Raman Ispat Pvt. Ltd.*, the Supreme Court ruled that the Code overrides the provisions of the Electricity Act, 2003. The provisions of the Code treat the dues payable to secured creditors at a footing higher than the dues payable to the Government. The Court also noted that decision in *State Tax Officer v. Rainbow Papers Ltd.* is limited to the facts of that particular case. This has created uncertainty and without legislative intervention, ongoing and completed liquidations face disruption, highlighting the urgent need for lawmakers to address this issue.

Group Insolvency – need for adoption

Numerous corporations operate with subsidiaries and associates, leading to intricate economic ties. Resolving these complexities under the current legal framework causes delays. While in January 2023, the MCA had issued a discussion paper proposing amendments to the Code for a group insolvency procedure, no further action has been taken. Recently, the necessity for a group insolvency framework became evident during the resolution

processes of CDs such as the Videocon Group. Therefore, there is a need of implementing a group insolvency structure under the Code.

Cross border insolvency – the wait game continues

In today's global economy, businesses operate across borders with assets and creditors located in many countries, posing challenges for insolvency proceedings. India's current cross-border insolvency framework governed by Sections 234 and 235 of the Code, relies on bilateral agreements. Despite proposals to incorporate the UNCITRAL Model Law into the Code as Part Z *(read more **here**)* and the publication of draft rules and regulations in 2020 *(read more **here**)*, adoption is still pending as of the end of 2023.

In the case of Jet Airways (India) Limited, which faced simultaneous insolvency proceedings in India and the Netherlands, the existing framework's constraints became apparent, particularly in scenarios where the CD possesses assets across international borders. Initially, NCLT, Mumbai rejected the Dutch court's jurisdiction due to the lack of a bilateral agreement with Netherland. However, NCLAT later overturned this by permitting a protocol between Indian and Dutch counterparts, defining their roles in the insolvency proceedings, highlighting the potential of cross-border cooperation. A cross-border insolvency framework will make it possible for India to deal with issues arising for the Indian companies with foreign assets and vice-versa. Introduction of cross-border insolvency will mark an epochal change in the Code by bringing it at par with mature regimes globally.

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