DELAYS IN CORPORATE INSOLVENCY RESOLUTION PROCESS: HAS THE IBC MET ITS PURPOSE?

by

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ABSTRACT

The efficacy of the corporate environment in a country is measured not only by the ease at which businesses are allowed to flourish in the market but also by the efficiency of the mechanisms that allow businesses to take an exit from the market with minimum loss to the creditors. In India there had been various legal mechanisms that allowed such an exit to corporate entities for many decades. But the fact that there was a need for a complete overhaul of the insolvency resolution mechanism speaks clearly about the performance of the earlier legislations. The Report of The Bankruptcy Law Reforms Committee states that despite many reforms, the credit mechanism has always failed in the country. The main reason for this failure is ineffective insolvency resolution mechanisms. Therefore in order to bring dramatic changes, the Insolvency and Bankruptcy Code was enacted in 2016. The two main objectives of the Code were, less time for insolvency resolution and higher rate of recovery for the creditors. This paper analyzes whether the IBC has come to realize its objectives in over five and a half years of its existence. The relevant data shows that the timelines provided in the Code and it subsequent regulations have not been adhered to in their entirety. This has resulted in loss of value of the assets of the debtor resulting in low recovery rates. On the other hand, data also shows that despite the flaws, IBC is evolving and actively trying to adapt to the market conditions. This fuels the belief that IBC will surely be able to meet its objectives in the near future.

Keywords: Insolvency, Recovery Rate, Bankruptcy Law Reforms Committee, Creditors, Corporate Debtor

Literature Review:

The issue of the efficacy of IBC has been discussed far and wide. The major literary sources utilized for this paper are as follows:

1. The report of the Bankruptcy Law Reforms Committee Volume I: Rationale and Design: The report was presented by the Committee on Bankruptcy Law Reforms in November, 2015. It was designed as a framework for the upcoming Insolvency and Bankruptcy Code. It provides, inter alia, the objectives of the legislation, the need for reforms in the bankruptcy law sector, features of the I&B Code, the institutional framework and the processes involved.
2. The report by Alvarez and Marsal India titled The Next Phase of IBC must Focus on Efficiency: This report provides a comprehensive analysis of the timelines of insolvency cases in India while simultaneously providing a picture of the impact of delays on stakeholders. It further provides some key recommendations in order to improve the current state of things.
3. A research titled "Assessment of Corporate Insolvency and Resolution Timeline" conducted by the Insolvency & Bankruptcy Board of India: This paper is an intricate and detailed research conducted by the IBBI to find out the delays caused in the Insolvency process at various stages of the process. It also aims to find out any relation between various sectors and the size of the debt to the delays caused in CIRP.

Research Methodology:

This paper uses qualitative research and secondary data to explore upon the current state of the I&B Code and its timelines. These methods are used to provide reasons for delays caused in the Insolvency Resolution Process and shed light on the impact of such delays on the stakeholders. The paper provides suggestions to reduce the delays caused in the completion of the resolution process while simultaneously establishing the benefits of the Code.

Insolvency Resolution Procedures in India

Before the enactment of the Insolvency and Bankruptcy Code, the legislative groundwork in India dealing with the insolvency and restructuring procedures for individuals, corporate entities and partnership firms was very complex and scattered across multiple legislations. Here are a few examples of the different laws that governed this topic: The Companies Act, 1956; The Presidency Towns Insolvency Act, 1908; The Provincial Insolvency Act, 1920, The Sick Industrial Companies (Special Provisions) Act, 1985 (SICA); The Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (SARFAESI Act); The Recovery of Debts due to Banks and Financial Institutions Act (RDDBFI Act), 1993 etc. The presence of multiple laws, forums and complexities was an inherent barrier to the efficacy of insolvency laws which resulted in delays in the timely resolution of the distressed individuals, entities and partnership firms. In addition to this, the delays also lead to the devaluation of assets of the debtor making the insolvency negotiations redundant. These different laws had different trigger amounts (minimum amount of money owed to a creditor which can lead to initiation of a resolution process), objectives, adjudicating authorities, governing authorities and timelines. While the objectives of the SICA were to rehabilitate and revive sick entities, the RDDBFI was concerned with the establishment of authorities like the Debt Recovery Tribunal and its concerned appellate authorities in order to recover the money that is owed to lending institutions. While the SICA and RDDBFI provided protection to both the secured and unsecured creditors, the SARFAESI Act only provided protection to secured creditors. Thus it is quite evident that the situation before the enactment of IBC was in a disarray, to say the least. It caused unease in the minds of entrepreneurs to open a business in India since the resolution mechanisms in here were not up to the global standards.

IBC

It was the need of the hour to streamline the process of insolvency resolution and restructuring in order to bring clarity to the corporate entities. The Insolvency and Bankruptcy Code (IBC), 2016, was designed to create an atmosphere in India that helps businesses that may still be effective, to stay afloat and allow an easy exit to those businesses that cannot exist any further without

causing loss to the stakeholders. Before the IBC, India had neither an efficient resolution mechanism nor an easy exit for business/corporate entities. The various mechanisms working simultaneously in the country were redundant as well as not competent enough to meet the needs of the changing times. The IBC came in and offered a new approach. The IBC proposed to be flexible and compatible enough to provide a market oriented resolution to insolvency proceedings and/or dissolution process within a specific timeframe. In order to observe the effectiveness of the IBC we must look at the timeframe provided in the code.

Timeline of CIRP

Section 12 of the IBC Code provides for a particular timeline of an insolvency resolution proceedings (CIRP). Section 12 (1) states that

> *"Subject to sub-section (2), 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 such process."*[1]

Furthermore Section 12(2) provides that the timeline for the CIRP can be extended by a period of 90 days by filing an application to the NCLT. It must be stated that this extension can be provided only once. Furthermore it is provided that if the CIRP goes into court then a further extension of 60 days can be allowed. Thus, accordingly a CIRP must be mandatorily completed in 330 days from the insolvency commencement date, including any extension period granted and the time taken in legal proceedings in relation to the resolution process.

Despite the clear timeframe provided under the Code it has become a common practice to delay the CIRP. Therefore we see that a majority of the CIPR extend way beyond 330 days. In an Indian Express Report titled *"In five years of IBC regime, lenders took 61% haircut on claims"2* it is stated that*, "As of March 31 this year, 79 per cent of the total 4,376 cases under IBC had been pending for more than 270 days, and the average time taken for the completion of*

[1] Insolvency and Bankruptcy Code, 2016, § 12 (1), No. 31, Act of Parliament, 2016 (India)
[2] The India Express, https://indianexpress.com/article/business/economy/ibc-regime-corporate-insolvency-resolution-indian-economy-7423869/ (last visited January 19, 2022)

insolvency resolution was 492 days." "If we include the time for appeals beyond the NCLT (to NCLAT and Supreme Court) and subsequent litigation, the true time for the resolution increases sharply."3

The statistics as provided hereinabove only provide the picture of the CIRP proceedings. In a lot of cases the CIRP in not able to provide a resolution to the stressed entities; this leads to the commencement of liquidation proceedings. When the Liquidation Process begins the liquidator has the duty to complete the process in one year from the date of commencement of liquidation as per Regulation 44 of the IBBI (Liquidation Process) Regulations, 2016. Despite a predetermined timeframe provided under Regulation 47 of the IBBI (Liquidation Process) Regulations, 2016 the NCLAT recently clarified that such timelines are directory in nature[4]. Even though the intention of the appellate authority was to categorically state that it is the duty of the Liquidator to conduct the business of the corporate debtor for its beneficial liquidation, it cannot be denied that this leads to further delays in the resolution/dissolution process and depreciates the value of the assets of the Corporate Debtor.

Reasons for delay

A combined reading of the reports titled *"The Next Phase of IBC must Focus on Efficiency"* by Alvarez and Marsal India and *"Assessment of Corporate Insolvency and Resolution Timeline"* by the IBBI provides key insights into the reasons for delay in the IBC process. There are various phases and bodies involved in a CIRP and each provide different issues that cause a delay.

a. Courts and Tribunals: A major source of delay comes in through slow processes in courts and the Adjudicating Authority. These include delays in admission of CIRP application and acceptance of a resolution plan. Section 7 (4) of the IBC provides that the Adjudicating authority has to ascertain the validity of an application filed by a creditor and determine the existence of a default within 14 days of the receipt of such application. But the reality is different. In majority of the cases the application filed by the creditor gets dragged into litigation by the corporate debtor on several grounds such as existence of disputes or technical faults in the application or jurisdiction of the adjudicating

[3] Nikhil Shah, Khushboo Vaish, THE NEXT PHASE OF THE IBC MUST FOCUS ON EFFICIENCY, Alvarez & Marsal India, https://www.alvarezandmarsal.com/sites/default/files/122880_india_remaining_ibc_report_07.pdf
[4] Prakash Chandra Kapoor v. Vijay Kumar Iyer Liquidator, IA 2484 of 2021 CA (AT)(Ins) No 140 of 2021

authority. This leads to long litigations that eventually causes the admission of an application take over a year.

In order to bring efficacy in admission process under Section 7 the Code has been amended. The Adjudicating Authority is required to record reasons in writing in case an application u/s 7 takes more than the stipulated time.

In order to further speed up the process, the Ministry of Corporate Affairs has proposed some changes in the Code and invited public opinions in a notice dated 23.12.2021[5]. The major change proposed is the utilization of Information Utilities (IU) in determining the default for the purpose of admission of a Section 7 Application. According to the proposed changes the Adjudication Authority will be required to consider records authenticated by the IU to determine default u/s 7 of the Code.

Similarly, delay is caused when it comes to the acceptance and approval of resolution plan by the adjudicating authority. In many cases the manner in which the debts owed to the creditors will be repaid by the prospective Resolution Applicant is questioned. This causes further delays in the resolution process, erodes the value of the assets and further discourages other prospective resolution applicants. In some cases, interested parties whose resolution plan has been accepted wish to make changes in the proposed plan. Such acts are shunned upon since they defeat the entire object of the CoC meetings and CIRP proceedings. This issue has now been addressed by the Supreme Court in the case of Ebix Singapore Private Limited vs Committee of Creditors of Educomp Solutions Limited & Anr. The court said that *"NCLT cannot allow the modification and/or withdrawal of a successful resolution plan and that it would lead to further negotiations that would be difficult to regulate by the IBC."*[6] Furthermore in the same case the Supreme Court reiterated the importance of following the timelines provided in the Code.

b. Lack of Cooperation by the corporate debtor (CD): Section 19 of the IBC provides that the CD and all persons associated with its management must assist the Interim resolution Professional (IRP) in any and all ways possible in order to assist him/her to manage the affairs of the CD and that the IRP can make an application to the Adjudicating Authority

[5] Ministry of Corporate Affairs https://www.mca.gov.in/bin/dms/getdocument?mds=iVdBkodmd%252Fjr1s5IH22XXQ%253D%253D&type=open (last visited January 20, 2022)

[6] Ebix Singapore Private Limited vs Committee of Creditors of Educomp Solutions Limited & Anr, 2021 SCC OnLine SC 707

for necessary directions in case the CD does not cooperate with the IRP. It is generally seen that the CD does not cooperate with the RP. The Ministry of Corporate Affairs in its notice dated 23.12.2021 has proposed changes in Section 19(1) of the Code. The proposed change suggests that Section 19(1) of the Code must be amended such that IRP or the RP can obtain requisite cooperation for getting information for the normal continuation of the CIRP.

c. Multiple Applications: It is observed very oftenly that where there is a CD, multiple applications are filed by different creditors with their own IRP. This may eventually lead to a dispute between creditors. The Adjudicating Authority has to spend time addressing every application which causes delay in the admission of an application

d. Marketing Stressed Assets: India has a huge amount of stressed assets which if marketed properly can have great potential. Yet if an investor is interested in assets that are undergoing CIRP/liquidation they haven't got a one stop place where they can assess the available assets as per their own requirement and make the requisite investments.

e. Competence of relevant authorities: The efficacy of the CIRP depends highly upon the efficacy and competence of authorities like the IRP, RP, CoC as well as the NCLT/NCLAT. It is imperative that all the relevant appointments must be made based on the competence of the appointee. In majority of the situations the orders of NCLT and/NCLAT are appealed to higher authorities. During all this time we must keep in mind that the assets of the Corporate Debtor depreciate on a daily basis.

f. COVID-19: These unprecedented times have brought difficult challenges. The nationwide/localized lockdowns imposed by the various governments in order to curb the spread of the virus have adversely affected the resolution process. The judicial and quasi-judicial bodies are flooded with extension applications which are generally approved because the conduct of the CIPR/liquidation process was severely affected. Even though digitization has helped in combating the issues caused by the pandemic, the overall process has slowed down.

Impact of delays on stakeholders

There are various stakeholders in a CIRP and the objective of the IBC is to recover most of the value of the assets involved in the proceedings so that the creditors can be done justice to. As we have already established that the timeline followed in a CIRP is not as watertight as it was supposed to be, there are definitely consequences for the same. As time passes the value of the assets involved deteriorates expeditiously. The creditors (operational and financial) as well the employees of the entity undergoing CIRP suffer the most. An Indian Express report[7] states that *"Public and private sector banks, non-banking financial institutions, and other financial lenders to companies undergoing corporate insolvency resolution process (CIRP) have taken a cumulative haircut of Rs 3.22 lakh crore or 61.2 per cent of their admitted claims since the Insolvency and Bankruptcy Code (IBC) regime was rolled out five years ago."* This effect is more prominent in case of Operational Creditors which, according to the same report, *"have managed to recoup only 13.9 per cent of their total admitted claims, having lost more than Rs 5.17 lakh crore in all."* The report states that operational creditors were only able to recover 12.5 percent of their claims in cases where claims where made over 5000 crore rupees. Furthermore, operational creditors did not recover anything from at least 58 of the 348 cases where a resolution plan was approved by March 31, 2021. This is due to the fact that IBC gives priority to financial creditors over operational creditors. In most of the cases a longer delay leads to a more likely chance of liquidation which is a far worse situation to be in. Creditors of entities who underwent liquidation recovered only 3.4 % of all the claims that they had made.

A famous example that can be taken up is that of the Jet Airways which was grounded in 2019. Its resolution process began in June 2019 when an insolvency petition was filed by SBI-led lenders' consortium. Back in mid-2021 when the NCLT approved the resolution plan by the new promoters comprising UAE-based entrepreneur Murari Lal Jalan and London-based Kalrock Capita, there was genuine hope that the Airliner would start operations by early 2022. But Punjab National Bank (Creditor) was aggrieved by the resolution plan submitted by the resolution applicants. This led to further litigation which delayed the resolution process. As of now the new owners of the Airways have stated that they will be able to resume operations in the

[7] The India Express, https://indianexpress.com/article/business/economy/ibc-regime-corporate-insolvency-resolution-indian-economy-7423869/ (last visited January 19, 2022)

first quarter of 2022. A report published by Bloomberg Quint[8] states that the creditors of Jet Airways (India) Ltd will only be able to recover 5 percent of their overall claims. While delay isn't the only cause of this low recovery rate, it has surely played a substantial role in giving a blow to the lenders.

Suggestions to avoid delays

There are steps that can be taken to improve the efficacy of the CIRP.

a. Courts and Tribunals: It has already been established that judicial delays impact the process of CIRP. It is imperative that the involvement of courts should be made infrequent. The commercial wisdom of the CoC should be given more importance. Furthermore the idea of having specialized judges and practitioners in the field of Insolvency can surely help in expediting the process.

b. Digitization: As stated earlier, prospective investors do not have a go to place where they can explore their options. This severely undermines the potential that stressed assets can have. High profile insolvency cases catch the attention of everyone but this doesn't happen with cases that do not involve huge corporations. The idea of a common web portal where stressed assets can be displayed for sale or auction can dramatically decrease the delays cause in realizing to value of the assets and improve the total recovery rate.

c. Penalties for non-cooperation: It is common practice that the corporate debtors do not cooperate with the RP. Section 19 of the IBC does not specifically provide for the kind of orders that can be passed by the adjudicating authority. The act of non-cooperation should be specifically provided in the legislation and strict penalties must be provided in case where the debtors refuse to cooperate.

d. Documents of the Debtor: A lot of the times delay is caused because the records maintained by entities undergoing CIRP are ambiguous and not properly maintained. This does not allow the RP to work efficiently. Proper use of technology must be introduced to make to the process of maintaining records simpler.

[8] Bloomberg Quint, https://www.bloombergquint.com/law-and-policy/jet-airways-20-a-5-recovery-for-financial-creditors (last visited January 19, 2022)

Conclusion

In conclusion, it is crucial to remember that the IBC was brought in as a key reform in the corporate sector in India. Before IBC the situation was in disarray. It surely has made a positive impact. A 2020 report by the Hindu BusinessLine[9] states that India has made an improvement of 56 places, from ranking 108 in the year 2019 to 52 in 2020, in terms of the World Bank Index of 'Resolving Insolvency.' The same report also provides that the recovery rate for creditors has jumped from 26.5 cents to 71.6 cents on the dollar. Furthermore the average time taken for insolvency resolution had reduced dramatically from 4.3 years to 1.6 years. Therefore we can clearly see that in its five and a half years of existence the IBC had helped India make significant improvements. It is also important to note that there are some hurdles in achieving the perfect mechanism for insolvency resolution, yet the important part to remember is that the IBC is still a new legislation, enacted in 2016. As more time will pass the legislation will adapt itself by means of amendments to better suit the needs of the country. Amendments have been made in the provision on a regular basis to bring in key reforms. A clear example for the same is the introduction of Pre-Packaged Insolvency Resolution Process for MSMEs in the April of 2021 which bypasses the lengthy and costly process of the regular CIRP and allows a cost effective and less time consuming alternative to smaller entities to resolve their debts. Therefore it would be correct to say that the IBC has had more hits than misses since the date of its enactment.

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