



CENTRE FOR
LAW & POLICY
RESEARCH

Towards Insolvency Law Reform: Learnings from Case Law

Presentation at BLRC Conference

Aparna Ravi
July 31, 2015



How does a Company in Distress go through the Legal System?

Analysis of judgments on insolvency and insolvency related proceedings to assess:

- Where bottlenecks and inefficiencies in the process lie
- Principal causes of delays

Current Insolvency Regime

Act	Purpose	Applies to	Forum
CA 1956	Liquidation/ winding up	All corporates	High Court
SICA 1985	Rescue and rehabilitation	Industrial companies only	BIFR
RDDBFI Act, 1993	Debt recovery	Banks and financial institutions, debt of Rs 10 lakh or more	DRTs/DRATs
SARFAESI Act, 2002	Enforcement of security	Secured creditors	Does not require court involvement (appeals to DRT)



Methodology

Review of 45 High Court Judgments

- References from BIFR for liquidation
- Winding up petitions
- Appeals from BIFR or AAIFR decisions (interpretation of SICA)
- Appeals from DRT/DRAT (SARFAESI/RDDBFI Act)



Methodology

Review of 15 DRT/ DRAT decisions

- Challenges to SARFAESI enforcement action
- Enforcement under RDDBFI Act

Time Period – from 2003 onwards (post enactment of SARFAESI)

Judgments chosen on the basis of variations in number of creditors, debt structure, large and small companies and from different HCs and DRTs/DRATs



Learnings from Case Law

Numerous instances of parallel proceedings initiated by different parties and in different fora:

- Debtor makes reference to BIFR, while creditor files winding up petition in HC
- Secured creditors seek to enforce under SARFAESI while BIFR is considering sickness
- One creditor initiates action under RDDBFI Act while another files winding up petition



BHEL v Arunachalam Sugar Mills Ltd., decided on 12.04.2011 (Madras HC)

- Secured Creditor 1 filed an application in the DRT for debt recovery
- Secured Creditor 2 filed a company petition for winding up
- Secured Creditor 3 entered into an MOU with Secured Creditor 1 to get paid upon Secured Creditor 1's recovery
- Trade creditor that had leased machinery to the debtor initiated proceedings invoking the arbitration clause in the contract
- Secured creditor 4 initiated proceedings under SARFAESI and sold assets by auction
- Unsecured creditor that had supplied a boiler to the debtor filed for debt recovery in the civil court



Has resulted in...



Little Clarity for Creditors on Overall Position of Debtor

Kritika Rubber Industries v. Canara Bank (Karnataka HC, 13.06.2013)

- Parallel proceedings initiated by two groups of creditors in DRT and HC.
- DRT ordered attachment of secured property and sale in auction, while HC appointed an OL to wind up the company.
- OL got sale in auction set aside
- Secured creditors claimed to have no knowledge of winding up petition (filed in 1999) until they received notice of OL's action to set aside the sale authorised by the DRT (2008)

Conflicts between Laws and Over Jurisdictions

Can sale be made under SARFAESI Act without leave of company court once winding up proceedings have commenced?

- *Indian Bank v. Sub-Registrar (HC of AP and Telangana, decided on 11.11.2014)* – Yes
- *BHEL v. Arunachalam Sugar Mills (Madras HC, decided on 12.04.2011)* – No, need consent of OL
- *Krithika Rubber Industries v. Canara Bank (Karnataka HC, decided on 13.06.2013)* – DRT cannot order sale without consent of OL

Conflicts between Laws and Jurisdiction

Can secured creditors initiate proceedings under SARFAESI while proceedings under the RDDBFI Act were pending?

- *M/S Digivision Electronics Ltd. v. Indian Bank (Madras HC, decided on July 7, 2005)* – No, need leave of DRT
- *Bank of India v. Ajay Finsec Pvt Ltd and Ors (OA No. 167 of 2001, decided on 28.11.2003)* – DRT ruled that banks could proceed with enforcement under SARFAESI while RDDBFI proceedings were pending
- *M/S Punea Cold Storage v. State Bank of India (AIR 2013 Part I; II (2013) BC 501 Patna HC)* - Cannot initiate proceedings under RDDBFI Act if SARFAESI enforcement action had begun

Time Periods - High Court Cases

Time Taken	No. Of Cases	Comments/ Breakdown
0 – 2 years	8	<ul style="list-style-type: none">• Winding up petitions – 4 (3 involved FCCB holders)• SARFAESI/RDDBFI - 4
2 - 5 years	10	<ul style="list-style-type: none">• Appeals from BIFR/AAIFR – 5• SARFAESI/RDDBFI – 5
5 – 10 years	7	<ul style="list-style-type: none">• References from BIFR – 2• Winding up Petition – 1• Appeal from BIFR – 1• SARFAESI/RDDBFI – 3
10+ years	17	<ul style="list-style-type: none">• References from BIFR – 8• Winding up petitions – 3• Appeals from BIFR – 3• SARFAESI/RDDBFI – 3

Time Periods - DRT/DRAT

Time Taken	No. of Cases	Time Taken/Breakdown
0 – 2 years	5	
2 – 5 years	1	
5 - 10 years	5	1 case took 6 years in DRT but 17 in total
10+ years	2	



Reasons for Delays

- Pro-rehabilitation stance of courts – Line of Supreme Court precedents that former directors can explore rehabilitation after issuance of winding up order
- Deference to BIFR's jurisdiction despite the process being dysfunctional
- Winding up order does not signal the end –
 - Years between passing of winding up order and completion of liquidation
 - Debtors often file applications to stay winding up orders

SARFAESI Enforcement Actions

Overriding effect of SARFAESI often upheld in courts, but...

14 of 45 HC cases and 5 of 15 DRT/DRAT cases reviewed involved applications by debtors to stay SARFAESI actions:

- Civil courts have issued interim stays on SARFAESI proceedings (overturned by HCs)
- DRTs/DRATs have gone on to determine quantum of liability or set conditions on SARFAESI enforcement when considering efficacy of SARFAESI action
- HCs have issued stay on SARFAESI proceedings or determine that others laws get precedence



Learnings

- Multi-layered framework is a significant contributor to the delays and bottlenecks in the insolvency process
- Delays also caused by poor understanding of the law, pro-rehabilitation stance of courts and huge delays between winding up order and liquidation
- Is it the law or its implementation?