

The Insolvency and Bankruptcy Code, 2015
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Issues with the current processes- the imperative for reform

- **Multiplicity of laws**
- **Arbitrage:** secured / unsecured; domestic / foreign lenders; banks / nonbanks
- **Trigger is either too early or too late**
 - **SICA:** 50% of net worth
 - **SARFAESI:** 90 days of NPA declared
 - **JLF:** slightly earlier (SMA 0, 1 and 2) but applies only to banks
 - **SDR-** exit related issues
 - **Winding up:** INR 500 default (Companies Act 2013- INR 100,000 proposed)
 - **Companies Act 2013 (to be notified):** 50 per cent of secured creditors
- **No collective action process**
- **“Sick companies but no sick promoters”- divine right**
- **“Liquidation reluctance”**
- **Distribution waterfall complex and unclear**





The Fallout

- Misplaced emphasis on secured bank credit
- Corporate bond market non-existent
- Recovery rate estimated at 20%, capital stuck.
- Value destruction in corporate distress
- Credit for individuals and SMEs limited

The Processes proposed in IBC

Insolvency Resolution Process (IRP) will involve a process of negotiation between debtors and creditors, outside the court through the Resolution Professional (RP), leading up to a repayment plan.

Liquidation is a process led by the Adjudication Authority, once the IRP has failed.

Fast track IRP A truncated version of IRP for smaller firms or those with simpler debt structures.

How is IBC different?

- **Distinction between financial and operational creditors**
- **Trigger: Operational creditor, financial creditor, debtor**
- **Moratorium**
- **Debtor not in control during IRP**
- **Business Decisions by a Creditor Committee**
- **Insolvency resolution through managed, time-bound negotiations**
- **Liquidation:**
 - **Failure of the creditors' committee to reach an agreement during the period stipulated above;**
 - **A decision of the creditors' committee to proceed with liquidation during the IRP; or**
 - **Failure of the debtor to adhere to terms of the resolution plan approved by the NCLT.**
- **Voidable transactions**
- **Distribution waterfall**
- **Penalties:**
 - **Frivolous triggers; concealment of property; defrauding creditors, fraudulent trading; contravention of moratorium, contravention of resolution plan.**



Distribution Waterfall

- **Costs of IRP (including any interim finance raised) and liquidation);**
- **Secured creditors and workmen dues (capped up to 3 months from the start of IRP);**
- **Employees' salaries (capped up to 3 months);**
- **Dues to unsecured financial creditors and debts payable to workmen in respect of the period 12 (twelve) months before the commencement of liquidation;**
- **Any amount due to the relevant State Government and/or the Government of India in respect of the whole or any part of the period of 2 (two) years prior to the date of commencement of liquidation;**
- **Any debts of secured creditors for any amount unpaid following the enforcement of security interest;**
- **Any remaining debt; and**
- **Remaining surplus to be distributed to shareholders.**

All distributions as per the above waterfall will be net of the liquidator's fees, which will be deducted proportionately from each stage of the waterfall in order to incentivise the liquidator to ensure quicker recovery for each class of recipient.



Institutional infrastructure

- **A private competitive industry of Information Utilities**
- **A private competitive industry of Insolvency Professionals**
- **Efficient and well functioning tribunals**
- **An independent and well-governed regulator**



Present status

- **Tabled before Lok Sabha- December 2015**
- **Referred to Joint parliamentary Committee- Report by March 2016**
- **Setting up of institutional infrastructure in parallel *Eg.* NCLT**
- **Aligning related laws and regulations critical.**

Present status

- Should infrastructure building precede the implementation of the law to ensure better capacity; or develop organically?
- Is the requirement to force a decision within a defined timeframe likely to lead to sub-optimal resolution (to meeting the deadline); or excessive liquidation?
- Should there be a mechanism for the monitoring of a resolution plan? What is the best possible one that has the least stress on the judiciary but cannot be manipulated?
- In corporate resolution, is the balance of power between operational and financial creditors appropriate? How will it affect debt and equity finance?
- Is the treatment of secured creditors fair? What are some additional possible safeguards: Adequate protection clauses? Numerosity in addition to value of debt?





THANK YOU