INDIAN INSOLVENCY REGIME: IMPACT ON EASE OF DOING BUSINESS AND INVESTMENT

- Raghav Pandey and Advaith Govind*

I. INTRODUCTION

India, despite being one of the fastest growing economies in the world has seen its worst slump in the past six years; in terms of investment as well as employment. There is a mounting Non-Performing Asset (NPA) crisis along with the lack of sufficient legislations to curb the same. This has affected the lending habits of the banks and has increased the capital risks in the market as well. In order to address this issue and to consolidate the highly fragmented framework on insolvency laws, the government of India enacted the Insolvency and Bankruptcy Code, 2016 (hereinafter '**IBC**').

IBC was introduced in 2016 to, "consolidate and amend the laws relating to reorganisation and insolvency resolution of corporate persons, partnership firms and individuals in a time bound manner."[1] The IBC

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* Raghav Pandey is an Assistant Professor at the Maharashtra National Law University, Mumbai. Advaith Govind is an LL.M. candidate at the Maharashtra National Law University, Mumbai.

[1] The Insolvency and Bankruptcy Code, 2016, No. 31, Acts of Parliament, 2016 (India), preamble [hereinafter IBC, 2016].

applies to companies as well as individuals. It strives to expedite the time taken for the Corporate Insolvency Resolution Process (CIRP) by several institutions such as Insolvency Professionals, Insolvency Professional Agencies, Information Utilities, and Insolvency and Bankruptcy Board.

It has diverged from the tangential policies that had been made to conform to the prior statutes like, the Sick Industrial Companies (Special Provisions) Act, 1985; the Recovery of Debts Due to Banks and Financial Institutions Act, 1993; the Securitisation and Reconstruction of Financial Assets and Enforcement of Securities Interest Act, 2002; and the Companies Act, 2013.

Recently, the Doing Business Index has highlighted that India has made resolving insolvency easier by promoting reorganization proceedings in practice', in a 2020 Report on 'Business Reforms in India'.[2]

A. Ease of Doing Business

Ease of Doing Business Index (hereinafter '**EDB Index**') is a ranking system established by the World Bank. The index ranks countries on the ease of doing business and the simplicity in the regulatory framework for setting up a business. The EDB Index, in the recent times,

[2] *Business Reforms in India*, DOING BUSINESS, https://www.doingbusiness.org/en/reforms/overview/economy/india.

has been recognised as a measure of economic development and liberal policies of the government towards investments.[3]

EDB Index is a measurement tool that is confined only to the measurement of the regulatory framework that subsists within a country and its sole effect on the governance of business in that country. It compares and contrasts the regulations, from country to country, that affect businesses and does not consider any general or traditional pre-requisites such as larger markets, advanced technology or infrastructural capabilities, or economic behaviours.

The EDB Index comprises 10 sub-indices that are used to formulate a nation's ranking:[4]

a) Starting a business – Procedures, time, cost, and minimum capital to open a new business

b) Dealing with construction permits – Procedures, time, and cost to build a warehouse

c) Getting electricity – procedures, time, and cost required for a business to obtain a permanent electricity connection for a newly constructed warehouse

d) Registering property – Procedures, time, and cost to register commercial real estate

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[3] *Ease of Doing Business*, MAKE IN INDIA, http://www.makeinindia.com/eodb.
[4] *Methodology*, DOING BUSINESS, https://www.doingbusiness.org/en/methodology.

e) Getting credit – Strength of legal rights index, depth of credit information index

f) Protecting investors – Indices on the extent of disclosure, extent of director liability, and ease of shareholder suits

g) Paying taxes – Number of taxes paid, hours per year spent preparing tax returns, and total tax payable as share of gross profit

h) Trading across borders – Number of documents, cost, and time necessary to export and import

i) Enforcing contracts – Procedures, time, and cost to enforce a debt contract

j) Resolving insolvency – The time, cost, and recovery rate (%) under bankruptcy proceeding

These sub-indices analyse the regulatory framework in a country and how much it complements the businesses therein. Each tool analyses a different aspect of the legal framework and how it helps make the economy investment-friendly. Out of these, 'Resolving Insolvency', analyses the time, cost, and recovery rate under the bankruptcy proceeding. It looks at the effectiveness of the insolvency process in a given legal regime.

B. Indian Law and the EDB Index

India has improved its ranking in the 2019 World Bank's Ease of Doing Business Index.[5] It has gone up 14 places to be ranked at the 63rd position in the EDB Index. Much has to be attributed to the Insolvency and Bankruptcy Code, 2016 that has changed the overall bankruptcy and insolvency regime in the country. In addition to this, India also went 56 places up the ladder to be ranked 52nd in the 2019 'Resolving Index' in the IDB Index. IBC has helped improve the insolvency resolution practices and behaviours in the country over the past 3 years. IBC has been an area of debate and discussion, since its inception, due to the lack of effectiveness in its predecessor legislations in curbing the NPA (Non-Performing Asset) crisis and in dictating a proper mechanism of insolvency resolution process. The previous regime had no single legislation, and due to the multiplicity of laws, the judicial process took a lot of time and also created overlapping jurisdictions.

One of the key aims of the IBC is to provide an "effective legal framework for timely resolution of insolvency and bankruptcy which would support development of credit markets and encourage entrepreneurship." The legislature thereby intended to improve the Ease of Doing Business, and facilitate more investments leading to higher economic growth and development.[6]

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[5] *Ease of Doing Business Rankings*, DOING BUSINESS, https://www.doingbusiness.org/en/methodology.

[6] REPORT OF THE JOINT COMMITTEE ON THE INSOLVENCY AND BANKRUPTCY CODE, 2015, LOK SABHA, ¶ 3 (2016) [hereinafter REPORT OF THE JOINT COMMITTEE].

Since the advent of the IBC, around 21,000 cases have been referred the National Company Law Tribunal (NCLT), which is the adjudicating authority under the code.[7] Out of these, 8,500 cases were settled prior to admission and 1,500 companies were ordered to be liquidated.[8]

IBC has drastically improved the recovery rate of debts. The Corporate Insolvency Resolution Process (CIRP) as mandated by the IBC, has been incidental in improving the recovery rates as well as reducing the time and cost of the resolution processes. The recovery rate has come up from 26.5% in 2018 to 71.6% in 2019. In addition to this, the average recovery time for a corporate insolvency resolution process has also improved from 4.3 years in 2018 to 1.6 years in 2019.[9]

A report published by the Reserve Bank of India (RBI) on Insolvency and Bankruptcy Code and Bank Recapitalisation, discusses about the recovery of NPA and the role of different factors on the same. The report identified the recovery rates of banks to have improved after the enactment of the IBC.[10]

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[7] IBC, 2016, *supra* note 1, § 5(1).

[8] Dipak Mondal, *How IBC helped improve India's ease of doing business rankings*, BUSINESS TODAY, Oct. 24, 2019, https://www.businesstoday.in/current/economy-politics/how-ibc-helped-improve-india-ease-of-doing-business-rankings/story/386544.html.

[9] *Govt took several steps for ease of doing biz: MCA*, THE ECONOMIC TIMES, Dec. 16, 2019, https://economictimes.indiatimes.com/news/economy/policy/govt-took-several-steps-for-ease-of-doing-biz-mca/articleshow/72737217.cms?from=mdr.

[10] *Insolvency and Bankruptcy Code and Bank Recapitalisation*, RESERVE BANK OF INDIA, Dec. 21, 2017, https://www.rbi.org.in/scripts/PublicationsView.aspx?id=18060#FT3.

C. Relevance of Insolvency Regime

The Joint Parliamentary Committee Report on the Insolvency and Bankruptcy Code hailed the new insolvency law as an effective legal framework for the timely resolution of insolvency and bankruptcy proceedings. The report also noted that the code will facilitate more investments and eventually improve the ease of doing business leading to higher economic growth. [11]

The IBC shifted the existing Debtor-in-Possession (DIP) regime to a Creditor-in-Control (CIC) regime, taking cue from the U.K Insolvency law and conforming to the international best practices. While countries like France and Italy have debtor-friendly insolvency laws conforming more to the DIP standards; UK, Germany, and Sweden predominantly favour a CIC regime, granting a higher pedestal to the rights of the creditors. Meanwhile, USA has a hybrid regime, providing for both liquidation (in Chapter 7) and restructuring of debts (in Chapter 10).[12]

A DIP regime allows a debtor to carry on its business and allows the gradual repayment to its creditors. Under this regime, the debtor continues to run the business along with the possession of the assets (including the ancillary equipment and the vehicles). Emphasis is laid on the debtor’s interests and the law necessitates the debtor to formulate a reorganization plan that would detail the payment to its creditors and the timeframe for the same. However, one of the key shortfalls of such laws

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[11] REPORT OF THE JOINT COMMITTEE, *supra* note 6.
[12] *Id.*

are the inabilities bestowed upon the debtor companies to generate sufficient income as there are is a dearth of adequate resources, and also the subsistence of impending supervision by the bankruptcy court.[13]

Meanwhile, a CIC regime places the creditors in control of the affairs of the company under scrutiny. Once the company is admitted into any insolvency resolution process, the power of the company shall fall into the hands of the creditors.

One of the foremost Acts that was evolved to address the issue of bad loans were the Sick Industrial Companies (Special Provisions) Act, 1987 (SICA) which was passed in public interest, with a view to securing the timely detection of sick and potentially sick companies owning industrial undertakings.[14] The Board for Industrial and Financial Reconstruction (BIFR) was enacted under the act to deal with the rehabilitation of sick units. However, the BIFR was largely ineffective and the borrowers took unwarranted advantage of the indefinite moratorium provided under the SICA.

The Securitisation and Reconstruction of Financial Assets and Enforcement of Securities Interest Act, 2002 (SARFAESI Act) was enforced to "regulate securitisation and reconstruction of financial assets

[13] Will Kenton, *Debtor in Possession (DIP)*, INVESTOPEDIA (May 14, 2019), https://www.investopedia.com/terms/d/debtorinpossession.asp.
[14] The Sick Industrial Companies (Special Provisions) Act, 1985, No. 1, Acts of Parliament, 1986 (India), preamble.

and enforcement of security interest and to provide for a Central database of security interests created on property rights."[15]

This Act provided the secured creditor with several rights to take charge and enforce the security interests of the debtor/borrower.[16] The account of the borrower was to be classified as a Non-Performing Asset (NPA) in the event of any default in the repayment of the loan to the secured creditor. Such NPAs could be sold by the secured creditors (Banks and Financial Institutions) to Asset Reconstruction Companies (ARCs) for the revival of the same. However, even the SARFAESI Act failed to withhold the incidence of mounting NPAs.

In the meantime, several mechanisms were instituted by the RBI to curb the rising NPA crisis. The Corporate Debt Restructuring (CDR) mechanism, the Joint Lenders' Forums (JLFs) initiative, and the Strategic Debt Restructuring (SDR) mechanism were amongst the few of those. These initiatives did not address the case of the unsecured creditors, and failed to achieve the desired results.

Moreover, the RBI, vide several master circulars, catered took up the incidence of 'Wilful Defaults' by borrowers against secured creditors such as Banks and FIs. The case of wilful default was initially taken up by the RBI vide a circular dated February 20, 1999, which was issued for the collection and dissemination of Information on cases of wilful default of

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[15] The Securitisation and Reconstruction of Financial Assets and Enforcement of Securities Interest Act, 2002, No. 54, Acts of Parliament, 2002 (India), preamble [hereinafter SARFAESI Act, 2002].
[16] *Id.* § 13.

Rs.25 lakhs and above. This was done pursuant to the instructions of Central Vigilance Commission for the collection of details of wilful defaults of Rs. 25 lakhs and above.[17] The master circular, though regulatory in nature and dictating a proper method to classify wilful defaulters, has been riddled with unwarranted disputes and adjudications.

The Insolvency and Bankruptcy code, 2016 was enacted and notified in May, 2016. It was sought to be made the exclusive law dealing with insolvency and bankruptcy in the country. Individuals, companies, limited liability partnerships (LLP), and partnership firms fall within the purview of the IBC.

II. IBC AND THE IMPACT ON INVESTMENT

One of the key drivers of the Indian economy is the infrastructure sector. In 2018, India was ranked 44th out of 167 countries in World Bank's Logistics Performance Index (LPI) 2018. While India is en route to becoming a $3 trillion economy, the government is planning to invest ₹102 trillion over five years to develop social and economic infrastructure.[18] Moreover, there is a requirement of investment worth Rs. 50 trillion (US$ 777.73 billion) in infrastructure by 2022 to have sustainable development in the country. A sound insolvency law that

[17] *Wilful Defaulters and action there against*, RESERVE BANK OF INDIA (Jul. 29, 2003), https://www.rbi.org.in/scripts/NotificationUser.aspx?Id=1279&Mode=0.

[18] Shreya Nandi, *FM unveils ₹102 tn infra push to reignite growth*, LIVE MINT (Jan. 01, 2020, https://www.livemint.com/news/india/fm-unveils-102-tn-infra-push-to-reignite-growth-11577814770788.html.

protects the rights of investors would go a long way in instilling much required confidence in them to invest in the Indian Economy.[19]

The Insolvency and Bankruptcy Code, 2016 has been formulated along the lines of the UNCITRAL Legislative Guide and the World Bank Principles on insolvency reforms. This has been reflected in statement of objects of the IBC.

Maximisation of the Value of Assets is one of the primary motives of the legislation. This is in fact one of the objects of the act. The IBC caters to offer incentives to achieve maximisation of value of the assets to the concerned parties ensuring higher distribution to the stakeholders thereby reducing the burden in insolvency. The Legislative Guide on Insolvency Law by UNCITRAL[20] shares a similar view to any insolvency law. It recommends that a balance of risk has to be achieved between the parties involved in an insolvency proceeding.

By virtue of Section 13 and 14 of the IBC, the adjudicating authority i.e. the National Company Law Tribunal (NCLT) shall declare a moratorium prohibiting all other judicial proceedings against the corporate debtor.[21] Meanwhile this qualifies as a constructive means to keep available the assets of the corporate debtor for the CIRP; it may affect the value of the assets when the process becomes a long-drawn out one.

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[19] *Infrastructure Sector in India*, INDIA BRAND EQUITY FOUNDATION (Jan. 2020), https://www.ibef.org/industry/infrastructure-sector-india.aspx.

[20] UNCITRAL, Legislative Guide on Insolvency Law, (2005), with amendments as adopted in 2006, UNO, https://www.uncitral.org/pdf/english/texts/insolven/05-80722_Ebook.pdf.

[21] IBC, 2016, *supra* note 1, §§ 13-14.

However, this has to be achieved by the NCLT in consonance with the other judicial authorities.

Another key aspect of the IBC is the Access to Finance/ Credit. In order to facilitate this, an insolvency law ought to be predictable and transparent. Only then, shall it encourage constructive investments that help the economy as well. According to UNCITRAL's Legislative Guide on Insolvency Law, a law on insolvency should also be transparent and predictable. A predictable law assists the potential lenders and creditors to assess the risks associated in the event of insolvency. [22] A similar view has been iterated by the Supreme Court at length in *Mobilox Innovations v. Kirusa Software*.[23]

The IBC has a well-structured reasoned procedure for CIRP. Section 4 of the code provides a minimum threshold of one lakh rupees for the initiation of a CIPR process.[24] Such a process can be initiated either by the corporate debtor himself or the financial creditor or an operational creditor[25] and an application for the same has to be filed before the adjudicating authority (NCLT) for the initiating the insolvency resolution process. An Interim Resolution Professional (IRP) would be appointed by the creditors and would be made in charge of the affairs of the company. The resolution professional is given a time frame of 180 days, which can be extended by 90 more days to draw out a resolution plan, which has to

[22] *Supra* note 20.
[23] Mobilox Innovations v. Kirusa Software, (2018) 1 SCC 353.
[24] IBC, 2016, *supra* note 1, § 4.
[25] *Id.* § 6.

be approved by the Committee of Creditors (COC) so constituted. However, the insolvency resolution process shall not exceed a maximum of 330 days.[26]

One of the shortfalls of the former insolvency regime was the failure to Harmonize Liquidation and Reorganisation process.[27] This was obviously detrimental to prospective investment in the country.

Under the SARFAESI Act, 2002, a secured creditor could enforce the security interest and needlessly put a stop to the business of the debtor company.[28] In the long run, this could invariably harm the economy. The problem mounts when the so secured assets remain unproductive failing to secure a buyer or be revived duly. The Legislative Guide by UNCITRAL identifies this and necessitates the need for balancing liquidation and reorganisation. The IBC, cater to fix this lacuna in the erstwhile laws.

The Code allows restructuring of doubtful assets and initiates liquidation only in the event restructuring goes futile. The NCLT, being the adjudicating authority, is bestowed with the power to order liquidation of the corporate debtor.

Section 12-A, recently added by the Insolvency and Bankruptcy Code (Second Amendment) Act, 2018 allows for the withdrawal of an insolvency application admitted under Section 7, 9 or 10, but the same has

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[26] *Id.* § 12.
[27] SUMANT BATRA, CORPORATE INSOLVENCY LAW AND PRACTICE 41 (Abhinandan Malik eds., 1st ed. 2017).
[28] SARFAESI Act, 2002, *supra* note 15.

to done with the approval of at least ninety per cent voting shares of the COC.[29]

The IBC facilitates the balancing of the Interests of all stakeholders**.** This is enunciated in the objects of the act. Stakeholders who are equally placed are treated equally by the new act. The code does not differentiate between the rights of foreign creditors and Indian creditors.

Section 53 of the IBC dictates the waterfall mechanism for the distribution of the proceeds from the sale of asset of the corporate debtor in a certain order of priority. As per Section 53 of the IBC, the order of priority is as follows:[30]

a) The insolvency resolution process cost and the liquidation costs paid in full.

b) The following debts which shall rank equally between and among the following:

i. workmen's dues for the period of twenty-four months preceding the liquidation commencement date; and

ii. debts owed to a secured creditor in the event such secured creditor has relinquished security in the manner set out in section 52;

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[29] IBC, 2016, *supra* note 1, § 12 A.
[30] *Id.* § 53.

c) wages and any unpaid dues owed to employees other than workmen for the period of twelve months preceding the liquidation commencement date;

d) financial debts owed to unsecured creditors;

e) the following dues shall rank equally between and among the following:

i. any amount due to the Central Government and the State Government including the amount to be received on account of the Consolidated Fund of India and the Consolidated Fund of a State, if any, in respect of the whole or any part of the period of two years preceding the liquidation commencement date;

ii. debts owed to a secured creditor for any amount unpaid following the enforcement of security interest;

f) any remaining debts and dues;

g) preference shareholders, if any and

h) Equity shareholders or the partners as the case may be.

As far as Section 53 of IBC is concerned, the costs associated with the insolvency process and liquidation fall the highest in priority of repayment, followed by the payment due to the workmen for the past 24 months preceding the liquidation, along with the debts owed to the secured creditors, who are the financial creditors of the corporate debtor.

The National Company Law Appellate Tribunal (NCLAT) in *State Bank of India v. Moser Baer Karamchari Union,*[31] ruled on the scope and extent as to which 'workmen dues' have been covered under Section 53 of IBC.

According to Section 36 of the IBC, the liquidator is mandated to create a liquidation estate[32] wherein the "liquidator shall hold the liquidation as a fiduciary for the benefit of all the creditors".[33] However, sub clause (a)(iii) of clause (4) of Section 36 categorically states that no social security benefits in the form of provident, gratuity or pensions fund forms a part of the liquidation estate.

The NCLAT reasserted the same in the *Moser Baer case*. The Appellate authority entailed in a harmonious approach in interpreting 'workmen's dues' under Section 53 of the Code along with Section 36 of the Code and Section 326 of the Companies Act, 2013 (hereinafter referred to as the '2013 Act'). The NCLAT explained that the purpose of Section 326 of the 2013 Act is to give priority to certain amounts while Section 53 deals with the distribution of proceeds from the sale of liquidation asset.[34]

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[31] State Bank of India v. Moser Baer Karamchari Union, 2019 SCC OnLine NCLAT 447, (India).
[32] IBC, 2016, *supra* note 1, § 36(1).
[33] *Id.* § 36(2).
[34] Anshul Prakash & Deeksha Malik, *India: Liquidation Waterfall: NCLAT Rules Against Inclusion of Social Security Dues under 'Workmen's Dues'*, MONDAQ, Aug. 30, 2019, http://www.mondaq.com/india/x/841238/Corporate+Commercial+Law/Liquidation+Waterfall+NCLAT+Rules+Against+Inclusion+Of+Social+Security+Dues+Under+Workmens+Dues.

Homebuyers or allottee of real estate project were also brought under the ambit of the IBC by the Insolvency and Bankruptcy Code (Second Amendment) Act, 2018. The Supreme Court in the case of *Pioneer Urban Land and Infrastructure Limited v. Union of India*,[35] dictated the Real Estate (Regulation and Development) Act, 2016 to be read harmoniously with the IBC and held that homebuyers ought to be construed as financial creditors under the code.

The operational creditor falls lower to the workmen and secured creditors in the in hierarchy of the repayment mechanism under this provision. The position of the financial creditors' vis-à-vis the operational creditors in the priority of payment at the time of liquidation has been a bone of contention since the inception of the Code. The Bank Law Reforms Committee Report has iterated that there is a lack of an effective implementation mechanism to enable operational creditors to trigger the resolution process.[36]

Financial Creditor, under IBC, has been defined in Section 5(7) as "any person to whom a financial debt is owed and includes a person to whom such debt has been legally assigned or transferred to"[37] while an operational creditor is "person to whom an operational debt is owed and includes any person to whom such debt has been legally assigned or transferred."[38] The relation of the financial creditors to that of the

[35] Pioneer Urban Land and Infrastructure Limited v. Union of India, 2019 SCC OnLine SC 1005.
[36] The Report of the Bankruptcy Law Reforms Committee, ¶ 4.3.4 (2015).
[37] IBC, 2016, *supra* note 1, § 5(7).
[38] *Id.* § 5(20).

company is purely financial, on the other hand, the operation creditors' liabilities are in the form of future payments in exchange of goods or services already delivered.[39]

The case of *Swiss Ribbons Pvt. Ltd. v. Union of India,*[40] clarified the position of financial and operational creditors in the waterfall mechanism purported under the IBC. One of the key grounds was the unequal or the inferior treatment of the operational creditor vis-à-vis financial creditors in the event of corporate insolvency resolution process. The Supreme Court in this case noted that the "financial creditor are in the business of moneylending; banks and financial institutions are best equipped to assess viability and feasibility of the business of the corporate debtor."[41] The court opined that such a difference is neither discriminatory nor arbitrary.

The Supreme Court in the recent *Essar Steel Judgement*[42] reiterated the role of the committee of creditors (CoC) and held that the operational and financial creditors are distinct and their claims are different. The financial creditor is necessarily a secured creditor and cannot be equated to an operational creditor who is an unsecured one.

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[39] The Report of the Bankruptcy Law Reforms Committee, ¶ 5.2.1 (2015).
[40] Swiss Ribbons Pvt. Ltd. v. Union of India, AIR 2019 SC 739.
[41] *Id*.
[42] Committee of Creditors of Essar Steel India Limited v. Satish Kumar Gupta, 2019 SCC OnLine SC 1478.

The Insolvency and Bankruptcy Code (Amendment) Act, 2019,[43] amended Section 30(2) (b) in order to restore the rights of the financial creditors. The amendment provided that a resolution place should provide either the liquidation value or the debt or the amount that would have been received by the operational creditor if the amount distributed under the resolution plan was done in accordance to Section 53 of the Code.

The ICRA report, that was released on June 19, 2019, has made comparisons of the haircuts for operational creditors vis-à-vis financial creditors in India. The findings were premised on the 92 Corporate Insolvency Resolution Plans (CIRPs) that have yielded a resolution plan before March 31, 2019 under the IBC. The ICRA's estimation is that the haircuts for the operational creditors is not 'materially different' from that of financial creditors. [44]

Payments due to the government are ranked below the claims of the unsecured creditors along with the residuary payment unpaid to the secured creditor after the enforcement of the security interest. Government dues however used to be given a higher priority in the earlier liquidation regime which no longer subsists under the new one. While the preference and the equity shareholders are one of the lowest stakeholders within the priority of repayment is concerned.

[43] The Insolvency and Bankruptcy Code (Amendment) Act, 2019, No.26 of 2019, Acts of Parliament, 2019 (India).

[44] *ICRA: Haircuts for operational creditors have been in line with that for the financial creditors*, ICRA, June 19, 2019, https://www.icra.in/Media/OpenMedia?Key=b51602bc-0043-4545-9dd9-fd65096e0849.

'Timely and Efficient Resolution' is yet another defining feature of the IBC. The new law is ambitious when it comes to timely resolution of the insolvency process. The recent Insolvency and Bankruptcy Code (Amendment) Act, 2019 has extended the deadline for a CIRP from 270 days to 330 days.[45] This extension of deadline is to be seen as a positive move, imbibing the progressive changes from the two years of its functioning.

The Institutional Infrastructure maintained by the IBC is one of its kinds in India. The IBC boasted of several institutions which put together a dynamic insolvency regime. The World Bank in its report on 'Principles and Guidelines for Effective Insolvency and Creditor Rights Systems' necessitates the importance of an effective insolvency law and creditor rights system.[46]

According to the report, strong institutions and regulations are crucial for the smooth functioning of any insolvency system. The three main aspects of any insolvency law should be:[47]

a) Institutions formulated under the system for the insolvency process

[45] The Insolvency and Bankruptcy Code (Amendment) Act, 2019, No.26 of 2019, Acts of Parliament, 2019 (India).
[46] World Bank, *Principles and Guidelines for Effective Insolvency and Creditor Rights Systems*, WORLD BANK GROUP (Apr. 2001), http://siteresources.worldbank.org/GILD/PrinciplesAndGuidelines/20162797/Principles%20and%20Guidelines%20for%20Effective%20Insolvency%20and%20Creditor%20Rights%20Systems.pdf.
[47] *Id.*

b) Operational system for processing cases and decisions

c) Requirements for preserving the integrity of the system

Under the IBC, there are four main institutions: the Insolvency and Bankruptcy Board of India (IBBI), the Adjudicating Authority, the Insolvency Professionals (IP) and the Information Utilities.

a) ***Insolvency and Bankruptcy Board of India (IBBI)*****:** IIBI acts as the regulator for insolvency proceedings under the IBC. The IBBI overlooks and manages the functions of information utilities, insolvency professional agencies and insolvency professionals.

b) ***Adjudicating Authority*****:** National Company Law Tribunal (NCLT)[48] and Debt Recovery Tribunal (DRT)[49] are the adjudicating authorities under the code. While the NCLT is for corporate insolvency process, the DRT is for individual insolvency. An appeal from the NCLT shall go to the National Company Appellate Tribunal (NCLAT) and thereafter to the Supreme Court while an appeal from DRT lies on the Debt Recovery Appellate Tribunal (DRAT) and thereafter to the Supreme Court.

c) ***Insolvency Professionals*****:** Section 3(19) of the Code defines an 'insolvency professional' as person enrolled under section 206 of the Act with an insolvency professional agency as a member and

[48] IBC, 2016, *supra* note 1, § 5(1).
[49] *Id.* § 79(1).

registered under the IBBI.[50] Insolvency professionals run the business of the debtor during the CIRP.

d) ***Information Utilities (IU)*:** IU stores financial information pertaining to the borrowings made, default occurred, type of interests created and so on. They act as a repository of all the financial transactions as far CIRP is concerned and are incidental to the process. National E-Governance Services Limited is the first IU in India.

III. KEY CONCERNS UNDER IBC

The concerns of the borrowers are one of the primary drawbacks in a CIC system of law. There is a certain tendency to favour liquidation under the current IBC regime. By September 2018, while 80% of the cases admitted ended up in liquidation, only 20% were successfully resolved.[51] When it comes to insolvency restructuring under the IBC, 2016, it fails to provide any pre-insolvency restructuring solution to any company who failed to pay its debts. The power wielded to the Committee of Creditor (or the creditors at large) is one of the jurisprudential drawbacks of the Insolvency Bankruptcy Code, 2016. The question as to the genuinity of the interests of the creditors as far as the revival of the company goes is doubtful. Rather, the interests of the creditors would always be the

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[50] *Id.* § 2(19).

[51] Pratik Datta, *Value destruction and wealth transfers under Indian Insolvency and Bankruptcy Code, 2016*, OXFORD BUSINESS LAW BLOG, Feb. 08, 2019, https://www.law.ox.ac.uk/business-law-blog/blog/2019/02/value-destruction-and-wealth-transfers-under-indian-insolvency-and.

recovery of their own claims. Since, the IBC follows a 'creditor-in-control'[52] regime; it could lead to a 'value destruction of a profitable business'.

The IBC is yet to make its deterrent effect more conspicuous, and right now it has only a passive influence on companies and its promoters. Moreover, the incidence of several vague provisions being added into the law ended up in a state of quandary for both the adjudicators as well as the practitioners. Section 29A inserted by virtue of the Insolvency and Bankruptcy Code (Amendment) Act, 2018 was identified as a favourable measure introduced into the IBC to rule out the involvement of various actors who may affect the credibility of the insolvency process.[53] However, IBC is silent as to the instance of the non-defaulting promoters taking part in the resolution process. This is still an area of ambiguity and was conspicuous in the case of *RBL Bank Ltd. v. MBL Infrastructure Ltd.*,[54] wherein the non-defaulting promoters were eventually allowed to submit a resolution plan upon the interference by the NCLT.

Another area of concern is the indifference propelled towards the operational creditor vis-à-vis the financial creditor. The IBC ought to prioritise the rights of the operational creditors in order to make the economy more investment-friendly. The operational creditors who have to

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[52] Ashu Kansal, *Whether It Is a Creditor or Investor Regime*, MONDAQ, Nov. 03, 2017, http://www.mondaq.com/india/x/642766/Insolvency+Bankruptcy/WHETHER+IT+IS+A+CREDITOR+OR+INVESTOR+REGIME.

[53] The Insolvency and Bankruptcy Code (Amendment) Act, 2016, No. 26, Acts of Parliament, 2018 (India), Statement and Objects.

[54] RBL Bank Ltd. v. MBL Infrastructure Ltd., 2017 SCC OnLine NCLT 12612.

undergo unwarranted haircuts can delve into more litigation and this can lead to the CIRP being a long-drawn process, thus decreasing the value of the assets in the long run.

An insolvency resolution process in India takes around 4.3 years on an average in contrast to 1.5 years in U.S.A and 1 year in U.K. IBC being credited as a massive improvement from its predecessor laws, it should be analysed and compared in relative terms to the insolvency laws prevailing in other developed countries and not just to the pre-existing laws.[55] The IBC does not have any provision for mediation or conciliation within it. Alternate Dispute Resolution (ADR) is time saving and is often favoured by investors and corporates. An investment-friendly insolvency regime ought to offer ways of alternatively resolving disputes.

The IBC should differentiate "financially distressed" and "economically distressed" companies. The IBC should seek to identify the type of 'distresses' that a company is under. "When the present value of the expected profits of a company is less than the total value of the assets of the company,"[56] it is said to be economically distressed. On the other hand, if a company is just not able to service its debt due to several reasons like high fixed costs, illiquid assets or revenues that are sensitive

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[55] *India's Insolvency and Bankruptcy Code: 3 years of Hits and Misses*, NEWSBARONS, https://www.newsbarons.com/real-estate/indias-insolvency-and-bankruptcy-code-3-years-of-hits-and-misses/.

[56] Nikita Kwatra, *The IBC has an incentive problem*, LIVE MINT, Jan. 02, 2019, https://www.livemint.com/Industry/nYs7QsAfNqtgGoQHZw2zBJ/The-IBC-has-an-incentive-problem.html.

to economic downturns, then such company is said to be under financial distress.[57]

While those companies under irreversible economic distress have to be liquidated, a company running through a certain financial distress could be rescued through financial restructuring or selling it to new investors. Thus, the key is to find a conducive remedy for the distressed company.

IV. CONCLUSION

There are a host of investment opportunities for foreign investors within the subcontinent. A law that is conducive towards investor-interests helps the economy grow. Asset Reconstruction Companies (ARC), Non-banking financial companies (NBFC), Alternative investment fund (AIF), foreign portfolio investment (FPI) and External commercial borrowing (EBCs) are some of the various ways in which a foreign company can invest in India. A strict and an effective insolvency law is one that protects an investor’s interests. IBC aims to create a strict insolvency regime where the investors are free to function and stand up to protect their interests, if required.

The major issue relating to the definition and scope of operational creditors and financial creditors. Though the judicial approach has been similar treatment of both operational creditors and financial creditors,

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[57] *Enterprise Value of Firms under Insolvency*, MONDAQ, Jul. 08, 2019, http://www.mondaq.com/india/x/822768/Insolvency+Bankruptcy/Enterprise+Value+of+Firms+Under+Insolvency.

there is still is a lot of scope for statutory clarity on these aspects. It is common knowledge that in the operations of any decently sized corporation, hue operational debts are owed.

If the law refuses to give parity to these creditors, with financial creditors, in at least certain aspects, these operational debtors will stand at a huge disadvantage. This situation may trigger a knock on effect and can further result in a bankruptcy of the corporations in the entire supply chain, of which the corporate debtor is a part of.

As enumerated earlier, the IBC regime does not attempt to find out the cause of distress in a corporate debtor. The IBC simply demands a default on a payment as a ground for triggering in the IBC process. This can be problematic if the causes are not distinguished between financial and economic causes. A corporation, for instance, which is in the business of an outdated technology, is bound to go out of business, regardless of the resolution efforts, the law may put into. However, a corporation undergoing stress due to a general distress in the economy, can be salvaged through the law, by the concerned entities coming up with a resolution scheme. Hence, the cause of distress plays a role in determining the tailor made resolution. The IBC in its current doesn't cater to this issue.

While the Insolvency and Bankruptcy Code, 2016 has largely been an ambitious drive, striving towards a world-class insolvency regime, it suffers from several lacunas that have to be effectively dealt with. In short, the law is an experimental one. However, the road ahead looks more promising than ever.