

India: A new Insolvency and Bankruptcy Code 2016

On 28 May 2016, the Insolvency and Bankruptcy Code 2016 (IBC) received Presidential assent in India and was published in the Official Gazette. The Government of India has notified several sections of the IBC for commencement since then. On 1 December 2016, the sections of the IBC related to resolution of corporate insolvency and corresponding regulations made by the Insolvency and Bankruptcy Board of India (the Board) became operational. While several critical provisions of the IBC (including those on liquidation) are yet to be notified, the IBC signals a radical change in how future reorganisations and formal liquidation will be conducted in India.

Introduction

Recent press reports indicate that there are over 75,000 cases pending in debt recovery tribunals across the country. This number does not even take into account the other cases pending before the Board for Industrial and Financial Reconstruction under the Sick Industrial Companies (Special Provisions) Act 1985 or those pending before various High Courts or the National Company Law Tribunal.

Main aims of the new law

This huge pendency of cases is attributed to the inefficiencies of the patchwork of legislations that governed corporate and personal insolvency prior to the IBC. The main aims of the IBC are therefore focused on improving the time it takes to effect either a rescue or liquidation and on maximising the returns for stakeholders. The appointment of an insolvency professional to achieve these aims is seen as key, as it seeks to run the processes largely outside of the court system. In addition, the IBC

hopes to promote entrepreneurship, especially in relation to individuals who will have access to a "fresh start" bankruptcy process. The IBC appears to take much of its inspiration from international best practices and is consistent with many bankruptcy reforms taking place around the globe at present.

Overview

In this briefing we focus on the aspects which apply to corporates only (i.e. companies, limited liability partnerships etc) and look at some of key themes:

1. Single track entry for both corporate insolvency resolution and liquidation
2. Appointment of a Resolution Professional
3. Approval of the Resolution Plan
4. Fast track Resolution
5. 180 day moratorium
6. Priority of claims
7. Avoidance actions
8. Cross-border Insolvency

Key issues

- Key features of the IBC include:
 - 180 day moratorium
 - Appointment of resolution professional
 - Resolution plan can be proposed by debtors or creditors
 - Ability to cram down creditors
 - Financial creditors have control
 - New defined list of priority
- 9. Implementation
- 10. Comparison with other regimes.

At the end of this note we take a quick look at the current World Bank Doing Business Rankings for Resolving Insolvency to see how India compares at present with other

jurisdictions from which it has taken its inspiration during the reform process, namely, the United States, the United Kingdom and Singapore.

Single track entry for corporate insolvency resolution and liquidation

Under the IBC, both the debtor and creditors will be able to commence the corporate insolvency resolution process. The triggers are related to defined liquidity tests, which are set out in the legislation and depend upon the types of claim that have caused a default. Creditors are divided into two types for the purposes of the IBC, financial creditors (essentially those who provide finance or credit, e.g. banks) and operational creditors (e.g. trade creditors, employees). Very significantly, a default in payment of a debt, however small it may be, is sufficient for the creditor to be able to apply to the Adjudicating Authority for initiating the corporate insolvency resolution process.

The sections of the IBC relating to liquidation have not yet become operational.

Appointment of a Resolution Professional

No matter who commences the corporate insolvency resolution process, a Resolution Professional is appointed to supervise the process. This aspect of the reforms has clearly taken its lead from the English approach of appointing an independent insolvency practitioner to facilitate the insolvency resolution process which is designed to free up the courts from adjudicating on every aspect of the process. Financial creditors commencing the process must nominate an interim Resolution Professional, who must then be approved by 75% of the financial creditors by voting share. If

operational creditors initiate the corporate insolvency resolution process, then they have the option of nominating an interim Resolution Professional. However, if they do not choose to do so then the Board (the new regulator established to lay down regulations under the IBC and regulate the functioning of insolvency professionals) will decide. Once an interim Resolution Professional is appointed, the responsibilities of debtor's management cease, although they are required to cooperate with and assist the Resolution Professional during the process. The Resolution Professional has 180 days from the date of admission of the application to initiate the process to facilitate a resolution plan to either restructure or liquidate the debtor. This period may be extended by a further 90 days in complicated cases where the Adjudicating Authority is of the opinion that the process cannot be completed in 180 days. The Resolution Professional must consult with a creditors' committee on all material matters such as disposals, funding or settlements. The creditors' committee comprises of financial creditors only. While directors or partners of the debtor and a representative of the operational creditors can attend the meetings of the creditors' committee, they cannot vote at the meetings. If there are no financial creditors or if all financial creditors are related parties of the debtor, then the creditors' committee shall consist of 18 largest operational creditors by value and one representative each of the workmen and employees of the debtor.

Approval of the Resolution Plan

Any person, including a prospective lender or investor, may put forward a resolution plan in respect of the

debtor. The Resolution Professional must ensure that the resolution plan(s) (more than one plan can be put forward) provides for (i) all costs of the insolvency resolution process to be paid in priority; (ii) operational creditors to receive no less than they would receive on a liquidation; (iii) the management of the affairs of the debtor; and (iv) implementation and supervision of the resolution plan. The Resolution Professional must also ensure that no laws are contravened and all other requirements of the Board have been satisfied. The resolution plan(s) needs the approval of 75% of the financial creditors by voting share and the approval of the Adjudicating Authority to be binding on all creditors. If the debtor's situation cannot be resolved within the time allowed or the creditors reject the plan for resolution, the debtor is placed into liquidation and the Resolution Professional becomes the Liquidator who must realise the assets and distribute in accordance with a new order of priority (see below).

As can be seen from the appointment and approval process, financial creditors have significant power and influence in the process and ultimately decide on whether the debtor is restructured or placed into liquidation.

Fast Track Corporate Insolvency Resolution

For debtors that have assets or income which fall below certain financial thresholds (to be specified by the Central Government), a fast track procedure is available, which provides for the resolution to take place in a more condensed period of 90 days. The provisions relating to the fast track procedure are yet to become operational.

180 day moratorium

No doubt this aspect of the IBC takes its inspiration from the US Chapter 11 process. The IBC does not set out a prescribed form of resolution plan and so the moratorium allows time to formulate and negotiate a resolution plan with the various stakeholders. The moratorium is wide ranging and protects the debtor from litigation or other legal proceedings, enforcement of security, third party owners and lessors recovering their own property and prevents suppliers from terminating essential supplies to the debtor. The moratorium continues until the resolution order is passed or the debtor is placed into liquidation. In exceptional cases, the moratorium can be extended for a further 90 days. There does not appear to be any option for those affected by the moratorium to be able to seek relief, although the Resolution Professional is under an obligation to pursue liquidation if it transpires that a resolution is not likely.

Priority of claims

One of the main criticisms of the current regime was that creditors of a distressed debtor were often left with competing claims launched in a variety of separate procedures. The IBC not only seeks to prevent this by encouraging a collective resolution procedure with the protection of a moratorium, but also in the context of liquidation, defines the order of priority of claims.

The order is broadly as follows:

1. the costs of the insolvency resolution and liquidation;
2. certain payments to workmen and payments to secured creditors (who also have the option of realising their security), which rank equally;

3. payments due to employees (e.g. unpaid wages);
4. financial debts owed to unsecured creditors;
5. government debts and debts due to unpaid secured creditors, which rank equally;
6. other creditors; and
7. shareholders.

Avoidance actions

The IBC also has avoidance rules for transactions at undervalue, preferences, transactions defrauding creditors and extortionate credit transactions. Challenges can be made by either the Resolution Professional or the Liquidator. There are exemptions for transactions in the ordinary course of business and transactions carried out in good faith and for value similar to those applicable under the English insolvency regime.

Cross-border Insolvency

The IBC treats foreign and domestic creditors of a debtor alike. However, the IBC summarily addresses concerns that may arise in a cross-border insolvency situation by providing that the Central Government may enter into agreements with other countries for enforcing the provisions of the IBC. Where a debtor's assets are located outside India, the IBC empowers the Adjudicating Authority to issue a letter of request to a foreign court or tribunal seeking its assistance.

Implementation

Much of the IBC relies upon the appointment of an insolvency professional and that professional implementing the new regime effectively. It is therefore perhaps not surprising to see that an entire Part of the IBC is dedicated to regulation of insolvency professionals and

insolvency professional agencies under the supervision and monitoring by the Board. The Board has recently notified regulations governing insolvency professionals and insolvency professional agencies. So far, 2 insolvency professional agencies have been registered with the Board.

In addition on 1 June 2016, the Government of India issued a notification constituting the National Company Law Tribunal (NCLT) and National Company Law Appellate Tribunal. The NCLT will be the adjudicatory body for the corporate aspects of the IBC. There are also other practical aspects that the IBC seeks to address and will rely upon by way of infrastructure, including the establishment of information utilities which are essentially registers where information about the debtor and the progress of the insolvency resolution process is maintained and available to stakeholders. These aspects will need to be up and running before the IBC can result in comprehensive reform.

Comparison with other regimes

It will be interesting to see whether the reforms in the IBC, have the effect of encouraging investment and inspiring growth in the Indian economy. No doubt it is hoped that the introduction of the IBC will at least improve India's rankings in the World Bank league table for Resolving Insolvency. As can be seen from the extract below, in comparing India to other jurisdictions from which it has taken its inspiration in the reform process, namely, the US, UK and Singapore, it has everything to play for.

Extract from the World Bank Doing Business Rankings for Resolving Insolvency 2017

	India	England & Wales	Singapore	USA
World Bank Rankings for Resolving insolvency	136	13	29	5
Recovery rates (cents on the dollar)	26.0c	88.6c	88.7c	78.6c
Time taken	4.3 years	1 year	0.8 years	1.5 years
Cost (as % of estate)	9%	6%	4%	10%

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