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Insolvency and Bankruptcy: Consequences of Pandemic in India

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ABSTRACT

Economic laws are inherently empirical and change throughout time as a result of experimentation. No different, the 2016 Insolvency and Bankruptcy Code (Code) has been a road under construction for legitimate reasons. It planned to start with simple, standard procedures but anticipated quick course changes to keep the business and economy running smoothly. India's economy has suffered greatly from COVID-19's effects, much like the rest of the world. Several businesses saw declining top and bottom lines as a result of the supply chain interruptions and demand contraction brought on by COVID-19 and the ensuing state-wide lockdown, as well as some of them perhaps failing to make their debt payments. Another experiment was necessary for this unusual condition, one that required choosing between two opposing courses of action: suspending the Code's activities or keeping them going as normal.

This article examines choices taken by the State and the efforts/responses with regard to I&B laws, during the course of the pandemic as well its aftereffects. This paper first discusses the Insolvency and Bankruptcy Code, 2016 along with its objectives. This is followed by an overview of covid-19, along with a short examination of its effects. Next, the response of the State during the pandemic, which is followed by protective measures taken and a short examination of the moratorium period. Next, a short discussion on the effects of the response and finally, concludes by presenting the personal opinions of the authors about the response and prevalent current scenario.

Keywords: *Insolvency and Bankruptcy Code, 2016; COVID-19; Effects of Pandemic; India.*

I. INTRODUCTION

The advent of the Insolvency and Bankruptcy Code, 2016 added a drastic trade in the Indian insolvency regime. It turned into certainly a major structural reform within the Indian insolvency regime in which there was a consolidation of all the insolvency laws in a new shape with a new infrastructural setup unique from the previously existing structure in India which became in a scattered shape. The pandemic inflicted two kinds of shocks on countries: a health shock and an economic shock. The Covid-19 pandemic has unleashed a spate of commercial

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disputes. The pandemic and the lockdowns have inflicted heavy losses on sales and incomes of many businesses—big or small, formal or informal. Consequently, many companies and enterprises are finding it difficult to meet their contractual obligations. Given the severity problem, the Reserve Bank of India (RBI) has issued a moratorium on repayment of all term loans. Similarly, in an effort to ameliorate the liquidity crisis faced by the debtors, the Government of India has suspended the initiation of insolvency and bankruptcy proceedings under the insolvency and bankruptcy code (IBC). So far, these moratoria have helped companies and other debtors defer servicing of their debt obligations.

II. INSOLVENCY AND BANKRUPTCY CODE- AIMS AND OBJECTIVES

The Insolvency and Bankruptcy Code (IBC) is a law enacted in India to consolidate and amend the laws relating to insolvency resolution and bankruptcy for individuals, partnership firms, and corporate entities. The primary aims and objectives of the IBC are as follows:

- i. A process that is efficient and time-bound is what the IBC strives to provide for the prompt resolution of insolvency cases. It establishes stringent deadlines to guarantee that settlement or liquidation actions are finished within a certain time frame, preventing delays and fostering resource efficiency.
- ii. Asset value maximization: The IBC seeks to increase the value of all assets used in the insolvency procedure. It aims to accomplish this by assisting in the restoration and continuance of profitable enterprises or, alternatively, by facilitating the transparent sale of assets to maximize their value.
- iii. Striking a balance between the interests of different stakeholders, such as creditors, shareholders, and employees, is a goal of the IBC. It seeks to distribute assets among these parties in a fair and equitable manner, taking into account each party's rights and claims.
- iv. promoting entrepreneurship and investment: By establishing a reliable and effective insolvency resolution structure, the IBC seeks to foster an environment that is favorable for entrepreneurship and investment. It builds confidence among lenders and investors and supports entrepreneurship by offering a method for the prompt relief of financial difficulties.
- v. Encouragement of a disciplined and creditworthy culture: The IBC aims to promote a disciplined and creditworthy culture among creditors and borrowers. By offering a transparent and strong structure for insolvency resolution and ensuring that non-

performing assets are dealt with quickly and effectively, it aims to deter defaulters.

- vi. Consolidating and streamlining bankruptcy and insolvency rules: The IBC attempts to harmonize and combine numerous insolvency and bankruptcy provisions that were previously dispersed throughout numerous statutes. It offers a uniform framework for handling insolvency matters, streamlining the court system and increasing effectiveness.
- vii. Losses to creditors are kept to a minimum: One of the IBC's main goals is to keep creditors' losses to a minimum when there is insolvency. It strives to lessen losses experienced by creditors and enhance overall recovery rates by offering a time-bound resolution process and encouraging the maximisation of asset value.
- viii. The bankruptcy and Bankruptcy Code's overall goal is to establish a strong and effective framework for bankruptcy resolution that fosters prompt settlement, maximises asset value, safeguards the interests of stakeholders, stimulates entrepreneurship, and reduces losses to creditors.

III. COVID-19 AND ITS EFFECTS ON TRADE AND COMMERCE

The COVID-19 pandemic has had significant effects on trade and commerce in India. Here are some key impacts:

Change in consumer choices and behaviour: The pandemic resulted in a change in consumer preferences and behaviour. Consumers are turning to online shopping, contactless transactions, and basic items due to health and safety concerns. While sectors like travel, hotel, and retail faced substantial challenges, others, like e-commerce, healthcare, and food delivery, saw increases in demand.

Policy interventions: The Indian government made a number of policy changes to lessen the pandemic's effects on trade and commerce. To boost the economy, assist enterprises, and encourage exports, policies like fiscal stimulus packages, liquidity support, and sector-specific relief measures were put in place.

Economic downturn: Lockdowns and limitations brought on by the pandemic caused a substantial slowdown in India's economy. Numerous companies were forced to temporarily close their doors or operate at reduced capacity, which resulted in the loss of jobs, decreased consumer spending, and a fall in economic activity. This in turn had an impact on trade and business across numerous industries.

Growth in e-commerce and digital transformation: The pandemic hastened India's adoption of digital technologies. Businesses increasingly turned to online platforms to maintain operations

as physical retail shops faced closures and restrictions. The panorama of trade and commerce was altered as a result of the increase in e-commerce activities and digital transactions.

IV. MEASURES TAKEN TO MINIMIZE IMPACT OF PANDEMIC IN INSOLVENCY AND BANKRUPTCY

The Indian government declared a statewide lockdown beginning on March 25, 2020, and it lasted for around two months with the aim of stopping the spread of the virus. With the exception of some interstate transportation that was granted towards the end of April and towards the beginning of May to allow migrant workers, stranded pilgrims, vacationers, and students to get back to their native destinations, all non-essential facilities and businesses, which include retail establishments, educational facilities, and places of worship, remained closed throughout the nation during this time. This still stands as the largest lockdown in terms of the virus in the history of the entire globe. At the time, it was the most extensive reaction by any nation to the pandemic. The economy had a protracted period of decline due to the enduring national lockdown, the worldwide economic slump, and the resulting breakdown of both demand and supply linkages.

The corporate Insolvency Resolution Process under the provisions of the IBC is distinctive from the previous function since it proceeds without the involvement of the court and in a timely manner. The unanticipated global pandemic brought our nation as well as many other nations throughout the world, an assortment of economic issues.

In order to provide credit to financially disrupted companies, governance organizations have implemented measures related to a moratorium on debt payments, sector-specific delays, injections of liquidity into the financial system, relaxation of asset classification banking norms, elasticity in director obligations to initiate insolvency proceedings, relief from compliance with certain legal obligations, etc. The Indian government has also introduced a variety of solutions to ease COVID-19-related discomforts. To prevent MSMEs (micro, small, and medium-sized enterprises)³ from being compelled into bankruptcy proceedings, the limit of default for filing an insolvency application was raised from Rs. 1 lakh to Rs. 1 crore. The time for resolution under the prudential model was extended by 180 days, while the RBI granted financial institutions a 6-month extension to the ban on term loan payments.

³ *Suspension of IBC during COVID-19: A mere mask while what is needed is a vaccine* (no date) *IBC laws - insolvency & bankruptcy (IBC), Companies Act & Sarfaesi*. Available at: <https://ibclaw.in/suspension-of-ibc-during-covid-19-a-mere-mask-while-what-is-needed-is-a-vaccine-by-anvit-seemansh/?print-posts=print> (Accessed: 12 June 2023).

i. CIRP AND COVID 19

According to regulation 40B of the Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) (Third Amendment) Regulations, 2020, this additional regulation needs to be added: - “40C. Special time-related provision. The entire period of lockdown imposed by the Central Government in the wake of the COVID-19 outbreak will not be taken into account for the sake of the time-line for any activity that was unable to take place due to such lockdown, with regard to a corporate insolvency resolution process, despite the deadlines set forth in these regulations but subject to the provisions in the Code.

The Suo Moto Order of NCLAT declared that the confinement period would not be included in calculating the CIRP duration. “That the time frame of lockdown ordered by the Central Government and the State Governments, which includes the period as may be extended either in whole or part of the country, where the registered office of the Corporate Debtor may be located, shall be excluded for the purpose of counting the time frame for ‘Resolution Process under Section 12 of the Insolvency and Bankruptcy Code, 2016, in all cases where Corporate Insolvency Resolution Process’ has been initiated” it was possessed.

ii. MORATORIUM PERIOD:

The Statement on Developmental and Regulatory Policies have published by RBI.

The Statement outlines numerous legislative and regulatory initiatives that directly alleviate the strain on the economy brought on by COVID-19. "All commercial banks (including regional rural banks, small finance banks, and local area banks), co-operative banks, all-India financial institutions, and NBFCs (including housing finance companies and micro-finance institutions) ("lending institutions") are being permitted to allow a moratorium of three months on payment of instalments in respect of all term loans outstanding as of March 1, 2020. As a result, the term for such loans, the repayment schedule, and any subsequent due dates may all be pushed by three months.⁴

iii. STATE RESPONSE:

It was further stated by the Minister that the Insolvency and Bankruptcy Code (Second Amendment) Act, 2020 with effect from 5th June 2020 provides for insertion of Section 10A to the Code for temporary suspension of initiation of corporate insolvency resolution process (CIRP) under Section 7, 9 and 10 of the Code for a period of six months or such further period

⁴ *Moratorium – meaning and objective in Insolvency & Bankruptcy Law (2023) Taxmann Blog*. Available at: <https://www.taxmann.com/post/blog/moratorium-meaning-and-objective-in-insolvency-bankruptcy-law> (Accessed: 12 June 2023).

not exceeding one year from 25th March 2020, as follows:

1. All corporate debtor defaults that take place between March 25, 2020, and the conclusion of the suspension term will be covered by the benefit of the suspension.
2. For the purpose of initiating CIRP under the code as a permanent carve out, such defaults arising from March 25, 2020, and up until the end of the suspension term, will remain as Non est.
3. Directors are now exempt from personal liability for COVID period defaults thanks to a change to Section 66.
4. According to notification number SO-4638 (E) dated December 22, 2020, the time period under Section 10A of the Code has been extended for an additional three months starting on December 25, 2020.⁵

V. PROTECTIVE MEASURES

i. Suo Moto Writ Petition at Supreme Court of India in cognizance for extension of Limitation

In light of the COVID-19-related circumstances, the Supreme Court issued an order extending the limitation period from March 15, 2020, until future orders, regardless of whether it is condonable or not under general or special law. The goal is to make sure that attorneys and litigants do not need to physically travel to the respective Courts or Tribunals across the nation to file their petitions, applications, suits, appeals, or other proceedings within the time frame required by the general law of limitation or by special laws.

ii. Increase in Payment Default Threshold

The threshold for starting insolvency resolution procedures under the Insolvency Code was raised from INR 1 lakh to INR 1 crore as a result of a notification 3 dated March 24, 2020. Given that the previous threshold⁶ of INR 1 lakh was very low, this move is anticipated to be advantageous for micro, small, and medium-sized businesses (or "MSMEs") and is generally welcomed by corporate debtors. The notification does not limit the application of the raised threshold to the period of the pandemic or any other time period, unlike the suspension of insolvency procedures detailed below.

⁵ <https://ibbi.gov.in/uploads/legalframework/741059f0d8777f311ec76332ced1e9cf.pdf>

⁶ *Increase in the threshold amount for insolvency under IBC (2020) SCC Blog*. Available at: <https://www.sconline.com/blog/post/2020/04/17/increase-in-the-threshold-amount-for-insolvency-under-ibc/> (Accessed: 12 June 2023).

iii. Exclusion of Lockdown Period from Timelines

Regulations under the Insolvency Code were changed in March-April 2020 to state that any activity or job in the Corporate Insolvency Resolution Process ("CIRP") or liquidation process, as applicable, that was unable to be performed as a result of the shutdown would not be included during that time. The National Company Law Appellate Tribunal ("NCLAT") issued an order 4 dated 30 March 2020, pursuant to which the period of lockdown was required to be excluded from such statutory period in respect of cases where the CIRP was pending. Despite the fact that this amendment did not extend the statutory timeline of 180 days (which may be extended to 270 days) for completion of the CIRP specified under Section 12 of the Insolvency Code, this amendment did not change that timeline.

iv. Suspension of Insolvency Proceedings

The Insolvency and Bankruptcy Code (Amendment) Ordinance, 2020 (the "Insolvency Ordinance") came into force on June 5, 2020. The Insolvency Ordinance amended Section 66 of the Insolvency Code (Fraudulent Trading or Wrongful Trading) and included a new Section 10A (Suspension of Initiation of Corporate Insolvency Resolution Process).

The filing of applications under Sections 7, 9, and 10 of the Insolvency Code (by financial creditors, operational creditors, and corporate debtors themselves, respectively) for the initiation of CIRP of a corporate debtor with respect to defaults occurring during the six (6) month period starting on and including March 25, 2020 (the date of the national lockdown), which may be extended up to one (1) year ("Restricted Period") is prohibited by Section 10A of the Insolvency Code. Additionally, the filing of applications for the initiation of CIRP by a corporate debtor in respect of any such default is permanently outlawed by Section 10A of the Insolvency Code. However, for defaults made by the corporate debtor before March 25, 2020, Section 10A of the Insolvency Code will not be applicable.⁷

v. Suspension of Liability for Wrongful Trading

The directors or partners (in the case of a limited liability partnership) of the corporate debtor may be required to personally contribute to the corporate debtor's assets under Section 66(2) of the Insolvency Code during the CIRP of the corporate debtor and upon an application filed by the resolution professional with the relevant National Company Law Tribunal ("NCLT") if the director or partner knew or should have known that there was no reasonable prospect of avoiding the obligation.

⁷ <https://www.mca.gov.in/content/dam/mca/pdf/IBC-2016-20230118.pdf>

The Insolvency Ordinance has added subsection (3) to Section 66 of the Insolvency Code, which forbids filing any applications under Section 66(2) with regard to any failure for which CIRP has been suspended under Section 10.

vi. Special Insolvency Framework for MSMEs

Section 240A of the Code

Pre-Packaged Insolvency Resolution method ("PPIRP") was developed during the Covid-19 pandemic to give corporate individuals classed as MSMEs access to an effective alternative insolvency resolution method. It aims to deliver quicker, more affordable, and more valuable results for all parties involved in a way that minimizes disruption to the ongoing operation of their business and supports the preservation of jobs.

VI. EFFECTS OF RESPONSE

i. SECTION 10(A) - A BANE OR A BOON?

According to this new clause, no application under sections 7, 9, or 10 of the IBC may be made against a corporate debtor for any kind of fault that occurred on or after March 25, 2020. Additionally, the new legislation contains a clause that specifies that "no application shall ever be filed against a corporate debtor during this period, i.e., from March 25, 2020, until the suspended period. The regulation also stipulates that any application made against a corporate debtor before the time of March 25, 2020, must be deemed maintainable in order to avoid any misunderstandings. Even while the ordinance is quite effective at protecting India's economy from any sort of domino effect brought on by occurrences of force majeure, it gives room for a variety of interpretations for many of the current problems.⁸

ii. IF AMENDMENTS ARE INHERENTLY PROSPECTIVE OR RETROSPECTIVE?

Regarding applications that were submitted and were still pending as of the day the ordinance was promulgated, it makes no mention of the maintainability issue.

It was upheld that "the ordinance shall have retrospective applicability to all applications regardless of their date u/s 7, 9, & 10 of IBC" by the NCLT Chennai Bench in the case of Arrow line Organic Products Private Limited v. M/s Rockwell Industries Limited. The NCLT Kolkata's ruling in the case of Foseco India Limited v. Om Boseco Rail Products Limited⁵ affirmed that "the ordinance will not have retrospective applicability in the absence of a specific mention," despite the fact that the aforementioned interpretation is in conflict with it.

⁸ <https://ibbi.gov.in/uploads/resources/d710f5e800ca901b7ce129e861316fce.pdf>

iii. DIFERRENT SITUATIONS FOR INTERPRETATION:

The following three scenarios are likely to occur and will continue to be a topic of discussion after COVID-19:

- Default that develops before 25th March 2020.
- Default that develops throughout the suspension.
- Default that develops after the suspension time.

The declaration related to this section specifically stores defaults made before March 25, 2020. As a result, breaches that occur before March 25, 2020, and implicitly those that occur after the conclusion of the six-month or extended term, are not subject to the conditions established by Article 10A for filing insolvency applications.

However, the submission of such claims for default is constrained by the time frame, starting on March 25, 2020, and lasting until the conclusion of the six-month or extended period, as applicable. The clause in Article 10A provides more justification for this stance. Due to such deficiencies, any unresolved claims that were also presented between March 26, 2020, and June 5, 2020, shall be legally rejected in contravention of this decision. Since it also affects any pending claims that were submitted between March 25, 2020, and June 5, 2020, this order is practically retroactive. According to the modification, if a corporate debtor's default amount reaches Rs. 1 Crore, bankruptcy procedures may be started against them. No application may be submitted for the same in circumstances when the default amount is less than the prescribed amount. Since they won't be able to collect the amount that debtors owe them, certain financial creditors would suffer losses as a result of this. Until the matter is resolved by the adjudicating authorities, all three of the aforementioned eventualities will be a topic of discussion during litigation.

PURPOSE AND GOAL OF THE AMENDMENT:

No insolvency law can neglect the business since there can be no insolvency if there is no business. The following primary IBC objectives must be kept in mind when we examine the ordinance:

- Decision against liquidation.
- Maximisation of Corporate Debtor Assets.
- Encouragement of entrepreneurship.

We must be aware that IBC was created in such a way that it can handle both types of situations:

1. A company's or corporate entity's success.
2. If a company or commercial entity is struggling.

The main goal of the code is to save the company's existence. Currently, forcing businesses into liquidation will result in a premature liquidation and the realisation of the enterprises' premature obligations. As a result, every effort must be made to prevent the firm from dying too soon, and the IBC must never be used as a weapon to do so. Everyone deserves a fair shot to survive, thus we must consider the firm's objectives and future plans. Let us understand this with the help of some examples.

Mistakes That Could Be Corrected Versus Mistakes That Could Not Be:

Scenario 1: If there had been no such ordinance and the standard IBC had been in operation, "many viable firms would have been forced under liquidation."

Scenario 2: The IBC has currently prevented "many viable firms from going into liquidation" when it is not in effect.

Therefore, if you liquidate a viable business in the first case, the business will no longer exist, and the error cannot be corrected. On the other hand, if you are unable to liquidate a viable corporation for a specific period of time in the second case, that error can be corrected.

VII. CONCLUSION

Despite the fact that this government action has received widespread support, it has also drawn some criticism. This action aims to prevent numerous businesses from going out of business as a result of late payments. This is viewed as needless, though, given the government has already increased the threshold for starting insolvency procedures from Rs. 1,00,000/- to Rs.1,00,00,000/- The government has prevented a sizable number of businesses from going bankrupt in the absence of financial support by raising the threshold limit. Therefore, the overall impact of both policies is the same, but the suspension of IBC brings a slew of additional problems with it.
