IBC Second Amendment Bill: Salient Features

A holistic approach to overcome loopholes

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Background

In exercise of the powers conferred in article 123 (1) of the Constitution, the Hon'ble President promulgated the much awaited Insolvency and Bankruptcy Code (Amendment) Ordinance, 2018 on 6th June, 2018 in order to bring relief to various stakeholders by balancing their interest under the Insolvency and Bankruptcy Code, 2016 ('IBC/ Code') especially interest of home buyers and Micro, small and medium enterprises (MSMEs). The Ordinance also proposed to reduce the minimum voting threshold of the Committee of Creditors to 66% from 75% for key decisions.

The Insolvency and Bankruptcy (Amendment) Bill , 2018 was proposed in Lok Sabha on 23rd July, 2018 and was eventually passed in the Rajya Sabha on 10th August, 2018.

In this write up we have briefly covered the major amendments proposed in the Bill.

Applicability

The Provisions of the Bill shall be effective prospectively w.e.f 6th June, 2018 (being date of promulgation of the Ordinance), i.e. the same will apply to all the ongoing proceedings and to those which commence on or after 6th June, 2018, and not to the proceeding that has been concluded as on the date of introduction of the Ordinance.

Significate Amendments proposed in the Bill

The Insolvency and Bankruptcy (Amendment) Bill, 2018 can be seen as a holistic approach towards overcoming the loopholes in the existing Code. The Bill lays focus on substantial legal amendments as well as procedural changes so as to ensure removal of hindrances and conduct of a smooth CIRP.

Following are the significant amendments introduced in the Bill:

(a) Home Buyers are recognised as Financial Creditors

The entire hullabaloo as to the position of "Home Buyers" in the Code came to rest with the introduction. Having a substantive role in cases like Jaypee and Amrapali, the home buyers were earlier not recognized as creditors at all under IBC.

However, the Bill now identifies "Home Buyers" as financial creditors under the Code, which means that home buyers are also in the list of eligible applicants for initiation of CIRP and they also get representation in the CoC.

(b) Withdrawal of CIRP Application with the approval of 90% of CoC members

The newly inserted section 12A of the Code provides for withdrawal of application after admission, if the same is approved by atleast 90% of the CoC members. Prior to the Bill, withdrawal of Application after initiation of CIRP was not permitted, as CIRP once initiated cannot be rolled back. Considering the preference of resolution over liquidation and settlement over resolution, it was realized that there might be a situation wherein the Corporate Debtor agrees to settle the dues with its creditors by way of an out-of-court settlement; and thus, if atleast 90% of the CoC gives assent to such withdrawal, the same shall be allowed.

(c) Extension in the tenure of IRP till the appointment of RP

Once CIRP is initiated, the Board and Management of the Corporate Debtor stands suspended and the control shifts to the hands of the IRP/ RP. Section 16(5) of the Code provided that the tenure of the IRP shall not exceed beyond thirty days of his appointment, whether or not the RP is appointed. Thus in situations where the RP was not appointed by the tenure of RP expired, the Corporate Debtor was technically left un-administered. Thus, to make up for this lacuna, section 16(5) of the Code has been amended to provide that the tenure of IRP shall continue till the RP is appointed.

(d) Requirement of special resolution in self-filing cases under section 10 of IBC

Section 10(3)(c) of the Ordinance provides that in case of self-filing of Application u/s 10 of the Code for initiation of CIRP, a Special Resolution (SR) must be passed by the shareholders of the Corporate Debtor.

Prior to this Amendment, filing of such Application was decided upon among the directors of the Corporate Debtor themselves. Hence, to rule out chances of misutilization of this power bestowed upon the directors by the Code and to prevent the BoD of the Corporate Debtor from taking a unilateral decision in this regard, this provision was introduced by way of the Ordinance.

(e) Reduction in voting percentage for key decisions

As per the Code, decisions w.r.t the resolution process, there existed a voting threshold of atleast 75%. However, a voting threshold as high as this was frustrating the essence of the Code i.e. "Resolution over Liquidation." It was observed that Resolution Plans were not approved by the CoC. It was finally in the case of **Synergy-Dooray**, where the NCLT, Hyderabad Bench passed an order for approval of Resolution Plan with 66% votes in favour.

Thus, with a view to effectuate a smoother CIRP, voting thresholds were reduced from 75% to 66% and 51% for serious decisions and routine matters respectively.

As a result, the voting threshold was reduced from 75% to 66% for the following matters:

(a) Approval of Resolution Plan

(b) Extension of CIRP

(c) Appointment of CIRP/ IRP

(d) All section 28 matters

Whereas, the voting threshold for all matters other than (a)-(d) as mentioned above, has been reduced to 51%.

(f) RP to take necessary approvals of the statutory authorities as may be required for implementation of Resolution Plan

The newly inserted sub-section (4) of Section 31 of the Code states that once a resolution plan is approved, the Resolution Applicant must obtain requisite approvals from respective authorities within 1 year of approval of the Plan.
This is to ensure timely execution of the Plan and to avoid any procrastination.

(g) Shareholding by virtue of conversion of loan into equity shall not be treated as Related Party.

Section 21(2) provides that those persons who became a "related party" solely on account of conversion of any loan or debt into equity, shall be exempted from the prohibition of being a Resolution Applicant.
The very rationale behind such exemption is that conversion of loan/ debt into equity after a particular time-period or on happening of any trigger event, happens to be a very common clause of several loan/ debt agreements executed between the lender

and borrower. Thus the conversion that takes place is only on account of an agreement which was essentially of a debt nature.

(h) Procedural changes in CIRP

➢ Commencement of CIRP

Under normal circumstances, the IRP is appointed vide the same Order pursuant to which the application for initiation of CIRP is admitted by Adjudicating Authority. However, there might be some cases where the IRP is not appointed in the Order. Until now, CIRP was deemed to commence from the date of Order of the Adjudicating Authority, regardless of the fact whether the IRP was appointed or not.

However, the newly inserted proviso to sec 5(12) of the Insolvency and Bankruptcy Code, 2016 ("**Principal Code/ Code**") provides that, in cases where the IRP is not appointed vide the same Order pursuant to which application for CIRP is allowed, CIRP shall commence from the date of appointment of IRP.

The intent behind providing this flexibility is to ensure achievement of the ultimate motive of promoting resolution over liquidation. As and when CIRP is initiated, the role of the Directors of the Company comes to an end and passes on to the hands of the IRP followed by the RP. Thus, the time gap between Order of initiation of CIRP and appointment of IRP is loss of valuable time in the already stringent moratorium period of 180/ 270 days.

Thus, deemed commencement of CIRP from the date of appointment of IRP is in harmony with the timelines as well as the spirit of the Code in its truest sense.

➢ Approval of CCI prior to approval of CoC

In order to ensure a smooth and hindrance free execution of the Resolution Plan, the Ordinance provided that, the Resolution Applicant shall obtain all necessary approvals required for execution of plan, within one year of approval of Plan by the Adjudicating Authority.

While the Bill is in line with the above-mentioned requirement, it also provides that where a Resolution Plan contains a provision of any "Combination" u/s 5 of the Competition Act, 2002. The Resolution Applicant is required to take a prior approval from the Competition Commission of

India ("**CCI**") before the Plan is proposed to the Committee of Creditors ("**CoC**") for approval.

The aforementioned amendments warrants for removal of ambiguity w.r.t. adherence of applicable laws and ensures synchronization amongst laws.

Despite the benefits that the requirement of this prior approval carries, a major loophole that lies herein is that the term "prior" does not denote any specific time period by which the approval of CCI must be obtained.

Another glitch that comes to light is that the fees for seeking approval of CCI in Form I and Form II is as high as Rs. 15 Lacs and Rs. 50 Lacs respectively. Hence, the question that arises here is that, in the present conditions where the odds of approval of a Resolution Plan is bleak, would it be viable for the Resolution Applicants to play a gamble of such high fees, keeping in mind the high uncertainty of approval of Resolution Plans?

Thus, a more practical approach is required to be adopted to ensure that laws that are being implemented are not just suited in text but also in spirit and can fit into the real-life practices.

Analysis

The Bill comes out to be a big leap of positive changes ensuring that the Code is in the benefit of the stakeholders in the truest sense. However, there still lies certain areas of ambiguity. Section 30(1) of the Amendment provides that the Resolution Applicant shall submit an affidavit to stating on oath therein that the Resolution Applicant is not ineligible as regards to the erstwhile section 29A. However, clarity is not drawn whether the RP is to solely lay his reliance on such affidavit or he/she remains liable to carry out an independent scrutiny of the details of the Applicant so as to ensure eligibility. Now that the home buyers have been identified as Financial Creditors, they can see the light at the end of the tunnel. However, the question that arises is that how long is this tunnel? Despite being classified as FC, they still remain to be unsecured Financial Creditors and thus stand 4th in the order of priority in the "Waterfall Mechanism" provided u/s 53 of the Code. The Bill clearly speaks of exclusion of converted equity shareholders from the scope of Related Party. However, such exclusion is given for the CIRP. The Bill however remains silent as to the treatment of such equity holding in case of liquidation. There exists ambiguity whether such equity holders will be considered as Financial Creditors or Equity Holders as the FCs are given priority while distribution of monies during liquidation.

The Road Ahead

Now that the bill has been passed in Rajya Sabha, the only formality now required is the assent of Hon'ble President. The amendments proposed in the Bill have majorly been inspired by the various on-going cases of CIRP and/ or liquidation and the ILC Reports. Practical glitches that have come to light in cases like Jaypree Infra, Amrapali, Synergy-Dooray, AMR Infrastructure Limited etc have led to these amendments as mitigatory measures for futures cases. Thus, the upcoming cases of CIRP and Liquidation shall be looked into with a much practical approach in line with the current business dynamics.