

Insolvency and Bankruptcy Act (IBA)
(06 January, 2022)

What is Insolvency?

Insolvency is a situation where individuals or companies are unable to repay their outstanding debt.

What is Bankruptcy?

Bankruptcy, on the other hand, is a situation whereby a court of competent jurisdiction has declared a person or other entity insolvent, having passed appropriate orders to resolve it and protect the rights of the creditors. It is a legal declaration of one's inability to pay off debts.

Insolvency and Bankruptcy Act (IBA), 2016

UPSC GS Study Notes

- This was enacted for reorganization and **insolvency resolution** of corporate persons, partnership firms, and individuals in a time-bound manner for maximization of the value of assets of such persons.
- IBC was spearheaded by the Ministry of Finance but now from 2016, the administration is transferred to the **Ministry of Corporate Affairs since 2016**.
- It deals with debt default of companies and limited liability entities, partnership firms, and individuals.
- It was based on **T K Vishwanathan Committee** on Bankruptcy Law Reforms Committee (BLRC) in 2014.
- It proposes a framework to ensure
 1. Early detection of stress in a business,
 2. Initiation of insolvency resolution process by the debtor, financial creditor, or operational creditor;
 3. Liquidation of unviable business and
 4. Avoiding destruction of the value of the failed business.
- Two key drivers for the IBC are relatively short time-bound processes, and the **focus on prioritizing resolution rather than a liquidation** to support companies falling within its ambit.
- Its core implication has been to allow credit to flow more freely to and within India while promoting investor and investee confidence.

5 Objectives of IBC, 2016

- Promote Entrepreneurship
- Availability of the credit
- Balance the interests of all stakeholders.
- Maximization of the values of assets
- Greater clarity in the law.

Features of IBC, 2016

- Insolvency and Bankruptcy Code, 2016 provides a **time-bound process for resolving insolvency in companies and among individuals**.
- The Government implemented the Insolvency and Bankruptcy Code (IBC) to consolidate all laws related to insolvency and bankruptcy and to **tackle Non-Performing Assets (NPA)**.
- Establishment of an **Insolvency and Bankruptcy Board of India** to exercise regulatory oversight over insolvency professionals, insolvency professional agencies, and information utilities.
- **Insolvency Professionals (IPs)** handle the commercial aspects of the insolvency resolution process.
- **Insolvency Professional Agencies (IPAs)** develop professional standards, codes of ethics and be the first-level regulators for insolvency professionals members leading to the development of a competitive industry for such professionals.

UPSC GS Study Notes

- In March this year, the government raised **the threshold for invoking insolvency under the IBC to Rs 1 crore** from Rs 1 lakh with a view to preventing the triggering of such proceedings against small and medium enterprises that are facing currently the heat of coronavirus pandemic.
- The **IBC is both flexible and dynamic**, which makes it impactful, given how forward-thinking the concept of omnibus legislation of its nature actually is.
- The IBC goes beyond other similar pieces of legislation across the world, and through the Insolvency and Bankruptcy Board of India (IBBI), it has established an unprecedented organization that both regulates and develops insolvency policy and assesses market realities.

IBC separates commercial aspects of the insolvency proceedings from judicial aspects.

- **Insolvency Professionals (IPs)** will deal with commercial aspects such as affairs of the corporate debtor, a committee of creditors.
- Judicial issues will be handled by proposed Adjudicating Authorities (**National Company Law Tribunal /Debt Recovery Tribunal**).
- **'Information Utility'** is created which would store financial information in electronic databases.

[Click here to read about the Insolvency and Bankruptcy Board of India \(IBBI\)](#)

[Click here to read about National Company Law Tribunal, 2013 and NCLAT](#)

Other provisions of IBC, 2016

- The Code also provides a fast-track insolvency resolution process for **corporates and LLPs**. This will be an enabler for **start-ups and SMEs** to complete the resolution process **in 90 days** (extendable to 45 days).
- When a corporate entity defaults on its debt, control shifts from shareholders/promoters to the **Committee of Creditors (CoC)**. CoC has **180 days** to evaluate the case (90 days extendable).
- IBC empowers **operational creditors** (workmen, suppliers, etc.) also to initiate insolvency proceedings.
- During waterfall (liquidation) financial debts owed to **unsecured creditors are kept above Government dues**.
- IBC has amended India's **Corporate insolvency resolution** process. Prior to the approval of the resolution plan, the antecedents, creditworthiness and credibility of resolution applicants including Promoter are considered by the Committee of Creditors.



UPSC GS Study Notes

- Recently India amended IBC and prohibited near relatives, their CA, Promoters in the Bidding process during Insolvency.
- Even RBI allowed External Commercial Borrowing (ECB) for re-bidding under IBC.
- RBI allowed faulty organizations to bid for their subsidiary organization if they pay interest over the loan in which default is taken place.
- The Code also addresses **cross-border insolvency** with a detailed framework soon.

IBC Amendment of 2019

ASPIRE IAS

UPSC GS Study Notes

- Time-bound resolution. voting rules for financial creditors
- Homebuyers as creditors. Can initiate proceedings.
- 330 days deadline, Creditors who voted against majority can receive minimum liquidation value, Resolution plan to be binding on all.

Insolvency and Bankruptcy Code (Amendment) Ordinance, 2021

- Insolvency and Bankruptcy Code (Amendment) Ordinance, 2021 promulgated on 4th April 2021 provides for a pre-packaged insolvency resolution process (PPIRP) for corporate debtors classified as micro, small and medium enterprises.
- [Click here to read more about IBC Ordinance 2021](#)

Impact of IBC, 2016

- It has successfully instilled confidence in the corporate resolution methodology as IBC has streamlined insolvency processes in a sustainable, efficient, and value retaining manner.
- Improvement in India's Ease of Doing Business Rankings to 63rd place.
- According to the Resolving Insolvency Index (a component of Ease of Doing Business), India's ranking improved to 52 in 2019 from 108 in 2018, which is a leap of 56 places.
- The Recovery Rate improved nearly threefold from 26.5% in 2018 to 71.6% in 2019. And the overall time is taken in recovery also improved nearly three times, coming down from 4.3 years in 2018 to 1.6 years in 2019.

Issues in IBC, 2016

- According to the data from the Insolvency and Bankruptcy Board of India (IBBI), of the 2,542 corporate insolvency cases filed between December 1, 2016 and September 30, 2019, about 156 have ended in approval of resolution plans — a mere 15%.
- The high number of liquidations is a cause for major worry as it violates IBC's principal objective of resolving bankruptcy.
- The slow judicial process in India allows the resolution processes to drag on, this was the same reason for slow recovery under SICA or RBBD.

Way forward:

- Other legislative measures that will further improve the investment climate, including the rolling out of the commercial courts, commercial divisions, and the Commercial Appellate Divisions Act, 2015, to allow district court-level commercial courts, and the removing of over 1,500 obsolete and archaic



UPSC GS Study Notes

laws.

- Bringing in technology would help ease of access to justice and greatly help ease of doing business from a process and efficiency standpoint as well.

ASPIRE IAS