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Decoding the IBC (Amendment) Ordinance, 2020: Opening the Pandora's Box



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The impact of COVID-19 pandemic has been seen globally. India has been affected not only because of its domestic slowdown but also because of international recession.

At the commencement and during the pandemic lockdown, two initiatives have been undertaken by the Government of India:

- a On 24.03.2020, the threshold for initiation of Corporate Insolvency Resolution Process (for short “CIRP”) under the Insolvency and Bankruptcy Code, 2016 (for short “IBC”) against corporate debtors was increased from Rupees 1 lakh to Rupees 1 crore, vide MCA Notification No. S. O. 1205 (E) (for short ‘the Notice’). This action was taken to save a lot of businesses, which were already facing a threat of default and thus avoid large scale insolvencies.
- b On 24.03.2020, Ld. Finance Minister in a press conference has also stated that if current situation continues beyond 30.04.2020, the Government may also consider suspending the application of Sections 7, 9 and 10 of the IBC for a period of 6 months.
- c On 17.05.2020, the Indian Government in order to sustain the economy has introduced the ‘Atma Nirbhar Package’. The Finance Minister announced that under the umbrella of the Atma Nirbhar Package, significant changes were to be brought to the IBC, with the sole object to promote the ease of doing business.
- d In view of the above, the President of India has promulgated an Ordinance on 05.06.2020, to amend the IBC. The Insolvency and Bankruptcy (Amendment) Ordinance, 2020 (for short “Ordinance”) has been brought into force, which states that it shall come into effect at once i.e. date of publication, for suspension of bankruptcy proceedings against persons impacted by the outbreak of COVID-19.

Key Takeaways of the Ordinance:

- 1 Suspension of Initiation of CIRP

a Section 10A has been inserted to Section 10 of IBC.

b Section 10A of IBC is as follows:

“Section 10A: Suspension of initiation of corporate insolvency resolution process.

[10A. Notwithstanding anything contained in Sections 7, 9 and 10, no application for initiation of corporate insolvency resolution process of a corporate debtor shall be filed, for any default arising on or after 25th March, 2020 for a period of six months or such further period, not exceeding one year from such date, as may be notified in this behalf:

Provided that no application shall ever be filed for initiation of corporate insolvency resolution process of a corporate debtor for the said default occurring during the said period.

Explanation: For the removal of doubts, it is hereby clarified that the provisions of this section shall not apply to any default committed under the said sections before 25th March, 2020.”

c Section 10A provides that no insolvency proceedings shall be initiated under Section 7, 9 and 10 of IBC for a period of six (6) months, w.e.f. 25.03.2020, which can be extended up-to maximum of (1) year.

d Hence there is suspension of CIRP:

- Initiation of CIRP by a financial creditor under Section 7 of IBC
- Initiation of CIRP by an operational creditor under Section 9 of IBC
- Initiation of CIRP by a Corporate Applicant under Section 10 of IBC

e The Ordinance states that it shall come into force, at once and shall apply to defaults arising on or after 25.03.2020 for a period of six (6) months, which may be extended up to one (1) year.

f The said period being from 25.03.2020 to a period of six (6) months, initially and extend the same for

further period not exceeding one (1) year in totality. (for short “disruption period”)

- g The proviso inserted to Section 10A uses the words “no application shall ever be filed”, this means that the proviso gives a protection in perpetuity for the defaults occurred by debtors during the disruption period. However, whether the default is in nature of an isolated one or continuing one, will always be a matter of facts and may lead to situation where the protection under the proviso to section 10A may not be available to the debtor in the times to come.
- h The Explanation to Section 10A provides that the provisions of the Ordinance shall not be applicable to CIRP initiated prior to 25.03.2020. i.e. defaults that occurred before 25.03.2020, may be subject to IBC proceedings.

Bar on Initiation of Fraudulent or Wrongful Trading by Resolution Professional

- 1 Clause 3 has been inserted to Section 66.
- 2 Section 66(3) of IBC is as follows:
“In Section 66 of the Principal Act, after sub-section (2), the following sub-section, shall be inserted, namely:
(3) Notwithstanding anything contained in this section, no application shall be filed by a resolution professional under sub-section (2), in respect of such default against which initiation of corporate insolvency resolution process is suspended as per Section 10A.”
- 3 Section 66 (2) of the IBC provides that, if, the directors allow a corporate debtor to trade where they knew or ought to have known that the any business of the corporate debtor has been carried on with intent to defraud creditors or any fraudulent purpose, the corporate debtor can be held personally liable.
- 4 Section 66(3) provides that resolution professionals will be barred from initiating fraudulent trading or wrongful trading application against directors of companies where the IBC process is suspended as per Section 10A. Section 66 (3) has to be read in consonance with Section 10A.
- 5 As per Section 10A, initiation of CIRP is suspended under Section 7, 9 and 10 of IBC. Similarly, under Section 66 (3) no application for fraudulent or wrongful trading can be filed during this disruption period while the initiation of CIRP is suspended.

Major Concerns and Conclusion

- 1 The primary object behind the Ordinance is to protect the interest of business entities/ debtors who have suffered economic distress because of COVID 19 pandemic.
- 2 However, it may not end up completely absolving the business entities/ debtors from liability in times to come.
- 3 The liability will be subject to IBC and this Ordinance provides only a breather period to the business entities/ debtors.

- 4 The intention of the notice issued by the government to increase the threshold from Rs. 1 lakh to Rs. 1 crore, is to relieve the companies from financial distress during the ongoing crisis.
- 5 The revision of threshold vide the notice will indeed come as a savior to small and medium sized companies, vulnerable to the wrath of lenders during these tough times. Further the increase is permanent in nature i.e. not limited to time.
- 6 The ordinance grants a blanket protection to corporate debtors for the defaults committed during the disruption period.
- 7 The use of the words “no application shall ever” in proviso to Section 10 makes it clear that even after the disruption period is over, no IBC proceedings shall be initiated for the default committed in the disruption period.
- 8 However, whether the default is in nature of an isolated one or continuing one, will always be a matter of fact and may lead to situation where the protection under the proviso to section 10A may not be available to the debtor in the times to come.
- 9 A blanket and ‘forever’ protection would rather actually incentivize a debtor to accelerate default during disruption and avail a permanent escape. This cannot be the intent of the law.
- 10 The default for which protection is sought under Section 10A has to be established. The Debtor seeking protection has to establish that it is not an old continued default but caused due to Covid 19 pandemic.
- 11 The intent of the Ordinance is commendable, however the concerns raised in this article might be points for future litigation. Now it is upon the Courts how they interpret the Ordinance.