

SAMVĀD: PARTNERS

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COVID-19: INSOLVENCY AND BANKRUPTCY CODE (AMENDMENT) ORDINANCE, 2020

The much anticipated Insolvency and Bankruptcy Code (Amendment) Ordinance, 2020 (“**Ordinance**”), was promulgated on June 5, 2020 and came into immediate effect. The Ordinance provides for a limited suspension on the initiation of proceedings under the Insolvency and Bankruptcy Code, 2016 (“**IBC**”), with the aim of giving businesses some breathing room in light of the devastating economic impact of the COVID-19 pandemic. The key features of the Ordinance are set out below:

- The Ordinance introduces Section 10A of the IBC, which provides for a suspension of proceedings under Sections 7, 9 and 10 of the IBC in relation to all defaults that have arisen after March 25, 2020 and for a period of six months thereafter or till a date notified by the Central Government up to a maximum limit of one year (“**Suspension Period**”). The proviso to Section 10A goes a step further to provide that no application for commencing the corporate insolvency resolution process (“**CIRP**”) shall ever be filed for defaults that have arisen during the Suspension Period. The explanation to Section 10A makes it explicit that this protection will not apply to defaults before March 25, 2020.
- The Ordinance also amends Section 66 of the IBC to provide that a resolution professional may not file an application against directors and partners for fraudulent trading with respect to defaults that have arisen during the Suspension Period. Section 66(2) permits the adjudicating authority, on an application from the resolution professional, to direct directors or partners of the corporate debtor to make a contribution to the corporate debtor’s assets if he or she knew that the corporate debtor had no prospect of avoiding commencement of the CIRP and had not exercised due diligence in minimizing the loss to creditors. The Ordinance ensures that such applications cannot be filed for defaults during the Suspension Period.

Key Takeaways:

- The Ordinance does not allow any CIRPs to be initiated for defaults arising during the Suspension Period, including voluntary applications that might be filed under Section 10 by the corporate debtor itself. On the other hand, other types of proceedings and recovery mechanisms outside the IBC, including security enforcement actions and out-of-court restructuring schemes, will continue to be available for defaults that occur during the Suspension Period.
- Interestingly, the Ordinance does not place any bar on initiating IBC proceedings against personal guarantors of corporate debtors that have committed defaults during the Suspension Period.
- The Ordinance will have no effect on defaults that occurred prior to March 25, 2020 and IBC applications with respect to such defaults can continue to be filed in the ordinary course. However, it should be noted that the threshold for defaults was recently increased from Rs. 1 lakh to Rs. 1 crore and any application for CIRP must meet the revised default threshold.
- There is some ambiguity over whether the Ordinance is retrospective or prospective in nature and its effect on CIRP applications that have already been filed for defaults that occurred after March 25, 2020. While the Ordinance does not state it is retrospective, given its intention of reducing the economic distress to businesses caused by the COVID-19 pandemic, it might be interpreted to mean that no applications (including those that have already been filed) may be admitted for defaults that have occurred during the Suspension Period.
- A surprising feature of the Ordinance is the proviso to Section 10A which effectively means that the IBC may never be resorted to for defaults that have occurred during the Suspension Period. The impact of such a permanent prohibition remains to be seen, but it could have a particularly detrimental effect on operational creditors who have often used the possibility of initiating IBC proceedings as a mechanism to instil payment discipline in debtors. Such a prohibition might also lead to creditors tightening the extension of credit during the Suspension Period.

The Ordinance has been much awaited ever since the Finance Minister's announcement in March on the proposed suspension of the IBC. It is

helpful that the Ordinance has been crafted narrowly to apply only to those defaults that occurred after the imposition of the nationwide lockdown as a blanket suspension on initiating CIRPs could have had significant unintended consequences for insolvency resolution. As discussed above, there are some ambiguities and peculiar features of the Ordinance, which it is hoped will be clarified in the days to come.

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