

Bankruptcy Law working in Covid-19

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Abstract

In the light of the current situation under the outbreak of the Corona virus, the world economic equilibrium seems to have not only been disturbed but devastated. Large scale lockdowns have been imposed globally as the infection is said to have been contagious through droplets of saliva or heavy sneezing or coughing. Social distancing is the key requisite for public safety and since people are unable to leave their houses, all hierarchies of occupation seems to have come to a standstill. Prime Minister Narendra Modi brought into effect a nationwide lockdown on March 25th because of which around 70 percent of economic activities like investments, exports, discretionary consumption halted while allowing the rudimentary aspects like agriculture, utility services and the like. Majority of the country's private sectors have reported a steep decline in their operations and profits due to the pandemic. As a response to that, the Indian government deemed necessary to adopt measures to revive to economic normalcy by considering all finance generating sections before the country falls into the pit hole of insolvency and bankruptcy. The Insolvency and Bankruptcy Code introduced in 2016 by our current Prime Minister was voted by the Rajya Sabha to go under certain amendments to benefit the cause. In 3rd world countries, like in the US, the Coronavirus Aid Relief and Economic

Security Act was brought into law, the German and Australian government have brought about changes in their legislation with regard to insolvency laws. The global market is approaching towards a downhill recession and hence, it is mandatory that insolvency laws allow certain levels of pliability that would prevent business that fill a country's economic vault to revive from its unprecedented losses under a life threatening pandemic.

Keywords: situation, economic, corona virus, equilibrium

Introduction

The Narendra Modi govt. introduced the insolvency and Bankruptcy Code in 2016 to resolve claims involving the insolvent companies. It was brought into the scenario to tackle the bad loan problems that were affecting the Banking Sector grievously. According to "Time to resolve Insolvency" World Bank, In the year 2015 insolvency resolution took 4.3 years on an average which is comparatively high enough compared to other countries like United Kingdom taking the least time of 1 year on an average, United States taking 1.5 years, followed by South Africa with 2 years and so on. Hence, such delays were caused due to the time taken by the court in passing its judgement due to the lack of clarity about the current bankruptcy law prevailing. Due to the introduction of Insolvency and Bankruptcy code back in 2016, India achieved the biggest jump from 108th to 52nd rank in "Resolving Insolvency" category^[1].

The Purpose of Introducing the Insolvency and Bankruptcy Code

Previously there were laws dealing with the Bankruptcy and Insolvency Issues like the SARFAESI Act, Sick Industrial (Special Provisions) Act, Provincial Insolvency act etc.

Each of them had their own way of dealing with the issues of insolvency and many a times due to the lack of clarity in such laws they tend to conflict with each other making the process more cumbersome and time taking, Hence the process of discharging an insolvent case was very lengthy which sought the need of Insolvency and Bankruptcy Code

as under this code all the various laws relating to Companies insolvencies and bankruptcies were brought in under one code making it clear and giving it proper clarity for a better understanding of the judges in delivering judgements on cases. The Insolvency and Bankruptcy Code 2016, not only gave clarity to the laws but also gave proper direction in dealing with a case by making it time bound to discharge the case within 180 days and in few cases can be extended for not more than 90 days, so that faster judgements can be passed and cases don't tend to last for years.

Hence, the purpose to introduce the Insolvency and Bankruptcy code can be summarized in two folds:

1. To bring changes in laws relating to insolvency and bankruptcy under the Company Act in order to meet with the modern economic standards.
2. To remove the outdated laws for the insolvency and Bankruptcy in the company act and to ensure that there is a paradigm shift towards aiding the Creditors and to ensure the maximum availability of Credit in market.

Covid-19 impact on Economy

In the year 2019, Coronavirus outbreak was first reported in the city called Wuhan situated in China. Before getting into the impacts created by Coronavirus on the economy globally let us discuss a bit about the Novel Coronavirus.

According to the reports of World Health Organization Coronavirus is a disease affecting the respiratory system of an Human Being and is most likely to have mild to moderate respiratory illness which can be recovered without requiring special treatment, but it has also been said that it is a cause of tension for the old people and the one's who has

underlying medical problems like Cardiovascular disease, diabetes, chronic respiratory disease and Cancer [2]. The Covid-19 virus spreads rapidly through the droplets of Saliva or from the discharge of nose when someone coughs or sneezes. Till date no such vaccine has been approved for such a dangerous virus hence to safeguard oneself from such a disease one should wash their hands after a certain interval with alcohol based hand wash or sanitizers and avoid touching their face as much as possible and most importantly wearing a mask as it not only protects a person from the virus but also reduces the chances of spreading from an infected person.

With the intention of bringing down the spread of such a virus Prime Minister Narendra Modi brought the effect of a complete nationwide lockdown on 25th March that brought around 70% of the Economic Activities, investment, exports and discretionary consumption into standstill except for the essential goods and services such as the agriculture, mining, utility services and some financial, IT and public services which are allowed to operate. The pandemic has brought into more problems for Indian Economy as it hit the economy at such a time when the economy was on the process of recovery after a strong fiscal/monetary measure. According to the research held by the Centrum Institutional Research, it is said the the country again stares at the possibility of low single digit growth for the Financial Year 2021(April 2020 to March 2021). It even included that “Nationwide complete Lockdown is likely to shove off atleast Rs7-8 Trillion [3]”

Normal life as how people knew it has come to a stop as almost the entire country is in total lockdown. Restaurants, Schools, Colleges, offices etc. and almost every establishment has come to a halt due to the pandemic as instructed by the government. To be precise, the government has prevented the workers from working for their livelihood and consumers for spending except for only on essential commodities. The slow down brought down by the government is not only intentional but also unavoidable as it has been brought down by the public health emergency. It is like a putting a hard stop on the production, consumption and investment and these are damaging the economy as the core of every economy is based on these factors. Production of most goods and services are plummeting as the worker are kept out of the work place for the safety of the workers and others. Many service tasks can be done remotely but most production of good requires social proximity which is going to break the Social Distancing. In the short run companies may have inventories the meet up with demands of the people but what about in the long run? Sooner came to a situation where people started hoarding goods back at their homes leaving behind no goods available in market which with time started getting sold at higher price as stocks were getting exhausted. Such a situation is been seen by the people because of the sudden stoppage of the production and supply chain of the goods due to the lockdown or many other reasons bringing down the economic growth. The Coronavirus pandemic is creating a “deep impact” on Indian businesses and has caused an unprecedented collapse of economic activities to the Indian business in the last few weeks, says n industry survey. This survey was jointly conducted by the Ficci and the tax consultancy Dhruva Advisors by looking after responses from 317 companies across all sectors of Indian economy, also said that businesses are falling with “tremendous

uncertainty” about their future [4].

Impact of Covid-19 on business and measures to sustain the business.

According to the business confidence survey made by Ficci,

1. A majority of the participating companies said that the corona virus pandemic has had an adverse impact on their businesses.
2. Around 72% of the respondents to the survey have said that their operations have been impacted due to the pandemic.
3. On addition, 90% of the participants said that their supply chains have been severely impacted due to the pandemic.
4. Many participants felt that they were majorly dependent on imports for their raw material’s supply and are now looking at developing alternate local supplies to meet their requirement.
5. Moreover, with globally supply chains coming to a standstill, participating companies are also focusing more on serving the domestic customers.
6. Companies are trying to be more flexible in their product mix execution.
7. Apart from all this companies are watching their cash flows and liquidity closely and are undertaking required steps to cut costs.
8. Big businesses have implemented heir existing contingency and business continuity plan. Others are carrying out forecasts to implement future course of actions in maintaining inventory.
9. Respondents were hopeful about the future and were of the view that the impact of Covid-19 would significantly lower over next 12 months.

Indian Insolvency Law responds to the Covid-19 Pandemic.

With more than thirty-five lakh confirmed cases and three lakh deaths across 190 countries, the coronavirus pandemic has created an unprecedented damage to the economic activities from which India couldn’t remain untouched. The pandemic has forced the governments to impose restrictions on working and travelling conditions as well as human movement too.

For such a crucial moment the government needs to look after all the section of the economy taking quick and decisive actions for the prevention of deep impact to the economy. This is when the Rajya Sabha brought down certain new amendments in The Insolvency and Bankruptcy Code by voice vote which was approved by Lok Sabha on march 6th 2020 to benefit the businesses from getting insolvent or bankrupt due to the pandemic.

Changes brought in the Code

1. The increase in minimum default:

The 1st amendment brought in the Insolvency and Bankruptcy code was dated on 24.03.2020, according to this notification it revised the amount for initiating a corporate insolvency procedure from One Lakh to One Crore [5], however the amount for the non-corporate firm still remains the same i.e. One Thousand. Such a notification to the code was brought in for the companies to focus on stabilizing the the business operations without having the constant fear of getting insolvent. This amendment may even shift the burden of payment from the Corporate Debtors to Personal

Guarantors but however would play a sigh of relief for the MSME's. Due to the introduction of the amendment the no. of applications filled by the creditors would be substantially reduced due to the rise in amount of default.

Illustration 1: ABC Pvt. Ltd., has committed default of Rs.2 Crore from Bank A. Can A file an application?

Answer: Yes, as per Section 4 of IBC, minimum threshold of Rs.1Cr satisfies. Hence A can file an application against ABC Pvt. Ltd.

Illustration 2: In above situation, can B (A Financial Creditor) having o/s of Rs.10 lakh (not defaulted) file an application?

Answer: Yes, as per Section 7(1) of IBC, a FC can file claim for default of any financial debt. Also appreciated by insolvency Reforms Committee- "The default can be to any financial creditor to the entity and not restricted to the creditor who triggers the IRP..."

Illustration 3: ABC Pvt. Ltd., has committed default of Rs.50 Lakhs of Bank A and of Rs.75 Lakhs of all other FC's- Can A file application?

Answer: As per Section 7, a FC can file an application on grounds of aggregated financial debt(defaulted). Thus, total defaulted amounts sums to Rs.1.25. Cr. Hence A, can file an application.

Illustration 4: ABC Pvt. Ltd. Has committed default of Rs.50 lakhs. There are other FC's of Rs.75 lakhs of which Rs.45 lakhs is defaulted -Can A file application?

Answer: No, as per Section 7, a FC can file application on grounds of aggregated financial debt. (defaulted). Thus, total defaulted financial debt in this case is Rs.50L+45L=95L. Hence, threshold u/s 4 of IBC not satisfied. A cannot file an application.

Illustration 5: ABC Pvt. Ltd. Has committed default of Rs.50 lakhs of Bank A. There are other FC's of Rs.40L. ABC has also defaulted OC's- Rs.60 L. -Can A file an application?

Answer: No, as per FC can file application on grounds of aggregated financial debt. Only- not operational. Thus total defaulted amount is Rs.50+40=Rs.90L. Hence, threshold under section 4 not satisfied for which A cannot file for an application.

Illustration 6: ABC has also some Operational Creditors Viz. M, N and O to the tune of Rs.20L,1.5Cr, and Rs.85L.

a. Who can file application in individual capacity?

Answer: Only N meets the minimum threshold of Rs.1Cr. Hence, only N can file an individual application and not M and O.

b. Can there be an application for combined debt?

Answer: The code does not provide for combined application being filed by operational creditors. Hence, even though the total operational debt exceeds Rs.1Crore,

application cannot be filed towards cumulative Operation Debt.

Illustration 7: ABC also has total salaries outstanding to the tune of Rs.5Crores-However, the dues of no individual employee exceeds Rs.1Crore. Can an employee file an application?

Answer: Employees fall under the definition of "Operational Creditors", which makes them qualified to file an application under this code. In the above scenario, no such employee has an outstanding amount amount of Rs.1 Crore as mentioned hence an employee alone cannot file for an application but as ABC has a total amount of Rs.5Cr debt there is still an option to file a combined application by all the employees through a representative.

The same is going on in certain cases right now and has also been clarified by the hon'ble NCLAT in the case of Mr. Suresh Narayan Singh Vs. Tayo Rolls Ltd. Co. appeal (AT)(insolvency) No. 112 of 2018 ^[6].

Applicability of the amendment to existing cases

So it is clear that with the changes brought down on 24th March 2020, any application filed under this code for initiation of insolvency will have to have a minimum default amount of Rs.1 Crore or more, but what about the existing cases which already have been filed? So we can draw three scenario in existing cases-

- a. Where Demand Notice is served but application is not filed: This case is only applicable to the Operational Creditor. So considering the previous threshold the minimum amount was Rs.1 lakh, hence if an Operational Creditor who has served a Demand notice on the basis of previous threshold would not be accepted if the default amount still remains below Rs.1Crore. The Demand notice has to be revised and can only be filed if the default amount suffices the minimum threshold i.e. Rs.1 Crore.
 - b. Where the application has already been filed but the admission still remains pending: In this case a rectification window may be given to the applicant to meet with the revised threshold. Anyway there is no such formal clarity with respect to the same, it has been inferred as similar rectification window was given in case of revision of threshold under IBC (Amendment) Bill, 2020 for application by Real-Estate Creditors ^[7].
 - c. Applications which have been admitted: So the applications which have already been admitted remains unaffected because the amendment is not on retrospective basis and hence the applications which are once admitted cannot be withdrawn.
2. Relaxation in timelines under Corporate Insolvency Resolution Process (CIRP): The next amendment to The Insolvency and Bankruptcy Code was brought under notification dated 29.03.2020, this notification amended the regulation and inserted regulation 40(C). This amendment provides relaxation for the initiation of Corporate Insolvency Resolution Process by not including the total lockdown period for purpose of calculating timelines under the CIRP regulations. So suppose there is a matter which has been admitted into insolvency filed two days prior to lockdown and as we are all aware public announcement has to be done within three days of commencement of insolvency,

hence the Insolvency Professional has to submit the reports on the first day of opening after the lockdown. Hence the period of lockdown will be excluded for the purpose of considering time line under the court but this does not mean that the overall time limit under this code will also stand increased, this has been clarified by IBBI through the press release that although the timeline for a particular individual activity has been relaxed the overall limit be subjected to 180 days [8].

3. The 3rd Amendment in the Insolvency and Bankruptcy Law was through an Ordinance. Amendments to the Insolvency and Bankruptcy Code would help the banks to restructure loans. According to sources it is stated that the Union Cabinet decided to amend the Insolvency law by suspending three sections of IBC for a year [9]. Section 7,9 and 10 of the Insolvency and Bankruptcy Code remains to be suspended for a period of six months and can be extended up to one year depending on the Economic situation going forward. As per existing norms, if there is a default in payment beyond 90 days then the lender concerned has to refer the account for the process of resolution under IBC or other mechanism permitted under the Reserve Bank of India (RBI). Presently under the norms of RBI, it prohibits restructuring of loans and hence resolution has to be done under IBC. The step by the government would be

a relief to the business organizations during such a Pandemic.

4. The Insolvency and Bankruptcy Code (Amendment) Act, 2020 notified on March 13, 2020 by the Ministry of Law & Justice by way of an amendment way of an amendment with retrospective effect from December 28,2019 due to prior Ordinance), vide amending sections 5(15) of IBC, authorized the government to notify any debt as interim finance, which means that such loans are considered to be the priority loans for the purpose of repayment. Due to the global pandemic of Covid-19 various banks have already extended emergency credit lines to ease the liquidity crisis of the borrowers. Once the lockdown is removed and businesses starts its processes and if the defaulters fail to pay the amount the emergency credit then the banks may face immense liquidation crisis. In order to keep the banks working the government should consider exercising its power under Section 5(15) of IBC and thereby notifying these emergency credit lines as interim finance preventing the unnecessary defaults in repayment of emergency credit [10].

The summary of changes in Insolvency and Bankruptcy are listed below with a help of a table, this amendment are made by government as a step towards tackling the Pandemic.

Summary of Timeline: -

Numberin #	Particular	Definition	Timeline	Relaxation provided (Yes/No)
1.	Section 16(1)	Public Announcement for intention to start Corporate insolvency resolution process	T + 3	Yes
2.	Section 12 & Reg 40	CIRP period extension	T+180 (+90)<330	No
3.	Section 15(2)(C)/ Reg(2)(C) & Section 12(1)	Submission of Claims	T + 14(allowed till T + 90 by the virtue of Reg 12 (2)	Yes
4.	Reg 13(1)	Verification of Claims	T + 21	Yes
5.	Section 21 (6A)(B)/Reg eg 16 A	Application for Appointment of AR	T + 23	Yes
6.	Reg 17(1)	Report verifying Committee of Creditor(COC)	T + 23	Yes

Fig 1

7.	Reg 22(1)	1 st meeting of COC	T + 30	Yes
8.	Reg 36(A)	Submission of proof of claim in respect to liquidation under IBC(FORM G)	T + 75	Yes
9.	Reg 36(B)	Evaluation of member	T + 105	Yes
10.	Reg 39(4)	Submission of COC (approved Plan)	T + 105	Yes

Fig 2

Changes brought in bankruptcy law around the globe

To fight the Covid-19 pandemic several governments have brought changes to its working Insolvency Law's for the development of the economy which have been significantly affected due to the crisis posed by the Covid-19 pandemic ^[11].

In Italy, to resolve the effects caused due to the pandemic emergency on Italian enterprises, the Italian Government has taken a series of measures, providing for derogations from usual procedures. Law Decree 23 of April 8 2020 (Decreto Liquidità) has provided several measures concerning – inter alia – the insolvency of companies.

In United States, the government has not implemented any such direct changes to the insolvency laws. However, on March 27, 2020, the Coronavirus Aid Relief and Economic Security (CARES) Act was brought into the law. The CARES Act includes US \$2 trillion stimulus package which is the biggest economic stimulus in recent US history. Such an Act would not only help businesses affected by the public health and economic crisis with additional financing options to minimize the risks but also would also provide protection to American families, workers etc.

In Germany, the government has brought number of changes to the Insolvency and related laws due to the effect of Covid-19 which includes suspension to file for a bankruptcy.

In Australia, the government has enacted new legislation that significantly brings a change to the current insolvency laws due to the effect of Covid-19. The Australian Government has brought The Coronavirus Economic Response Package Omnibus Act 2020 (Response Act) on March 25 2020, to provide a temporary relief to companies experiencing Financial Distress as a result of ongoing rapidly changing economic slowdown caused due to the Covid-19. The amendments brought in the Response Act are temporary and will only be valid for 6 months i.e. till September 23, 2020.

In Belgium, the government has introduced a moratorium on Insolvency proceedings which would benefit all businesses who are affected due to the effect of Covid-19 and even in such cases where the businesses are not in a state of cessation of payments on March 18, 2020. Such a moratorium came into force on April 24, 2020 and would expire on June 17, 2020.

Switzerland and Spain have temporarily suspended insolvent trading norms which means that the Director can wish to continue the business of the company even though it is indebt due to Covid-19. Germany has even proposed for a similar relaxation which are expected to be put in place shortly. However, while continuing the business if the director seeks to incur further debt without a careful plan to revive the business once the restriction is eased out will not protect the directors ^[12].

Conclusion

Such an unprecedented event has pushed the global economy into recession which means that instead of growing the economy has started shrinking. Due to such a pandemic millions of people have been filing for unemployment benefits. As per the Reuters report, since March 21, more than 36 million have filed for unemployment benefits which is almost a quarter of the working age population. In India, Financial Minister Nirmala Sitharaman has announced some of the details of

the Atmanirbhar Bharat Abhiyan package to provide relief to all medium, small and Micro Enterprises (MSME's) in the form of an increase in credit guarantees. Many advanced economies have rolled out support packages, while India's economic stimulus package is 10 percent of its GDP, Japan's is 21.1 percent, followed by the US which is 13 percent, then Sweden that is 12 percent, Germany (10.7 percent), France (9.3 percent), Spain (7.3 percent) and Italy which is 5.7 percent ^[13]. The changes introduced in Insolvency Law's by the government due time are much needed and beneficial to the businesses affected due to the Pandemic as it would provide relaxation for the businesses who have incurred heavy losses due to the closure of business activity and would help them sustain their business from getting insolvent. While such changes brought in so far are welcomed, few more aspects can be considered for an holistic approach to the crisis.

1. Priority Financing: Section 5(15) of the IBC was recently amended by the government of India to provide an ability to identify certain debts of a company which may qualify as 'Super-priority' loans in the insolvency of the company. The government recently initiated such a right to identify debts raised from the Special Window for affordable and middle-income Housing investment Fund to be "Super-priority" loan. According to some news reports few banks are offering Covid-19 affected borrowers an emergency line of credit to tide over the crisis ^[14].
2. Ongoing restructuring: There have been many cases considered for restructuring under the guidelines of Reserve Bank of India dated 7th June 2019 and Creditors have signed inter-creditor agreements to agree on the restructuring terms. The guidelines contemplate implementation of the restructuring within 180 days. Therefore, the Indian government may need to consider whether extensions are needed for cases where a restructuring has been agreed upon and is pending implementation. The guidelines also require rating of the company's debts before restructuring.

Hence, during such an unprecedented and tough times for business the insolvency regime needs to show flexibility to take into account such factors to sustain the losses incurred due to the pandemic.

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