BAR ON PHOENIX ARRANGEMENTS: AN ANALYSIS OF LAYERS OF INELIGIBILITY UNDER SECTION 29A

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ABSTRACT

When the Insolvency & Bankruptcy Code, 2016, came out three years ago, it brought with it a promise of an efficient, modern means for lenders of Corporate Debtors to realize the amount owed to them. At the same time, it offered an alternative to liquidation. However, while the Code seemed impressive on paper when it came to its application, the realization set in that there were countless questions to be answered through judicial interpretation. And ever since then, the lenders, corporate debtors, promoters, and all other concerned parties have been involved in back-to-back litigation. Where questions of interpretation can be expected to follow the introduction of any new legislation, one must wonder whether the implementation of the Code could have been done in a better way or whether its drafters could have given its provisions more clarity. Is the Insolvency & Bankruptcy Code, 2016 effective in meeting its objectives as it has been made to appear? After giving a brief overview of the history of the Code, this paper dwells into the issue of phoenixing under Section 29A and the layers of ineligibilities it has introduced. The paper throws light on the scope and nature of Section 29A and the bidding paradox present in the system. This is followed by an assessment of the overall impact of the Code as per the currently available data and a concluding note.

Keywords: IBC, 29A, Ineligibility, Bidding, Morality, Phoenixing, Relevant time, BLRC

INTRODUCTION

According to the BLRC report[1], there are two kinds of failure: financial failure and business failure. Financial failure pertains to a situation where there exists a mismatch between payments and receipts in the books of accounts with revenue still being generated. In business failure, the business plan fails. There is no revenue income, and the debts are heavy. It is through business failures that the resources are shuffled and reallocated in the economy. This whole phenomenon is called the market process of creative destruction. Financial failure, on the other hand, can be dealt with if given a fair chance. The IBC aims at doing exactly that. *"IBC is not intended to be a substitute to a recovery forum."*[2] One of the Code's objectives is "to promote entrepreneurship and balance the interests of all the stakeholders."

To fully appreciate the benefits and the shortcomings of the Insolvency and Bankruptcy Code, 2016, an analysis must be made to develop bankruptcy and insolvency laws in India. Prior to 1985, the only law to deal with corporate insolvency and bankruptcy was the Companies Act, 1956. Individual bankruptcy came under the ambit of two pre-Independence laws, namely, the Presidency Towns Insolvency Act, 1909, which pertained to individuals residing in Calcutta, Bombay, and Madras, and the Provisional Insolvency Act, 1920, which covered individuals residing elsewhere. While the Companies Act, 1956 covered the resolution process, it was only a half measure. *"The legislation failed to provide a framework for the dissolution process, and these official liquidators were not equipped with adequate knowledge of the company's operations or knowledge of how to handle corporate insolvencies."*[3]

The Supreme Court in *Excel Ware v. Union of India*[4] had declared S. 25 (O) of the Industrial Disputes Act, 1947 as unconstitutional, thus allowing closure of industries running in losses by the employers. As a result, the government had to take on the interim management of these sick industries to balance the interests of the employers and the employees. Therefore, "*instead of giving dissolution as an option to the failing companies, the Sick Industrial Companies Act, 1985 (or SICA) was introduced with an attempt to revive them and keep unemployment in*

[1] Dr T K Vishwanathan, *The report of the Bankruptcy Law Reforms Committee Volume I: Rationale and Design,* DEPT. OF ECONOMIC AFFAIRS (Nov., 2015), https://dea.gov.in/sites/default/files/BLRCReportVol1_04112015.pdf.
[2] Mobilox Innovations Private Limited v. Kirusa Software Private Limited, (2017) 1154 SCC 90.
[3] Ashish Pandey, *The Indian Insolvency and Bankruptcy Bill: Sixty Years in the Making*, 8 (1). IMJ 26, 28 (2016).
[4] Excel Ware v. Union of India, AIR 1979 SC 25.

check."[5] This was followed by the Recovery of Debts Due to Banks and Financial Institutions Act, 1993 (RDDBFI). In 2002, the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act (SARFAESI) were introduced, which provided a medium for the efficient recovery of non-performing assets (NPAs) of banks and financial institutions. "*Neither of the two legislations offer a rehabilitation or dissolution process. There was also confusion about the jurisdictional priority between SARFAESI and RDDBFI as they have parallel jurisdictions."*[6]

With this knowledge of the background of the development of insolvency and bankruptcy laws in India, an analysis can be made of the 2016 Code. For the first time, a proper restructuring and reorganization process was introduced through this Code, along with the existing remedy for the dissolution of a company.

INTRODUCTION OF SECTION 29A

Synergy Dooray Automobiles Ltd was the first case of CIRP filed in NCLT Hyderabad in January 2017. The balance sheet reflected a total debt of Rupees Nine Hundred and Seventy-Two Crore. The main issue of contention was that the promoters tried to escape their way out of the system by buying the stressed loans.[7] The promoters found loophole mechanisms and were back in control of the company. The resolution plan provided a haircut of ninety-four percent to the creditors, and the CoC and the tribunal approved the same. This set a dangerous precedent by way the promoters could easily regain the management of the troubled company and, this time, with a full proof plan in their hands.[8] The government tried to rectify this precedent by introducing the Ordinance of November 2017, which inserted Section 29A into the Code. "The idea was to attract 'clean and credible people' to the resolution process and exclude the culprits." Section 29A laid down certain disqualifications for the bidders, including

[5] Dr Sanjay Solanki, *Sick Industries with special reference to the Board of Industrial and Financial Reconstruction (BIFR) and the Appellate Authority for Industrial and Financial Reconstruction (AAIFR)*, 3 (1). IJLMS (2018).
[6] Nimrit Kang & Nitin Nayar, *The Evolution of Corporate Bankruptcy Law in India, Money & Finance,* RESEARCH GATE (Jan 03, 2004), https://www.researchgate.net/publication/228430659_The_Evolution_of_Corporate_Bankruptcy_Law_in_India.
[7] Veena Mani & Ishan Bakshi, The curious case of Synergies Dooray & its implications on insolvency code | Business Standard News, https://www.business-standard.com/article/companies/flaws-in-the-insolvency-code-117091900999_1.html (last visited Jul 7, 2021).
[8] NCLAT rejects Edelweiss pleas challenging Synergy resolution plan - The Financial Express, https://www.financialexpress.com/industry/nnclat-rejects-edelweiss-pleas-challenging-synergy-resolution-plan/1414408/ (last visited Jul 7, 2021).

defaulting promoters, related persons, etc. The scope of ineligibility is very wide. The amendment was introduced mostly to restrict the moral hazards that existed initially, but it may be prudent to revisit some of the ineligibilities.

The Insolvency and Bankruptcy (Amendment) Act Memorandum added the terms "in concert with" and clarified the net of ineligibilities provided by the provision. The Section is fairly wide and inclusive in nature. It includes everyone acting in concert with any individual/person submitting the plan for approval.

The Statement of Object and Reasons of the First Amendment Bill, 2018 laid down:

"Apprehensions have been raised those persons who have contributed to the defaults of companies or are otherwise disadvantageous, may abuse this situation due to lack of restrictions to take part in the resolution or liquidation process, and regain control of the debtor. This may undercut the processes laid down under the Code as the dishonest person would be seen to be compensated at the cost of the creditor."[9]

Section 29A lays down the following layers of ineligibility:

"i. 29A (a) to (i) lays down that the resolution applicant should not be disqualified under conditions like undischarged insolvent, unwilful defaulter, NPAs, convicted for certain offences punishable with imprisonment, disqualified to act as a director, prohibited by SEBI to trade securities, etc.
ii. the second layer under 29A(j) provides that the connected persons of the resolution applicant should not attract any of the conditions under clauses (a) to (i).
iii. the third layer provides that the related persons of the resolution applicant should not attract any of the conditions under clauses (a) to (i).
iv. the fourth layer provides that the persons acting jointly or in concert with the resolution applicant, or the connected person, or the related person of the connected person of the resolution applicant shall be ineligible if they attract any of the conditions mentioned above."

[9] The Insolvency and Bankruptcy Code (Amendment) Bill, 2017

THE BIDDING PARADOX

Ever since the introduction of the Code, the bidding process has attracted a lot of controversies. There have been major issues like eligibility, amount, and the principles governing them. Initially, there was no bar on promoters bidding for their own companies, which naturally resulted in allegations such as malfeasance, etc. This lack of prohibition also resulted in unscrupulous practices, promoters acquiring the company at dirt-cheap prices, and creditors suffering huge haircuts for no fault of their own. But via subsequent amendments, the IBBI first made changes in the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016[10], *"making it compulsory for the applicant to disclose important details such as identity, past criminal record, identification as a wilful defaulter by any bank, etc."* A proper disclosure mechanism has thus been set up, and there is no blanket bar. Only a defaulting promoter who has not paid their dues in NPA accounts is barred from the process.

In a country like India, where there is no dearth of pending cases and a very rigid timeline, is it really wise to restrict the sources of economic and financial opportunities? There is a vast disparity in income distribution, and only a handful of people have enough resources to make any sort of large investment. Moreover, most businesses in India are run by joint families. Everyone knows everyone, and it becomes very difficult to find an unrelated party. Even if someone comes up with a plan, it cannot be said that it will be better than those disqualified applicants could have offered. Keeping these and many other associated complexities in mind, it is not really feasible to interpret the Section stringently, although many provisions are relaxed when it comes to MSMEs.

Apart from this, there are some other fundamental issues too. Is the RP required to give details to bidders whose bids have been rejected? If yes, to what extent? The reasons may be qualitative as well as quantitative. Moreover, what if a higher bid is submitted after the deadline or after the H-1 bidder is finalized? Even considering the latter bid may seem technically wrong. Still, it has to be kept in mind that the purpose of IBC is reviving the entity, and if that is not possible, recovering as much as possible. The creditors are expected to approach the adjudicator if the highest bid is not accepted, and litigation will be sought if creditors know there is a higher bid out there but were not opted for because of technicalities. After all, at the end of the day, all the creditors care about is money.

[10] Via the notification of November 7th 2017.

The need for and importance of relaxing these ineligibilities and laying down clear answers to these questions can be seen through the cases of the Binani Cements and the Essar Groups. In *Binani Cement*, after the H-1 bidder was finalized, the promoter, backed by Ultratech Cement, offered to pay substantially more. The Supreme Court, without laying down any precedents, allowed the bid to be considered.[11] On the contrary, in the case of Essar Steels, the subsequent higher bid of the promoters was rejected, and the process was continued with the initially finalized H-1 bidder. "The promoters then sought withdrawal of the CIRP proceedings under Section 12A, which the lenders also rejected. These two cases are the epitome of the existing confusion and scope of interpretation." The process is way too much dependent on the sweet will of the courts. No matter how high the subsequent bid is, if it is after the deadline, it has to be disqualified. There cannot really be any other course of action. But then again, the same needs to be held either in the form of an amendment or by the courts as a precedent.
There is one more class of applicants eligible to submit their plans, the employees. At the very first, about two hundred employees of Reid and Taylor formed an association to save their company. The employees have the option to seek the liquidation of the firm as a going concern to save their jobs. Countries like India do not have the concept of participatory management. It will be interesting to see how a group of people who work for the company will manage the same.

SCOPE OF SECTION 29A

Clause (c): The NPA Disqualification

Under clause (c*), "any person or a person acting jointly with such a person who has an account declared and classified as an NPA by the Reserve Bank of India itself is made ineligible to submit a resolution plan."*[12] The clause also covers all the promoters and other persons in management whose account is declared an NPA by the Reserve Bank of India (RBI). This classification should be a minimum of one-year-old, entailing that one year has been lapsed between the classification by the RBI and the commencement of CIRP. The ineligibility can be done away with when the defaulter deposits the overdue amounts and any incurred interest

[11] Binani Industries Ltd. v. Bank of Baroda, 2018 SCC OnLine NCLAT 521.
[12] Section 29A (c)

in relation to the NPAs.

If we take a situation where *"after a successful procurement of a corporate debtor having accounts turned NPAs, the applicant, then, will be in control of or in the management of such accounts, and will be barred to submit a plan in any CIRP for other corporate debtors for being in breach to clause (c). The Section gives a period of three years to the applicant, which starts from the date of acquisition of the corporate debtors with NPAs, until which the effect of the clause will not be applicable on the applicant on any of their future bids."*[13]

Clause (d): Disqualification on account of Criminal Convictions

Suppose the applicant or any of the connected persons have been convicted of an offence involving the imprisonment of two or more years. In that case, they are disqualified under clause (d) of the Section. Some experts were of the opinion that these offences must be in nexus with the ability to bid and execute a plan; otherwise, the conviction should not matter. Subsequently, Schedule XII was added, which lays down more than twenty-five Indian laws covering various social and economic statutes of "money laundering, pollution, taxation, forensic, capital markets, etc. Moreover, suppose anyone is awarded imprisonment for seven years or more. In that case, it will lead to a complete ban on participating in the bidding process irrespective of whether the Schedule covers the impugned offence or not."

Clause (g): Vulnerable Transactions

Clause (g) deals with vulnerable transactions like a "preferential, undervalued, fraudulent, extortionate or other kinds of transactions. Any person or promoter in charge of these transactions or part of the deciding body passing the vulnerable transactions is ineligible under Section 29A."[14]

Clause (h): Guarantor executing guarantee

[13] Major Amendments introduced to the Insolvency and Bankruptcy Code, AZB & Partners, https://www.azbpartners.com/bank/major-amendments-introduced-to-the-insolvency-and-bankruptcy-code/ (last visited Jul 7, 2021).
[14] Vinod Kothari Consultants, Ineligibility criteria u/s 29A of IBC: A net too wide! – Vinod Kothari Consultants, http://vinodkothari.com/2018/02/section29a-ibc-a-net-too-wide/ (last visited Jul 7, 2021).

The ineligibility list also includes the guarantors of the Corporate Debtor. Many creditors prefer having someone signing a guarantee deed for the Corporate Debtor. So when the debtor defaults, such guarantors cannot participate in the bidding process. This ineligibility is only attracted when the guarantee was given in favor of the creditor who applied for the CIRP or is involved in it. In the case of *RBL Bank Ltd. v MBL Infrastructures Ltd.*,[15] NCLT was of the view that this particular ineligibility should be construed restrictively. The Code does not advocate "banning all promoters for merely issuing guarantees." "They should be banned only when the promoters did not pay off the already involved guarantee and are also banned by other clauses of the Section." Therefore, where a guarantee has not been invoked, or the creditor has not demanded the same, it will not act as a barrier to bid.[16]

Clause (j): Connected persons

The connected persons have been divided into three categories under Explanation I of the clause:

"(i) any person who is the promoter or in the management or control of the resolution applicant; or

(ii) any person who shall be the promoter or in management or control of the business of the corporate debtor during the implementation of the resolution plan; or

(iii) the holding company, subsidiary company, associate company or related party of a person referred to in clauses (i) and (ii)."[17]

The concept is nothing new and has been around for a long time in various statutes of SEBI Regulations and Companies Act, 2013. The idea is to discourage the promoters from bidding indirectly when they are explicitly barred.

Scope of the terms 'acting jointly' and 'in concert'

NCLT took up the charge of declaring the eligibility of resolution applicants, but there is still a looming doubt under Section 29A. the phrases 'acting jointly' and 'in concert' have not yet

[15] C.A. (I.B.) No. 270/K.B./2017.

[16] Section 29A of IBC Impact and Recent Developments, https://lakshmisri.com/insights/articles/section-29a-of-ibc-impact-and-recent-developments/ (last visited Jul 7, 2021).

[17] Section 29A Explanation I.

been defined under the Code. The Hon'ble Supreme Court in *Arcelor Mittal v Satish Gupta*[18] did try to decipher the terms by stating "that "acting jointly" means that the substantial thing to be taken under consideration is whether if a certain person got together and were acting jointly in the sense of acting together.[19]" This is similar to criminal jurisprudence, which lays down that the arrangement need not be formal per se. Still, if they are acting together, they will be liable jointly and severally.[20] This sort of interpretation can lead to a potential impact on Joint Venture (JV) Companies. "A JV is a type of business model where two or more persons/companies come together for a specific commercial purpose. The parties share their resources for a mutually agreed objective.[21]" This essentially also involves sharing control on the affairs of an entity.[22] If Section 29A is applied to the JVs, it will render all the companies in a JV ineligible to submit a resolution plan where any companies are ineligible.
If any term is not defined under the Code, it will be defined according to Section 3(37), which provides a list of statutes. The phrase 'in concert' has been given the same meaning as that under Regulation 2(1)(a) of the takeover code (SEBI Substantial Acquisition of Shares and Takeover Regulation 2011) by the Court in the very same case.

The takeover code aims at preventing hostile takeovers of companies and protecting the interest of small shareholders. The Regulation requires that "the acquirer should not act in concert with other companies to gain control over the target company."[23] The term is used under the takeover code to cover the cases where the threshold limit is only met when clubbed together with the voting powers of the person acting in concert. The same was restated in the Achuthan Committee Report of 2010.[24] In the Arcelor Mittal case, the same principles were applied, and the Court reached the conclusion that the ultimate management and control of the companies would be considered, and because it was the same, they were deemed to be acting in concert under Regulation 2(1)(q)(2i). The Bhagwati Committee[25] recommendations led to the grouping

[18] ArcelorMittal India Private Limited v. Satish Kumar Gupta (2019) 2 SCC 1.
[19] *Ibid.*
[20] Thomas Jefferson, LAW IS INTERPRETED BY COURTS TO DETERMINE 1) WHETHER IT IS "CONSTITUTIONAL" 2)WHO IS RIGHT OR WRONG 137.
[21] Jonathan Hughes & Jeff Weiss, Simple Rules for Making Alliances Work, Harvard Business Review, 2007, https://hbr.org/2007/11/simple-rules-for-making-alliances-work (last visited Jul 7, 2021).
[22] Faqir Chand Gualati v. Uppal Agencies Pvt. Ltd. Anr. (2008) 10 SCC 345.
[23] Takeover Code Dissected, Nishith Desai, https://www.nishithdesai.com/fileadmin/user_upload/pdfs/Ma%20Lab/Takeover%20Code%20Dissected.pdf (last visited Jul 7, 2021).
[24] Mr C Achuthan, TAKEOVER REGULATIONS ADVISORY COMMITTEE 139 (2010).
[25] REPORT OF THE RECONVENED COMMITTEE ON SUBSTANTIAL ACQUISITIONS OF SHARES AND TAKEOVERS UNDER THE CHAIRMANSHIP OF JUSTICE P. N. BHAGWATI, https://www.sebi.gov.in/takeover/takeoverreport.pdf (last visited Jul 7, 2021).

of twelve entities together who shall be deemed to act in concert amongst themselves. Although suitable for the SAST Code, this interpretation does not work when it comes to the Code and its recovery-oriented approach. Even the SAST Code makes room for the existence of common objects for deemed acting in concert assumption.[26] This seems to be absent from the I&B Code. Any such interpretation or reading has to be done by keeping in mind the context of the provisions but also the objectives of the statutes. The present construction can defeat the very purpose of recovery and revival by eliminating a large pool of perfectly good applicants irrespective of whether they played any part in the downfall of the company or not. As soon as this happens, it ultimately leads to a reduction in competition amongst the resolution applicants, thus adversely affecting the value and quality of proposals.

DETERMINATION OF RELEVANT TIME UNDER SECTION 29A

NCLT Mumbai, in the case of *Wig Associates Pvt Ltd.*,[27] opined that Section 29A has a prospective application given that it has altered the existing legal rights. The order held: *"It is unfair to change the rules of the game once the game has started."*[28]

This order seems redundant given that Section 30(4) of the Code, which was introduced by the amendment of 2018, provides that all the plans submitted by ineligible applicants under Section 29A before the ordinance of 2017 will have to be submitted again with fresh invitations and will not be approved otherwise. The order was anyway discarded given that the IBBI, a regulatory body, filed the present appeal when it had no locus to do so.

A three-judge bench in the Homebuyers case[29] had held that section 29A is a valid provision and projects larger public good. "*The Section aimed at curbing the then-existing loophole of giving leeway to the management and can be used prospectively as well as in a limited fashion, retrospective. This retrospective application will happen when the plan had been submitted before the 2017 ordinance but had also not been approved.*[30]"

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[26] SEBI | Funds Mobilised and Total Assets- Private, Public & UTI, https://www.sebi.gov.in/satorders/hitachi.html (last visited Jul 7, 2021).
[27] Insolvency and Bankruptcy Board of India v. Wig Associates, Company Appeal (A.T.) (Insolvency) No. 415 of 2018. (N.C.L.A.T).
[28] Wig Associates Pvt. Ltd. - NCLT Mumbai Bench - IBC Laws, https://ibclaw.in/wig-associates-pvt-ltd-nclt-mumbai-bench/ (last visited Jul 7, 2021).
[29] Anuj Jain v Axis Bank Limited. CIVIL APPEAL NOS. 8512-8527 OF 2019.
[30] *Ibid.*

Retrospective application of the law is allowed when it cures a defect that is prima facie evident. This "curing effect" of the law is an exception to the prospective application rule. Therefore, ineligible parties will be excluded whether there is a prospective or retrospective application of Section 29A.

In *RBI v MBL Infrastructure Ltd*[31], the CoC was led to believe that even the non-defaulting promoters of the CD were barred from participating in the resolution plan under Section 29A. On the other hand, the Resolution Professional considered that the promoters are not included under the standard ineligibility of Section 29A. NCLT subsequently allowed the promoters to submit their plans.

In the case of *Standard Chartered Bank v Ruchi Soya Industries Pvt Ltd.*,[32] Adani Wilmar was deemed the most eligible bidder by the CoC, and the resolution plan was almost finalized. Patanjali, the next highest bidder in line, challenged Adani's eligibility under Section 29A. The main contention was "based on the spouse of the MD of Adani Wilmar being the daughter of a defaulting promoter. Adani subsequently withdrew the bid before the issue could be settled.[33]"

THE PHOENIXING ENIGMA

Phoenixing is a commonly referred practice whereby *"the management of a company puts it into resolution or liquidation solely to buy the same business back and set up a new 'phoenix' company in the same or similar business, shorn of the debts of the old company."*[34]

The biggest moral and economical dilemma that crops up is whether the promoter of a debt-ridden company is permitted to buy back the assets or the business itself at a huge discount. This was largely highlighted in the controversial case of Essar Steel. Essar Steel defaulted on its loan repayments and eventually went into insolvency. Having control over the company,

[31] C.A. (I.B.) NO. 270/K.B./2017.
[32] C.P. NO. 1371&1372/N.C.L.T./ M.A.H./2017
[33] *Ibid.*
[34] Pratik Datta, Promoter buy-back in insolvency: 'Phoenixing' in India, Oxford Law Faculty (2017), https://www.law.ox.ac.uk/business-law-blog/blog/2017/12/promoter-buy-back-insolvency-phoenixing-india (last visited Jul 7, 2021).

the Essar Group tried to buy back the business by submitting a resolution plan as an applicant under the Code. Subsequently, the Hon'ble Supreme Court, while piercing the corporate veil, held the Numetal bid ineligible.[35] The entire CIRP for ESIL took eight hundred days. A Code which aimed at wrapping up the process within a year took almost three years because of the shortcomings and

discrepancies it brought along. Ever since the introduction of the Code, the bidding and plan approval process has attracted many controversies. There have been major issues like eligibility, amount, and the principles governing them. There have been inconsistencies within the SC judgments as well. In pursuance of economic efficiency, the literal interpretation of the Code was side-lined when Article 142 was invoked to allow the applicants to pay off their debts first, in the ArcelorMittal case. Moreover, the issue of the H-1 bid was also raised in these cases. Honest attempts have been made through various amendments to bridge these gaps, but the process is way too much dependent on the sweet will of the courts at the end of the day. ArcelorMittal took a long journey to get court approval through a lengthy legal battle for acquiring Essar Steel for Rs 42,000 crore.

THE MORALITY ARGUMENT BEHIND SECTION 29A

Law and morality often go hand in hand. But John Austin and other scholars raised serious concerns about the same and even said that law and morality have nothing to do with each other.[36] Insolvency law is supposed to be an empty vessel according to the normative theory where all the economic and social goals are the problem of other laws.[37] Yet, the validity of any piece of legislation is heavily derived from its conformity with moral perceptions of the community.[38]

In *Lac Minerals Ltd. v. International Corona Resources Ltd.*,[39] it was observed that "It is simply not the case that trade and accepted morality are mutually exclusive spheres."[40] A

[35] Civil Appeal Nos.9402 – 9405 /2018.
[36] William C Starr, Law and Morality in H.L.A. Hart's Legal Philosophy, 67 19.
[37] G Eric Brunstad et al., The Three Faces of Bankruptcy Law 408.
[38] Andrei Marmor & Alexander Sarch, The Nature of Law, in The Stanford Encyclopedia of Philosophy (Edward N. Zalta ed., Fall 2019 ed. 2019), https://plato.stanford.edu/archives/fall2019/entries/lawphil-nature/ (last visited Jul 7, 2021).
[39] Lac Minerals Ltd. v. International Corona Resources Ltd., [1989] 2 S.C.R. 574
[40] Supreme Court of Canada, Supreme Court of Canada - SCC Case Information - Search (2001), https://scc-csc.lexum.com/scc-csc/scc-csc/en/item/516/index.do (last visited Jul 7, 2021).

similar stance was taken in the case of *Standard Investments Ltd. v. Canadian Imperial Bank of Commerce*,[41] where the bank was held liable for a "breach of the high standard of moral conduct towards its customers when it exhibited favoritism towards one customer over the other." In the case of *Harry v Kreutziger*[42], an Indian fisherman was permitted to rescind the contract where he was tricked into transferring his license and boat to another fisherman for one-third of the actual value because he did not understand the repercussions of the contract. The continued struggle of legal certainty versus moral standards has been attempted to be balanced in Section 29A. Preservation of public interest by curbing fraud and malpractices introduces commercial morality to the Code itself. Whenever a company cannot pay off its debts and goes insolvent, the creditors and other stakeholders in the society also suffer with them, and it becomes of utmost importance that minimum possible damage is done. Section 29A, through its barring provisions, has installed a check post ensuring that dishonest promoters do not buy back the business at deeply discounted rates. But at the same time, the Section has put the same barrier for honest, hard-working promoters who invest their best years and money in the business. Therefore, how far is this blanket ban justified?

Keeping aside the moral percept argument, such an exclusion not only hampers the chances of a successful recovery of the business but also affects the economy as a whole. Hundreds of workers and employees and the competition in the market by excluding any lucrative bud from the promoters suffer heavily. Some businesses genuinely fail or never even take off, and the promoters are bombarded with suspicion even though they might not have contributed to the NPAs. But the Code does not seem to shake off the notion that "the person who created insolvency pays a small percentage of the sum and returns into management." The distinction between malfeasance and business failure was also highlighted in the BLRC Report, where business failures are to be seen as something very legitimate and normal in any economy and cannot be presumed to be an act of malfeasance without further evidence like wrongdoing or absence of trust between creditors and promoters. Further, if doubt and hesitation is surrounding a promoter's bid, other options can be availed. Still, if they are not feasible or sound enough, it does not make any sense to reject the former plans merely on suspicions or a blanket bar.

[41] Standard Investments Ltd et Al v Canadian Imperial Bank of Commerce 22 DLR 4th 410
[42] (1979), 95 D.L.R. (3d) 231

In *Bishopsgate Investment Management Ltd v Maxwell*[43], the Court held that it is in the best interest of the society that insolvent companies get a fresh start, and the people involved should not be treated harshly unless they have acted dishonestly or with malafide intent. Therefore, if the morality argument weeds out dishonest promoters and officers in default, it should also encourage honest promoters to bid and not subject them to the same treatment as culprit promoters.

CORPORATE RESPONSE TO IBC

The Code turned heads from the moment it was introduced. The response from the legal fraternity has been enormous. Some are all praises for this bold attempt, while some even challenged its constitutionality. According to the RBI report,[44] *"1,953 cases went to bankruptcy courts involving Rupees 2.32 trillion, of which Rupees 1.05 trillion was recovered during the fiscal year 2020. Recovery from insolvency and bankruptcy (IBC) cases stood at 24% as of March, which does not include the top nine cases referred by the RBI.[45]"* According to Macquarie, the recovery rate of the top nine cases was around fifty-six percent.

The long-term impact of the IBC is yet to be seen. However, certain indicators may be considered to measure the impact up till now. The pandemic has certainly interfered with the recovery rate; it becomes pertinent to understand the data pattern before the pandemic hit.

SHIFT IN ATTITUDE

The IBC has been responsible for promoting responsible corporate behavior on the part of promoters and the management of companies. Perhaps the most significant reason for this is that the Code has created the very real threat of losing control of the company. Such a threat has forced a substantial number of corporate debtors to pay off their debt prior to the initiation of insolvency proceedings.

As of February 2019, 6079 cases involving a total amount of Rs. 2.84 lakh crores have been

[43] [1992] 2 All ER 856 at 871
[44] Reserve Bank of India - RBI Bulletin, https://www.rbi.org.in/Scripts/BS_ViewBulletin.aspx?Id=20203 (last visited Jul 7, 2021).
[45] *Ibid.*

withdrawn before admission under the IBC. Also, according to the RBI, Rs. banks have received 50,000 crores from previously non-performing assets. Further, another Rs. 50,000 crores have been converted from non-standard to standard assets. All this is indicative of a major behavioral shift. S. 12A of the Code allows companies to withdraw CIRP proceedings with the consent of 90% of the financial creditors. It was held that the withdrawal of CIRP u/s 12A read with Reg 30A (withdrawal not to be allowed after inviting EoI) is only directory depending upon the facts[46] , which clears even more roads for withdrawal. Since the incorporation of Section 12A via amendment in 2018, almost 5% of admitted cases, 91 to be precise, have been withdrawn. This must-have followed an acceptable resolution by the corporate borrower in each case.[47]

In February 2018, the RBI issued an unpopular circular[48] on stressed assets. The circular provided that defaulting companies would be referred under the Code from the first day of the default. As much as this step aimed at bringing discipline to our country's lending and borrowing culture, it also put at risk a large number of people losing their companies. The Supreme Court quashed the same, declaring it ultra vires S. 35AA of the Banking Regulation Act.[49] This may seem like a procedural judgment, but it can prove to have farfetched impacts. For instance, where do those twelve defaulter companies stand, which were announced by the RBI on June 13th, 2017? We do not have these answers. But would it not have been better than this taken for granted system of borrowing huge amounts (s) of money, running a business, and being exonerated on account of being bankrupt be thrown out of the picture even if it is at the cost of a few genuine but incompetent business owners who cannot pay their debts timely? If the creditors want, they can still opt for it. The discretion lies in their hand as to when to call for CIRP and is purely voluntary as decided by the Apex Court when it quashed as the order of the NCLAT, which appeared to be threatening the appellant to initiate the CIRP.[50]

INCREASE IN RESOLUTION OF STRESSED ASSETS

The NCLT admitted the first case under the IBC on January 17, 2017, just a month after the

[46] Brilliant Alloys Private limited vs Mr. S. Rajagopal & Ors., Special Leave to Appeal (C) No(s). 31557/2018.
[47] IBBI, *Monetary Management and Financial Intermediation*, IICA (March 2019), https://iica.nic.in/images/echap03_vol2.pdf.
[48] DBR.No.BP.BC.101/21.04.048/2017-18 dated February 12, 2018.
[49] Dharani Sugars and Chemicals Ltd v. Union of India, (2019) 5 SCC 480.
[50] Transmission Corporation of Andhra Pradesh Limited v. Equipment Conductors and Cables Limited, 2018 SCC OnLine SC 2113.

Code was operational. The first resolution plan was approved in August, the same year. Within 27 months of operationalization, i.e., by February 2019, 14,000 applications had been filed for initiation of CIRPs, and as of March 31, 2019, the NCLT had ordered the commencement of CIRP of 1,858 Corporate Debtors (CDs).[51] According to data by the Insolvency & Bankruptcy Board of India (IBBI), 152 of the total cases admitted were closed on appeal, review, or settlement. Ninety-one cases were withdrawn as a result of settlement under S. 12A of the Code. Ninety-four cases yielded resolution, whereas 378 wound up in liquidation.

The IBC has exhibited a much better recovery rate than the other mediums for debt recovery. According to CRISIL, a rating agency, "*the recovery rate under the IBC for the 94 cases resolved through IBC by fiscal 2019 is 43%, compared with 26.5% through earlier mechanisms.*"[52] According to the RBI[53], "*a total recovery of Rs. Seventy thousand crores were made through the IBC in fiscal 2019.*[54]"

While the IBC should ideally be oriented towards the revival of the stressed asset, a majority of the cases admitted have resulted in liquidation. On the one hand, the Code is not an alternative means of liquidation of stressed assets. On the other hand, one of its objectives has also been to allow companies to be liquidated swiftly to maximize value if resolutions cannot be reached.

CONCLUSION

The Code crossed its three-year mark in June 2019 and has had its hits and misses. India passed premature legislation, which is still developing through judicial pronouncements and leapfrogged its way into solvency laws. "*The Code brought in a creditor-in-control regime, a time-bound resolution process and reduced scope for judicial intervention*[55]," which did not

[51] IBBI, *Monetary Management and Financial Intermediation*, IICA (March 2019), https://iica.nic.in/images/echap03_vol2.pdf.
[52] *In three years of IBC, more hits than misses*, CRISIL (May 14, 2019), https://www.crisil.com/en/home/newsroom/press-releases/2019/05/in-three-years-of-ibc-more-hits-than-misses.html.
[53] *Reserve Bank of India's report on Trend and Progress of Banking in India,* RBI (June 30, 2018), https://rbidocs.rbi.org.in/rdocs/Publications/PDFs/0RTP2018_FE9E97E7AF7024A4B94321734CD76DD4F.PDF.
[54] *Ibid.*
[55] UNDERSTANDING THE INSOLVENCY AND BANKRUPTCY CODE, 2016 ANALYSING DEVELOPMENTS IN JURISPRUDENCE (Vidhi Centre for Legal Policy, IBBI 2019).

work out so well. Economic legislation cannot be expected to have zero judicial interference. It develops and continues to develop via precedents. "Time is of the essence under the Code, which requires the NCLT and all stakeholders to act under extreme pressure of an insufficient deadline.[56]"

Thus, it is not always the fault of the promoters who might have been honest throughout the company's lifetime, and yet it fails. Several other factors contribute heavily to a company falling on its feet. The onus comes on the promoters to rectify things. They should thus be given a chance to pick up the entity if there were no malafide intentions on their part. Section 29A was introduced to identify these intentions and curtail malafide phoenixing. "But these intentions and factors were not defined as legitimate or illegitimate like done in other jurisdictions of Australia, New Zealand, etc. The two situations, first where a company fails because of the promoters' fault and second where it fails because of the economy, should not be treated at par.[57]" Section 29A as claimed by the legislature, was enacted after considering public interest and morality, but no distinction was made between honest and dishonest promoters. Terms like 'acting jointly' and 'in concert' have only made the pool of bidders small, impacting the aim of value maximization directly. The same was reaffirmed by the Hon'ble Court in *Swiss Ribbons v Union of India,*[58] where it held that "persons who are incompetent of serving their debt are not qualified to act as a resolution applicant.[59]" NCLT, on the other hand, in *RBL Limited v MBL Infrastructures Ltd.*[60], observed that "just because there existed a default in payment by the borrower, it did not imply him to be dishonest and could be allowed to bid.[61]"

The three essentials of a sound market are the freedom to start, continue and discontinue the business. Therefore, a sound and balanced exit system must be developed where the creditors are able to recover their debts with equal relief to promoters in terms of insolvency procedures enabling them to undertake new businesses in the future. Maximization of valuation of assets, the balance between liquidation and reorganization, the equitable treatment of similarly placed lenders, timely and efficient resolution, and transparently modeled resolution process is the need of the hour.

[56] JK Jute Mills Company Ltd. v. M/s Surendra Trading Company, Company Appeal (AT) No. 09 of 2017.
[57] *Ibid.*
[58] Swiss Ribbons & Anr. v. Union of India & Ors., (2019) 4 SCC 17.
[59] *Ibid.*
[60] RBL Limited v. MBL Infrastructures Limited, (2017) SCC OnLine 4323.
[61] *Ibid.*

India occupies the 63rd rank in the Ease of Doing Business Survey[62] conducted by the World Bank. Maximum recovery of NPAs also play a very important role in these rankings. “Section 29A impedes this objective by interfering in the debtor-creditor-friendly setup. The Indian business structure is highly promoter-oriented, and barring them from the resolution process will only push these entities into accepting lower bids.[63]” So many countries where the recovery rates are on the higher side do not have similar ineligibility conditions. The attempt of India to introduce the morality factor in business traditions has hampered the objective of the Code.

It takes years to give these legislations principles which are tested on a case-to-case basis. In this milieu of crony capitalism, the Insolvency Bankruptcy Code sure has come as a sigh of relief. It may not be the best, the advantages may not be absolute, but if we keep the pre-code regime in mind, it is relatively much better. The foundation principles of the present Code are based on the core features that most developed nations share. “IBC proves to be a method of cleaning up the mess of companies that were in serious chaos and will finally end the amount of NPAs in the bank’s books, but doesn’t help the banks get back much money.[64]” The Code has come a long way and survived many challenges. Irrespective of its deficiencies, the Code certainly is here to stay. So, to conclude, our economy is evolving, and so is the IBC.

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[62] Explore Economies, World Bank , https://www.doingbusiness.org/en/data/exploreeconomies (last visited Jul 6, 2021).

[63] Critical Analysis of Section 29A of the Code - IBC Laws, , https://ibclaw.in/critical-analysis-of-section-29a-of-the-code/ (last visited Jul 8, 2021).

[64] Examining the rise of Non-Performing Assets in India, PRSIndia (2018), https://www.prsindia.org/content/examining-rise-non-performing-assets-india (last visited Jul 8, 2021).