

Suspension of Section 7, 9 and 10 of Insolvency and Bankruptcy Code, 2016

Introduction

The COVID-19 outbreak has not only adversely affected human lives but has also hampered the economic growth of all countries throughout the world including India. To combat the effects of the pandemic, the Government of India imposed a nationwide lockdown on March 24, 2020 which restricted the movement of persons as well as goods and services which brought the commerce and businesses in the country to a standstill. Consequently, various companies especially the Micro Small and Medium Enterprises (MSMEs) started facing liquidity crisis and the threat of running out of business. In pursuance to this, a number of measures were adopted by the Government of India

Amongst these, one measure was suspension of section 7, 9 and 10 of the Insolvency and Bankruptcy Code, 2016 (hereinafter referred to as, 'the IB Code'), which provides for initiation of insolvency proceedings by financial creditors, operational creditors and by the corporate debtor himself, respectively. The same was done through an ordinance dated June 05, 2020 which added section 10A to the IB Code. By virtue of this section, the filing of applications for initiation of corporate insolvency resolution proceedings by any financial creditor, operational creditor and corporate debtor were barred in respect of any default arising on or after March 25, 2020 for a period of 6 months. The section further clarified that no such application shall ever be filed for such defaults.



*Suspension of
initiations of
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proceedings
against
debtor under
the IB Code
extended till
December 25,
2020*

Section 10A empowered the Central Government to extend this period of 6 months for a further period, not exceeding 12 months. In exercise of these powers, the Central Government issued a notification dated September 24, 2020, extending this period for further 3 months i.e. till December 25, 2020.

Implications of adding section 10A to the IB Code:



On creditors

The Central Government enacted section 10A with the objective of preventing corporate entities from being forced into insolvency proceedings by financial or operational creditors because of the unprecedented COVID-19 outbreak. Resultantly, the financial creditors under section 7 and operational creditors under section 9, are barred from filing an application for initiation of insolvency proceedings against the corporate entity for any default committed in the stipulated time span.

Another objective behind this suspension was to prevent the corporate entities from going into liquidation as in these unprecedented times, it would have been hard to find prospective resolution applicants for effective resolution of the corporate debtor. The liquidation of the corporate debtor would in turn not have been beneficial for the creditors themselves.

Furthermore, various alternate remedies are still available to the creditors for recovering their debts such as the Securitisation of Assets and Enforcement of Security Interest Act, 2002, Recovery of Debts due to Banks and Financial Institutions Act, 1993, institution of recovery suits under the Code of Civil Procedure, 1908. In addition to these, the creditors also have an option to go for compromise and arrangement under section 230 and 231 of the Companies Act, 2013. Thus, the suspension of filing of application under section 7 and 9 is justified and in turn, beneficial to the creditors.

On corporate debtor

In addition to the creditors, section 10A also bars the initiation of insolvency proceedings by the corporate debtor themselves. Under the IB Code, a distressed corporate debtor is given an opportunity to revive its business with the help of a prospective resolution applicant by filing an application under section 10, however, this opportunity has now been taken away.

Furthermore, in the case of *Excel Wear and Ors. v Union of India*¹, wherein a number of writ petitions were filed by the employers of different organizations contending that laws which impose restrictions on the right to close down the business are unreasonable and arbitrary. It was observed by the Hon'ble Supreme Court that the right to close down a business is covered under the ambit of right to carry on business guaranteed to the citizens under Article 19(1)(g) of the Constitution of India.

Thus, the suspension of the right of corporate debtor to close down its business in turn infringes the fundamental right guaranteed under Article 19(1)(g) of the Constitution of India.

On personal guarantors of the corporate debtor

Under the IB Code, an application can be filed for initiation of insolvency proceedings against the personal guarantors of the corporate debtor under section 95, however, section 10A is



silent on the same. This means that the financial and operational creditors are not barred from initiating insolvency proceedings against the personal guarantors of the corporate debtor, even during the COVID-19 outbreak.

Taking into consideration that the liability of a personal guarantor coincides with the liability of the principal debtor, the creditors still have the option to initiate insolvency proceedings against these personal guarantors, who are mostly the directors and promoters of the corporate debtor, which in turn affects the debtors.

Conclusion

In these unprecedented times, when the economies across the world have come to a halt and the businesses have been incurring huge losses, such a striking move by the Central Government was required to a certain extent.

However, the enactment has received a lot of criticism because of various reasons like the everlasting bar on initiation of insolvency proceedings against a corporate debtor for defaults occurring during the stipulated time, as this can be misused by the debtors; and bar on initiation of insolvency proceedings by the corporate debtor themselves as even when a corporate debtor is unable to pay salaries to its employees or repay its loans, then also the corporate debtor is forced to run the business.

Even though the suspension of section 7 and 9 can be considered to be in the interest of the corporate debtor as well as the creditors because the creditors still have the alternate remedies available to them, but the suspension of section 10 cannot be justified as the debtors do not have any alternate to voluntary initiation of insolvency proceedings against themselves.

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