

COMPARATIVE STUDY OF INSOLVENCY AND BANKRUPTCY CODE OF INDIA AND U.S.A

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ABSTRACT

This paper seeks to comparatively examine the Bankruptcy and Insolvency Legislation of India and the United States of America. The author seeks to give a detailed description of the insolvency procedure of both countries and compare the differences in the procedure of the two countries. The impact of the legislation on the business transactions in the two countries and their inter-relations and cross-border insolvency procedure. the introduction of this paper deals with the history of the development of legislation in India and the United States of America and explains the emergence of the present insolvency laws in India. This study discussed in detail the procedure and criteria for the Resolution Process in India and USA. The author also attempts at pointing out the shortcomings of the legislation and tries to suggest the changes that could be introduced by both countries. The status of both the countries in implementation and effectiveness and what steps can be taken by India and the U.S.A for further improvisation.

Keywords: (IBC), Resolution Professional (RP), Liquidation, Committee of Creditors (CoC), Interim Resolution Professional (IRP).

INTRODUCTION

Insolvency means the inability to pay off the liabilities in due course of business rendering the creditor debt to be mounted. Insolvency is referred to a stage when the liabilities of a person or the company are more than the assets and income. The situation of insolvency arises when liabilities calculated altogether surpass resources available on the whole.

Though more often than not Bankruptcy and Insolvency are used interchangeably in actuality both terms signify different situations. Bankruptcy is a legal procedure carried out at the orders of the Court to recover unpaid debts from the debtor or relieve the debtor from some or all of its liabilities. The procedure of Bankruptcy strives to give relief to the creditors and

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at the same time not to torment the debtor to recover the debt that he is already unable to pay off.

The introduction of the Insolvency and Bankruptcy Code has changed the scenario of Corporate Business transactions. The first ever legislation for dealing with matters of Bankruptcy and insolvency was introduced in the United Kingdom known as the Statute of Bankrupts, 1542. Subsequently, all other nations started adopting Bankruptcy laws considering it the need of the time. India and the U.S.A. being the former colonies of the British derive a substantial part of their legislation from the laws propounded and followed in the United Kingdom. In recent years, significant changes have been introduced by both countries exhibiting the spirit of changing times and free spirit.

INSOLVENCY AND BANKRUPTCY CODE

History

In India, separate Insolvency and Bankruptcy Code was introduced in 2016. Earlier, matters relating to insolvency and bankruptcy were dealt with under the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest (SARFAESI) Act, 2002, Companies Act, 1956, and Sick Industrial Companies (Special Provisions) Act, 1985. The new act of 2016 was introduced with the motive to overcome the shortcomings of other pieces of legislation in the Insolvency procedure. In the U.S.A., the first bankruptcy law was introduced in 1800¹ and was repealed afterward in 1803. Subsequently, many insolvency laws were introduced and repealed thereafter. Modern Bankruptcy law was introduced by the Bankruptcy Reform of 1978 and the Chapter 11 of the Code provides with insolvency framework. U.S. Bankruptcy Code of 1978 is also known as **Title 11**. The U.S. Bankruptcy is further divided into six chapters under Title 11. These chapters are 7,9,11,12,13 and 15. The six chapters contain provisions ascertaining the rights of individuals and corporates to file a petition seeking relief. Bankruptcy Abuse Prevention and Consumer Protection Act, 2005 is the most recent amendment made to the 1978 law.

¹ Federal Bankruptcy Act, 1800

INITIATION OF PROCEEDINGS

In India, under the Insolvency and Bankruptcy Code, 2016 initiation of resolution can be taken by Creditor as well as the Debtor². Application for resolution process is made to the National Company Law Tribunal after giving prior 10 days' notice to the debtors, in case the resolution process is initiated by the financial creditors. The condition precedent for Debtors while filing for the resolution³ process is, that they have to file the consent of the Board of Directors. A resolution process can be initiated if the debt amount is more than 1 lakh rupees to 1 crore rupees. The Code suggests two methods: 1) Liquidation and 2) Insolvency Resolution Process. In the Liquidation process, the assets of the debtor are sold out to pay off the liabilities. The Insolvency Resolution Process offers a more rational approach by giving the option to retrieve the business. The financial creditors have the option to assess whether the business of the debtor is retrievable or not. Failure of the Resolution process provides the option of liquidation to cover the losses.

In the U.S.A., the petition can be filed by the debtor company or individuals in the bankruptcy court under chapters 7,9, 11, 12,13, and 15 attesting to the list of creditors, assets, and liabilities of the company. Chapter 7 deals with the liquidation of assets. Under this chapter, a trustee is appointed by the Bankruptcy Court to collect the liable assets to sell and pay the proceed to the creditors. Chapter 11,12 and 13 contains provisions for the reorganization of a business.

PROCEDURE

In India, after filing the resolution, Adjudicating Authority⁴ appoints Interim Resolution Professional (IRP), to start the Corporate Insolvency Resolution Process (CIRP) and management of the corporation lies with the IRP. According to Section 18 of IBC, the responsibilities of the IRP include gathering all the information on the company's assets and liabilities, constituting the Committee of Creditors (CoC), management of finances of the company, and checking creditors' claims against the indebted company. IRP works until the

² Creditor is a person, entity or institution which extends credit to other person, entity or institution with a promise of repayment of the credit. Whereas, a debtor is an entity, institution or person who receive credit and is obliged to repay the credited amount.

³ a detailed planned structure to resolve the issue of debtor entity to pay off the debts

⁴ According to Section 5 (1) of IBC, it means National Company Law Tribunal (India Code); see here:

https://www.indiacode.nic.in/show-data?actid=AC_CEN_2_11_00055_201631_1517807328273§ionId=784§ionno=5&orderno=5
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Resolution Professional is appointed and with the voting of the Committee of Creditors, even IRP can become the Resolution Professional (RP). IRP's role is temporary and he deals with the matter till the Resolution Professional is appointed.

Chapter 11 of the U.S. Bankruptcy Code lays down the procedure for the reconstruction of the debtor's assets. This provision is open to corporations, partnership firms, and even individuals, but in most cases, corporations and partnership firms go with this method. Under the provisions of this chapter, the management of the company continues in a normal phase and the debtor retains the possession of the indebted company and most of the assets. This approach is known as **Debtor in Possession**. This approach is followed in the U.S.A. because the management of the indebted company becomes very complex when an outsider is given the authority to look after it. Newcomer has their own ups and downs in learning and understanding and that will affect the normal course of management of the company. Moreover, if the power is given to an outsider, it will affect the confidence of people associated with the company, and reviving the indebted corporation becomes difficult in such situations.

The debtor according to the U.S.A code, can substantively sell the assets of the company to recover from the debt, but in India, since the management is looked after by IRP and RP, only they can sell the assets with permission from the Committee of Creditors.

TIME PERIOD FOR INSOLVENCY PROCESS

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According to Section 12 of the Insolvency and Bankruptcy Code, 2016, after filing the application with NCLT, the insolvency process shall be completed within 180 days. During the period of 180 days, proposals will be made to the NCLT for the revitalization. The debtor has 330 days to file the resolution plan. The Resolution Professional shall file an application for extending the period for the insolvency process beyond 180 days, provided that the instruction was given by a resolution passed in the meeting of the Committee of Creditors by a vote of 66 percent of the voting shares. Under Clause (b) of Section 1121 of Chapter 11 of the U.S. Code, the Debtor has 120 days to file the resolution plan. The time period may be extended up to 18 months by the orders of the Court but in no circumstances, it can be extended beyond 18 months.

Moratorium: Section 14 of the IBC states the power of Adjudicating Authority to declare a moratorium. After the commencement of the insolvency procedure, it is prohibited to institute

suit against the corporate debtor, and recover assets, security, or any property for the time being. In the U.S.A, after filing the application in Bankruptcy Court, the Corporate Debtor gets immunity by the moratorium.

Management: Section 16(1) of the IBC states that the Adjudicating Authority on the date of commencement of Insolvency shall appoint an Interim Resolution Professional. The interim Resolution professional will be responsible for the business of the Corporate Debtor. Accountants, officers, managers, and other officials of the debtor shall report to the Interim Resolution Professional and provide every document and report as required by the IRP. The Board of Directors or the partners of the corporate director and all the powers vested in them shall be ceased. As per the provision of Section 17(2), the IRP shall have the authority to act on behalf of the Corporate Debtor and performs an act as specified by the Board, and shall have access to all the records of the company. Section 18 specifies the duties of the IRP.

According to U.S. Bankruptcy Code, the Debtor remains in Possession of the corporation and is entitled to perform all the functions except the investigative functions and duties performed by the Trustee. The Court has the power to appoint a Bankruptcy Trustee to deal with the Debtor's estate and cater to the demands of the debtor. The trustee cannot act without the permission of the Court. The duties and role of the trustee differ from case to case. In cases underlying Chapter 7, the trustee has the power to manage the nonexempt property of the debtor and distribute the proceeds to the creditors. The Debtor in Possession is also required to report to the Trustee in matters of the monthly income distribution, expenses, opening up of new bank accounts, and tax payments. In case, the Debtor in Possession fails to comply with the reporting requirements, the Trustee can take action against him and also a plea to the court to dismiss the case.

Committee of Creditors

In India, the Committee of Creditors consists of Financial Creditors⁵. In absence of Financial Creditors, the Operational creditors and one representative from workmen and employees can form the Committee of Creditors. The logic behind giving Financial Creditors preference to form CoC is that the debts and finances made by the Financial Creditors are huge in amount as compared to Operational Creditors. In presence of Financial Creditors, the operational Creditors will only get a place in the Committee of Creditors if the amount of unrecovered

⁵ Creditors who have financed the Corporate Debtor against the time value of money.

debt amounts to more than 10%. In the meetings of the Committee of Creditors, the IRP will act as a chair. The Committee of Creditors is responsible for the task of passing the resolution plan for the Corporation. It plays a key role in decision-making and has the power to confirm the position of IRP as a Resolution Professional and can also substitute insolvency professionals with resolution professionals. The restoration of the corporate debtor is determined by the CoC. Assent of the CoC is required to pass the resolution plan. The Committee can suggest alterations if required.

The position is different in the U.S.A. The Committee of Creditors constitutes the unsecured creditors and the seven largest unsecured claims against the debtor. The U.S. Trustee is responsible for forming the Committee. As per the provision of Section 1102, the Committee of Creditors along with the Trustee is in charge of operating the business and also keeping a check on the Debtor. The Committee has also the responsibility to formulate the plan of resolution. According to Section 1103 of Chapter 11, by the orders of the court, The Committee of Creditors can hire an attorney to represent or any other professional required for performing the duty or for assisting the committee.

INSOLVENCY RESOLUTION PROCESS FOR INDIVIDUALS AND PARTNERSHIPS

The reorganization or Insolvency Resolution Process involves a plan for repayment of debt to the Creditors by the debtor. The plan is required to get the approval of the creditors. In case, the plan is approved the Debt Recovery Tribunal (DRT) pronounces the order binding the debtor and the creditor to the plan. When the plan is rejected, the creditor or debtor is allowed to seek an order for Bankruptcy. The DRT is required to appoint the resolution professional after receiving confirmation from the Board. The Resolution Professional shall submit the report to the DRT after the assessment of the insolvency report. DRT shall accept or reject the report within 14 days and issue notice within 21 days of receiving the report calling upon the creditors for their claims. Creditors are instructed to register claims with the Resolution Professional. Resolution Professionals on receiving the claims by the creditor are required to prepare a list mentioning all the creditors. Resolution Professional is required to call the meetings of the creditor to pass, reject, or made changes in the resolution plan. Decisions regarding modification or approval or denial of the resolution plan can be concluded with 75% votes. Resolution Professional prepares the minutes of the meetings of the Creditor and submits them to the DRT.

Chapter 11 of the U.S. Code includes Insolvency Resolution Process for Individuals and Partnerships. There are some additional requirements for Individuals for the Resolution process. Unlike the Indian Bankruptcy Code where creditors shall register claims, Section 301 and Section 303 of Chapter 11 of the Code ascribe the debtor to file the liabilities and assets with the court. Attesting the details of the current income and expenditures, financial statements, executory contracts, and unexpired leases. Apart from this, individuals debtors are needed to file the certificate of Credit Counselling and if prepared any debt repayment plan developed during Credit Counselling, a statement of an anticipated increase in income after the filing procedure, details of interest the debtor has on the federal educational institution on tuition accounts.

CROSS BORDER INSOLVENCY

United Nations Commission on International Trade Law (UNCITRAL) has laid down the procedure and legal framework for setting up Cross Border Insolvency Procedure. However, India currently only serves domestic demands and deals with domestic insolvency issues. National Company Law Tribunal emphasized the need to adopt the UNCITRAL model for cross-border insolvency in 2019 in *State Bank of India v. Jet Airways (India) Ltd.*

Chapter 15 of the U.S. Bankruptcy Code adopted the UNCITRAL model for cross-border insolvency. It lays down the procedure and requirement which needs to be fulfilled for the commencement of the Cross Border Insolvency. To start the case under Chapter 15, the petition must be filed by the representative for recognition. Attesting a copy of the document or any other evidence of foreign proceedings and appointing a representative for the purpose of representing the debtor in the proceedings. Then the question arises whether the foreign proceeding is main or non-main and it is at the discretion of the court to decide. The proceeding is non-main if the proceeding is outstanding at the place where the debtor has only establishment, it is main if the "Centre of Main Interest" lies at the place of proceeding. While deciding the cases of Cross-Border Insolvency, the U.S. Courts corroborate the law with international treaties to reach a conclusion and make sure that the decision is in accordance with the legal framework prescribed in UNCITRAL and by European Union. After recognizing the proceeding as main or non-main, the court can provide relief to the debtor on the request by the representative. Relief can be provisional relief or automatic relief depending on the circumstances of each case.

SUMMING UP THE PROCEDURE

In India, the insolvency procedure shall come to an end within 180 days of initiation of the process and can be extended up to 90 days, failing which the court has the power to order the liquidation of assets. More so like, after the acceptance of the resolution plan, the debtor is released from its previous obligations except the ones proposed in the plan. In case, the plan is not approved then the Bankruptcy process will start as per the provisions of Chapter 7.

CONCLUSION

Before the coming up of the Insolvency and Bankruptcy Code of 2016, India did not have any prior separate law for the Insolvency Procedure and was governed by the Companies Act, Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002, and Sick Industrial Companies Act. However, the U.S. was much ahead of time when it introduced its first Insolvency law in the year 1800. Though many changes were introduced and the law of 1800 was repealed thereafter. The Present law is also quite old even so, the provisions are extensive and include advanced concepts like that of Debtor in Possession and prescribe procedures for Municipality insolvency and Cross Border Insolvency. India has still a way to go and provided that it is a developing nation, India needs to make considerable changes in the law. It's high time that concept of Cross Border Insolvency as is cleared from the recent cases, is included in the Insolvency Code. Although, there are many similarities between the U.S. and Indian Bankruptcy Codes. Both legislations provide for separate procedures for Individuals and corporations, summing after approval of the plan or disapproval of the resolution plan.

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