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## IBC, 2016: A Revolution in Bankruptcy Laws

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*When we speak of the laws relating to corporate governance it is inevitable to exclude the laws relating to bankruptcy and insolvency. Though the insolvency laws in India have been adopted from the English laws, our country has witnessed tremendous advancement and improvement in the same over the past years. Often insolvency and bankruptcy are used interchangeably. However, there is a difference between the two which is elaborated on in the following research paper. A new dimension was provided in the field of insolvency laws with the enforcement of the Insolvency and Bankruptcy Code, 2016. The said code provides a road map for corporate persons, partnership firms, and individuals to deal with matters relating to insolvency. Corporates or individuals who have defaulted in the payment of their financial debts resort to the IBC, 2016. Also, they are provided with an opportunity to make their default good and revive their business. The said Code also opens the doors for the financial creditor and operational creditor to seek relief by appealing to the National Company Law Tribunal (NCLT) and National Company Law Appellate Tribunal (NCLAT) with respect to insolvency matters. The following research paper gives a brief idea about insolvency, bankruptcy, the evolution of the insolvency laws in the country, the legality of the IBC, 2016, and also the establishment of specific tribunals for bearing matters relating to insolvency.*

**Keywords:** *insolvency, bankruptcy, corporate debtor, creditor.*

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### INTRODUCTION

Insolvency is a situation wherein a corporation or an individual is unable to meet financial obligations because of the insufficiency of an asset to pay off the debts. Under this code,

insolvency refers to a “state” where the debtor has defaulted in repayment of his dues. Bankruptcy is a legal process where insolvent individuals seek relief from the defaults in their financial obligations; whereas liquidation takes into account insolvent corporates seeking relief. Insolvency is before bankruptcy and/or liquidation. Bankruptcy initiates with the proper filing of a petition in the courts and court orders are intended to resolve such insolvency. Bankruptcy and insolvency are often used interchangeably; however, there is a difference between them<sup>1</sup>. Insolvency is a state whereas bankruptcy is the legal status of a person; it is a formal declaration of insolvency. Insolvency and Bankruptcy Code, 2016 came into force to consolidate the existing framework of insolvency laws. The main object of IBC, 2016 was to provide for the resolution process of the corporations, partnership firms, and individuals in a time-bound manner.

### HISTORY OF IBC, 2016

Insolvency laws were adopted from English laws. The earliest insolvency laws can be traced back to relevant provisions of the Government of India act 1800. Further, there was a development of insolvency laws with the passing of the Indian Insolvency Act, 1848; however, the said Act was inadequate therefore, the following two acts were passed and dealt with personal insolvency.

- a. The Presidency Towns Insolvency Act 1909
- b. Provisional Insolvency Act 1920.

To examine and make a recommendation with respect to the existing insolvency laws following committees were setup:

Sr. No.	Name	Year	Few significant recommendations

<sup>1</sup> Harshal Sadhwani, Indian Bankruptcy laws and how they are different from US and UK' (*Legal Indian Service*) <<https://www.legalserviceindia.com/legal/article-3356-the-indian-bankruptcy-laws-and-how-are-they-different-from-uk-and-us.html#:~:text=The%20Law%20of%20insolvency%20in,rudimentary%20provisions%20as%20to%20bankruptcy>> accessed 21 July 2022

1.	<b>Eradi Committee</b>	1999	<ul style="list-style-type: none"> <li>i. Remedial changes in erstwhile Companies act,1956</li> <li>ii. Revival/Rehabilitation Plans for companies.</li> </ul>
2.	<b>N.L. Mitra Advisory group.</b>	2001	<ul style="list-style-type: none"> <li>i. Comprehensive Bankruptcy code.</li> <li>ii. Recommended establishment of the dedicated bench in each high court for insolvency proceedings.</li> <li>iii. Time-bound process for bankruptcy proceedings.</li> </ul>
3.	<b>JJ Irani Committee</b>	2005	<ul style="list-style-type: none"> <li>i. Establishment of NCLT and providing a commercial approach to resolve the dispute.</li> <li>ii. Definite time frame for the liquidation process.</li> </ul>

**BANKRUPTCY LAW REFORMS COMMITTEE (BLRC)**

Insolvency Bankruptcy Code, 2016 derives its base from the recommendations of the Bankruptcy Law Reforms Committee (BLRC) and it plays a vital role in the formation of the said Code. Here are a few significant recommendations:

- Jurisdiction of Debt Recovery Tribunal (DRT) over individuals and unlimited liability partnership firms and National Company Law Tribunal (NCLT) over companies.
- Debt Recovery Appellate Tribunal (DRAT) and National Company Law Appellate Tribunal (NCLAT) as appellate jurisdictions.
- Establishment of an Insolvency Regulator to monitor the operations of the insolvency professional, insolvency professional agencies, and information utilities.
- Swift Corporate Insolvency Resolution Process (CIRP) for companies and limited liability entities. The committee also recommended fast track insolvency resolution process for specific categories of entities.
- Bankruptcy for individuals and unlimited liability partnerships

## LEGAL FRAMEWORK

“Bankruptcy Law Reforms Committee” (BLRC) was constituted for the drafting of IBC, 2016.

IBC, 2016 repealed the following Acts:

1. Presidency Towns Insolvency Act, 1909
2. Provisional Insolvency Act, 1920
3. The Sick Industrial Companies (Special Provisions) Act, 1985

It also made amendments in the various Acts and a few of them are as follows:

1. The Companies Act, 2013
2. Indian Partnership Act, 1932
3. The Securitisation and Reconstruction of Financial Assets and Enforcement of Securities Interest Act, 2002 (SARFAESI Act, 2002).

Insolvency and Bankruptcy Code, 2016 consists of 255 sections organized into 5 Parts. The Code also consists of 11 Schedules. Insolvency Resolution and Liquidation for corporate persons are dealt with under Part 2 where the minimum amount of default is one crore rupees whereas Part 3 lays down the procedure for insolvency resolution and bankruptcy for individuals and partnership firms. Section 7, section 9 and section 10<sup>2</sup> of the said Code deal with the Corporate Insolvency Resolution Process (CIRP) of the financial creditor, operational creditor, and corporate debtor itself respectively. Sections 33 to 54<sup>3</sup> deal with the law relating to the insolvency process for corporate persons. The manner of distribution of assets in case of liquidation and order of priority of distribution which is also known as the “Waterfall Arrangement” is laid down under section 53<sup>4</sup> of the said Code.

IBC, 2016 also provides for the establishment of the National Company Law Tribunal (NCLT) and National Company Law Appellate Tribunal (NCLAT). All the matters of the corporate debtor, financial creditor, or operational creditor wherein the provisions of the IBC are

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<sup>2</sup> Insolvency and Bankruptcy Code 2016, ss 7, 9 and 10

<sup>3</sup> Insolvency and Bankruptcy Code 2016, s 34-54

<sup>4</sup> Insolvency and Bankruptcy Code 2016, s 53

applicable shall be referred to the above-mentioned tribunals. The corporate insolvency resolution process (CIRP) shall be completed within a period of one hundred and eighty days (180 days) from the date of admission of the application to initiate such a process. If the Adjudicating Authority is satisfied that the CIRP cannot be completed within the said period of 180 days, it may by order extend the duration by a further period as it thinks fits, but not exceeding 90 days. However, the CIRP has to be mandatorily completed within a period of three hundred and thirty days (330 days) from the date of the commencement of insolvency. This said period shall include any extension of the period of CIRP and the legal proceedings in relation to the corporate debtor

## CASE LAWS

*Is IBC, 2016 constitutionally valid?*

**Swiss Ribbons Pvt. Ltd. & Anr v Union of India & Ors<sup>5</sup>**

The above case is noteworthy with respect to the legality of the IBC, 2016. This case dealt with many issues but here we are referring only to the constitutional validity of the said Code therefore we are not going into the individual facts of the case. The petitioner has challenged Section 53 of the Code as it differentiates between financial creditor and operational creditor. There is intelligible differentia between financial debts and operational debts. The Code recognizes various kinds of unsecured debts and guarantees protection of legitimate interests thus achieving the object of the statute in question. Thus, there is no obstruction of Article 14<sup>6</sup>. Hence, the challenge to section 53 of the Code has failed.

The earlier laws had many flaws and enforcement of the said code gave a new direction to bankruptcy laws. The experiment contained in the code to be judged by the generality of its provisions and not by so-called inequities of the code stated by the petitioners passes the constitutional muster. In the short period, there have been amendments and the process is also ongoing with involves the stakeholder's interest. After the implementation of the credit flow from financial and non-financial sectors has increased. Ultimately, the flow of resources to the

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<sup>5</sup> *Swiss Ribbons Pvt. Ltd. v Union of India* (2019) Writ Petition (Civil) No. 99/2018

<sup>6</sup> Constitution of India 1950, art 14

commercial sector and foreign went up. Approximately, 3300 cases of court settlement between creditors and debtors have been disposed of by adjudicating authority. This shows that the experiment conducted by the legislature has been a great success. Therefore, the IBC, 2016 is constitutionally valid.

*Under what circumstances and at whose instance are the winding up proceedings pending before the High Court transferred to the NCLT?*

**Kaledonia Jute & Fibres Pvt Ltd v Axis Nirman & Industries & Ors<sup>7</sup>**

The second respondent M/S Girdhar Trading co-filed a petition for winding up of the first respondent before Allahabad High Court; the company court-ordered winding up of 1<sup>ST</sup> respondent on the grounds that the respondent is unable to pay the debt. Accordingly, the court ordered the appointment of the official liquidator and directed him to take over all assets and books of accounts. However, the 1<sup>st</sup> respondent paid the petitioner and applied to recall the winding up, but the official liquidator opposed such an application. Things stood thus, the application was also filed with NCLT under section 7<sup>8</sup> of IBC, 2016. Here two parallel proceedings are undergoing. The object of IBC, 2016 will be hampered if two parallel proceedings are allowed in two separate forums. Thus if the NCLT proceeds with the inquiry of section 7 and the company court proceed with winding up, there will be unnecessary and the entire object of IBC, 2016 will be thrown away into the winds. Hence the appeal is allowed and the high court order is set aside. The proceeding before the Allahabad high court is transferred to NCLT. Therefore, it is noticed that all pending cases before the Company court related to winding up shall be transferred to NLCT.

*Does IBC, 2016 has an overriding effect over all other laws?*

**Duncans Industries Ltd v A J Agrochem<sup>9</sup>**

In this case, the corporate debtor is a company who owns and looks after the management of 14 tea gardens. The Central Government has control over 7 tea gardens under the Tea Act, of

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<sup>7</sup> M/S Kaledonia Jute And Fibres Pvt. Ltd v M/S Axis Nirman And Industries and Ors (2020) Civil Appeal No. 3735/2020

<sup>8</sup> Insolvency and Bankruptcy Code 2016, s 7

<sup>9</sup> Duncans Industries Ltd. v A.J. Agrochem (2019) Civil Appeal No. 5120/2019

1953. The appellant corporate debtor continues to be in control of the tea gardens despite the notification under section 16E<sup>10</sup> of the Tea Act, 1953. The respondent initiated proceedings under section 9<sup>11</sup> of the IBC against the appellant corporate debtor before the NCLT. The Tea Act requires the consent of the Central Government to initiate any action against them. Therefore, NCLT dismissed the application as the consent of the Central Government was not obtained. Hence, the corporate debtor filed an appeal to the Supreme Court.

Supreme Court was of the opinion that according to section 238<sup>12</sup> of the IBC, the provisions of the IBC have an overriding effect over the Tea Act, 1953. If the appeal was to be allowed it would mean that consent of the Central Government is to be obtained before the initiation of proceedings under section 9 of the IBC, it would hamper the object and purpose of the IBC which is to complete the corporate insolvency resolution process in a time bound manner. Thus, the appeal was dismissed and the proceedings could continue under NCLT. Hence, no approval of the Central Government as envisaged under the Tea Act is required and the IBC shall have an overriding effect.

## CONCLUSION

IBC, 2016 came into force with a vision of a time-bound process for solving matters relating to insolvency of corporations, partnership firms, and individuals. The enforcement of IBC, 2016 gave a chance for the revival/rehabilitation of the corporates or individuals. The Code has also proved to be constitutionally valid. All matters relating to insolvency have to be strictly referred to the National Company Law Tribunal (NCLT). The Insolvency and Bankruptcy Code as legislation deals with the economy of the country as a whole. With the adoption of the said code, the flow of financial resources into the commercial sector has increased due to an exponential increase in the repayment of financial debts. The said Code has proved to be a boon to the economy of the country and has been largely successful. The defaulter's paradise is lost. It has helped to regain the economy's rightful position.

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<sup>10</sup> Tea Act 1953, s 16E

<sup>11</sup> Insolvency and Bankruptcy Code 2016, s 9

<sup>12</sup> Insolvency and Bankruptcy Code 2016, s 23