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Critical Analysis of Cross-Border Insolvency under Insolvency Bankruptcy Code 2016

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The article focuses on how Cross border Insolvency is a going concern for International traders and investors. Due to Globalisation and open Market economies, investors all over the world ante now able to make direct investments in companies across nations. There is a need for a proper mechanism for the regulation of insolvency proceedings by that of international standing since stakeholders often find themselves within the Labyrinth of initiation of multiple proceedings in multiple jurisdictions simultaneously, affecting the dissolution or reorganization process. Thus to address the said issue, UNICTRAL introduced the Model Law which strengthens and smoothens the insolvency procedure by aiding cooperation between different jurisdictions. However, said changes need to be adopted by India in its Insolvency and Bankruptcy code 2016 since Sec 234[1] *& 235*[2] *fail to resolve the said issue. Taking into consideration the Draft law Part Z, this article focuses on niches that need to be addressed whilst adopting the Model Law.*

Keywords: *insolvency, cross border, ibc.*

[1] Insolvency and Bankruptcy Code 2016, s 234

[2] Insolvency and Bankruptcy Code 2016, s 235

INTRODUCTION

Cross border Insolvency is a situation where the insolvent debtor has assets in various countries. When the insolvent is unable to pay off his debts, the lenders also known as the creditors of the company try to recover their assets either by liquidation or gaining control of the company. Due to globalization and a rapid surge in industrialization, import, and export, the geographical distances between countries have reduced. As a result, companies can now directly venture into these new countries and can explore the markets by 'setting up' their business. This also results in increased investments from creditors located in different parts of the world. Thus, due to the increased number of foreign creditors, market investors, and multiple corporate debtors- the assets of the companies are now established in various corners of the world. Thus, during the insolvency of these companies, the recovery of these assets becomes difficult. This is because of the limitation of territorial jurisdiction which hampers the recovery process of a foreign creditor. Plus, the onus lies upon the creditors to institute multiple legal proceedings against the corporate debtors in various other countries. As a result, simultaneous foreign proceedings can become cumbersome on the rights of creditors for just and timely relief.

Cross border Insolvency is also known as International Insolvency. In technical terms, it is the treatment of financially distressed debtors, where such debtors hold assets in more than one country. Similarly, it includes creditors, who have lent financial support to the companies, located in various countries. There is a need for proper mechanisms and regulation of cross-border insolvencies because it is often observed that the national insolvency regulations are ill-equipped to deal with such situations, especially in providing equal relief to all foreign creditors. To resolve this issue, the United Nations intervened to regulate smooth international trade and commerce between the countries it instituted the United Nations Convention on International Trade Law (UNCITRAL) in 1966. In 1985, to harmonize international and national arbitration laws UNCITRAL adopted the Model law. The signatory countries, that adopted the Model Law, as per the guidelines of the UNCITRAL, incorporated the same within their national insolvency laws.

In India, the issue of cross-border insolvency is incorporated in section 234[3] and section 235[4], with enables the Central Government to formulate bilateral agreements with reciprocal foreign countries to resolve the issues of Cross-border insolvencies. This proviso is however not based on the UNCITRAL Model Law and has many inconsistencies. The method is time-consuming, taxing, and expensive[5]. As a result, it limits the chances of fair and equal relief to the foreign creditors, making investments in companies unattractive to the foreign investors, as there is no or limited assurance of recovery.

PROBLEMS WITH CROSS-BORDER INSOLVENCY

Even on an International level, many countries, including India face issues while dealing with cross-border Insolvencies. These issues form the basis on which the Model law frames regulations and laws for non-taxing procedures, which takes into account the interests of the domestic insolvency laws and jurisdictional power. As of 2021, India has not incorporated the UNCITRAL Model Law in the Insolvency and Bankruptcy Code 2016, to resolve Cross-Border Insolvency issues. However, in 2018, the Insolvency Law Committee (ILC) shed light on the topic of Cross-border insolvency. It also drafted rules and regulations for cross-border insolvency to be incorporated under Insolvency Bankruptcy Code (2016), under the Part Z draft law. The draft was formulated taking into account the applicability of the UNCITRAL Model Law in the Insolvency Bankruptcy Code (2016). Based on the report on 23rd January 2020, the Cross-Border Insolvency Rules/regulations Committee (CBRIC) was established. Later, Part Z was also extended to Group Enterprises Insolvency adopting the UNICTRAL Model law.[6] Some key issues need to be dealt with under the current Insolvency Bankruptcy Code (2016) sec. 234-235 along with the proposed draft to implement Model Law.

[3] Insolvency and Bankruptcy Code 2016, s 234
[4] Insolvency and Bankruptcy Code 2016, s 235
[5] Ministry of Corporate Affairs, *Report of the Insolvency Law Committee* (2018)
[6] Ministry of Corporate Affairs, *Report of Insolvency Law Committee on Cross Border Insolvency* (2018)

THE MAIN ISSUES

Recognition in Foreign States: While capital lends from different countries are recognized as foreign creditors of a company, these creditors might enjoy certain privileges from the nations to increase their foreign direct investments and preserve their foreign reserves. On the contrary, the same investing creditors might face difficulties when they are in search of relief from foreign nations. Domestic national laws become very stringent and rigid when it comes to liquidating the assets of corporate debtors and providing relief to creditors. Often, it is the domestic creditors of the default company who are prioritized and secured. Thus, it results in unequal relief to all the invested creditors. Apart from this, the foreign creditors also need recognition in the foreign states to initiate their suits for recovery. These creditors operate through foreign representatives. Barring the application of Model Law, originally the foreign representatives of the creditors did not have direct access to the jurisdiction of another country. They have to seek permission and meet the procedural aspect to gain recognition to institute a suit in a foreign jurisdiction.

As per Part Z, draft law, the applicability of the drafted regulations shall only apply to the principle of legislative reciprocity that includes those countries that have adopted the UNICTRAL Model law and are to be added to the list of nations whose foreign creditors or debtors have direct access to the adjudication authority located within the jurisdiction of India. Thus, foreign representatives of creditors of these countries can have direct access to the courts within the jurisdiction of India. Part Z[7] also specifies that it applies only to corporate debtors and not individuals, partnerships, and other forms of entities insolvent. This is because the application of such is experimental and premature in nature. Once the individuals and partnerships gain experience the Part Z Draft Law can be extended to them. Foreign companies are also to be included in the definition of corporate debtors. The main aim of IBBI is to provide hassle-free and timely access to foreign representatives without any distinction or discrimination against them in a competent court of law.

[7] Insolvency and Bankruptcy Code 2016, s 235

Concurrent or Multiple Proceedings: When a company is declared to be insolvent, all creditors, including foreign representatives initiated simultaneous proceedings for the recovery of assets. The main question arises, since all countries where the assets of the insolvent debtor are located initiate concurrent proceedings simultaneously, then how does a creditor administer assets located in foreign nations and where shall the main proceedings be initiated? The UNICTRAL Model law pens two different kinds of proceedings, namely:

- **Foreign Main Proceedings -** Where the Insolvent Debtor has his main interests or assets, that nation-country initiates Foreign Main Proceedings.
- **Foreign Non-main Proceedings -** Where proceedings are initiated in other foreign countries, other than the main proceedings.

As per Art 4[8] of the UNICTRAL Model Law, the proceedings are to be initiated in the Competent Court of Jurisdiction in a foreign state. In India, National Company Law Tribunal is the competent court authority to deal with Cross-Border Insolvencies. As per the recommendations of the CBRIC, the insolvency procedure against Indian Insolvent debtors is to be dealt with in the competent court of jurisdiction. And in case, where the debtor with limited liability is located outside India, the matter is to be dealt with by the Principle bench of the National Company Law Tribunal,[9] it is the duty of the court to notify the foreign creditors about the proceedings filed under Cross-Border Insolvency. It is also responsible to give the required time to these foreign creditors to file insolvency proceedings.[10] The court is also responsible to notify if there is any substantial change in the proceedings.[11] The creditors can initiate proceedings simultaneously with the main proceedings provided that there are assets of the debtor in that country. Thus, a foreign creditor cannot initiate insolvency proceedings against the corporate debtor, in his country unless his assets are located in that country.[12]

[8] UNCITRAL Model Law 1985, art 4
[9] Cross Border Insolvency Rules/ Regulations Committee, *Report on the rules and regulations for cross-border insolvency resolution* (2020)
[10] UNCITRAL Model Law 1985, art 14
[11] UNCITRAL Model Law 1985, art 18
[12] UNCITRAL Model Law 1985, art 28

The UNICTRAL Model law, unlike other laws such as the New York Convention on Arbitration law, does not mandate the principle of reciprocity when adopted in national insolvency laws[13]. Unlike India, Australia has set aside the principle of reciprocity. Foreign representatives from any country can initiate insolvency proceedings in Australia[14]. This enables, coordination between various jurisdictions and foreign representatives ensuring equal and fair allocation, proportional to the investments of the creditors. India faces a major challenge here. As of now, 44 countries have adopted the UNICTRAL Model law. The Asia-Pacific region has significantly abstained from adopting the same. India carries out the majority of its trade and investment commerce with the Asia-Pacific region. Thus, due to the limitation caused by the reciprocity clause, India resolves cross-border insolvencies through Section 234[15]-235[16]. Even if forming bilateral agreements between nations can prove to be beneficial to access foreign jurisdiction it is a time-consuming and costly affair. Thus, not all companies find it feasible to opt for this method. Along with that, the government and judicial authority are responsible for entertaining such applications, which is a cumbersome task. Another inconsistency with cross-border insolvency proceedings through Section 234-235 is that it enables representatives to access permission, but it does not list down or expand upon the procedure for insolvency once it is approved. This increases the chances of conflicts with the compliances established by the said agreement. UNOCTRAL Model Law on the other hand lists down methods of cooperation and coordination amongst the courts and foreign representatives.

The determination of the Centre of Main Interest (COMI) is important for determining the foreign main proceedings. The creditors and debtors in India, do not decide or negotiated upon COMI. It is determined by the competent court of Jurisdiction, based on the location of his assets. Number/value of assets, debtors center of administration, etc. Thus, the decision of the Court

[13] 'UNCITRAL model law on international commercial arbitration (1985), with amendments as adopted in 2006' (*United Nations*) <https://uncitral.un.org/en/texts/arbitration/modellaw/commercial_arbitration> accessed 01 February 2023

[14] Robert McDougall, 'Recognition of Foreign Insolvency Proceedings – An Australian Perspective' (*The Supreme Court of New South Wales*, 03 November 2018) <https://www.supremecourt.justice.nsw.gov.au/Documents/Publications/Speeches/2018%20Speeches/McDougall_20181103.pdf> accessed 01 February 2023

[15] Insolvency and Bankruptcy Code 2016, s 234

[16] Insolvency and Bankruptcy Code 2016, s 235

of Main foreign proceedings shall have a binding effect on all the other courts where the Non-main proceedings are carried out. The question arises, if the Indian law, based on UNCITRAL Model law, is founded on the principle of reciprocity, then shall the judgment of the Competent Court of Jurisdiction carrying out main proceedings within India will have a binding effect on the other courts entertaining Non-Main Proceedings. In case bilateral treaties or agreements are to be executed with countries who have not adopted the said law, the onus will be on the government to ensure that proportional equal relief is provided to all creditors including adoptees of Model law and those negotiating via bilateral agreements. This however will be contrary to what is proposed in the Model law, which states that, in case of Bilateral agreements between nations, and a conflict arising between the application of laws under the agreement and model law, the former shall prevail. Thus, more clarification is required on the execution of the laws based on the CBRIC report.

Relief to the Creditors: Before the application of Model law, even under sections 234-235, the major question was how to alienate the assets of debtors in a foreign jurisdiction. While under Insolvency Bankruptcy Code 2016, section 234-235 India has to constantly seek approval from the government, and other statutory provisions for either liquidating assets or gaining control of the same. There is no prescribed procedure to alienate property under the IBC 2016 and the parallel codes of the signee country. As a result, many recovery procedures are still pending authorization within the nation. Under the UNCITRAL Law, the foreign representatives have similar access to the jurisdiction to that of domestic creditors.

As per the draft law Part Z, the domestic secured creditors will be given preference over the foreign creditors in case the Main proceedings are initiated in India. The foreign Non-Main proceedings can grant relief to creditors however they must be consistent with the main-proceedings. As a result, Main-proceedings shall have an overriding effect on Non-main proceedings. However, as per Article 38[17] of the UNICTRAL Model law, if one creditor receives some relief in one jurisdiction, he may apply for the remainder of the relief in another jurisdiction, provided proportional relief is provided in another jurisdiction. Thus, the foreign

[17] UNCITRAL Model Law 1985, art 38

representative must inform the court of simultaneous or cross-border proceedings. *In Jet Airways (India) Ltd. v State Bank of India and Anr*[18] set a precedent that both parties should not hamper the procedure of liquidation which could be detrimental to the creditors and the company. It advocated cooperation between the Adjudicating authorities, the court, and the foreign representatives of creditors to seek a smooth liquidation procedure.

The CBRIC report 2021, makes recommendations based on the ILC Draft Law Part Z, which suggests that the adjudicating authority is not empowered to give interim relief in domestic cases and should be empowered to do so. Part Z, Clause 18, provides power in hands of adjudicating authority to provide discretionary relied[19]. The competent court is empowered to grant a stay order, Injunction on the property, restriction on right to transfer of property of the debtor, examining witnesses, and entrusting an administrator, etc. Thus, instead of burdening the courts with the liquidation process, the court acts as an appointing and monitoring authority which ensures a smooth functioning of the insolvency procedure.

CONCLUSION

The Cross-Border Insolvency mechanism based on Model Law creates confidence amongst the creditors {financial and operational} for recovery of assets in case of Insolvency. Thus, encouraging foreign and National financial creditors to provide loans and financial credit in case of a default, without any geographical restriction. The application of the central government forming bilateral agreements under sections 234[20]-235[21] is very limited, taxing, and cumber on the judiciary. In addition, the future insolvency process is not prescribed or standardized, which makes it difficult for creditors to set new agreements meeting the compliances and conditions while framing bilateral agreements. Apart from that, there is no guarantee that the foreign creditor shall be given the same treatment as a domestic creditor. This makes creditors fearful of investing in companies in India, as asset recovery in the case of Insolvency is difficult. With

[18] *Jet Airways (India) Ltd. v State Bank of India & Anr* (2019) NCLT NATIONAL COMPANY LAW TRIBUNAL, Company Appeal (AT) (Insolvency) No 707/2019
[19] Ministry of Corporate Affairs, *Report of Insolvency Law Committee on Cross Border Insolvency* (2018)
[20] Insolvency and Bankruptcy Code 2016, s 234
[21] Insolvency and Bankruptcy Code 2016, s 235

the recent reports of CBRIC and ILC, India has shown active interest in adopting the UNICTRAL Model law. However, there are some aspects within the report which need a new outlook. For better implementation and gradual experimentation, the aim of adoption of Model law within the IBC 2016 should focus on lessening the burden on the court, ensuring coordination between adjudicating authority and Foreign representatives, and maintaining the status quo during liquidation proceedings in all jurisdictions so that the actions of any court are not detrimental to any creditor or company seeking relief.