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Transforming Real Estate Insolvency in India: Project-Wise Corporate Resolution and Homebuyer Empowerment

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The Insolvency and Bankruptcy Code (commonly known as ‘the Code’, ‘IBC’, or ‘Code’) was enacted in India in 2016 with the intention of reforming the country's bankruptcy laws. It contained rules for the insolvency process for a number of industries, including the real estate industry. While real estate significantly contributes to the nation's economy, it faces its challenges to the point where it is pushed down to the verge of being bankrupt. This article explores the intricate relationship between bankruptcy and Indian real estate. It delves into the challenges faced by developers, the impact on homebuyers and investors, the reforms introduced, and potential opportunities. Key to this discussion is the development of real estate allottees and Project-wise Corporate Insolvency Resolution. The article also discusses the concept of project-wise Corporate Insolvency Resolution, a proposed IBC amendment. This approach is believed to expedite the resolution of stalled real estate projects by focusing on distressed assets within a specific project. It also highlights recent case laws and legal developments and emphasizes the benefits of project-wise CIRP. In conclusion, the article provides a comprehensive overview of the evolving landscape of insolvency procedures in real estate sectors in India. It emphasizes the need for innovative solutions to protect homebuyers and stakeholders while ensuring the efficient resolution of distressed real estate projects.

Keywords: *ibc, real estate, homebuyers, corporate insolvency, corporate resolution.*

INTRODUCTION

The enactment of IBC envisaged to bring about a significant shift in the legal framework. Its primary objective is to tackle the existing challenges surrounding insolvency and winding up procedures. The scope of the Code encompasses various entities including companies, limited liability entities, firms, and individuals (excluding financial service providers). The Code aimed to revolutionize and instigate a cultural shift in the field of insolvency and bankruptcy through three main avenues:¹

- The establishment of a comprehensive code governing insolvency and bankruptcy matters for both corporations and individuals;
- The creation of a novel structure comprising a committee of creditors (CoC) and specialized adjudicating authorities (AA) dedicated to handling insolvency resolution and liquidation and
- The introduction of judicial discipline throughout the process.

Each of these three components aimed to tackle the issues that had been impacting the bankruptcy system in India. Despite the presence of provisions for winding up companies in the Companies Act 1956 and 2013 and the laws for industries experiencing financial difficulties under the Sick Industrial Companies Act (SICA), they were deemed insufficient. Beyond establishing a legal structure for insolvency resolution and bankruptcy, it created the Insolvency and Bankruptcy Board of India (IBBI) as the overseeing authority, endowed with the ability to proactively adapt to evolving circumstances through its regulatory capabilities. The IBC has triumphed in shaping a distinct legal precedent for insolvency resolution. Both the government and the IBBI have taken proactive measures to elucidate and resolve emerging challenges as they arise during the implementation of the statute.

¹ Mani Gupta et al., 'Overview of India's Insolvency and Bankruptcy Code' (*Global Restructuring Review*, 09 September 2022) <<https://globalrestructuringreview.com/review/asia-pacific-restructuring-review/2023/article/overview-of-indias-insolvency-and-bankruptcy-code>> accessed 04 October 2023

Thus, bankruptcy constitutes a legal procedure strategically crafted to offer assistance to both individuals and businesses grappling with burdensome debts and financial hardship. It allows debtors to restructure their finances or seek a fresh start by liquidating assets, with the ultimate goal of distributing the proceeds among creditors. Through bankruptcy, either individuals or businesses can repay their debts over time under a court-approved plan or have certain debts discharged, providing them with a chance to regain financial stability and begin anew.

Now, the real estate sector in India is a significant contributor to the country's economy. According to a media outlet – India Brand Equity Foundation, which do the Department of Ministry of Commerce and Industry, Government of India the real estate industry in India is projected to experience substantial growth, with its market size expected to, establish reach US\$ 1 trillion by 2030. Additionally, it is anticipated that the sector will contribute around 13% to the country's GDP by 2025.²

The domain of real estate encompasses various segments such as residential, commercial, retail, and hospitality. It has demonstrated remarkable growth in the nation over the recent decades. This sector has played a pivotal role in propelling India's economic advancement, making substantial contributions to the GDP, employment creation, and the inflow of foreign investments. The real estate realm in India has a far-reaching influence, directly and indirectly affecting more than 250 supplementary industries including cement, steel, and construction materials, thus driving the overall economic progress.³ IBEF even proceeded to mention that the real estate sector's contribution to India's GDP has exhibited a consistent upward trend, constituting roughly 7% of the GDP in 2020 according to the National Statistical Office (NSO) and projected to account for 13% of the country's GDP by 2025. However, the challenge of real estate insolvency in India is notable due to the capital-intensive nature of the sector, coupled with susceptibilities to delays and expenditure exceedances.

² 'Real Estate Industry Report' (India Brand Equity Foundation, 2023) <<https://www.ibef.org/industry/real-estate-india>> accessed 04 October 2023

³ 'Impact of IBC On Real Estate Developers in India' (King Stubb and Kasiva, 24 February 2023) <<https://ksandk.com/real-estate/impact-of-ibc-on-real-estate-developers/>> accessed 04 October 2023

Thus, the real estate industry is one of the most important pillars of the Indian economy, driving development, employment, and investment opportunities. However, a less glamorous reality – a landscape riddled with financially distressed projects and unstable developments – lies beyond the glittering façade of residential and commercial constructions. Thousands of homebuyers are receiving delayed possession of their residential/commercial property or are still waiting to get the key to their dream home as numerous real estate companies, including Supertech Limited, Amrapali Group, and Jaypee Infratech, have undergone or are currently undergoing insolvency proceedings. Based on the data provided by IBBI, as of March 2023, the real estate sector accounts for the initiation of 21% of the corporate insolvency resolution process ('CIRP') in India.⁴

We need to pay attention to and comprehend the intricate relationship that exists between bankruptcy and real estate in India. For instance, to address the woes of the homebuyers, the Real Estate (Regulation and Development) Act was introduced and certain amendments were brought within IBC to solve similar issues. In this article, an attempt has been made to connect these two realms, exploring the challenges faced by developers, the impact on homebuyers and investors, the reforms brought in, and the potential opportunities amidst the trials. Specifically, this article is going to be focused on the development of real estate allottees and Project-wise Corporate Insolvency Resolution.

THE DEVELOPMENT OF THE STATUS OF THE REAL ESTATE ALLOTTEES OF THE PROJECTS UNDERGOING CORPORATE INSOLVENCY

The provisions of IBC 2016 clearly state that in the event of a corporate debtor's default, a financial creditor, an operational creditor, or the corporate debtor itself⁵ can carry out the initiation of a corporate insolvency resolution process. This application is made before the National Company Law Tribunal (NCLT). A Financial Creditor (abbreviated as FC) is a person

⁴ 'Leveraging Behavioral Change' (2022) 24 Quarterly Newsletter of the insolvency and Bankruptcy Board of India <<https://ibbi.gov.in/uploads/resources/2022-11-16-184743-zunjid-92a2b5cb9c6906035c2864fa225e1940.pdf>> accessed 04 October 2023

⁵ Insolvency and Bankruptcy Code 2016, s 6

to whom a financial debt is owed and a financial debt as per the code⁶ means a debt, including any accrued interest, provided in exchange for the concept of the time value of money. In addition, Subsection 20 of Section 5 provides that an Operational Creditor (abbreviated as OC) is the one to whom 'operational debt' is owed. An 'operational debt' includes claims in goods and services provided to the Corporate Debtor.

Before the 2018 Amendment to the Code, homebuyers found themselves bogged down in a profound predicament when a real estate agency underwent bankruptcy. The crux of the issue lay in the homebuyers' lack of categorization as either financial creditors or operational creditors. Consequently, they were not provided with the ability to instigate the Corporate Insolvency Resolution Process (CIRP) on their own accord, leaving them reliant on the magnanimity of the Committee of Creditors (CoC) and other creditors once the Adjudication Authority initiated the CIRP. Homebuyers were left with no choice but to pursue alternative means of redress, such as turning to the National Consumer Disputes Redressal Commission ('NCDRC') or submitting applications under the Real Estate (Regulations and Development) Act, 2016 ('RERA'), to recoup their financial investments. However, when a 'moratorium' is issued under section 14 of the IBC Code, it means that no lawsuits or other legal actions can be launched against the company that is undergoing insolvency resolution. As a result, the homebuyers' ability to request control from the Consumers Court and Authorities under the RERA Act was suspended, placing them in a hazardous situation.

In the landmark verdict of *Chitra Sharma & Ors v Union of Ind*⁷, the Supreme Court took notice of the predicament of such home buyers. The primary contention in this case centered on the difficulties that the homebuyers were experiencing as a result of being left without any recourse because they weren't classified as either financial creditors or operational creditors and were instead instructed to submit their claims as 'other creditors'. The main issue with this was that because homebuyers were ranked lower in the distribution system under Section 53 of the Code, they would get exceedingly low funds. Therefore, they would neither be promised to

⁶ Insolvency and Bankruptcy Code 2016, s 5(8)

⁷ *Chitra Sharma & Ors. v Union of India* Civ WP No 744/2017

have their houses allotted to them nor would they receive appropriate compensation for the loss they incurred.

Thus, The Supreme Court in the exercise of its powers under Article 142 of the Constitution directed to have the CIRP be reinstated and to protect the interest of the homebuyers established a feasible structure by designating a representative of the homeowners in the CoC to safeguard their interest in the lack of any consolation for the homebuyers within the framework of the IBC, per the judgment of Justice DY Chandrachud.

The 2018 revision to the IBC intended to remedy this obvious gap in light of the difficult circumstances homeowners confront. Homebuyers now have the status of financial creditors thanks to this revolutionary development, giving them the power to take part in the CIRP and make sure their opinions are heard throughout the insolvency procedures. This significant change is welcomed as a key safety for homeowners, giving them more power and protection against the bankruptcy of real estate agencies. As a result, the revised Code brought about an equal environment while properly recognizing and defending the rights and concerns of homebuyers. In this amendment, the allottees were given the identity of a financial creditor by the inclusion of any amount raised from an allottee under a real estate project into their definition of what construes as a 'financial debt'.

The 2018 Amendment Act, however, was subject to legal objections before the Supreme Court, which led to a reassessment of its constitutionality. The Supreme Court supported the legality of the 2018 Amendment Act in the case of *Pioneer Urban Land and Infrastructure Ltd. v Union of India*⁸, solidifying its status as sound legislation. Yet, worries about the hazards posed by lone, unsatisfied customers starting insolvency proceedings emerged, which may endanger an entire project and affect many parties. It was feared that if one homebuyer, who was considered a financial creditor, filed for bankruptcy against a real estate developer, it might put the interests of all other homebuyers and creditors at risk. A threshold cap was suggested for homebuyers who file for insolvency under the Code to prevent such eventualities.

⁸ *Pioneer Urban Land and Infrastructure Ltd. v Union of India* (2019) SCC OnLine SC 1005

The threshold limit for homeowners was subsequently adopted by the Insolvency and Bankruptcy Code (Amendment) Act, 2020 ('2020 Amendment Act'). It required that an insolvency application be filed against the real estate developer by a minimum of 100 homebuyers or by no less than 10% of the total number of homeowners in the same project, whichever was fewer. This change sought to achieve a compromise between defending homebuyers' interests and avoiding potential abuse of the Code's provisions.

In the case of *Manish Kumar v Union of India*⁹, the 2020 amendment was contested before the Supreme Court and the Court upheld the addition of this new threshold by emphasizing that allowing individual homebuyers to use the insolvency process would result in abuse of the Code's provisions. To sum it up, the journey of homebuyers under IBC has been fraught with challenges. The 2018 Amendment acknowledged them as financial creditors, granting them a say in the insolvency process. Nonetheless, concerns arose over the individual buyers initiating insolvency and potentially endangering projects and stakeholders. The 2020 Amendment introduced a threshold, mandating a minimum number of homebuyers to file an application. While aiming to strike a balance, the predicament of homebuyers and the intricacies of insolvency proceedings remain under scrutiny and judicial exploration.

PROJECT-WISE CORPORATE INSOLVENCY RESOLUTION

Since its establishment in 2016, IBC has played a crucial role in resolving insolvent entities across various industries, including infrastructure, telecom, energy, and real estate, among others. Although the Code is universally applicable to different sectors, past experiences have highlighted the pressing need for a distinct insolvency resolution mechanism tailored specifically for the real estate sector. This arises from the fact that the real estate sector accounts for the second-highest number of insolvency resolution cases, making up 21 percent, as reported by the Insolvency and Bankruptcy Board of India (IBBI) newsletter (September 2022)¹⁰ Over 1200 real estate cases have been admitted under the IBC, affecting numerous homebuyers. Furthermore, the real estate sector not only registers one of the highest numbers

⁹ *Manish Kumar v Union of India* (2021) SCC OnLine SC 30

¹⁰ Leveraging Behavioral Change (n 4)

of insolvency cases but also exhibits the lowest resolution rates. As a result, a significant number of cases remain unresolved and pending, creating challenges for homebuyers who have invested their life savings in purchasing real estate properties.

On January 18th, 2023, the Government issued a paper proposing amendments to IBC, intending to alleviate the challenges faced by homebuyers entangled in prolonged legal battles with real estate developers, leading to delays in obtaining possession of their homes. A key highlight of this proposal is the introduction of project-wise Corporate Insolvency Resolution. Under this new concept, if an application is filed against a builder with multiple projects, the insolvency proceedings will be initiated solely for the specific project where the default occurred. The objective behind these proposed changes is to expedite the resolution of stalled projects, thereby enhancing the likelihood of successful resolution by focusing on distressed assets within a particular project rather than the entire company

Thus, if an application is submitted to initiate corporate insolvency for a company that is a promoter of multiple real estate projects, and the default pertains to one or more of these projects, the Adjudicating Authority has the discretion to admit the case but apply the CIRP provisions exclusively to the defaulted real estate projects. This allows these projects to be treated as distinct entities within the larger company solely for the purpose of resolution, as proposed in the amendments.

Embracing this approach offers two significant advantages. Firstly, by resolving stressed projects separately, which led to the corporate debtor's insolvency, the company can concentrate on its other projects, ensuring the interests of relevant stakeholders, particularly the allottees of the specific project, are met. Secondly, this approach allows for a customized resolution plan based on the status of the real estate project and the specific objectives of relevant stakeholders, especially the allottees of that particular project. This tailored approach ensures that the resolution process is well-aligned with the unique requirements of each project and its stakeholders.

The idea of 'Reverse CIRP' an unconventional approach to closing off stalled projects, is

recognised in the proposed IBC modifications pertaining to real estate matters. With this strategy, promoters can provide funds directly to the impacted projects and concentrate on their resolution rather than the recovery of the entire business. The ideas behind project-wise and reverse CIRP originate from a significant case in IBC history which is the Flat Buyers Association v Umang Realtech case. In this matter, the Hon'ble NCLAT adopted an approach that was practical in an attempt to preserve the interests of stakeholders as well as the sustainability of the firm.

The case involved 'Financial Creditors', Mrs. Rachna Singh and Mr. Ajay Singh, who were allottees of an apartment in the Winter Hills-77 Gurgaon Project. They filed an application under Section 7 of the IBC, seeking to initiate the Corporate Insolvency Resolution Process (CIRP) against the real estate company, M/s. Umang Realtech Private Limited. The Tribunal accepted the application and instructed the Financial Creditors to deposit funds with the Interim Resolution Professional (IRP) to cover the expenses of maintaining the company's operations. However, the Flat Buyers Association of Winter Hills-77 Gurgaon (the Appellant) appealed the order, arguing that the CIRP was hindering the completion of the Project, which was almost finished and expected to be completed by October 2019.

Subsequently, Uppal Housing Private Limited (referred to as 'Uppal'), one of the promoters of the Respondent, proposed to remain outside the Corporate Insolvency Resolution Process (CIRP) and act as a lender/financial creditor to the Respondent. The main objective of this proposal was to ensure that the allottees could take possession of their flats/apartments in the Project during the CIRP without any involvement from third-party resolution applicants. The Appellant accepted Uppal's proposal and agreed to cooperate on the condition that it would receive 30 percent of the amount paid by the allottees at the time of flat registration. Additionally, the Financial Creditors aligned with the Appellant and became members of the joint initiative.

After recognizing that the project was projected to be completed within 4-5 months, the National Company Law Appellate Tribunal (NCLAT) authorized the implementation of reverse CIRP and set a specific timeframe for the promoter (Uppal) to complete the project. The

NCLAT also underscored the importance of the promoter adhering to their commitment to act as a financial creditor or cooperate with the interim resolution professional (IRP). Failure to comply with these conditions would result in the NCLT stepping in to complete the CIRP in accordance with the provisions of the Code.

The Hon'ble National Company Law Appellate Tribunal (NCLAT) referred to the landmark judgment passed by the Apex Court in the *Swiss Ribbons*¹¹ case, recognizing that the Code is an economic legislation dealing with economic matters and the overall economy of the country. The court highlighted that restricting the right to experiment with innovative approaches in resolving insolvency cases could have severe consequences for the nation.

In line with this principle, in the case of *Ram Kishor Arora v Union Bank of India & Anr*,¹² the NCLAT permitted a project-wise Corporate Insolvency Resolution Process instead of CIRP for the entire company. It also directed that construction on the other projects should continue under the overall supervision of the IRP. Moreover, the Hon'ble Supreme Court upheld the principle of reverse CIRP in the cases of *Anand Murti v Soni Infratech Pvt. Ltd.* and *Amit Katyal v Meera Ahuja*, further affirming the importance of embracing innovative approaches in the resolution of insolvency cases.

BENEFITS OF PROJECT-WISE CIRP

Project-wise Corporate Insolvency Resolution Process offers several benefits in the context of real estate corporate debtors. The uniqueness of the real estate sector has led to the evolution of innovative concepts like 'reverse CIRP' and 'project-wise CIRP' as the Code does not specifically address the sector's distinct challenges. One significant advantage of project-wise insolvency is the ability to treat individual projects within a real estate company differently. In many cases, only certain projects face default issues while others remain unaffected. Project-wise CIRP allows for the separate resolution of defaulted projects, safeguarding the interests of ongoing projects. This approach addresses the needs of various stakeholders, such as

¹¹ *Swiss Ribbons Pvt Ltd v Union of India* AIR (2019) 4 SCC 17

¹² *Ram Kishor Arora Suspended Director of M/s. Supertech Ltd. v Union Bank of India & Anr* Company Appeal (AT) (Ins) No 406/2022 & I A No 2387/2023

homebuyers, who can obtain possession of their flats and apartments in completed projects.

Moreover, adopting a specific resolution process for each project increases the likelihood of successful and prompt resolutions. By focusing on the specific default rather than the entire company, non-defaulted projects can continue without disruption. Initiating CIRP for the entire company might have impeded the progress of unaffected projects, making project-wise resolution a more practical and efficient approach.

Under Project-wise CIRP, distinct accounts are established for defaulted and non-defaulted projects, managed under the watchful eye of the IRP.¹³ The IRP's counter signature is required for any transactions involving the Corporate Debtor's accounts, reducing the risk of fund mismanagement or diversion. This stringent supervision ensures transparency and minimizes the chances of funds being siphoned off.

The incorporation of a comprehensive framework for project-wise CIRP and reverse CIRP within the Code offers the most fitting solution to address the challenges encountered by stakeholders in the real estate sector, with a specific focus on financial creditors and homebuyers. Allowing the Adjudicating Authority to initiate project-wise insolvency and/or reverse insolvency through enabling provisions is a critical aspect, but it is equally crucial to incorporate robust safeguards within the Code. These safeguards are essential to uphold the primary objectives of the Code and ensure that the interests of the homebuyers are fully protected throughout the resolution process. Striking the right balance is vital to prevent potential misuse and guarantee the integrity of the insolvency resolution process, benefiting all stakeholders involved. The introduction of this effective mechanism marks a significant step forward in addressing the intricacies of the real estate sector, providing an efficient resolution mechanism while prioritizing the interests of the concerned stakeholders.

¹³ Ayush Kumar, 'Project-Wise CIRP: A Necessary Evil?' (*Centre for Business and Financial Laws*, 07 July 2023) <<https://www.cbflnludelhini.in/post/project-wise-cirp-a-necessary-evil>> accessed 04 October 2023

CONCLUSION

The Insolvency and Bankruptcy of 2016 marked a significant shift in India's legal framework, aiming to streamline insolvency and bankruptcy proceedings for various entities, excluding financial service providers. IBC introduced a comprehensive code for insolvency, specialized adjudicating authorities, and a Committee of Creditors (CoC) to revolutionize insolvency processes.

India's real estate sector, contributing significantly to the economy, has faced its distinct challenges. The capital-intensive nature of real estate, coupled with project delays, led to a notable issue - real estate insolvency. Several renowned real estate companies, including Supertech Limited, Amrapali Group, and Jaypee Infratech, underwent insolvency proceedings, impacting homebuyers.

To address these challenges, the IBC was amended in 2018, acknowledging homebuyers as financial creditors, and granting them participation in CIRP. However, this raised concerns about individual homebuyers potentially endangering projects, leading to the 2020 Amendment Act introducing a threshold for the number of homebuyers required to initiate insolvency proceedings. Moreover, a recent proposal suggests project-wise Corporate Insolvency Resolution, focusing on specific troubled assets within a project. This approach allows for tailored resolutions for each project, ensuring the interests of homebuyers and other stakeholders are preserved.

These initiatives signify India's commitment to addressing the complex relationship between bankruptcy and the real estate sector. They aim to streamline the insolvency resolution process, safeguarding the rights and investments of individuals, businesses, and homebuyers while promoting economic growth.