



# PERSONAL INSOLVENCY IN INDIA

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- *Insolvency and Bankruptcy Code 2016 - a paradigm shift in the insolvency regime in the country leading several notch jump in "ease of doing business"*
- *Corporate Insolvency Resolution Process (CIRP) for the companies has fast developed successfully in just over two years - remarkable achievement*

On May 26 2016, Indian parliament passed the Insolvency and Bankruptcy Code (IBC). It covers a) companies & Limited Liability Firms for Corporates and b) Personal & Partnership firms Insolvency. The rules were notified for Corporate Insolvency Resolution Process (CIRP) & Liquidation for Corporate Persons. Over the two years CIRP has unfolded as a mature law with ever evolving jurisprudence. The regulator ie Insolvency & bankruptcy Board of India (IBBI) is progressive, adaptive and have responded to the situation as it evolved which has resulted into timely amendments to the IBC, rules

& regulations. Government on its part has acted to support the ecosystem to handle cases. Presently, more than 2500 Insolvency professionals are active to handle the insolvency cases. One Principal Bench & 13 NCLTs are working incessantly to handle the influx of the cases. Appellate tribunal NCLAT is also fully operative. Hon'ble Supreme Court has settled some of very important emerging issues during the over two years. The emergence of IBC has successfully demonstrated the debt resolution and fiscal discipline among the corporates leading to a very positive corporate governance. Speedy,

effective & adaptive IBC has been praiseworthy and created a right balance among the stakeholders.

Part III of the IBC, which deals with Personal Insolvency and Partnership firms, is covered but remains to be notified. Further, the Rules & regulation will also be notified. IBBI is having several deliberations on this issue for its right timings. The time seems to be quite near and hopefully notified very soon by IBBI. Bankruptcy Law Reforms 2015 has also recommended that the that the Individual (Personal) insolvency should be made more efficient and speedier.

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Presently personal insolvency is covered in India under "The Presidency Towns Insolvency Act 1909" & "The Provincial Insolvency Act 1920". These two laws are outdated and need has come now to implement the modern Insolvency law (i.e. IBC ) more so with unfolding financial credit market. These laws are still being used in India as Section 243 under Part III of IBC is yet to be notified.

The main objectives of the Personal Insolvency are a) financial affairs of insolvent individual b) effective release or relief from financial liabilities and c) structured process to make sure that both debtor & creditor work timely & successfully.

Part III of IBC provides for Fresh Start and Insolvency & Bankruptcy of individuals.

**F**resh Start Process (FSP) is covered under Chapter II of Part III from section 80 to 93 of IBC. Attractiveness of this option is that typical cost for running IRP may be much higher than the debt involved hence this option makes lot of sense. The application for FSP to Adjudicating Authority (Debt Recovery Tribunal or DRT) can be filed by the individual (debtor) or through an Insolvency (Resolution) Professional. Eligibility for FSP mainly is that i) gross income < Rs 60,000 per annum, ii) aggregate value of assets < Rs 20,000, iii) qualifying debt < Rs 35,000/- . Qualifying debt is defined as amount due including interest by the debtor but does not include Excluded debt (like court fine, amount to be paid for breach of statutory or legal obligation, student loan etc) . After the admission of application by AA, a moratorium period commences for 180 days. It provides a legal protection from both the current & future legal proceedings in respect of any debt. Debtor is also barred to act as a director of any company, dispose any assets, travel outside country without the permission of AA. Finally Resolution Professional submits the final list of qualifying debts to AA one week prior to the moratorium ends followed by the AA passing the discharge order (section 92).

**I**ndividual Resolution Process (IRP) is covered Chapter II of Part III of IBC from section 120 of IBC. This is different than the FSP as FSP can only be brought in if falls into the defined eligibility criteria. IRP enables a negotiation between the debtor & creditor managed by Resolution Professional under the supervision of AA. IRP can be undertaken by the debtor (individual or partner of the firm) or creditor, applying either personally or through Resolution Professional to AA. Application has to be complied with pre-requisites as per IBC (section 94 & 95 of IBC). After the application is filed, an interim moratorium is granted. After the application is accepted on submission of report by Resolution Professional, a moratorium (180 days) is granted by AA that ceases all present or future legal actions against the debtor. AA then publishes a public notice inviting claims from all the creditors with 21 days (section 102 of IBC). Debtor then prepares a Repayment plan in consultation with Resolution Professional by restructuring the debt or other financial liabilities. Resolution Professional will then submit the Repayment plan to AA. Repayment Plan should be complied with the extant law. The Resolution Professional then calls a meeting of the creditors for voting on the Repayment Plan. Voting share of each creditor is decided by the Resolution Professional based on the their respective admitted claim. Secured Creditors are also entitled to participate & vote in the meeting provided they shall forfeit their right to enforce the security (section 110 of IBC) . AA shall give an order either by approving or rejecting the repayment plan. Within 14 days of completion of Repayment Plan, the Resolution Professional has to submit a list of requisite documents to the stakeholders bound by the Repayment Plan. The Resolution Professional will also apply to AA for passing the discharge order (section 119 of IBC) for the debt as per the Repayment Plan. If the Repayment Plan comes to end prematurely then the Resolution Professional submit a report to AA and AA shall pass the order regarding the same. Creditor or debtor whose claim under the

Repayment plan have not fully satisfied shall be entitled for bankruptcy as per Chapter IV of Part III of IBC.

**B**ankruptcy under the IBC is dealt in Chapter IV of Part III of IBC from section 121 to 148. Bankruptcy could be initiated by the debtor or creditor within 03 months of the AA under the three conditions: a) rejection of insolvency application by AA, b) rejection of Repayment Plan by AA and c) premature ending of the Repayment Plan (section 121 of IBC). The application once filed can not be withdrawn without the permission of AA. Application for bankruptcy shall be supported by the requisite documents like IRP undertaken, statement of affairs & copy of AA order passed. Insolvency Professional will be proposed as Bankruptcy Trustee in the application. AA would pass Bankruptcy order after receiving the conformation/nomination of Trustee by the IBBI. After this order, estate of bankrupt will be vest with trustee. AA will issue the public notice inviting claims from the creditors within 10 days of bankruptcy commencement date. Bankruptcy Trustee shall prepare list of admitted claims, creditors voting rights, notices & convening the Creditors meeting. Bankruptcy Trustee shall conduct the administration and distribution of the estate of Bankrupt in accordance to the Chapter V of Part III of IBC. Bankruptcy Trustee shall apply for the discharge order (section 138 of IBC) on the expiry of 1 year or within 07 days of the approval of creditors of the completion of the administration. Water fall for money received from Bankrupt estate will be as per Section 178 of IBC ie firstly, cost & expense of Bankruptcy Trustee, secondly - workmen's dues for 24 months & secured creditors, thirdly - employees dues for 12 months, fourthly, govt dues and finally, all other debts including unsecured debt.

- *Insolvency & Bankruptcy Board of India (IBBI) is working on the fast implementation of Personal Insolvency (including Partnership firms)*
- *IBC code Part III already covers the Insolvency for Individual & Partnership firms.*
- *This involves Fresh Start Process and Individual Resolution process*
- *Fresh start process will then lead to Discharge*
- *Individual Resolution process will lead to either approved Repayment Plan or Bankruptcy*
- *Post this, discharge order is passed*

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- **Better credit market**
- **Lower cost of capital**
- **No coercion of individuals with social stigma**

The urge of resolving insolvency for the individual & partnership firms as per the IBC provisions, summarised above, has now become the need of an hour. This will immensely help a) the credit market including lower cost of capital and b) the borrowers can be out of the coercive collection practices followed by some of the creditors results in psychological trauma in the society.

Some of the issues, which needs an attention, will be ; a) how overloaded DRT can undertake additional load of personal insolvency, b) the FSP eligibility criteria - is it too low, c) IRP & Bankruptcy trustee cost - will individual/ partnership firms be able to bear which are already cash strapped d) FSP be an online process with no involvement of external parties ?

In summary, Personal Insolvency is going to bring paradigm shift in the society for its better evolvement.

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