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IBC DILUTING THE RIGHTS OF THE SECURED CREDITORS

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INSOLVENCY AND BANKRUPTCY CODE, 2016

The Insolvency and Bankruptcy Code (“**IBC**”) Bill has been passed by both the Houses of Parliament and has received the assent of the President on May 28, 2016. The IBC, *inter alia*, seeks to replace all existing laws related to bankruptcy resolution. This constitutes a vital transformation from the present system wherein multiple applicable laws were governing the insolvency and bankruptcy mechanism.

SECURITISATION AND RECONSTRUCTION OF FINANCIAL ASSETS AND ENFORCEMENT OF SECURITY INTEREST ACT, 2002

One of the existing laws dealing with the recovery of facilities / loans through enforcement of security interest is Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (“**SARFAESI**”), pursuant to which the security interest may be enforced by the secured creditors such as banks and financial institutions, without intervention of the Court.

IBC V/S. SARFAESI

Section 14(1)(c) of IBC states that on commencement of insolvency resolution process (“**IRP**”), the adjudicating authority shall, by order, declare moratorium period. Upon such order, all recovery proceedings get stayed including the enforcement of security under the SARFAESI Act.

It is pertinent to note that, once the insolvency resolution period ends, the entity will be either put on revival, or under liquidation. In case of revival orders, the eligibility of the lender to exercise SARFAESI powers will depend on what agreement has been made between the lenders in relation to revival of an entity. Upon a liquidation order being passed, the moratorium will be deemed to be lifted and the secured creditors may enforce their security interests under SARFAESI.

The stages of filing insolvency resolution process vis-à-vis SARFAESI is enumerated below:

1. **Application for insolvency resolution process filed but not admitted:** There will be no stay on SARFAESI proceedings.
2. **Admission of resolution application:** There will be stay on SARFAESI proceedings as may be ordered by the NCLT.

3. **Resolution plan ordered by Adjudicating Authority:** Pursuant to Section 31(1) of the Insolvency and Bankruptcy Code, 2016, the parties are bound to act in accordance with the resolution plan and terms specified therein.
4. **Commencement of liquidation proceedings:** There will be no stay and security interests may be enforced in accordance with Section 52 of the Insolvency and Bankruptcy Code, 2016.

In view of the above, the provisions of SARFAESI stand diluted to the extent mentioned above. It seems that the priority has been given to revival of the Company so that the interest of all the stakeholders could be protected. The Banks and Financial Institutions will not be allowed to take any action under SARFAESI, for enforcement of security, upon admission of the application for initiating the resolution process and until the period as may be decided by the NCLT.

The content of this article is intended to provide a general guide to the subject matter. Specialist advice should be sought about your specific circumstances.