

Cross-border Insolvency Resolution

“The lack of such regimes has often resulted in inadequate and uncoordinated approaches to cross-border insolvency that are not only unpredictable and time-consuming in their application, but lack both transparency and the tools necessary to address the disparities and, in some cases, conflicts that may occur between national laws and insolvency regimes. These factors have impeded the protection of the value of the assets of financially troubled businesses and hampered their rescue.”

United Nations Commission on International Trade Law

A sound and efficient insolvency regime is heralded as a key step towards fostering ‘Ease of Doing Business’, which in turn is important for attracting higher investments, development of competitive environment and innovations, and economic growth. It has a direct bearing on the efficient allocation of scarce resources in the economy. Recognising the need for development of a robust insolvency regime, India enacted the Insolvency and Bankruptcy Code (IBC / Code) in 2016. It reoriented its insolvency laws and marked a paradigm shift towards a time-bound legal mechanism financial distress resolution for individual and corporates. The Code, its subsequent amendments and evolving jurisprudence has contextualised and adopted global norms and best practices for insolvency resolution in India. Recognising the limitations of the ecosystem, which is evolving with time, gradualism underlines the ethos of ever evolving Code.

The requirement of a cross-border law has been felt during various insolvency proceedings initiated under the Code in India. The theme paper on the cross-border insolvency framework has been put out in the public domain for comments of stakeholders and the general public.

Existing provisions for cross border matters

The provisions of the IBC provides for cross-border insolvency cases through bilateral agreements and issuance of letters of request to foreign courts by Adjudicating Authorities (AAs) under section 234 and section 235. As suggested by the Insolvency Law Committee (ILC), this process is an ad-hoc framework that is susceptible to delays and uncertainty for creditors, debtors, and courts.¹ In this backdrop the ILC suggested the adoption of UNCITRAL Model Law (Model Law) with necessary modifications to suit the Indian context. The Model Law adopted by 50 countries covering 54 jurisdictions is a widely accepted legal framework for cross-border insolvency issues.² It is based on principles of (a) access to foreign and domestic courts by resolution professionals (RPs); (b) recognition of foreign proceedings; (c) co-operation between courts; and (d) co-ordination of two or more concurrent insolvency proceedings. The Model Law provides a broad framework, and it is left to individual jurisdictions to decide the operational details to suit their interests. The Draft Part Z incorporates elements from the Model Law to provide an effective mechanism for dealing with cross-border cases. The main objectives that the proposed cross-border framework aims to achieve are - firstly, co-operation between the AAs, RPs, Liquidators, corporate debtors (CDs), and other stakeholders. Second, it facilitates greater legal certainty for trade and investment. Third, the framework aims to create a fair and efficient administration of cross-border insolvencies that protects the interest of all stakeholders, and fourth, it aims to facilitate rescue of financially troubled businesses, thereby, protecting investment and employment.³

Imperatives for cross-border framework

The economic and financial imperatives for formulation of a cross-border

insolvency regime are many. The economic principle of allocative efficiency suggests releasing of idle resources for more productive uses. A cross-border framework that aims to minimise costs and value erosion of assets and improve gains from trade contributes significantly to overall growth prospects of the country. Several studies such as Williamson's Transaction Cost Economics (TCE) and Jason Jacks (2018)⁴ explore the benefits of cross-border insolvency regimes. The TCE theory suggests that an efficient cross-border insolvency regime results in lower co-ordination costs between creditors and courts, lower negotiation costs and reduces the overall uncertainty surrounding different laws in multiple jurisdictions. Jason Jack (2018) examines the relationship between foreign direct investment (FDI) and World Bank's Legal Rights Index. The Index measures the degree to which collateral and bankruptcy laws protect rights of creditors. The study concludes with a positive correlation between the Index and FDI levels. It suggests that strong legal mechanisms and institutions remove uncertainties and provide fertile grounds for greater investments. Such evidence strengthens the case for adoption of a cross-border regime in India.

India's increasing cross-border exposure

Several countries have adopted the Model Law to reap the benefits that flow from a cross-border insolvency regime. Increased interdependence of economies has increased international trade and investment levels. India's economic interaction with the rest of the world has been increasing over the last three decades since the start of liberalisation and more so with deepening of the financial markets. According to the World Investment Report 2021, overall FDI inflows to developing nations stood at \$663 billion and for the developed nations the levels were \$312 billion.⁵ Amidst the FDI inflows to developing nations, India received \$64 billion in FDI inflows in 2020 higher than the 2019 levels.⁶ India was the 5th largest host country for investments in 2020.⁷ About 27,801 Indian companies had FDI/ODI in their balance sheet & total flow of FDI (inwards and outwards) was ₹39,565 billion at the end of March, 2020.⁸ The inflow of FDI in India was largely driven by increase in mergers and acquisitions. Cross-border mergers surged 83 percent to \$27 billion with major deals involving ICT, health, infrastructure, and energy. Large transactions included the acquisition of Jio Platforms by Jaadhu (a subsidiary of Facebook, United States) for \$5.7 billion, the acquisition of Tower Infrastructure Trust by Brookfield (Canada) and GIC (Singapore) for \$3.7 billion and the sale of the electrical and automation division of Larsen & Toubro India for \$2.1 billion. Another megadeal – Unilever India's merger with GlaxoSmithKline Consumer Healthcare India (a subsidiary of GSK, United Kingdom) for \$4.6 billion – also contributed.⁹ India's financial sector is also increasingly interconnected globally with banks of Indian origin holding cross border positions of USD 168.4 billion in claims and USD 288.1 billion in liabilities by end of March 2021.¹⁰

With Indian businesses expanding operations across countries and with increasing financial market linkages, financing needs will also need to be met from resources across the world. Growing international trade is integrating domestic businesses into global value chains. This exposes the businesses to external influences and cross-border volatilities. Going forward, increasing cross-border interactions, in the form of shareholder-management, creditor-debtor, supplier-buyer, value chain partners, distributors etc., are expected to drive growth of corporates.¹¹ Inherent in growth prospects is also a possibility of failures and insolvencies with cross-border elements. This possibility will be inevitable, and India's insolvency regime requires cross border elements which is able to deal with the complexities these situations may present. Given this evidenced rise in cross-border cases and inherent risks, the time for a formal cross-border insolvency regime is imminent now.

Adoption of cross-border insolvency regime by India will further augment India's image as most improved jurisdiction in terms of insolvency resolution. It will be viewed as a progressive and forward-looking market reform by global investors and advanced jurisdictions. Through a formal framework, access and recognition of Indian proceedings will be easier in the jurisdictions that have already adopted the Model Law. The widespread and faster pace of adoption of Model Law by several important jurisdictions, including, United States of America, United Kingdom, Japan, Singapore, Brazil, South Africa and Mauritius, provides a strong basis for its adoption by India, tailoring and tweaking it to suit the requirement of the Indian jurisdiction.

Progress so far

The extant Indian insolvency law has at many instances dealt with insolvencies that involve cross-border elements. Lessons from such matters validate the need for a comprehensive cross-border insolvency

framework. Significant delays in procurement of data due to lack of co-ordination can be avoided if there are formal guidelines that set timelines, code of conduct, and facilitate greater communication. In the matter of SEL manufacturing, a CD undergoing insolvency proceedings in India, was able to access the assets in US due to co-operation extended to the RP by the US Bankruptcy Court. The professional has been granted rights, powers, protections, privileges, and immunities of a trustee in a bankruptcy in the US.¹² Another landmark precedent has been set in the matter of Jet Airways. The co-operation between the Dutch and Indian jurisdictions led to co-ordinated proceedings. This facilitated realisations in Netherlands and has been transferred to India. These matters are just a few examples of the possible benefits that can flow from a comprehensive framework for resolution of cross-border insolvencies.¹³

The proposed framework will govern all applications seeking recognition of foreign insolvency proceedings as well as applications from foreign jurisdictions seeking co-operation in Indian proceedings. An important addition to the recommendations made by ILC on the subject, it is being contemplated to make it applicable to personal guarantors (PGs) of the corporate persons as well.

The proposed cross-border framework has the potential to further strengthen India's insolvency laws. It will build capacity, empower the Insolvency Professionals (IPs) and creditors to access assets outside India, trace avoidance transactions having cross border implications, and achieve the core objective of value maximisation as envisioned by the IBC. With a rapidly transforming economy, comes the need for rapidly transforming institutions that support its growth. Once enacted, the cross-border framework will provide a robust, principle-based framework that Indian and foreign stakeholders can invoke to resolve cross border insolvency situations swiftly in a more efficient manner.

(Ravi Mital)

¹¹https://www.mca.gov.in/Ministry/pdf/CrossBorderInsolvencyReport_22102018.pdf p. 13

¹²https://uncitral.un.org/en/texts/insolvency/modellaw/cross-border_insolvency/status

¹³https://www.mca.gov.in/Ministry/pdf/CrossBorderInsolvencyReport_22102018.pdf P.50

¹⁴<https://scholarship.law.umn.edu/cgi/viewcontent.cgi?article=1286&context=mjil>

¹⁵https://unctad.org/system/files/official-document/wir2021_en.pdf p.22

¹⁶ibid p.23

¹⁷UNCTAD – World Investment Report, 2021

¹⁸Annual Census of Foreign Liabilities and Assets of Indian Direct Investment Companies, 2017-18, Reserve Bank of India.

¹⁹ibid p. 68

²⁰Bank of International Settlement as of end of March, 2021

²¹<https://ibbi.gov.in/uploads/resources/c3593c9f41984c6f31f278974de3cf37.pdf> p.5

²²<https://www.thehindubusinessline.com/opinion/a-cross-border-leap-for-insolvencyreforms/article37946459.ece>

²³<https://www.thehindubusinessline.com/opinion/a-cross-border-leap-for-insolvency-reforms/article37946459.ece>