

# Homebuyers under Insolvency and Bankruptcy Code(IBC)

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## **Manifest pedagogy:**

The real estate sector is of primary concern for lacs of homebuyers and key to transforming the economy. UPSC generally tends to look for analysis, provisions, bodies and laws governing the same be it IBC, RERA or steps taken by RBI and government to revive the sector

## **In news:**

- The Supreme Court recently upheld amendment in Insolvency and Bankruptcy Code (IBC) that gives homebuyers the status of financial creditors on par with lender banks

## **Placing it in syllabus:**

- Housing- Infrastructure

## **Static dimensions:**

- IBC
- IBC amendment bill, 2019
- RERA
- Delay in housing projects

## **Current dimensions:**

- Status of homebuyers
- Jaypee case and NBCC

## **Content:**

Recently a three-judge Bench led by Justice Rohinton Nariman

confirmed the constitutional validity of the Insolvency and Bankruptcy Code (Second Amendment) Act of August 2018, which gave home buyers the status of “financial creditors” with power to vote in the Committee of Creditors

### **Insolvency and Bankruptcy Code(IBC):**

The Insolvency and Bankruptcy Code, 2016 (IBC) is the bankruptcy law of India which seeks to consolidate the existing framework by creating a single law for insolvency and bankruptcy

### **Provisions:**

#### ***Resolution of Insolvency:***

The code lays down the separate insolvency resolving procedures for companies, individuals as well as partnership companies. It is possible to initiate the procedure either by the creditors or debtors. The insolvency resolution procedures must be fully completed in

- 180 days for company (can be stretched by 90 days)
- 90 days for start-ups , small organizations as well as other organizations (having less than Rs 1 crore worth of assets) ( can be stretched by 45 days)

#### ***Regulator of Insolvency:***

The Insolvency and Bankruptcy Board of India shall oversee the proceedings related to insolvency in the nation and also regulate all the organizations that have been registered by the board

#### ***Licensed Insolvency Professionals:***

The management of insolvency procedure shall be done by licensed insolvency professionals. They would also exercise control over the debtor's assets at the time of the insolvency procedure

### ***Insolvency and Bankruptcy Adjudicator:***

(i) the National Company Law Tribunal for organizations and Limited Liability Partnership companies;

(ii) the Debt Recovery Tribunal for overseeing insolvency resolution for individuals as well as partnership firms

### ***Procedure:***

- An insolvency plea is given to the authority that adjudicates (in corporate debtor's case it is NCLT) by operation of financial creditors or the corporate debtor.
- The plea can be accepted or rejected in a maximum time period of fourteen days.
- In case the plea gets acceptance then the tribunal appoints an IRP or Insolvency Resolution Professional for drafting a plan of resolution within a period of 180 days (that can be extended by ninety days).
- Following this, the court would initiate the process of resolving corporate insolvency.
- For that particular period, the company's directors shall remain suspended whereas the promoters shall have no say in the company management.
- The Insolvency Resolution Professional can seek the help of the management of the company for handling everyday operations
- In case the CIRP is unable to revive the organization, then the process of liquidation shall be initiated

### ***Amendments:***

Certain individuals are prohibited from providing any plan of resolution in case there are any defaults. Hence, wilful defaulters, management or promoters of company in case there is any non-performing outstanding debt for more than a year, as well as directors who have been disqualified cannot submit any plan. Apart from this, the bill also places a restriction

on the selling of a defaulter's property to any such individuals at the time of liquidation

### **IBC amendment bill, 2019:**

The Insolvency and Bankruptcy Code (Amendment) Bill, 2019 is passed by the parliament. The Bill amends the Insolvency and Bankruptcy Code, 2016. The Code provides a time-bound process for resolving insolvency in companies and among individuals

- Under the Code, a financial creditor may file an application before the National Company Law Tribunal (NCLT) for initiating the insolvency resolution process. The NCLT must find the existence of default within 14 days. Thereafter, a Committee of Creditors (CoC) consisting of financial creditors will be constituted for taking decisions regarding insolvency resolution.
- The CoC will appoint a resolution professional who will present a resolution plan to the CoC. The CoC must approve a resolution plan, and the resolution process must be completed within 180 days. ( can be extended by a period of up to 90 days).
- If the resolution plan is rejected by the CoC, the debtor will go into liquidation. The Code provides an order of priority for the distribution of assets in case of liquidation of the debtor. This **order places financial creditors ahead of operational creditors**. (In a 2018 Amendment, home-buyers who paid advances to a developer were to be considered as financial creditors. They would be represented by an insolvency professional appointed by NCLT).
- The **Bill addresses three issues:**

- 1) strengthens provisions related to time-limits.
- 2) specifies the minimum payouts to operational creditors in any resolution plan.
- 3) specifies the manner in which the representative of a

group of financial creditors (such as home-buyers) should vote.

- The amounts to be paid to the operational creditor should be the higher of: (i) amounts receivable under liquidation, and (ii) the amount receivable under a resolution plan, if such amounts were distributed under the same order of priority (as for liquidation). For example, if the default were for Rs 1,000 crore and the resolution professional recovered Rs 800 crore, the operational creditor must at least get an amount which they would have received if Rs 800 crore have been obtained through liquidation proceeds.
- Bill states that this provision would also apply to insolvency processes: (i) that have not been approved or rejected by the National Company Law Tribunal (NCLT), (ii) that have been appealed to the National Company Appellate Tribunal or Supreme Court, and (iii) where legal proceedings have been initiated in any court against the decision of the NCLT.
- In case the NCLT does not find the existence of default and has not passed an order within 14 days, it must record its reasons in writing.
- The resolution process must be completed within 330 days. This includes time for any extension granted and the time taken in legal proceedings in relation to the process. On the enactment of the Bill, if any case is pending for over 330 days, the Bill states it must be resolved within 90 days.
- The Code specifies that, in certain cases, such as when the debt is owed to a class of creditors beyond a specified number, the financial creditors will be represented on the committee of creditors by an authorised representative. The Bill states that such representative will vote on the basis of the decision taken by a majority of the voting shares of the creditors that they represent

## **Real Estate (Regulation and Development) Act (RERA):**

Its objective is to address grievances of buyers and to bring transparency and accountability in the country's real estate sector

### **Provisions:**

1. The developer can't make any changes to the plan without the written consent of the buyer. This provision will not allow the developer to increase the cost of their projects.
2. The law ensures that realty project is completed in time. If delayed, then the developer will have to pay interest on the amount paid by the buyer.
3. Registration is mandatory for all commercial and residential real estate projects where the land is over 500 square metres or includes eight apartments & which are under-construction.
4. Every phase of apartment will be considered a standalone real estate project, and separate registration needs to be obtained for each project.
5. It is compulsory for a state to establish a State Real Estate Regulatory Authority as per the new act. Buyers could approach this body for redressal of their grievances.
6. The property will have to be sold to buyers based on carpet area and not on super built-up area which will become illegal under the new law.
7. Failing to register a property will attract a penalty up to 10% of the project cost and a repeated violation could send the developer in jail.
8. The developer will have to place 70% of the money collected from a buyer in a separate escrow account to meet the construction cost of the project.
9. If the buyer finds any shortcomings in the project then buyer can contact the developer in writing within one year of taking possession.

10. The law has a provision of a maximum jail term of three years with or without a fine, for a developer who violates the order of the appellate tribunal of the RERA

### **Status of homebuyers:**

- *Insolvency and Bankruptcy Code (Second Amendment) Act of August 2018 has brought the home buyers on par with the creditor banks of the property builder.*
- Prior to the law, the assets of the bankrupt builder were divided among his employees, creditor banks and other operational creditors and home buyers were hardly figured.
- The Amendment Act allowed home buyers, as financial creditors, to trigger bankruptcy proceedings under the Insolvency and Bankruptcy Code of 2016 and have their “rightful place” on the Committee of Creditors (CoC).
- The IBC and the RERA operate in different spheres and can be used harmoniously for the interest of home buyers.
- The Supreme Court has reasoned that no home buyer would frivolously move the National Company Law Tribunal under the IBC because ironing out a resolution plan under the IBC is a long-drawn process



The experience of several homebuyers in terms of long delays and bad quality of construction has discouraged buyers, old and new, from investing in the real estate sector. According to a report by PropEquity, a Gurgaon-based real estate data, research and analytics firm, “total value of projects facing construction delays is above \$47 billion”.

The situation is worse in metro cities as compared to smaller ones. The worst part is that most of the units in delayed projects are already sold out. Projects are on hold for a variety of reasons including financial constraints, execution challenges, surplus supply due to over-ambitious launches by developers, environmental clearances and slowing sales.

The source of funds has dried up or funds are available at a high rate and that too only to select developers. Non-banking financial companies (NBFCs) are the only source of funds for developers at present and they too are very selective and cautious before lending money

Under-construction projects launched after RERA was enacted are relatively safer options. But besides a few states like Maharashtra and Uttar Pradesh, most states still don't have a fully functional website in place for homebuyers to verify information related to developers and projects. Homebuyers in these states should do proper due diligence about the developer and project before buying a home

### **Jaypee case and NBCC:**

- Jaiprakash Associates Limited (JAL) was the third largest cement manufacturer in the country with an annual capacity of 33 million tonnes.
- Jaypee Infratech (JIL), JAL's special purpose vehicle (SPV) and JAL announced as many as 27 real estate projects in 2007 period.
- Many non-residents, either returning to India or those remitting money invested in the projects.
- In 2012-13 when the real estate sector collapsed, the Noida region was the worst-hit.
- Banks curtailed lending and consumers withdrew.
- An adverse ruling in 2015 by the National Green Tribunal, banning all construction within a kilometre of the Okhla Bird Sanctuary, an area not far from Noida, further affected the situation.



- The November 2016 demonetization sucked the remaining life out of the informal sector, a key component of the real estate boom.
- The government enacted the IBC, 2016 to help lenders explore all options to recover their money within a time frame.
- JIL found its name in a list of 12 companies the Reserve Bank of India (RBI) had prepared and sent to the banks in June 2017 to invoke bankruptcy proceedings.
- Jaypee's bankruptcy case was unique as it affected not just the banks, but also around 26,000 homebuyers.
- RERA , an entity formed after Jaypee was admitted as a bankruptcy case, offered less hope to its stranded buyers.
- Now around 20,000 buyers are waiting for their dream home in one of the 12 projects that the Jaypee group planned to construct at its so-called "Wish Town" township.
- The apex court recently cancelled the licence of Amrapali Group and asked NBCC (India) Ltd to take over all its ongoing, unfinished housing projects and find a way to complete a slew of unfinished housing projects.
- This judgement has left a ray of hope in thousands of homebuyers who are stuck in the vicious cycle of real estate sector.
- Almost two years have passed by, since the National Company Law Appellate Tribunal ( NCLT) admitted the insolvency petition moved by IDBI Bank against JIL.
- On September 11, 2018, ICICI Bank had moved the NCLT against JAL over non-payment of Rs 1,200-crore dues.
- Launching action against the company liquidation because it could have jeopardised homebuyers' interest several buyers moved the Supreme Court (SC) against the IDBI Bank's move.
- In May 2018, the SC stayed the liquidation proceedings and asked the Jaypee promoters to deposit Rs 1,000 crore by June 15 to refund homebuyers.

- Later in July, the apex court reduced this amount to Rs 600 crore and said it would ask the NCLT to expedite the case and decide on revival or restructuring.
- Initially, Jaypee had planned to raise Rs 2,500 crore from the Yamuna Expressway project to refund buyers which did not work out.
- Plans of a takeover of the insolvency-hit company did not materialise.
- Jaypee offered to give 2,000 shares to each of its homebuyers and proposed to bear 50 per cent of stamp duty on first registration as part of the offer. This offer received a cold response.
- The sole winning moment for the affected homebuyers so far has been the awarding of 'financial creditors' in insolvency proceedings through an amendment in the Insolvency and Bankruptcy Code (Second Amendment) Bill, 2018,
- The NCLAT, on July 30, 2019, extended the insolvency period of JIL by another 90 days.
- This allows fresh bids to be submitted during this time. Of the 90 days, 45 days would be used to finalise new bids, while the remaining period will be used to weed out any discrepancies that may occur.
- All the previous bids stand invalid hereafter and will be considered, only if the bidders submit fresh plans. JIL's parent company, JAL will not be allowed to submit a fresh bid.
- Earlier in March 2019, state-owned NBCC had shown interest to monetise Jaypee's assets and had assured the homebuyers that it will deliver these projects in three years.
- However, NBCC's bid was later rejected by the Committee of Creditors (CoC).
- In its revised offer, now NBCC has proposed infusion of Rs 200 crore equity capital, transfer of 950 acres of land worth Rs 5,000 crore to banks and completing construction of flats by July 2023.

- As many as 13 banks and over 23,000 homebuyers have voting rights in the CoC of JIL.
- For approval of any resolution plan, at least 66 per cent votes should be in favour of NBCC