CROSS BORDER INSOLVENCY

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ABSTRACT

We are in a decade in which the markets are blooming and thriving globally which has resulted in the interconnectivity and interdependency between the economies of all the countries. With this being the outcome of globalization, there has also been an increase in the commercial transactions at an international level which means that the corporate debtors of a country are not only dependent on creditors of their home country but they are also dependent on the creditors of various other jurisdictions. Similarly, the foreign creditors also look forward to make investments not only in their own countries but also at an international level. Therefore, due to the ongoing current scenarios, the responsibility of safeguarding the rights of the corporate debtors so that the multiplicity of insolvency proceedings can be avoided against it and the rights of both the home/ foreign creditors rests upon the laws of all the countries including India, which, even though has more or less like a skeleton of cross border insolvency laws incorporated in its legal regime but the same is not sufficient to fulfil the responsibility that it has towards the abovementioned categories.

With this research paper, the aim is to understand the concept of cross border insolvency along with the various laws which have been incorporated in India regarding the same, the deficiencies which are still prevailing in our legal system, thus making the Indian economy handicapped when it comes to such issues and also as to how the polarity between the current trends relating to international insolvency across the globe and our nation can be covered.

Keywords: cross border insolvency, creditors, insolvency proceedings, corporate debtor

INTRODUCTION

India is a nation which is developing at a full tilt and which has opened up its economy at an international level to the foreign creditors for the purpose of investment and at the same time various Indian investors/ corporates are also making investments in the foreign companies or companies which have its assets located outside India, because of which it requires a detailed framework/regulations so as to protect the investors in case insolvency proceedings are initiated against such companies.

While under the Insolvency and Bankruptcy Code, 2016 (hereinafter referred to as "IBC"), Sections 234 and 235 provides for the provisions relating to insolvency at an international echelon, yet these two sections do not provide for a definite structure and acts only as an enabling provision for the same, thus making the efficacy of IBC debatable.

MEANING

Though the definition for international insolvency or cross border insolvency has not been provided for in the IBC, but conventionally it may be comprehended as insolvency of those debtors who have their assets/creditors in numerous jurisdictions, or are exposed to insolvency process in multiple jurisdictions. That being the case, the threefold characteristics of cross border insolvency are as follows -

i) Despite the fact that the foreign creditors of an insolvent company are not in the same country in which the insolvency process has been initiated they want their claim against that company to be protected.
ii) Assets of a company which is insolvent may have been located in a different jurisdiction which the creditor of that insolvent company may ingress as part of the insolvency process.
iii) The process of insolvency of a corporate debtor may have been initiated and continued in multiple countries.

HISTORICAL BACKGROUND

As far as laws relating to cross-border insolvency are concerned, under the regime of The Companies Act, 2013 (hereinafter referred to as the "Act"), "foreign companies" which have been defined under Section 2(42) of the Act were considered to be an unregistered company

for the purpose of winding up by an order of the court under Section 376 of Part II of Chapter XXI of the Act. Further, sub-section (2) of Section 391 of the Act clearly states that the provisions of Chapter XX shall apply mutatis mutandis, subject to Section 376 of the Act, for the purpose of closure/ winding up of the place of business of a foreign company in India. However, no specific procedure or provisions have been laid down by the legislature for the winding up or initiation of insolvency process of an Indian company whose assets are located outside India or in multiple jurisdictions and the same is dependent on the mere recognition of the foreign judgement or decree of any superior court of a reciprocating territory as passed by the Indian district court for the purpose of execution under Section 44A of the Code of Civil Procedure, 1908 (hereinafter referred to as "CPC"). This also resulted in creating difficulties for the resolution professionals and liquidators in assessing the assets of a corporate debtor as insolvency process or winding up proceeding could be initiated against the assets of a corporate debtor in any jurisdiction outside India where the assets of the same were located.

The abovementioned problem was first recognized in the Justice V. Balakrishna Eradi Committee i.e., The Report of the High Level Committee on Law Relating to Insolvency and Winding Up of Companies, 2000, which recommended that "The United Nations Commission on International Trade Law (hereinafter referred to as the "UNCITRAL") Model Law on Cross-Border Insolvency" as adopted by the United Nations General Assembly Resolution 52/158 dated 15th December, 1997, should be implemented by India after making suitable amendments to the same as India is a member of the United Nation and doing the same would result in facilitating the International trade. The Justice V. Balakrishna Eradi Committee also opined that amendments should be made to Part VII of the Companies Act, 1956 so as to correspond with the UNCITRAL Model Law on Cross-Border Insolvency and the same should be incorporated as a Schedule to the Companies Act, 1956, which shall thus apply to all cases of cross border insolvency.

It was in Dr. N.L. Mitra Committee i.e., the Report of The Advisory Group on Bankruptcy Laws that laid down detailed analysis regarding the exigency of cross border insolvency laws and also recognized the fact that insolvency laws of India have become out dated as they are not akin to the standards of international legal requirement and that cross-border relations have not been contemplated. It was observed by this Committee that trade, investment, commerce and industries at an international level are growing swiftly which has resulted in

setting the momentum of globalization and because the economies of the nations have also opened – up, the same has added to the necessity of a legal regime to provide protection to both foreign creditors and Indian creditors. While giving its final recommendations, the Dr. N.L. Mitra Committee propounded that to assimilate the laws or provisions relating to cross border insolvency or claims, there is a requirement of comprehensive bankruptcy code and it also recommended that principles on international insolvency should also be contrived in various matters which were enumerated by this Committee in its Report like granting relief on acknowledgement of foreign proceedings; participation of foreign representatives and access, notification to foreign creditors in relation to proceedings which have been initiated as per the laws of India; Protection being provided to creditors etc. Furthermore, this Committee also recapitulated the incorporation of the UNCITRAL Model Law on Cross-Border Insolvency in the laws of India.

While the abovementioned two Committees recognised and accentuated in detail the need for laws pertaining to insolvency at an international echelon, yet The Report of the Bankruptcy Law Reforms Committee, which was the foundation of IBC, bypassed this issue and proclaimed that the same would be dealt in its deliberations at the next stage.

THREEFOLD CHARACTERISTIC OF CROSS BORDER INSOLVENCY

The threefold characteristics as touched upon above is explained and discussed as follows –

1. **Foreign creditors of an insolvent company are not in the same country in which the insolvency process has been initiated, nevertheless, they want their claim against that company to be protected.**

   Section 3(23) of the IBC includes in the definition of "person" those persons who are resident outside India, which means that there is no differentiation or prejudice made between the domestic creditors and foreign creditors because of which under Section 5(7) and Section 5(20) which provides for the definition of "financial creditor" and "operational creditor" respectively, the foreign creditors are also included in the same, as the case may be, and can initiate Corporate Insolvency Resolution Process (hereinafter referred to as "CIRP") against a corporate debtor.

2. **Assets of a company which is insolvent may have been located in a different jurisdiction which the creditor of that insolvent company may ingress as part of the insolvency process.**
3. **The process of insolvency of a corporate debtor may have been initiated and continuing in multiple countries.**

These two characteristics have been dealt with under Section 234 and Section 235 of the IBC which became enforceable with effect from 1st April, 2017. Section 234 pertains to the Central Government entering into an agreement with the foreign countries with the purpose of enforcing the provisions of IBC, while Section 235 provides for a letter of request which may be issued by the Adjudicating Authority to a foreign court or authority which is competent to succour in the condition wherein the assets of the corporate debtor or debtor, as the case may be, are situated at any place in a country which is outside India.

IRIT MEVORACH'S TRI-THEORIES

Irit Mevorach in his book 'The Future of Cross-Border Insolvency: Overcoming Biases and Closing Gaps' has discussed three theories on the basis of which the cross border insolvency is woven and these are -

1. Theory of Universalism
2. Theory of Territorialism
3. Theory of Modified Universalism

1. Theory of Universalism

This theory states that the assets and liabilities of a debtor on a global basis should be orchestrated by a single forum by implementing a single licit regimen. This entails that the assets or properties of a debtor which are located in any of the jurisdiction across the globe are to be dealt solely by one court i.e., by setting up an international court for insolvency and bankruptcy and by applying a single law relating to insolvency and such proceedings undertaken by the court shall have a universal effect over all such assets or properties of the debtor. Thus, it means that all the matters, questions and decisions ranging from how the claim of the creditors is to be treated, to management and dissemination of the asset etc, has to be tackled and decided upon in a single proceeding which shall be applicable in all the jurisdictions where the assets

of the corporate debtor are stationed. The principle based on unity basically envisages that there will be a convention which will be applicable internationally and that it will create a system of unification of cross border insolvency.

2. **Theory of Territorialism**

Contrary to the theory of Universalism is the theory of Territorialism which states that the assets of a debtor are opened up to numerous proceedings in various nations which therefore means that the superintendence of insolvency of the debtor is bifurcated. This theory is incarcerated to the concept of sovereignty of the state which basically means all the sovereign states are independent of each other and that the laws of one sovereign state cannot have an impact on other sovereign states. Thus, if the insolvency process is initiated in one state it will have effect only on the assets of the debtor which are located in that particular state and the same shall not have any effect which is extraterritorial in nature. Furthermore, according to the principle of plurality, different nations can take autonomous action in accordance to their legal regimen by initiating the insolvency process against the assets of the debtor which fall under their jurisdictions, thus, paying no heed towards the proceedings of other foreign countries which have been instituted in contra to the same debtor.

3. **Theory of Modified Universalism**

Unlike the theory of Universalism which is impractical and unrealistic in nature, the theory of Modified Universalism has a rational essence to it even though the same has metamorphosed from the theory of Universalism. While being in conformity to the principle of universality which is the most quintessential theory, this theory acts as a pro tem solution as the theory of Universalism is not attainable as per the present scenario because it requires the insolvency process of every nation to mutate into an international insolvency process which is practically unattainable as the laws of all the countries are influenced by various factors which are uniquely identifiable to that particular country only. In the Modified Universalism theory, it is the Private International Law which is utilised, as in case of cosmopolitan default, the sovereign states are deprived of domination as they need to work side by side and be adaptable with the courts of those jurisdictions in which the chief insolvency proceeding is taking place, thus, fulfilling the raison d'être behind this theory.

With this theory not requiring the establishment of an international forum which would deal with all matters relating to insolvency in case of universal default, it places more reliance on those domestic courts and tribunals of a country within whose jurisdiction the principal business activities took place and therefore such courts will administer all the matters relating to the same.

Another prerequisite of the theory of Modified Universalism is the need of recognition i.e., the proceedings, decrees, decisions or the course of action which is undertaken by the courts or tribunals of the host country should be recognised, accepted and enforced by the courts of other countries as well. Thus, this theory is a combination of both the theory of Universalism and the theory of Territorialism because while the courts of one country initiate the primary insolvency process, the courts of another country initiate the auxiliary process so as to recognise and assist the primary insolvency process.

UNCITRAL MODEL LAW ON CROSS-BORDER INSOLVENCY

It is interesting to note that the UNCITRAL Model Law on Cross-Border Insolvency also espouses the theory of Modified Universalism as it is established on the fundamentals of:

1. **Access** – Direct ingress to the courts and tribunals at the domestic level is given to the foreign creditors and insolvency professionals. Furthermore, they are also allowed to set the ball of insolvency process rolling and can also take part in the proceedings relating to the same. Even in the IBC, the foreign creditors are given this right but the same has not been provided to the foreign insolvency resolution professionals.

   Article 9 of Chapter II of the same is the provision pertaining to right to access a court directly in a state which has incorporated the UNCITRAL Model Law on Cross-Border Insolvency as a part of its laws. This Article has been integrated as it is in the laws of United Kingdom and Singapore but certain modifications to the same has been made by The United States of America.

2. **Recognition** –The UNCITRAL Model Law on Cross-Border Insolvency permits that if the insolvency process which is undertaken by a foreign county is a main proceeding [in case the centre of main interest (hereinafter referred to as "COMI") of the corporate debtor is in that foreign country] or non – main proceeding (if the corporate debtor has his business or premises in that foreign country), then the same shall be recognised by the domestic country.
   Chapter III of the UNCITRAL Model Law on Cross-Border Insolvency deals with all the provisions which are in relation to recognising a foreign insolvency process.

3. **Cooperation –** Cooperation between the courts which are established both at the domestic and foreign level as well as between the domestic insolvency resolution professionals or domestic representatives and foreign insolvency resolution professionals or foreign representatives is an indispensable element of the UNCITRAL Model Law on Cross-Border Insolvency. Similarly, transmission of information to the courts established abroad and to foreign representatives is also an essential component of cooperation.
   Chapter IV of the same removes the disparity which can be seen in the laws of various countries as it gives the right to the courts to offer cooperation in respect of all the areas which are comprised in the UNCITRAL Model Law on Cross-Border Insolvency.

4. **Coordination –** By stimulating cooperation between both the domestic and foreign courts as well as between the domestic and foreign insolvency resolution professionals, the UNCITRAL Model Law on Cross-Border Insolvency also encourages cooperation between the parallel insolvency processes which may have been initiated by the courts which are set up at domestic and foreign echelon and the same is dealt in **Chapter V** of the same.

CONCLUSION

As of 2018, the UNCITRAL Model Law on Cross-Border Insolvency has been adopted by 46 states in 48 jurisdictions[2], yet even after various suggestions and proposals by the numerous committees like the Justice V. Balakrishna Eradi Committee and the Dr. N.L. Mitra Committee which enunciated the urgency behind enacting a legislation to deal with the issue of cross border insolvency or international insolvency, till date, there is no such legal regimen which would resolve and facilitate this lacuna which is currently present in the Indian legal system, thus affecting the overall economic activity and growth of the nation as it severely impacts the minds of both the foreign creditors investing in India as well as the Indian creditors or corporates who are investing in companies/ corporate debtors who have their assets located abroad or outside India.

While the Indian laws are based on the theory of Territorialism or principle of pluralism, there is a need to adopt the theory of Modified Universalism which has also been incorporated in the UNCITRAL Model Law on Cross-Border Insolvency as the same harmonises and protects the sovereignty of a state and at the same time it also makes a state more pliable and receptive towards the foreign insolvency resolution process. This is because the theory of Modified Universalism grates a hybrid nexus between the duplet theories i.e., the theory of Universalism and Territorialism. Thus, by adopting this theory or the UNCITRAL Model Law on Cross-Border Insolvency (by incorporating it as it is or after making certain modifications to it), it would be suffice to cover the gap which is prevalent between the economic need and the laws of our nation.

[2]https://uncitral.un.org/en/texts/insolvency/modellaw/cross-border_insolvency/status