

# IBBI plans to reinforce creditors' rights over personal guarantors

**BRINGING CLARITY.** Regulator issues discussion paper; seeks public comments by July 10

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New Delhi

The Insolvency and Bankruptcy Board of India proposes to make it unequivocally clear that the submission or approval of a resolution plan for a corporate debtor under the IBC does not automatically release guarantors from their liability to repay the debt.

The IBBI now seeks to amend its CIRP regulations to ensure that submitting a resolution plan does not prevent creditors from enforcing their rights against the personal guarantor. Insolvency law experts said the IBBI's plan is likely to provide legislative clarity, strengthen creditors' position, and boost recoveries from personal guarantors.

The IBBI has released a discussion paper addressing, among other things, the "release of guarantees in a resolution plan." The last date for public comments through electronic mode is July 10, IBBI has said.

## SC APPROACH

To clarify that approving a resolution plan does not auto-

## BOLSTERING RECOVERY

- The IBBI follows the SC's judgment which upheld that a resolution plan does not absolve personal guarantors of their obligations
- Legal experts believe the regulator's proposal will provide legislative clarity and strengthen creditors' positions, leading to better recovery from personal guarantors
- The proposed amendment is seen as reinforcing the sanctity of contractual obligations and improving the credit recovery process



matically discharge a personal guarantor's liabilities from an independent contract, the IBBI has followed the Supreme Court's approach in *Lalit Kumar Jain vs Union of India*.

In the *Lalit Kumar Jain vs Union of India* judgment, the Supreme Court upheld the November 15, 2019, MCA notification enforcing the IBC's provisions on personal guarantors' insolvency.

The court also ruled that approving a resolution plan does not absolve personal guarantors from their obligations or extinguish their liability.

## EXPERTS' TAKE

Sushmita Gandhi, Partner, INDUSLAW, said the case of *Lalit Kumar* is one of the many instances where judicial interpretation bridged the lacuna in the IBC, which is still a nascent law.

"The proposal indicates that the IBBI is cognizant of such gaps and is attempting to bridge the same to avoid ambiguity relating to the position of release of guarantees," she added.

Misha, Partner, Shardul Amarchand Mangaldas & Co., said the language of the proposed amendment raises concerns. "On a plain reading, it

suggests that a resolution plan cannot prevent creditors from enforcing their rights against the guarantors of the corporate debtor. This should not be the case where the creditors have agreed to discharge the guarantor along with the corporate debtor," she said.

Hari Hara Mishra, CEO of the Association of ARCs in India, said the IBBI proposal, if implemented, will be a shot in the arm for creditors and a boost to improve recovery from the enforcement of guarantees. "This will reinforce the sanctity of contractual obligations, the backbone of a robust framework of credit culture," he said.

Sumit Khanna, Partner, Deloitte India, said, "By prohibiting resolution applicants from extinguishing guarantees, this change strengthens creditors' positions, promising a more efficient recovery process. With creditors recovering close to 2 per cent of claims from PGs, this amendment is crucial for bolstering recovery."

Vishwas Panjiar, Partner, Nangia Andersen in India, said personal guarantors remain liable for the guarantees they have provided.

# Insolvency rules target guarantors

**R. SURYAMURTHY**

**New Delhi:** The Insolvency and Bankruptcy Board of India (IBBI) has come down hard on personal guarantors in its proposals to reform the resolution process, while it gave more powers to the resolution professional and eased the procedures for MSMEs.

The reform package is meant to bolster creditor rights and expedite corporate insolvency resolutions.

The centrepiece of the package is the clampdown on personal guarantors (PGs) of distressed companies, addressing a critical loophole in the existing framework.

Prior to the proposed changes, a worrying trend had emerged: resolution plans for insolvent firms were increasingly incorporating the release of personal guarantees, effectively allowing PGs to escape their financial obligations despite the company's default.

This lacuna in the system is underscored by the dismal recovery rate of merely 2.16 per cent for creditors from PGs under the Insolvency and Bankruptcy Code (IBC), according to the IBBI.

Seeking to bridge this gap and strengthen the CIRP process, the IBBI has invited stakeholder feedback by July 10 on a series of proposals.

The cornerstone of the reforms is the proposal to ensure creditors retain the right to pursue PGs for their dues even after a resolution plan is approved.

This aligns with a recent landmark Supreme Court judgment in the case of Lalit Kumar Jain vs. Union of India. The court decisively clarified that the approval of a resolution plan does not automatically absolve guarantors from their liabilities.

"Instances where resolution plans have been approved for the release of personal guarantees without the con-

## MAJOR REFORMS PROPOSED

- Creditors need to have the right to pursue personal guarantors after approval of resolution process
- Resolution plans have earlier released personal guarantees, without creditor consent. Personal guarantors escaped their obligations despite default by company
- The practice undermined

sent of the bank or creditor holding such guarantee or securities, highlight a significant divergence from the Supreme Court's position," said Mukesh Chand, senior counsel at Economic Laws Practice.

"Such actions jeopardise the sanctity of the credit evaluation process, which relies heavily on personal guarantees and collateral securities. The release of these securities should not be subjected to the

the principal of collateral security.

■ Insolvency professionals need to attend meetings of committee of creditors from a very early stage

■ In MSMEs, with stressed assets of less than ₹ 1,000cr, one valuer can be appointed for valuation, expediting the resolution process

majority decision of the Committee of Creditors (CoC) but should solely be at the discretion of the relevant creditor or bank," he said.

Another key proposal concerns the appointment of insolvency professionals (IPs). Under the revised framework, IP chosen by the highest-ranked financial creditor will be able to attend meetings of the Committee of Creditors (CoC) at an earlier stage. This

facilitates more effective participation by creditors in the CIRP process, ensuring their voices are heard throughout the resolution journey.

For stressed micro, small and medium enterprises (MSMEs) with liabilities under ₹1,000 crore, the IBBI proposes streamlining the valuation process.

Currently, two or three registered valuers are required to assess fair and liquidation values. The new proposal suggests appointing only one valuer, thereby reducing costs and expediting the resolution process for smaller companies.

Legal experts have lauded the IBBI's reform package. Sushmita Gandhi, partner at Induslaw, emphasises the alignment of the reforms with the Lalit Kumar Jain vs. Union of India case. "The case of Lalit Kumar is one of the many instances where judicial interpretation bridged the lacuna in the Code which is still

a nascent law," she said. "The proposal indicates that the IBBI is cognisant of such gaps and is attempting to bridge the same to avoid ambiguity relating to the position of release of guarantees."

Vishwas Panjari, partner at Nangia Andersen India, expects the reforms to usher in a stricter regime for guarantors.

"As a result, personal guarantors remain liable for the guarantees they have provided," he said. "This underscores the importance for personal guarantors to thoroughly assess the financial health and risks associated with the debtors for whom they are considering offering guarantees."

Sukrit Kapoor, partner at King Stubb & Kasiva, said the reforms were a positive step. "This is another nail in the coffin for the guarantors in the cat-and-mouse game that personal guarantors have been playing with lenders since the introduction of the Code," he said.