

Personal Guarantors and the Indian Insolvency and Bankruptcy Code

Adam Feibelman^Y

Introduction

Cases involving personal guarantors of corporate debt have recently become an important and complicated feature of the still-new Indian insolvency and bankruptcy system. India adopted a comprehensive Insolvency and Bankruptcy Code in 2016, which includes chapters for both corporate and individual debtors. The provisions for corporate debtors went into effect immediately, and since then, over 7,000 cases involving corporate debtors have been admitted.¹ The corporate insolvency and bankruptcy system has become a significant and growing component of the country's legal landscape and its economy. The government has not yet generally put the provisions for individual debtors into effect.

The creation and design of the Insolvency and Bankruptcy Code was heavily focused on the goal of increasing creditors recoveries from insolvent firms. While government officials and regulators in the insolvency and bankruptcy system have recently begun emphasizing the goal of rescuing and restructuring firms,² the system was designed primarily as a creditor's remedy. It was enacted against a backdrop of a legal system in which it is notoriously difficult to enforce contractual and financial obligations, especially unsecured debt. Thus, most cases in the system are involuntary, *i.e.*, creditor initiated. The path for survival of debtor firms in the system is relatively narrow, and most are effectively auctioned off to new owners and managers. The primary measure of success of the system continues to be how much creditors recovered from their debtor firms, either within the system or under its shadow.³

Substantial amounts of the claims against debtor firms in the insolvency and bankruptcy system were guaranteed by their owners, managers, and officers. Such personal guarantees by promoters and owners of firms in India are a crucial aspect of corporate finance in the country. After a few years, policymakers determined that these guarantees were an important potential source of recovery for debtor firms' creditors. They may also have been motivated by public concerns that some high-profile owners of failed firms in the country were perceived to be escaping responsibility for those failures. But creditors face the same challenges in enforcing such guarantors through the general legal system as they do in enforcing the underlying corporate debt. So the government

^Y Sumter D. Marks Professor of Law, Tulane University. Thanks for comments and conversation to Karan Gulati, Chitrakshi Jain, Renuka Sane, and Anjali Sharma. Comments welcome: afeibelm@tulane.edu.

¹ IBBI, Quarterly Newsletter, April-June 2024, at 11, <https://ibbi.gov.in/uploads/publication/9bc46bf1e4b86dab3b0310cb8284cb74.pdf>.

² See, e.g., IBBI, Annual Report 2020-21, *Chairperson's Statement*, at 1, <https://ibbi.gov.in/uploads/publication/290a3e0f6b5a0318e2a75282fe262d1c.pdf>

³ IBBI, Annual Report 2022-23, *Chairperson's Statement*, at 2, <https://ibbi.gov.in/uploads/publication/78358f458f7d24e182b28fa2fef55d9a.pdf> (“As a percentage of admitted claims, realisation by creditors has increased to 36% in 2022-23. Overall, resolution plans have yielded 169% of liquidation value and 84% of fair value for creditors.”). “One of the salient achievements of the Code has been the credit discipline instilled by it amongst the debtors by way of a behavioral nudge. Thousands of debtors are settling their dues even before admission of CIRP under the Code.” *Id.*

decided to employ the Insolvency and Bankruptcy Code to enforce personal guarantees of claims against firms that were debtors under the Code.

Because the guarantors are individuals and not firms, this required putting the personal insolvency and bankruptcy provisions of the Code into effect for that particular group of debtors, which the government did in November 2019.⁴ Since then, over 3,000 applications involving personal guarantors have been filed, and approximately 450 have been admitted by the adjudicating tribunal, the National Company Law Tribunal.⁵ As with any personal guarantee for a corporate debtor, these cases have two crucial dimensions – one affecting the recoveries of creditors of the firm and the other affecting the personal finances of the guarantor. Thus, these cases are a test for both the corporate and personal insolvency and bankruptcy systems under the IBC and will likely influence the development of both.

The stakes are particularly high for the latter. Among other things, these cases could potentially create a template for the operation of the personal insolvency system more generally. Unfortunately, we have only limited information about these cases that might shed light on the patterns that are emerging from them. The public information about the operation of the IBC for personal guarantors is mostly limited to 26 cases (of the 3,000 filed and 450 admitted), in which an order accepting a repayment plan has been entered. Information about cases in which a proposed repayment plan was rejected, including the details of the proposed plan or the reason for rejection, is not available.

But this small handful of orders approving repayment plans for personal guarantors are a peak into the operation of the IBC for this category of debtor. They suggest, preliminarily, that recoveries against personal guarantors are very modest and perhaps unlikely in a significant number of cases. And most of those recoveries come from real estate assets pledged as security or from funds given voluntarily by the debtor's friends or family. If these circumstances represent systemic features of cases involving personal guarantors, this strongly indicates that the Insolvency and Bankruptcy Code will not be a good tool for significantly increasing the recoveries of creditors to insolvent corporate firms. They do highlight one potential weakness in the legal framework – the personal insolvency regime may effectively insulate fraudulent and preferential transfers. If so, addressing this weakness should be considered as a potential reform, which could significantly alter the function of the insolvency system for personal guarantors.

Furthermore, these cases do not appear to be good candidates for serving as a template for broader application of the personal insolvency and bankruptcy provisions of the Code. These cases involve mostly secured claims, dominant financial creditors, and individual debtors with substantial property holdings or other resources. The broader category of personal insolvencies will likely involve substantially more unsecured claims, and many debtors who have far fewer assets and who cannot rely on voluntary assistance from friends and family. They will likely have a broader array of creditors and types of creditors, and will be more likely to need to fund their repayment plans with future income.

Even if this first generation of cases involving personal guarantors could provide an opportunity to think systematically about the potential operation of the personal insolvency system, that does not seem to be the approach that policymakers are taking. Rather, these cases appear to be proceeding ad hoc and piecemeal.

⁴ https://www.mca.gov.in/Ministry/pdf/Notification_18112019.pdf

⁵ IBBI, Quarterly Newsletter, April-June 2024, *supra*, at 24.

This article proceeds as follows: Part I provides a brief summary of India's Insolvency and Bankruptcy Code, including the goals that policymakers had in creating it and how those goals are reflected in its design. Part II describes the role of personal guarantees for corporate finance in the Indian economy as well as legal enforcement challenges that limit this role. Part III examines the extension of the Code to guarantors, summarizing the formal legal development. Part III then reports on the experience of cases involving personal guarantors under system thus far and addresses preliminary insights about these cases along with issues and questions they involve and raise.

I. The Code and System

The Indian Insolvency and Bankruptcy Code was enacted by the Indian Parliament in May of 2016 after a very expedited process of design and debate that began roughly 18 months earlier.⁶ There were two main motivations for adopting the Code, one acute and specific and the other more general.⁷ The acute motivation was to provide a mechanism for dealing with huge and long-standing non-performing loans in the Indian banking system. Adopting the Code provided a way to force the debtor firms responsible for these non-performing loans into a resolution process and to cause the creditor banks to finally realize their losses, viewed then as a prerequisite to recapitalizing the banking system. The broader motivation for adopting the Code and that guided its design, was to improve the prospects for enforcement of corporate debt in the Indian economy, to promote both domestic financial markets and foreign investments.⁸

As initially designed, rescuing and restructuring firms with net going concern value was, at most, a secondary concern. As described below, the system was primarily designed to be a creditor's tool or remedy to improve recoveries from debtors in financial distress. In recent years, policymakers in India have refocused the system somewhat to emphasize the goal of the saving firms. But this shift has only led to reforms on the margins of the system and not to its core design or functioning.

A. System for Corporate Debtors

The Code created a new insolvency and bankruptcy system for commercial debtors with a landscape comprised of existing and new institutional actors. These include a new regulatory entity, the Insolvency and Bankruptcy Board of India; the existing National Company Law Tribunals and judges; newly created resolution professionals; and new information utilities, which record information about the status of private obligations and defaults.

Both debtor firms and creditors are authorized to initiate corporate insolvency cases under the Code by filing an application if the debtor has defaulted on a debt of at least 100,000 rupees (approximately \$1,200). Of the roughly 7,800 corporate insolvency cases initiated since the Code went into effect, approximately 460 of those were initiated by the corporate debtor – most are filed

⁶ Adam Feibelman, *Legal Shock or False Start? The Uncertain Future of India's New Consumer Insolvency and Bankruptcy Regime*, 93 AM. BANKR. L.J. 429, 435-36 (2019).

⁷ *Id.* at 457-58.

⁸ *Report of the Bankruptcy Law Reforms Committee Volume 1: Rationale and Design*, INDIA DEP'T OF ECON. AFF., Executive Summary (Nov. 2015), https://ibbi.gov.in/BLRCReportVol1_04112015.pdf.

by the firms' creditors.⁹ Upon filing of the application, a broad moratorium on legal actions against the debtor is automatically initiated, and an interim resolution professional proposed by the applicant is appointed to the case. The resolution professional then appoints a committee of "financial creditors," which in turn approves or replaces that resolution profession. Resolution professionals take over management of the corporate debtors.

Resolution professionals prepare information memoranda about the debtors' financial affairs, based on which bidders can propose resolution plans. In most circumstances, owners of the debtors are prohibited from proposing a plan. The committee of financial creditors then votes among proposed plans and can approve one based on a 75% majority. The plan must protect the claims of "operational creditors." This process is supposed to be concluded within 180 days, but many cases to date have taken much longer. If the committee approves a plan, it must be reviewed for consistency with statutory requirements and approved by the Tribunal.

Cases are generally resolved by auctioning off firms through a resolution plan or liquidating them. The adjudicating tribunal will initiate liquidation proceedings for the debtor if the creditors committee chooses this option, or if they do not approve a resolution plan, or if the Tribunal does not approve the plan selected by the creditors. Of the 7,800 corporate insolvency cases initiated under the Code since 2016, 2,500 of these have ended up in liquidation.¹⁰ And 1,100 of the total initiated cases have been withdrawn, approximately three-quarters of these withdrawals were due to settlement with one or more creditors.¹¹ Finally, under certain circumstances – *e.g.*, if the debtor can pay its debts in full – the debtor can opt to pursue a voluntary liquidation. To date, there have been approximately 1940 of these cases initiated, 36 of which have been withdrawn.¹²

Since the inception of the Code, recoveries to creditors under resolution plans that have been approved is approximately 32% of their claims, which the IBBI estimates is 162% greater than the liquidation value of the assets of the debtors firms involved.¹³ Total recoveries in liquidation have been low, but that is largely because most of the firms in liquidation (1959) were firms that had been in distress before the Code was enacted, many of which were effectively zombie firms.¹⁴

The Central Government created a "pre-packaged" insolvency process for small enterprises during the Covid pandemic.¹⁵ It is different than the general insolvency process in a number of important respects. It allows debtors and creditors to agree on a resolution plan before filing, for the debtor firm to continue managing its own affairs, and for owners of the firm to have the opportunity to continue as owners of the restructured firm by submitting their own resolution plans

⁹ IBBI, Quarterly Newsletter, April-June 2024, *supra*, at 12.

¹⁰ IBBI, Quarterly Newsletter, April-June 2024, *supra*, at 14.

¹¹ IBBI, Quarterly Newsletter, April-June 2024, *supra*, at 14.

¹² IBBI, Quarterly Newsletter, April-June 2024, *supra*, at 19.

¹³ IBBI, Quarterly Newsletter, April-June 2024, *supra*, at 13.

¹⁴ IBBI, Quarterly Newsletter, April-June 2024, *supra*, at 17.

¹⁵ IBBI, *Pre-Packaged Insolvency Resolution Process*, <https://www.ibbi.gov.in/uploads/whatsnew/a650764a464bc60fe330bce464d5607d.pdf>.

to their creditors.¹⁶ Despite the seeming appeal of the process to firms compared to the general insolvency process, only 11 firms have opted for it, and only 5 cases have been concluded. Those cases yielded a 25% recovery for creditors.¹⁷

B. System for Individual Debtors

The Code also created a system for individual – *i.e.*, personal – debtors, comprised of the same institutional actors, except that the Code provides that the “adjudicating authorities” in this system are the Debt Recovery Tribunals and judges. These Tribunals were created to provide a forum for expediting banks’ and other financial institutions’ enforcement of debts of 2,000,000 rupees (approximately \$24,000) or more. The Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act of 2002 also provides a more expedited process for banks to enforce security interests without requiring recourse to the Debt Recovery Tribunals.

1. Insolvency. The process designed for personal insolvencies is similar to the one described above for corporate insolvencies.¹⁸ Both creditors and debtors can initiate cases. Debtors can do so if they have defaulted on a debt of more than 1,000 rupees (approximately \$12), other than certain types of excluded debts, such as fines or other liabilities for breach of various legal duties. Creditors can initiate cases if their debtor has defaulted on a debt and failed to pay the amount owed after a demand is made. Upon filing, a moratorium on actions against the debtor comes into effect, and a resolution professional, selected by either the initiating party or the Tribunal, is appointed to the debtor’s case. The resolution professional must submit a report within 10 days proposing that the Tribunal approve or reject the application for the insolvency case, which the Tribunal is required to do within 14 days from receiving the resolution professional’s report.

The debtor, “in consultation with the resolution professional,” is responsible for preparing a resolution plan.¹⁹ The Code and regulations promulgated by the IBBI provide only limited guidance about the provisions that may or must be in a resolution plan.²⁰ The Code states only that a plan “may authorize or require the resolution professional to carry on the debtor’s business or trade . . . ; realize the assets of the debtor; or administer or dispose of any funds of the debtor.”²¹ The resolution professional must then submit a report on the plan to the Tribunal and to the creditors.²²

¹⁶ Sudipto Bhattacharya, *Pre-Packaged Insolvency Resolution Process (PPIRP) under IBC*, <https://taxguru.in/corporate-law/pre-packaged-insolvency-resolution-process-ppirp-ibc.html>.

¹⁷ *Pre-pack Insolvency a Success for Five Companies*, The Economic Times, May 24, 2024, <https://economictimes.indiatimes.com/news/india/pre-pack-insolvency-a-success-for-five-companies/articleshow/110373627.cms?from=mdr>.

¹⁸ Feibelman, *supra* note ____, at Part I.B.1. *See also*, Adam Feibelman and Renuka Sane, *Designing a Personal Insolvency Regime: A Baseline Framework*, https://www.nipfp.org.in/media/medialibrary/2020/10/feibelmanSane2020_personalInsolibbiyearbook.pdf

¹⁹ IBC 105(1)

²⁰ Feibelman, *supra* note ____, at 446-47.

²¹ IBC 105(2).

²² IBC 106.

The report must confirm that the plan complies with current law and that the plan "has a reasonable prospect of being approved and implemented."²³

The Code itself does not specify any limits on a debtor's assets or income that can be included in a repayment plan or any requirements for the inclusion or priority of certain types of debts. The IBBI published draft regulations for the personal insolvency provisions in 2017,²⁴ which would have provided that a repayment plan cannot affect excluded assets and that it must include, among other things, a duration, a schedule, a minimum budget for the debtor, and the terms of the debtor's discharge.²⁵ But these rules and regulations were never formally adopted. Excluded assets are a feature of the Code's bankruptcy provisions, discussed below, and are defined in the Code, presumably for that purpose. These include:

- (a) unencumbered tools, books, vehicles and other equipment as are necessary to the debtor or bankrupt for his personal use or for the purpose of his employment, business or vocation;
- (b) unencumbered furniture, household equipment and provisions as are necessary for satisfying the basic domestic needs of the bankrupt and his immediate family;
- (c) any unencumbered personal ornaments of such value, as may be prescribed, of the debtor or his immediate family which cannot be parted with, in accordance with religious usage;
- (d) any unencumbered life insurance policy or pension plan taken in the name of debtor or his immediate family; and
- (e) an unencumbered single dwelling unit owned by the debtor of such value as may be prescribed....²⁶

A debtor's creditors then vote to approve or reject the plan or modify it with the debtor's consent. Approval of a repayment plan by creditors requires the vote of more than three-fourths of the value of the claims of creditors.²⁷ If creditors approve the plan, then the Tribunal must either approve or reject it "on the basis of the report of the meeting of the creditors."²⁸ The Code does not specify any additional standards to govern Tribunal's decision on whether to approve or reject the plan.²⁹ If the Tribunal approves the plan, the insolvency professional is charged with

²³ IBC 106(2)(a),(b).

²⁴ IBBI, Draft Rules and Regulations for Personal Insolvency and Bankruptcy cases, https://ibbi.gov.in/Agenda_3_01122017.pdf (including discussion of public and working group comments).

²⁵ Insolvency and Bankruptcy Board of India, Insolvency Resolution Process for Individuals and Firms, Draft Regulations, § 22, 2017, available at <http://www.ibbi.gov.in/Draft%20Regulations%202017%20on%20Insolvency%20Resolution%20process%20for%20Individuals%20and%20Firms.pdf>; Feibelman, *supra* note ____, at 447

²⁶ IBC 79(14).

²⁷ IBC 106-111. Voting creditors cannot include a debtor's associates. IBC 109(4)(B).

²⁸ IBC 114(1).

²⁹ Feibelman, *supra* note ____, at 448-49.

implementing it³⁰ and applying for the debtor's discharge, generally upon completion of the plan.³¹ The Code does not specify whether any debts are non-dischargeable in the insolvency process as it does in personal bankruptcies, as explained below.³²

In sum, the Code and the draft rules and regulations leave many questions open for the asset-mostly dormant personal insolvency regime. Most notably, neither the Code provisions nor the draft regulations regarding personal insolvencies provide a framework for protective limits on the terms of repayment plans beyond excluding certain assets and providing for a minimum budget for the debtor. They do not expressly provide authority for resolution professionals to avoid and recover fraudulent or preferential transfers made by the debtor.³³

2. Bankruptcy. The Code also includes a "bankruptcy" chapter, available under limited circumstances, which provides a mechanism for liquidating a debtor's assets for the benefit of their creditors and to obtain a discharge of the unpaid balance of certain debts. Bankruptcy is available for an individual debtor if the debtor's application for insolvency was rejected by a Tribunal because it was filed fraudulently; if a Tribunal rejects the debtor's repayment plan; or if a debtor's repayment plan ends before completion.³⁴

The Code provides that a debtor or one or more of the debtor's creditors can initiate a bankruptcy proceeding by filing an application with a Debt Recovery Tribunal.³⁵ A moratorium goes into effect automatically upon the filing of an application, and the tribunal must either issue a bankruptcy order or dismiss the case within two weeks of the filing. Issuing a bankruptcy order creates a bankruptcy estate that vests in a bankruptcy trustee, which includes "all property belonging to or vested in the bankrupt at the bankruptcy commencement date."³⁶ The estate does not include "excluded assets," defined above, or property held by the bankrupt as a trustee, money due to workmen, or any other assets designated by the central government and financial regulators.³⁷ The trustee manages and marshal's the estate, primarily for the benefit of the debtor's creditors. The

³⁰ IBC 116.

³¹ IBC 119.

³² Feibelman, *supra* note ____, at 449.

³³ See Jha, *Personal Insolvency: Recent Judicial Interpretations*, *infra* note ____ ("A critical gap in the current framework concerns the need for robust asset-tracing mechanisms for [personal guarantors]. While the IBC includes provisions for avoiding fraudulent and preferential transactions in the case of [corporate debtors], these provisions do not extend to [personal guarantors]. This lack of safeguards opens the possibility of asset diversion by [personal guarantors] before the resolution professional takes control of the guarantor's estate. Without a mechanism to claw back such assets, the guarantor's estate may be improperly diminished, undermining the interests of creditors. The absence of asset tracing and recovery provisions creates significant enforcement challenges, reducing the efficacy of personal insolvency proceedings.")

³⁴ IBC, 121. See also IBC, § 100, 115, 118. The case must be filed within 3 months of one of these circumstances. IBC 121.

³⁵ IBC 121.

³⁶ IBC 155.

³⁷ IBC 155.

trustee may also seek to avoid certain fraudulent,³⁸ preferential,³⁹ and “extortionate” transactions⁴⁰ made by the debtor. These avoidance provisions are in the bankruptcy chapter of the Code, but not in the personal insolvency chapter, so, again, it is not clear if they are available in insolvency cases. Distributions are made to creditors according to the following priorities under the Code: trustee costs and expenses in full; “workmen’s” dues for the two years preceding the bankruptcy case and secured debts; wages to other employees for the one year preceding the bankruptcy case; government claims for the two years preceding the bankruptcy case; and then all other debts.⁴¹

1. Fresh Start. The Code also includes a “fresh start” chapter for individuals with relatively low income, few assets, or little non-excluded debt who are “unable to pay [their] debt.”⁴² Debtors are presumptively unable to repay their debt if it appears so from their application – only debtors can initiate a fresh start case. This chapter provides for the discharge of qualifying debts without any requirement of distribution to creditors from the debtor’s assets or income.

C. Conclusion

The personal insolvency, bankruptcy, and fresh start chapters of the Code represent a radical change in the legal framework affecting consumer debtor and creditor law in India. The insolvency and bankruptcy provisions are decidedly creditor-friendly, and the fresh start is equally decidedly debtor friendly. The government adopted draft rules for each of these provisions, and government officials have stated an intention to notify them, but they have not been generally notified. As discussed below, however, the personal insolvency and bankruptcy provisions were partially notified for one unique and important subset of individual debtors: those who had guaranteed debts incurred by firms in the corporate insolvency process.

II. The Problem of Personal Guarantors

As this Part explains, personal guarantees by firm owners, managers, and directors and their relatives play an important role in India’s corporate finance landscape. But that role has been limited over the years by challenges that creditors face in enforcing these guarantees, including when the underlying guaranteed claims have been drawn into the insolvency and bankruptcy system. The following Part describes how policymakers in India have tried to improve the functioning of these personal guarantees by employing the Insolvency and Bankruptcy Code.

³⁸ IBC 164.

³⁹ IBC 165.

⁴⁰ IBC 167.

⁴¹ IBC 178.

⁴² IBC 80. These limits are 60,000 rupees in annual income, 20,000 rupees in assets, and 35,000 in qualifying debts, approximately \$715, \$238, and \$417, respectively. See *Assessing the Borrower-Level Impact of the Insolvency and Bankruptcy Code 2016: A Study of the Fresh Start Process*, Dvara Research and Insolvency Law Academy (2024), <https://insolvencylawacademy.com/wp-content/uploads/2024/04/assessing-the-borrower-digital.pdf>; Dwijaraj Bhattacharya, *Estimating Eligibility for the Fresh Start Mechanism Under IBC, 2016*, Dvara Research (2020), <https://dvararesearch.com/wp-content/uploads/2024/01/Estimating-Eligibility-for-the-Fresh-Start-Mechanism-under-IBC-2016.pdf>.

A. Role of Personal Guarantees in India

India's economy has long been characterized by concentrated ownership of firms and management by firm promoters and owners.⁴³ These founders and owners often provide personal guarantees for debts incurred by their firms, a practice that expressly encouraged by the Reserve Bank of India, which regulates financial institutions in the country. A recent study finds that nearly 5 trillion rupees of business loans (nearly \$60 billion) are covered by personal guarantees, which is [x]% of the total advances to businesses.⁴⁴ There is an academic literature on personal guarantees, little of which examines practices in India in particular.⁴⁵ An important theme in the literature is that guarantees can affect firms' risk taking as well as serve as direct security for creditors' claims.

B. Enforcing Personal Guarantees

The most straightforward function of a personal guarantee is to provide a double layer of extra security for corporate borrowing in India – creditors have another source of potential repayment, and the guarantees themselves are generally secured by the guarantors' property.⁴⁶ This extra security is particularly important in India because of weaknesses in the legal system for enforcing business debts. Recoveries for bank lenders under the SARFAESI Act is roughly 22%, and 6.5% for banks and other financial lenders under the Recovery of Debts Due to Banks and Financial Institutions Act.⁴⁷ And cases under both regimes often take a commercially unreasonable amount of time. But these challenges in enforcing debts also affect the personal guarantees, limiting their function in facilitating corporate lending.⁴⁸

⁴³ *Ownership and Control of Widely and Closely Held Firms in India*, <https://journals.sagepub.com/doi/10.1177/0972262917738895>; *Ownership Trends in Corporate India 2001-2011: Evidence and Implications*, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2303684; Khanna T., & Palepu K. (2005), *The evolution of concentrated ownership in India: Broad patterns and a history of the Indian software industry*, in MORCK RANDALL K. (ED.), *A HISTORY OF CORPORATE GOVERNANCE AROUND THE WORLD: FAMILY BUSINESS GROUPS TO PROFESSIONAL MANAGERS* (UNIV. OF CHICAGO PRESS), <http://www.nber.org/chapters/c10272>; *Ownership Pattern of the Indian Corporate Sector: Implications for Corporate Governance*, <https://citeseerx.ist.psu.edu/document?repid=rep1&type=pdf&doi=2e240c28ba790992022d70bed48b4561ede67ca8#page=231>; Reserve Bank of India, *Master Circular - Guarantees and Co-acceptances*, <https://rbidocs.rbi.org.in/rdocs/notification/PDFs/03MCGUARCOA0104202471E5C2241C52434886F5183D7BF0CB19.PDF>.

⁴⁴ Awaiting permission to cite.

⁴⁵ See, e.g., *Breaking the Barrier to CEO Succession at SMEs: Japanese Reform on Personal Guarantees on Business Loans*, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4346926; *Personal Guarantees, Loan Pricing and Lending Structure in Finnish Small Business Loans*, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2084154; *Personal Guarantees on Bank Loans and SMEs' Risk-Taking*, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4692085; *'Keeping it Personal' or 'Getting Real'? On the Drivers and Effectiveness of Personal versus Real Loan Guarantees*, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2964709; *Entrepreneurial Finance: Analyzing the Demand for the Personal Guarantee*, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3754520.

⁴⁶ See Chatrakshi Jain, et al., *Early Evidence of a Working Personal Insolvency Regime in India*, working paper.

⁴⁷ *Id.*

⁴⁸ *Id.*

III. Personal Guarantors and the IBC

As noted above, a primary motivation for adopting its new insolvency system was to increase creditors' recoveries from their insolvent corporate borrowers, thereby promoting commercial lending. As noted above, aggregate recoveries from corporate debtors under the corporate insolvency system are improved, if modestly, over the status quo ante. As the Code provided a more robust tool for creditor recoveries against insolvent firms, policymakers' attention turned to the problem of enforcing personal guarantees to increase recoveries for banks and other financial creditors, and they decided to apply the Code's personal insolvency and bankruptcy provisions to them. They were also likely motivated by public attention to a few high-profile businesspeople whose firms had failed but had themselves seemingly escaped consequences for those failures.

This Part describes the formal mechanics of applying the Code to these debtors, some of the legal issues that this move has generated, and some of the preliminary data about insolvency and bankruptcy cases involving personal guarantors. It also evaluates some of the potential implications of these data and questions that they raise about the Code for cases involving both corporate and personal debtors.

A. Legal framework for personal guarantors

The Bankruptcy Law Reform Committee's report that formed the basis for drafting the Insolvency and Bankruptcy Code had expressly included personal guarantors among the types of debtors "to whom the individual insolvency and bankruptcy provisions shall apply, [along with] Sole proprietorships where the legal personality of the proprietorship is not different from the individual who owns it. ...; Consumer finance borrowers; Student loan borrowers; Credit card borrowers; Farmers; Micro-finance borrowers; [and] Partnership firms."⁴⁹ As is common in India, the Code provides that "[t] shall come into force on such date as the Central Government may, by notification in the Official Gazette, appoint ..."⁵⁰ And as noted above, the government immediately notified the provisions of the Code that apply to corporate debtors. Until November 2019, it had not notified any of the provisions of the Code that apply to personal or individual debtors. At that time, it notified most of the personal insolvency and bankruptcy provisions but only for debtors who are personal guarantors.⁵¹

At that time, as discussed above, the IBBI had only promulgated draft rules and regulations for the personal insolvency and bankruptcy regimes; none had formally been adopted. In December 2019, to make the Code operational for personal guarantors, the IBBI promulgated insolvency and

⁴⁹ *Report of the Bankruptcy Law Reforms Committee*, *supra* note ____, at 6.1.

⁵⁰ IBC, § 1.3.

⁵¹ https://www.mca.gov.in/Ministry/pdf/Notification_18112019.pdf

bankruptcy regulations⁵² and rules⁵³ specifically for cases involving those debtors. The Code, rules, and regulations combined provide only a broad framework for personal insolvencies and bankruptcies, leaving many issues and questions unaddressed.

A personal guarantor is defined under the rules as “a debtor who is a personal guarantor to a corporate debtor and in respect of whom guarantee has been invoked by the creditor and remains unpaid in full or part.”⁵⁴ Reflecting the fact that these cases are really adjunct to the corporate insolvency and liquidation system, the rules and regulations provide that the adjudicating authority for personal guarantor insolvencies and bankruptcies is the National Company Law Tribunal, which handles corporate insolvencies, rather than the Debt Recovery Tribunal, which is designated as the adjudicating authority for personal insolvencies under the Code.⁵⁵

1. Insolvency. The insolvency regulations for personal guarantors provide that repayment plan “shall provide”⁵⁶ the term of the plan and schedule of payments; that resolution costs get priority over other creditors; details about the financing for the plan; how the debtor’s business will be run, if relevant; the role of resolution professional; any treatment of claims against the debtor deemed “onerous”; and any excluded assets and debts. The Rules specify that the exclusion for unencumbered personal ornaments is 100,000 rupees⁵⁷ (approximately \$1,200) and the exclusion for dwelling units in urban areas is 2,000,000 rupees (approximately \$24,000) and 1,000,000 rupees (approximately \$12,000) for units in rural areas.⁵⁸

The plans must also provide:

a minimum budget for the duration of the repayment plan, to cover the reasonable expenses of the guarantor and members of his immediate family to the extent they are dependent on him, provided that at least ten percent of the realisable income of the guarantor shall be utilised for repayment of debts.

⁵² *Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Personal Guarantors to Corporate Debtors) Regulations, 2019*, <https://ibbi.gov.in/uploads/legalframework/2019-11-22-171205-h10bx-8573c02ee31bba941201aff84b95ae4.pdf> (as amended: <https://ibbi.gov.in/uploads/legalframework/1e8ee1a052b280a5d0076f13ae69e410.pdf>); *Insolvency and Bankruptcy Board of India (Bankruptcy Process for Personal Guarantors to Corporate Debtors) Regulations, 2019*, <https://ibbi.gov.in/uploads/legalframework/2019-11-22-172331-pdm3h-40c64dd41380b7d710b874a8d1152fe6.pdf> (as amended: <https://ibbi.gov.in/uploads/legalframework/99c0f343531f9fb9c08363a7dd3fdd33.pdf>).

⁵³ <https://ibbi.gov.in/uploads/legalframework/8e0ab9331455200b402d91257113805c.pdf> (insolvency); <https://ibbi.gov.in/uploads/legalframework/17662452f16d75fe4c221f39e303033f.pdf> (bankruptcy).

⁵⁴ PG Insolvency Rules, 3(1)(e).

⁵⁵ PG Insolvency Regulations, 3(1)(a); PG Bankruptcy Rules, 3(1)(a).

⁵⁶ PG Insolvency Regulations, Chapter V.

⁵⁷ PG Insolvency Rules, 5(a).

⁵⁸ PG Insolvency Rules, 5(a).

A repayment plan may also provide for the sale of assets; disposal of funds held by the debtor; the satisfaction or modification of security interests granted by the debtor.⁵⁹ Creditors vote on repayment plans in proportion to the amount of debt they hold,⁶⁰ and unless otherwise specified, decisions require a majority of voting share.⁶¹ An insolvency case involving a personal guarantor, the applicant can withdraw the case after it is admitted by the Tribunal, but the other creditors must agree.⁶²

2. Bankruptcy. As noted above, bankruptcy trustees play an important role under the Code.⁶³ Resolution professionals can serve as trustees.⁶⁴ The regulations promulgated by the IBBI specify aspects of the trustee's responsibilities, such as preparing preliminary, progress, and final reports.⁶⁵ The preliminary report must include details about the debtor's assets, including excluded assets and must be confidential, unless the Tribunal provides otherwise.⁶⁶ The debtor can seek an early discharge if the preliminary report reveals that the debtor's assets are insufficient for covering the costs of the bankruptcy process.⁶⁷ The bankruptcy rules provide the same limits on excluded assets as do the insolvency rules, noted above. A debtor in the bankruptcy process is not allowed to participate in financial or commercial transactions greater than 100,000 rupees.⁶⁸

3. Litigation.⁶⁹ The legality of the application of the Code to personal guarantors was challenged early on. The Supreme Court held, first, in *Lalit Kumar Jain v. Union of India*,⁷⁰ that the Central government had statutory and constitutional authority to notify the personal insolvency and bankruptcy provisions only for personal guarantors. That opinion also held that the liability

⁵⁹ Creditors cannot purchase assets, nor can “any company where the guarantor or a creditor is a promoter or director; [or] any associate of the guarantor, creditor or resolution professional.” PG Insolvency Regulations, 18.

⁶⁰ PG Insolvency Regulations, (11(2)).

⁶¹ PG Insolvency Regulations, (11(6)).

⁶² PG Insolvency Rules, 11(1).

⁶³ PG Bankruptcy Regulations, Chapter III.

⁶⁴ PG Bankruptcy Regulations, 3.

⁶⁵ PG Bankruptcy Regulations, 7.

⁶⁶ PG Bankruptcy Regulations, 8.

⁶⁷ PG Bankruptcy Regulations, 9.

⁶⁸ PG Bankruptcy Regulations, 15; IBC 141(1)(d).

⁶⁹ For a good summary of litigation over the application of the IBC to personal guarantors, see Ritik Kumar Jha, *Personal Insolvency: Recent Judicial Interpretations*, Metalegal Advocates, Sept. 2024, available at https://www.mondaq.com/india/insolvencybankruptcy/1523370/personal-insolvency-recent-judicial-interpretations?email_access=on#authors.

⁷⁰ AIR ONLINE 2021 SC 402, available at https://main.sci.gov.in/supremecourt/2020/26016/26016_2020_37_1501_28029_Judgement_21-May-2021.pdf.

of a guarantor is not discharged if the corporate debtor's obligation is discharged.⁷¹ Subsequently, in *Dilip B. Jivrajka v Union of India*,⁷² the Supreme Court upheld the constitutionality of the provisions as applied to personal guarantors, especially that a moratorium, the appointment of a resolution professional, and other powers of the Tribunal are triggered by the filing of a case, even before the existence of the guarantor's debt is established.

In *Mahendra Kumar Agarwal v. PTC India Financial Services Ltd*,⁷³ the Supreme Court upheld a decision by the NCLAT that a case can be brought against a personal guarantor to a corporate debtor regardless of whether any insolvency case against the corporate debtor has been initiated or is pending.

B. Data

As of June 2024, there have been 3,184 insolvency cases filed involving personal guarantors. Of these, 451 were initiated by the debtors and the rest were initiated by creditors; 220 have been withdrawn, dismissed, or rejected; 1542 have proceeded to the point of having a resolution professional appointed; and 468 have been admitted by the Tribunal.⁷⁴ Of these 468,

146 have been closed. Of these, 12 have been withdrawn; 108 have been closed on non-sub-mission or rejection of repayment plan; and 26 have yielded approval of repayment plan. In cases where repayment plans have been approved, the creditors have realized ₹ 102.78 crore, which is 2.16% of their admitted claims.⁷⁵

As noted above, bankruptcy is available for personal guarantors if the insolvency process fails for some reason. Of the insolvency cases filed, 56 of these have resulted in bankruptcy applications, one of these filed by the debtor.⁷⁶

The only publicly available information about these cases are the orders approving the resolution plans in the 26 cases that have advanced to that stage. This is a very small subset of the pending personal guarantor insolvency cases, so they offer only a peak into the operation of the system. But it is possible to make some general observations from this limited data. These cases involve guarantors of claims against four corporate debtors, all of which were the subject of corporate insolvency cases: Chadalavada Infratech, Vishwa Infra, Bluefern Ventures, and Pradeep Overseas.

⁷¹ See Jha, *Personal Insolvency: Recent Judicial Interpretations*, supra note ____ (“Under s. 128 of the Indian Contract Act, 1872 (‘Contract Act’), the liability of PGs is unequivocally co-extensive with that of the CD.”).

⁷² 2023 SC 1530, https://main.sci.gov.in/supremecourt/2021/24405/24405_2021_1_6_48185_Judgement_09-Nov-2023.pdf

⁷³ 2022 SCC OnLine SC 908.

⁷⁴ IBBI, Quarterly Newsletter, April-June 2024, supra note ____, at 24.

⁷⁵ IBBI, Quarterly Newsletter, April-June 2024, supra note ____, at 24.

⁷⁶ IBBI, Quarterly Newsletter, April-June 2024, supra note ____, at 24.

All of these cases were initiated by a bank, all but one by State Bank of India, which is a government-owned bank. Bluefern Ventures' guarantors cases were filed by the Bank of Baroda, which is also a public sector bank. All of these cases involved two or more owners of the firms or their family. Twelve of these cases, for example, involve guarantors of a single loan by a consortium of lenders to Vishwa Infra, of which the SBI was the lead bank. All of those debtors were either promoters of the firm or their relatives. Seven of these cases involve guarantors of a single loan by SBI to Chadalavada Infratech. In the Chadalavada cases, it appears that the SBI was the only financial creditor. In the Vishwa Infra cases, there were seven lenders in the consortium, all of which got to vote. It appears that an initial repayment plan by some of the Vishwa Infra guarantors was rejected. The Pradeep Overseas cases are consolidated for 5 guarantors; there are two for Bluefern Ventures.

In the Chadalavada cases, the plans were funded by the sale of property pledged as security and, in some cases, additional non-excluded assets. In the Vishwa Infra cases, the plans were funded by sale of some "liquid assets" but primarily from loans by family and friends of the debtors. In the case of one of Vishwa Infra's guarantors, Yerra Srinivas, the repayment plan was funded in part by half of the debtor's future income. Excluded assets claimed by many of the debtors include both jewelry and dwellings, but not any other assets.

Notably, nine of the debtors who were guarantors of Vishwa Infra had pledged real property as security for their guarantees, and had turned those properties over to the SBI outside of the repayment plan. Those properties yielded substantially more than the repayment plans themselves. The corporation's debt guaranteed by the individual debtors was 14.4 billion rupees. The various repayment plans of the guarantors provided for payments to the banks of 111 million rupees. The real property that the guarantors previously handed over to the banks yielded 280 million rupees.

As noted above, these 26 repayment plans provide for only 2.2% of the amount of the total claims guaranteed by these individuals. But in two cases, Bluefern Ventures and Chadalavada Infratech, the payments provided for under the plans are roughly 40% and 25% of the underlying claims, respectively. The available data do not reveal how many, if any, of these 26 plans have been successfully completed.

C. Impact and lessons

India's use of insolvency and bankruptcy law for personal guarantors is comparatively unique and complicated for the same reasons that the function of the Code in India is somewhat particular to that country. Many aspects of India's insolvency and bankruptcy system are a product of a seemingly intractable problem in the background legal system, *i.e.*, the difficulty in enforcing contractual obligations, especially financial ones. This explains, for example, why the system was designed primarily as a creditors' remedy and secondarily as a potential form of relief for debtors in financial distress. In countries where legal enforcement of debt is more streamlined, insolvency or bankruptcy law serves a very different function in general and with regard to personal guarantors. In those jurisdictions, the goals are more evenly balanced, and in some cases, reversed in order of importance.

In the United States, for example, if an individual guarantees a debt, that guarantee – whether secured or unsecured – can generally be enforced through the general legal system, so long as the guarantor is able to satisfy the obligation. Bankruptcy is available to individual guarantors in

that country who cannot satisfy all of their obligations, including the guarantee. Generally speaking, in bankruptcy, if the guarantee is secured, the claim will be satisfied up to the amount of the value of the property securing the claim and subject to discharge beyond that amount, depending on what other non-exempt assets the debtor has and what other debts they owe. In other words, in that jurisdiction, the non-bankruptcy system functions to enforce a security interest, and bankruptcy serves to solve a collective action problem among creditors, often leading to discharge of a significant amount of debt arising from a guarantee.

Based on the very preliminary available aggregate and case-level data, it is unclear how much the Code's extension to personal guarantors is serving its intended function. As noted above, aggregate recoveries from guarantors in the handful of repayment plans that have been approved are quite low, especially as a ratio of the claims involved. And we do not know how many of those approved or future plans will be completed or fail and lead to bankruptcy. We also do not know whether or how much recoveries under repayment plans exceed recoveries that creditor would get if the debtors proceeded directly to the bankruptcy system when the costs of the initial insolvency process are avoided. And to the extent that some of the approved plans were funded by loans from family and friends, it seems that they may just be redistributing losses to other creditors, and perhaps to creditors who are less able to efficiently absorb them.

On the other hand, two of the cases with approved plans had fairly high creditor recoveries in relation to the claims in those cases. And it is possible that the new threat of insolvency and bankruptcy is motivating personal guarantors to satisfy claims outside of the system. The handover of property securing claims by personal guarantors to Vishwa Infra in advance and outside of their repayment plans provides some support for believing this. It is possible that the creditors obtained that property from the debtors more quickly once the guarantors were in the insolvency system than they would have through non-insolvency debt enforcement actions. And if fraudulent and preferential transfer actions are not available in the insolvency process, then reforming the process to allow them could meaningfully increase the assets available to creditors to personal guarantors.

In sum, the available data suggest that it is possible that the insolvency process for personal guarantors could be serving its intended function of increasing creditor recoveries (and holding owners and managers of failed firms accountable) in at least some circumstances. But the data also suggest that there will be many cases, perhaps most, where the debtor's assets are simply too meager to justify the insolvency process. In those cases, repayment from income may become a more common approach or, if future available income is not sufficient, larger numbers of debtors will end up in the bankruptcy process. Resolution professionals already have the power to fast-track debtors from insolvency to bankruptcy if the debtor does not have assets sufficient to pay for the insolvency costs. Perhaps there should be a larger category of debtors who qualify for such a fast track, and perhaps those debtors could be authorized to file for bankruptcy directly.

Finally, there are reasons to be skeptical about whether the insolvency and bankruptcy system for personal guarantors is building the country's capacity for a broader personal insolvency and bankruptcy system. On the one hand, there are a few thousand cases that have been proceeding under the Code through the system. Tribunals and judges are getting some experience operating an insolvency and bankruptcy system for individual debtors, developing repayment plans, applying rules for excluded assets, and discharging qualifying debts. But, to be clear, these tribunals and judges are unlikely to be operating a more general personal and insolvency system – that will presumably fall to the Debt Recovery Tribunals or some other as-yet-unidentified entity.

More noteworthy, these cases involving personal guarantors bear little resemblance to what one would expect are the universe of other personal insolvency and bankruptcy cases that would be resolved through the system. In the 26 guarantor cases for which we have data, there are very large financial claims that dwarf other claims against the debtors, no other claims are addressed in the cases, no other creditors are authorized to participate in the process, and only one case thus far has involved payments from future income. One should expect that most personal insolvencies and bankruptcies would involve a larger number and different types of claimants. And perhaps the biggest challenge for the system will be determining amounts of debtors' income that should be available to creditors and how much income individuals debtors should be able to keep for a minimum budget.