

IBC amendment Bill 2019: Finding the middle ground a must

The onus is now on the SC to find a middle-ground whereby rights of homebuyers as financial creditors are not curtailed and the developers are not made to bear the brunt of unfettered rights vested in the hands of buyers

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Every individual dreams of owning a home someday. To fulfil this dream, people invest their savings in real estate projects hoping that the developer will stay true to his side of the bargain and ensure timely delivery of possession of the flat.

However, in recent years, there has been a rise in the number of housing projects that have been stalled due to the developer's inability to complete the project. Consequently, the monies invested by the homebuyers in such failed real estate projects are stuck, leaving the homebuyers with little or no resort other than indulging in protracted legal battles to recoup their investment.

In this scenario, it was important for the government to take measures to consolidate investor confidence in the industry. The government, therefore, introduced the landmark legislation Real Estate (Regulation & Development) Act, 2016 ('RERA'). At the same time, another legislation i.e. Insolvency & Bankruptcy Code, 2016 ('IBC') was also introduced though not specifically for the real estate sector but it had substantial bearing on real estate projects.

Here is a look at the impact of IBC on real estate projects.

Initially, IBC failed to consider 'homebuyers' as financial creditors. After the Supreme Court's decision in the landmark case of Chitra Sharma vs. Union of India, the government made an amendment in the IBC validating the status of homebuyers as financial creditors and vested in them rights to approach the National Company Law Tribunal ('NCLT') as financial creditors.

Subsequently, in the matter of Pioneer Urban Land and Infrastructure Limited & Others vs. Union of India, the builders approached the SC challenging the rights of homebuyers. In this matter, the apex court upheld the aforesaid rights of homebuyers. Consequently, several homebuyers who were facing delay in receiving the delivery of their units in the projects, approached NCLT and filed applications under the provisions of IBC.

However, the homebuyers received a setback once again when the central government promulgated an amendment in December, 2019 which mandated that a minimum threshold of homebuyers (100

homebuyers or 10% of total homebuyers in a project, whichever is less) would need to congregate in order to initiate proceedings as financial creditors against a defaulting builder. There were concerns that the said Amendment might substantially dilute the rights bestowed on the homebuyers by the SC. The said amendment was then referred to the Parliament Standing Committee on Finance by the Lok Sabha on December 23, 2020.

Homebuyers, had in January this year, been awarded a partial relief by the SC which directed that NCLT will have to maintain status quo with respect to the applications already filed by homebuyers and investors against errant builders, till the apex court decides the constitutional validity of the said amendment after hearing the arguments of both the parties.

The national lobby for homebuyers, Forum for People's Collective Efforts (FPCE), had also raised concerns about the said amendment. The primary contentions of FPCE are that the amendment imposes unreasonable conditions on homebuyers, decimates the level-playing field which existed prior to the introduction of the said amendment, and tilts the law in favour of real estate developers.

Therefore, the FPCE has been demanding that the proposed amendment should be dropped "in order to be fair and just with the homebuyers who are the backbone of the real estate industry." FPCE argued that if the said amendment comes into effect, a single homebuyer or a group of them, which falls short of the requisite threshold as per the said amendment, would be unable to initiate an insolvency resolution proceeding against the real estate developer.

On February 24, 2020, FPCE held a meeting with the parliamentary standing committee on finance, to raise concerns against the ordinance brought by the central government to amend the IBC. The committee was chaired by Jayant Sinha and is expected to submit its report on the said amendment within three months.

On the flip side, there has been a marked increase in instances whereby individual or handful of homebuyers have started to initiate insolvency proceedings against developers who had already managed to complete 80-90% of the project but had overshot their completion date by a few months.

This option has apparently been pursued by homebuyers who were looking for an exit option. It can, therefore, be presumed that the said amendment is primarily aimed at preventing a few potentially unscrupulous elements within the homebuyer community from abusing the spirit of the IBC by unsettling real estate companies at the behest of or in connivance with rival firms or to serve their self-interest.

At a time when the real estate sector is stuttering, the central government felt that it is in the best interests of all parties to give the highest priority in repayment to corporate debtors to prevent insolvency or liquidation, to provide immunity against unjust prosecution to the corporate debtor, to prevent action against the project of such corporate debtor and ensure its successful completion to enable the fruition of the contract homebuyers entered into with the developers initially.

The general consensus is that provisions of RERA are in addition to and not in derogation of the provisions of IBC and these laws provide parallel remedies to homebuyers.

It is also important to understand that, IBC is not meant to be merely a debt recovery mechanism. Moreover, once the homebuyer establishes a prima facie case of 'default', the burden shifts on the developer. The developer needs to prove that the homebuyer himself is a defaulter, or the process under IBC has been invoked fraudulently, with malicious intent or for any purpose other than insolvency resolution.

In certain cases the developer may also need to prove that the homebuyer is a speculative investor and merely wants to jump ship and is relying on IBC as a coercive measure to get back monies already paid by it. These added obligations often make it all the more difficult for the developer to avoid insolvency proceedings being initiated against him and his project in case he has defaulted only against a handful of homebuyers.

These proceedings often lead to stalling the entire project, limiting the options of the developer as well as those homebuyers who were not a party to the IBC proceedings.

As of November 2019, it is the residential real estate segment that had the maximum amount of stressed assets. India's residential sector has been reeling under the pressure of numerous delayed/stalled projects. While the government's cognizance for the need to amend the IBC is commendable, it needs to be undertaken in a time-bound manner. Also, a practical solution could be to further strengthen the RERA framework as the first point of grievance redressal.

If the parties fail to reach an amenable resolution at RERA and all other provisions get exhausted, majority homebuyers could only then approach the NCLT for insolvency resolution proceedings. Otherwise, there is serious apprehension that the IBC in its present form without the said amendment, might greatly overburden the NCLT with frivolous and trivial litigations therefore making it less effective than envisaged.

The government recently announced a special funding window of Rs 25,000 crore to ensure speedy completion and delivery of affordable homes locked in stalled housing projects. In this light, it is clear and obvious that the rationale of the government while dealing with stalled residential projects is to revive them immediately and efficiently without handing over the project to a new developer and weeding out miscreants looking to secure their self-interest in any manner.

For now, the interim order of the SC delivered in January 2019, has ensured the continuity of the cases pending before the NCLT and the constitutional validity of the ordinance will be tested before the Hon'ble SC. Now, the onus is on the SC to find a middle-ground whereby the right of homebuyers as financial creditors are not exponentially curtailed on the one hand and the developers are not put in a position where they have to bear the brunt of unfettered rights vested in the hands of homebuyers.

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