



Ninety-seven per cent of micro, small and medium enterprises are partnerships or proprietorships. BS PHOTO

# FISME KICK-STARTS MOVE TO DRAW UP INSOLVENCY LAW

*Stresses the need for a legal mechanism for bankruptcy*

BS REPORTER  
New Delhi

**A**t the request of the ministry of micro, small, medium and micro enterprises (MSME), the Federation of Indian Micro and Small and Medium Enterprises (FISME) has kick-started the process of developing a draft law on insolvency and bankruptcy for such enterprises.

Earlier this month it organised a meeting with economic and legal experts on insolvency. The meeting was attended by Sangeeta Saxena, an official of the ministry of MSME; Jiten Khosla of the Indian Institute of Corporate Affairs (IICA); Pallavi S Shroff, a partner in the legal firm Amarchand & Mangaldas & Suresh A Shroff & Co; economists Bibek Debroy and Laveesh Bhandari; Anil Bhardwaj, secretary-general of FISME and two others representing the federation.

The meeting agreed that since 97 per cent of Indian MSMEs were partnerships or proprietorships, issues arising out of business failure could only be addressed through a modern personal insolvency

law and an affordable litigation process-cum-administrative mechanism.

It also agreed that the proposed law could draw from the US bankruptcy code for its effectiveness and simplicity, while the litigation process/administrative mechanism needed to be chosen from the UK or other European Union countries to prevent it from becoming too “advocate-driven” and out of reach of most MSMEs.

While Ms Shroff will help draft the legislation and propose an administrative mechanism, IICA will provide research support in the endeavour, and Debroy and Bhandari will provide specific inputs requested by the research team.

FISME, member of the subgroup on insolvency and exit-related issues within the Prime Minister’s task force on MSMEs, had been asked to explore the contours of a law that will replace the Presidency Town Insolvency Act, 1909 and the Provincial Town Insolvency Act, 1920.

According to FISME, the insolvency mechanism for MSMEs in India, provided through the above legislation, is archaic and largely dys-

functional. Winding up and limited liability provisions under the Companies Act are also not applicable to MSMEs.

FISME says that a legal mechanism for insolvency and bankruptcy is indispensable for ensuring payment of unpaid dues to creditors, sharing of debtor’s assets fairly and an honourable exit for debtors.

In the absence of such a mechanism, whenever there is financial stress (voluntary or forced; temporary or terminal), there is no method for MSMEs to deal with the commercial-legal requirements of multi-agency creditors (involving statutory dues, debts of banks and financial institutions), since any of these creditors could stall the restructuring exercise, force the closure of an enterprise and secure a prison sentence for entrepreneurs.

There is no bankruptcy mechanism — neither a law nor a specialised body. There is no BIFR equivalent for MSMEs which could protect the entrepreneur from recovery proceedings of various statutory agencies even during the process of restructuring.

FISME argues that a progressive set of insolvency and

bankruptcy laws will allow an entrepreneur to disentangle himself from the fallout of a failed enterprise at a cost that the laws can lay down. Thereafter he will be free to begin life once again as a bona fide citizen — start another enterprise or work for someone else. An approach of this nature, it says, will attract bright young persons to entrepreneurship.

The PM’s task force had recommended that, “in place of the outdated Provincial Insolvency Act, 1920, action may be initiated to formulate and circulate a model Insolvency Act within six months, which will have enabling provisions for time bound revival and exit for unincorporated firms.”

It had also said that the model Act should take into consideration the need for four key elements — a specialised quasi-judicial body, to appraise viability and set up time-bound revival/closure plans; enabling provisions for a “holding period” for revival of the enterprise; segregation of business assets from personal assets on the basis of “reasonable” norms; and speedy winding up in case the business is determined as non-revivable.