

If a company has been sick for years, and its assets have been depleted, IBC may yield huge haircut: Dr. M S Sahoo, Chairman, IBBI

Synopsis

In a chat with Mohit Bhalla, the Chairman of the Insolvency and Bankruptcy Board of India, Dr. M S Sahoo, addresses questions about the recent challenges. Sahoo has held senior roles at India's stock market regulator Sebi and India's competition watchdog CCI in the past.



The insolvency and bankruptcy code (IBC), the most recent of India's laws to address corporate defaults and rising non-performing loans of banks has come in for recent criticism as certain companies that were undergoing bankruptcy proceedings have yielded recoveries as low as 5% for the financial creditors. India faces a bad loan pile that is estimated at Rs. 10 lakh crore making the efficiency of the law a critical success

factor for dealing with bad loans. In a chat with Mohit Bhalla, the Chairman of the Insolvency and Bankruptcy Board of India, Dr. MS Sahoo, addresses questions about the recent challenges. Sahoo has held senior roles at India's stock market regulator Sebi and India's competition watchdog CCI in the past. He admits that haircuts for banks are a problem but explains that they need to be understood in the context of the stage at which companies are brought into IBC proceedings.

Why are we seeing such low recoveries for banks in recent cases which have undergone bankruptcy such as Videocon, Jet Airways and Siva Industries?

The relevant question to ask is why does IBC process yield zero haircut in one case (Binani Cements and MBL Infrastructure) and 100% in another (Ghotaringa Minerals Limited, and Orchid Healthcare Private Limited)? It depends on several factors, including the nature of business, business acumen of creditors, market for distressed assets, and health of the economy. It, however, critically depends on at what stage of stress, the company enters the IBC process, as much as at what stage a patient arrives in the hospital. If the company has been sick for years, and the assets have depleted significantly, the IBC process may yield huge haircut or even liquidation. The companies, which have been rescued through IBC till March 2021, had assets valued, on average, at 22% of the amount due to creditors when they entered the IBC process not only rescued these companies, but also reduced the haircut to 61% for financial creditors.

The next question to ask is whether haircut should be seen in relation to claims of the creditors or the assets available on the ground?

Former may not be realistic as the claims are not marked-to-market and are often inflated. The latter may make better sense, because IBC maximises the value of the existing assets at the commencement of the process, not of the assets which probably existed once upon a time. Since it redeems a part of the going concern surplus, rescue is realising, on average, 190% of the value of the existing assets, generating 90% bonus, instead of haircut. Realisation will be higher if we consider the amount realisable through avoidance transactions and insolvency resolution of guarantors.

There is also the other issue of promoters of companies misusing IBC and taking their companies back after lenders take a big haircut. How are you addressing that?

There is no prohibition on promoters to retain their company through a competitive resolution plan. The prohibition is on a person, whether a promoter or not, who does not have credible antecedents. Any person, which is connected or related to the prohibited person, is also prohibited. He is also prohibited from buying assets in liquidation or participating in compromise or arrangement of the company. Therefore, what is of concern is an ineligible person wresting control of a company. I have not come across such instances.

How do our recovery rates compare with other global economies who also have well laid out bankruptcy laws?

It would be difficult to make a comparison because our law is just about five-year-old, while some jurisdictions have century old insolvency law. The most objective and mostly widely used metric to compare performance of economies is the World Bank Group's Doing Business Report, where India's rank moved up from 136 to 52 in terms of 'resolving insolvency' in the first three years of implementation of the Code. As per the Report released in October, 2019, recovery rates were: India (71.6%), US (81%), UK (85.4%), Brazil (18.2%), Russia (43%), China (36.9%) and South Asia (38.1%).

How are you ensuring that the IBC reform becomes stronger, and all stakeholders are made more accountable?

The foundation of IBC is extremely strong. Six amendments to the Code in about five years have strengthen it further. The apex court have settled contentious issues and resolved grey areas, with alacrity. With every judgement, the insolvency law has developed deeper and stronger roots.

IBC is a tool in the hands of the stakeholders to be used at the right time, in a right case in a right manner. They should use it in early days of stress, when value of the company is almost intact, and close the process quickly before value recedes further, to minimise or even avoid haircut.