

The Experts Corner – Dr. M. S. Sahoo, Chairperson, the IBBI

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We talk to Dr. M. S. Sahoo, the IBBI Chairperson and the flag-bearer of the Indian insolvency and restructuring industry, on a variety of issues.

As the regulator, you have opined that market forces influence the resolution of a debtor's insolvency. However, does the market respond differently to economic stress, as compared to the more contained financial stress? Especially when it is driven by a sense of collective responsibility to prevent a cascading economic effect?

The Insolvency and Bankruptcy IBC, 2016 (IBC) is a noble law because it takes care of a person who is in stress, be it a company, a LLP, a proprietorship or partnership firm, or an individual. A firm in a market economy may experience stress, mostly on account of competition and innovation:

1. The firm belongs to an industry where business is no more viable for exogenous reasons such as innovation. Most such firms have economic distress and are generally unviable. The only option available is to release the resources of the firm for other competing uses and the entrepreneur to pursue emerging opportunities. A few of these firms may, however, have resources to change the business and become viable.

2. The firm belongs to an industry where other firms in the industry are doing well, but the firm in question is not doing well for endogenous reasons such as inability to compete in the marketplace. Most such firms have only financial distress, and are generally viable. It is necessary to rescue the firm well in time to prevent financial stress turning into economic stress, by putting it in the hands of a credible and capable persons. A few of these firms may have significantly depleted resources and become unviable.

Stress is an outcome of market forces. The IBC enables the market forces to resolve stress. It empowers a committee of creditors (CoC), who has the commercial wisdom, to interact with the market to generate the most effective resolution plan for resolving stress. The CoC assesses feasibility and viability of competing resolution plans before approving the best of them. The market, more often than not, rescues a viable firm and closes an unviable one. There can be exceptions depending on market imperfections or factors beyond the market.

India will soon have a 'Bad Bank'. As a bad bank primarily aims to alleviate macroeconomic stress: what kind of changes or additions could be made to the IBC, which would not only allow its optimal use by a bad bank, but would also increase its compatibility with other options that a bad bank could resort to?

The establishment of 'bad bank' complements the IBC in resolution of stress. This will build specialised capacity for resolution of stressed assets. More importantly, with consolidation of loans, the bad bank would have requisite voting power, which will expedite decision-making by the CoC in corporate insolvency resolution process. It would also ensure swift decision-making regarding relinquishment or realisation of security interest during liquidation process. This will avoid the stalemate currently arising in case of multiple secured creditors having *pari-passu* charge over asset(s) of the corporate debtor and exercising different options. Since most of the banks and financial institutions would transfer their stressed assets to 'bad bank', the consolidation of group corporate entities undergoing insolvency resolution process separately will be smoother. Thus, the 'bad bank' would improve outcomes of processes under the IBC.

Most jurisdictions have a codified code of conduct for IPs, whose violation is sanctionable. In the Indian context, IPs are susceptible to non-cooperation and active delinquency by the promoters. Therefore, a sanctionable code of conduct as mentioned in the "Handbook on Ethics for Insolvency Professionals" could be weaponized against IPs. On this backdrop, how do you envision the functioning of a Code of Conduct, which circumvents this weaponization, and simultaneously promotes IP professionalism?

IPs are the backbone of all processes under the IBC, and the success thereof is largely contingent upon their conduct and competence. They must have accountability commensurate with their responsibility. To ensure that the IPs observe the highest standards of professional integrity, the detailed Code of Conduct for IPs has been laid down in [the IBBI \(Insolvency Professionals\) Regulations, 2016](#) and reinforced through the "Handbook on Ethics for Insolvency Professionals: Ethical and Regulatory Framework". To thwart its 'weaponization' against IPs, adequate safeguards for IPs for

any action taken or intended to be taken in good faith, has been provided under section 233 of the IBC. As an additional bulwark against its misuse, section 236(2) of the IBC provides that no Court shall take cognizance of any offence punishable under the IBC, except on a complaint made by the IBBI or the Central Government.

In a [Discussion Paper on liquidation by IBBI in 2019](#), it was discussed how there is no mathematical formula to determine viability of a CD and that leads to liquidation of viable CDs. Do you believe we are witnessing this due to a lack of involvement of appropriate experts in the insolvency resolution processes in India?

There is no formula to determine which company is viable and needs to be rescued. Since it is not amenable to formula, the Code envisages a collective mechanism in the form of CoC to decide the matters, and it needs to decide by vote. There is no substitute for market's wisdom. Market may go wrong in some cases, but the substitute for market is likely to go wrong more often. Therefore, the IBC provides two opportunities to rescue a viable company during the liquidation process also: Compromise or Arrangement, and Sale as a going concern. Further, insolvency ecosystem is rich in terms of availability of professional services which are used extensively by market participants.

The latest [Financial Stability Report](#) by the RBI has said that loans to MSMEs could be a pain point for the lenders in the coming fiscal year. The IBC offers the Pre-pack scheme for MSMEs. One of the major benefits that the Pre-pack method has to offer is early stress resolution by initiating it pre-default. But the model introduced in India does not allow pre-default initiation. Would that prevent stakeholders from extracting certain benefits from pre-pack that are offered in other jurisdictions?

There is no requirement that one needs to resolve stress through IBC. There are several competing frameworks. Each has a specific design, keeping in view certain objectives or certain circumstances. It is for the market to choose the one that suits its needs the best in a specific circumstance. It may resolve the stress outside, and not use, any framework.

The IBC is designed to address post-default stress. In fact, 'default' for initiating insolvency resolution process is a basic structure of the IBC. There are costs and benefits associated with an IBC process. These costs and benefits must be incurred judiciously in deserving circumstances.

Has the [Swiss Challenge model](#) incorporated in the Pre-pack scheme paved the way for [Management Buyouts \(MBOs\)](#) which have otherwise been rare in India due to legal roadblocks?

Prepack does not mandate *Swiss challenge* as such. It mandates a challenge mechanism where the CoC does not approve the base resolution plan and the best alternate plan is not significantly better than the base resolution plan. Nevertheless, the resolution happens through a resolution plan which requires approval of the CoC as in CIRP. Management is not prohibited to submit a resolution plan if it is eligible under section 29A.

Cryptocurrency has risen to global prominence, and contains noticeable value, combined across its variants. The treatment of encrypted digital currencies, when a debtor becomes insolvent, is something that has not been discussed in India. Would you agree that restructuring of crypto-assets is likely to be a rather difficult task for insolvency professionals, starting with determining their existence? How can they tackle these challenges efficiently?

IBC is sector neutral. If one sector gets a preferential treatment as compared to another, it would distort the level playing field and consequently misallocate resources, impinging on economic growth. The laws relating to resource allocation, namely, insolvency, competition, securities are always sector neutral. It is not material what kind of assets a corporate debtor has. The market has capacity to understand every business and the IP has the authority to appoint any professional to assist him.

Looking back on your tenure as the IBBI Chairperson, how do you feel? Is there anything you wish you could have done differently?

The Code has established the supremacy of markets. The early harvest has been excellent. From providing freedom of exit to rescuing companies in stress, to helping creditors realise their dues, and most importantly — bringing about a behavioural change among the debtors and creditors alike, while reinforcing the rule of law; the list of achievements of the Code is long. Not surprisingly, India's rank moved up from 136 to 52 in terms of 'resolving insolvency' in the first three years of implementation of the Code, in the World Bank Group's Doing Business Reports. I do not think, there is anything which could have been done differently. Everything has been done in the way it could have been done at that point of time.

Lastly, what would you say to young professionals considering joining the Indian insolvency ecosystem?

An IP is a key pillar of the insolvency regime under IBC and is the glimmer of hope for the person in distress and its stakeholders. Considering the ever-expanding mandate of the IBC from CIRP, liquidation process and voluntary liquidation process for corporate persons initially, and later on, of financial service providers, to personal guarantors to Corporate debtors, to pre-packaged insolvency resolution process, the ocean of possibilities for engagement in insolvency space is vast and shall expand further with the implementation of cross-border insolvency, group insolvency and individual insolvency. These require limitless performance.

(This interview was conducted by Parth Indalkar, with assistance from Aaryan Mohan, Vinisha Jain and Sandali Sharma.)