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RECORD CAFE

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Chairperson, Insolvency and Bankruptcy Board of India

A new system to avert future NPA crises

AFTER YEARS OF struggle, the government finally brought in the Insolvency and Bankruptcy Code, 2016, that subsumed many existing laws, including the Sick Industrial Companies Act, and became the overarching legislation to address corporate insolvency. The new law provides for requisite institution building in which the Insolvency and Bankruptcy Board of India (IBBI) plays a pivotal role. MS Sahoo, the chairperson of IBBI, in an interview with **Banikinkar Pattanayak** and **KG Narendranath**, dwells upon the nuances of the new regime. He says that although the extant NPA problem of banks needs to be addressed separately, an efficient insolvency resolution system will enable the lenders to act before things get out of control and pre-empt such crises in the future.

How does the new insolvency resolution process work and who can trigger it?

If a corporate has defaulted on a payment obligation—loan or otherwise, a financial creditor, an operational creditor, an employee, or the corporate debtor itself can trigger the corporate insolvency resolution process. It needs to make an application before the National Company Law Tribunal (NCLT) along with the evidence of default. If default is established, the NCLT admits the application and appoints an interim insolvency professional (IRP). The IRP practically becomes de facto managing director of the corporate and exercises the powers of the Board of Directors. The officers of the corporate report and the promoters extend all cooperation and assistance to the IRP. He runs the operations of corporate as a going concern up to 30 days during which he collects the claims of various people and forms a committee of creditors. The committee consists of financial creditors and, where there are no financial creditors, it consists of operational creditors. Thereafter, the committee gets to decide what to do with the corporate. It also appoints a resolution professional (RP) in place of IRP. If it feels that the insolvency isn't resolvable, it may decide to liquidate the corporate. If it does not approve a resolution plan within 180 days with 75% majority, the corporate also gets into liquidation. If it comes out with a resolution plan, the RP submits it to NCLT for approval.

Why aren't big lenders such as banks using this law much to recover their loans?

Banks as creditors, in fact, have many options to recover loans. Being sophisticated creditors, they evaluate suitability of various options and choose the one that works the best. The Code provides creditors an additional option to resolve insolvency, while they may work outside the Code. Banks need to have in a place a framework that would guide the hierarchy when to trigger a resolution, who to trigger it, what kind of insolvencies to be resolved, how to identify an appropriate IRP, etc. which may take a little time. It is not a fact that banks are not using this law. The very first application admitted (in the matter of Innoventive Industries Ltd) for resolution was filed by the ICICI Bank. It is, however, important to note that irrespective of the person who initiates the insolvency proceedings, the financial creditors form the committee of creditors and approve the resolution plan. Further, there is an alert as soon as there is a default of ₹1 lakh. This makes the parties to sit up and take a view at the earliest instance of default. This prevents ballooning of default to dangerous proportions. Second, the fear of loss of control over the corporate prevents the debtor from default unless it is absolutely unavoidable. This will reduce the incidence of default and build-up of NPAs.

What is sacrosanct about the threshold of 75% for creditors' committee to approve a resolution plan?

In a democracy, the majority should prevail, while the minority must not be suppressed. The Code balances their interests, keeping in view the objective of IRP that the corporate should resurrect, wherever possible, and only when it's not possible, it should be liquidated. Suppose, it is 60%. This means that stakeholders with 40% stake can dissent and walk away. If they exit with their stake, it may be difficult for the corporate to carry on as a going concern. On the other hand, if it is 90%, it may be difficult to have consent of stakeholders with 90% stake, and hence every other corporate may go for liquidation. Therefore, 75% strikes a balance.

If up to 25% can dissent and then walk away with their share of assets, will that not be an incentive for them to dissent?

It is about rights of stakeholders. The Code empowers the stakeholder to decide matters for them. However, a dissenting creditor would get proportionate share of liquidation value, not of the value of the corporate as going concern or the amount due to it.

Why has the government foregone the precedence it enjoyed over assets in case of liquidation of a company under the new law?

Earlier, the government had the highest priority over the proceeds of liquidation assets. Under the Code, the government has pushed down its priority below unsecured creditors. The resolution process cost and liquidation cost have the highest priority, followed by workers' dues, secured creditors and unsecured creditors, and thereafter comes the government.

This is not without reasons. The Code aims at an optimum utilisation of resources, all the time, either by ensuring efficient resource use through resolution of insolvency of the corporate, or by releasing unutilised or under-utilised resources for efficient uses through closure of the corporate. It is believed that if the productive resources that are currently unutilised or under-utilised for some reason or the other, can be put to more efficient use by the Code, the economic growth rate may well go up by 2 percentage points, other things remaining unchanged. This would give much higher income to the government in the long run. This is a win-win for all.

Does the tax department or any other government agency have the power to obstruct the insolvency resolution process?

No, the Code overrides all other laws. Besides, there is a moratorium on various actions against the corporate debtor during the insolvency resolution process period.

Since insolvency resolution is a relatively new discipline in India, where would you get so many IPs?

When you start something new, you generally start with the existing professionals. We started off with statutory regulated professionals such as CA, CS and advocates with 15 years of practice experience, in similar or related transactions. We, however, granted them registration with six-month validity. In this category, 977 insolvency professionals are registered. Simultaneously, we commenced the Limited Insolvency Examination. We registered these professionals with 10 years' of experience as well as graduates with 15 years' managerial experience on passing the examination. This is an online examination available from December 31, 2016 on all days from 100 plus locations across the country. In this category, about 100 IPs have been registered so far. These IPs have permanent registration.

Going forward, we are contemplating National Insolvency Examinations. The IBBI and IPAs are organising capacity building programmes for them.

Will the new system work optimally without addressing cross-border insolvency as well?

Sections 234 and 235 in the Code deal with cross-border insolvency. These contemplate agreements with governments of foreign countries for enforcing the Code.