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From questioning our competence, tribunals now seek IBBI's help to address regulatory gaps: MS Sahoo

M S Sahoo, chairperson, Insolvency and Bankruptcy Board of India

Synopsis

The insolvency regulator is gearing up for a change at the top even as it is at a crossroads. Though the ecosystem is slowly returning from the pandemic-imposed vacation, a standing committee has stirred the hornet's nest by asking a few tough questions. Even as Sahoo leaves behind a formidable legacy, his successor will have a few mountains to climb.

Speed has been the hallmark of the Insolvency Bankruptcy Board of India (IBBI) ever since its inception. It hit the ground running five years ago, entrusted with making the insolvency framework operational in just 60 days.

Today, banks and creditors have recovered more than INR2 lakh crore in more than 360 resolved cases. As he hangs up his boots today, MS Sahoo, chairperson, IBBI, speaks to ET Prime about how the ecosystem, consisting of professionals, creditors, promoters, and the adjudicating bodies, has evolved around the regulator.

In the meantime, India's ease of doing business ranking for insolvency parameter improved by 84 positions to 52 before the pandemic brought everything to a standstill. Though policymakers sought to address several immediate and urgent matters that the cases threw up, Sahoo believes that a few important issues took a back seat.

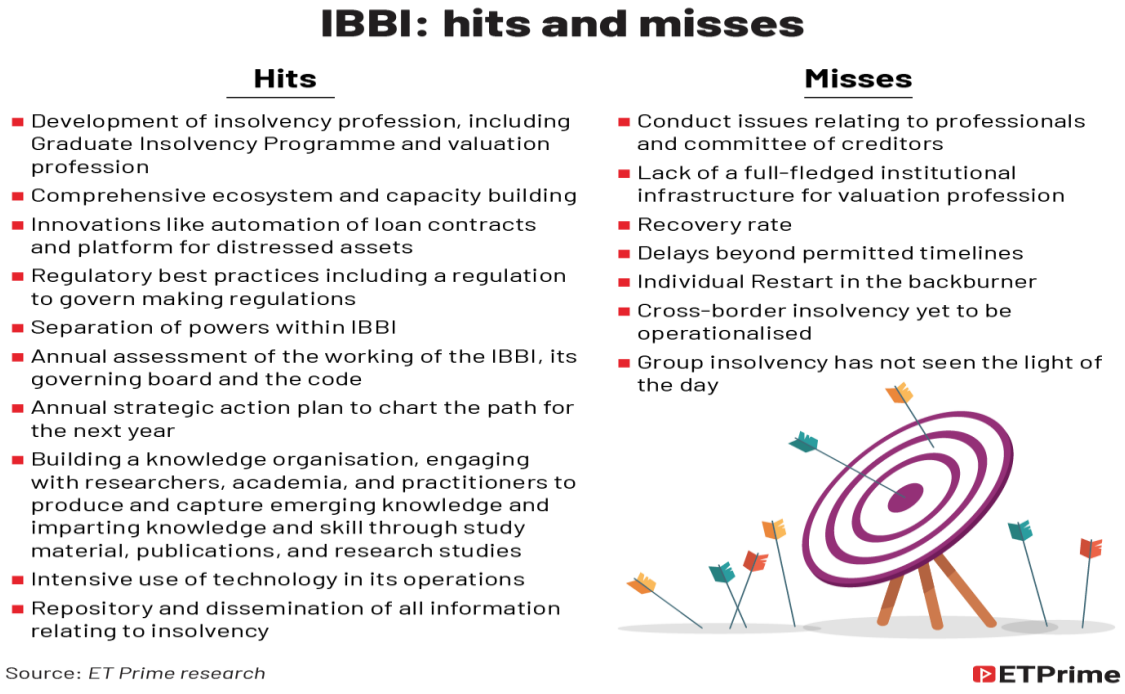
Edited excerpts:

The IBBI will soon complete five years. How has been the journey so far? What are the major hits and misses?
The journey of IBBI is intertwined with that of the Insolvency and Bankruptcy Code (IBC). In the last five years, the code has revolutionalised insolvency resolution and established the supremacy of markets and the rule of law in insolvency resolution besides professionalising the process of resolution.

From providing freedom of exit to rescuing companies in financial stress to releasing entrepreneurs and idle resources stuck up in inefficient uses to helping creditors realise their dues and, most importantly, bringing about a behavioural change amongst the debtors and creditors alike, the list of achievements is a long one. The improvement in India's rank in resolving insolvency from 136 to 52 in three years provides a summary measure of hits and misses.

What distinguishes an organisation from an institution is its legitimacy. An organisation needs to be accepted by the stakeholders for what it does and how, rather than only for its statutory mandate. To my understanding, the IBBI began the journey of legitimacy from its very inception. The kind of proactive engagement IBBI has with stakeholders, including numerous roundtables every year, has been unprecedented in many ways.

A distinguished visitor from the city of London found the IBBI similar to a startup. This sums up its illustrious journey. It is agile, proactive, innovative, and focused on outcome.



What were the major challenges the board faced in these five years? How were they overcome?

When the IBC and the IBBI were brought to life, there was no capacity or experience of insolvency resolution, as envisaged under the code. Established on October 1, 2016, the IBBI was instructed to commence corporate insolvency by December 1, 2016. The framework required creation and building capacity of IBBI to lay down rules of the game, an adjudicating authority to exercise effective oversight, insolvency profession to run business as a going concern and conduct the process with fairness and transparency, valuation profession to provide credible valuations, etc.

This also required acceptance of new norms of resolution by the market participants, namely firms, creditors including government agencies, and resolution applicants and development of their capacity to take commercial decisions.

With active support of the stakeholders and government, the IBBI delivered all these, ensuring roll out of corporate insolvency on December 1, 2016.

I am limiting my response to challenges specific to IBBI. As regards to the insolvency profession, we had two choices — either wait for qualified and experienced professionals to arrive from somewhere, or learn on the go with whatever professionals we had.

The first choice would have meant postponing the reform indefinitely. We preferred the second, but made rapid strides. The IBBI led an industry initiative to launch a two-year Graduate Insolvency Programme, or GIP, to take the insolvency profession to the next level.

The process under the code requires authentic valuations to serve as reference for evaluation of choices and decision making. But we did not have a valuation profession as such. As an interim arrangement, a framework was created under the Companies Act, 2013, enabling IBBI to groom the valuation profession. To take the profession to the next level, a committee of experts has recommended establishment of the National Institute of Valuers to steer regulation and development of the valuation profession.

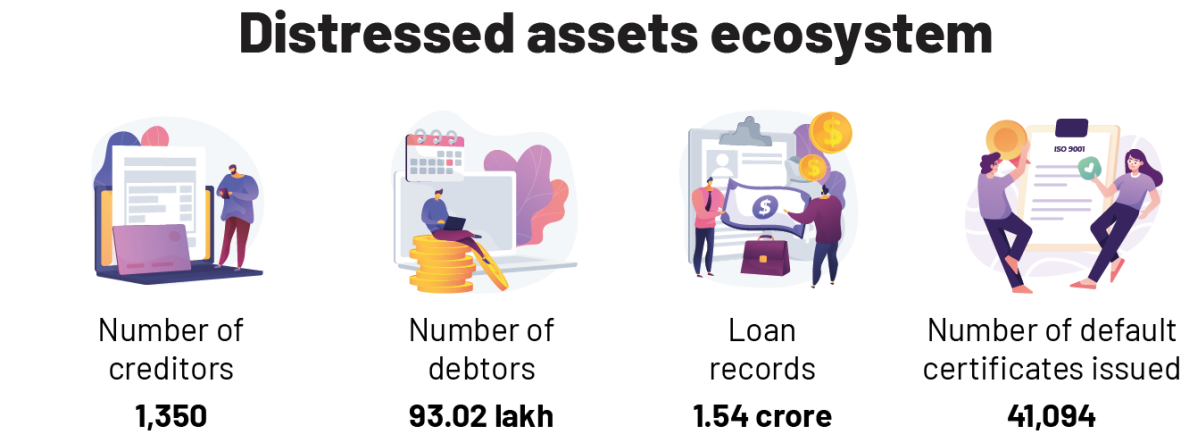
Could you share examples of some important cases where IBBI had to make difficult decisions?

In the resolution of Jaypee Infratech, a public announcement was made on August 10, 2017, seeking claims by August 24, 2017. It was not clear whether an allottee of a real-estate project would submit claims as a financial creditor or operational creditor. To ensure that claims are submitted by August 24, 2017, the IBBI amended the regulations on August 16, 2017, to enable submission of claims by allottees. In the course of time, the code was amended on June 6, 2018, to explicitly consider such allottees as financial creditors or FCs.

The first resolution plan under the IBC was approved on August 2, 2017, whereby the firm amalgamated with a group company while the creditors took a haircut of 94%. This appeared like rewarding the promoters, who probably drove the company to the ground, at the expense of the creditors.

To maintain integrity of the process, the IBBI amended the regulations on November 7, 2017, requiring disclosure of the antecedents — convictions, criminal proceedings, wilful defaults, debarments — of the resolution applicant and its connected persons to enable an assessment of the credibility of such applicant. Subsequently, the code was amended on November 23, 2017, prohibiting persons with such antecedents and the connected persons from submitting resolution plans.

In the early years, some regulations were struck down by the adjudicating authority and some others were challenged in the courts on the ground of competence of IBBI. However, on appeals, these regulations have been restored. It is now settled that legality and propriety of any regulation cannot be considered by tribunals and competence of IBBI has been upheld by the high courts and the Supreme Court. Nowadays, the adjudicating authority or the National Company Law Appellate Tribunal (NCLAT) calls upon the IBBI to make regulations/guidelines to address the gaps noticed by it and the IBBI makes best effort to address them expeditiously.



How did Covid-19 affect the progress of insolvency framework and the resolutions? How long will it take to make up for the lost time?

The IBC is designed to deal with a situation where either an industry or a firm is under stress. It is strictly not designed to deal with black-swan events such as Covid-19, when all the economies in the world experience stress. Many otherwise-viable firms came on the verge of default at this unusual time and it became difficult to find a firm that can rescue another. The unparalleled misery required a matching response to save 'lives', and that required saving 'livelihood', which in turn meant saving the lives of firms.

In recognition of this, the government suspended filing of applications for initiation of insolvency proceedings against a firm for any default arising during the one year starting March 25, 2020. This allowed firms some breathing space to recalibrate their operations and businesses to the new normal.

In recognition of the gravity of the pandemic, the Supreme Court excluded one year (from March 15, 2020) the period of limitation. The NCLAT excluded the period of lockdown for the purpose of counting of the period for resolution process. The insolvency courts moved to virtual hearings and e-filings. The IBBI made several accommodations. The pandemic affected timelines and stressed markets.

Though there has been a steady recovery from the unprecedented trough the economy had hit, it was observed that the pandemic has disproportionately hit micro, small, and medium enterprises (MSMEs) very hard and exposed many of them to financial stress. Considering the difficulties of normal resolution process at the time, the insolvency law was amended on April 4, 2021, to introduce pre-packaged insolvency-resolution process for MSMEs, which provides for debtor-in-possession along with creditor-in-control during resolution. It is available as an alternate option, should the stakeholders prefer to use it.

As the trajectory of the pandemic is fairly known and businesses have adapted to the new normal, the IBC is back on normal course.

There is a concern that the recovery rate has been falling. The recovery rate of financial creditors has fallen to 36% as of June 2021 from 45% in March 2020. Is the board working on improving it?

It is axiomatic that a company coming to IBC does not have adequate assets to fully repay all its creditors. The companies, which have been rescued by resolution plans till June 2021, had assets valued, on an average, at 21% of the amount due to creditors when they entered the insolvency proceedings. This means that the creditors were staring at a haircut of 79% to start with. One third of these were defunct. The IBC not only rescued these companies but also reduced the haircut to 64% for financial creditors.

About a year ago, Ghotaringa Minerals and Orchid Healthcare caught media attention. They together owed INR8,163 crore to creditors while they had no assets when they entered the IBC process. Obviously, creditors had to take a 100% haircut. On the contrary, Binani Cements and MBL Infrastructure have yielded zero haircut, in addition to rescuing the companies. The question that arises here is: why does IBC yield zero haircut in one case and 100% in another? It depends on several factors, including the nature of business, business cycles, market sentiments, and marketing effort.

However, it critically depends on at what stage of stress the company enters the IBC just like at what stage [of disease] a patient reaches a hospital. Even the best hospitals can do little if the patient reaches with substantial haircut to his health. Similarly, if the company has been sick for years and its assets have depleted significantly, the IBC may yield huge haircut or even liquidation.

Haircut is typically total claims minus the amount of realisation divided by amount of claims. This formulation may not tell the complete story. The amount of realisation often does not include the amount that would be realised from equity holding post-resolution, and through reversal of avoidance transactions and insolvency resolution of guarantors. The amount of claim often includes non-performing assets (NPAs), which may be completely written off, and the interest on such NPAs. It may include loans as well as the guarantees against such loans.

These factors project a higher haircut than it is.

What is the right way to look at the recovery and haircuts then?
It may be appropriate to see a haircut in relation to the assets available on the ground and not the claims of the creditors. It is because the market offers a value in relation to what a company brings on the table and not what it owes to creditors. The IBC maximises the value of assets at the commencement of the process, not of the assets which probably existed earlier. Since it redeems a part of the going concern surplus, rescue is realising, on an average, 180% of liquidation value of the existing assets, generating 80% bonus instead of haircut. In addition to rescuing the company, the IBC realises out of the available options for creditors the highest in percentage terms. Post disposal of the pre-IBC legacy matters, as relatively 'recent' stress cases are dealt, haircut may look decent.

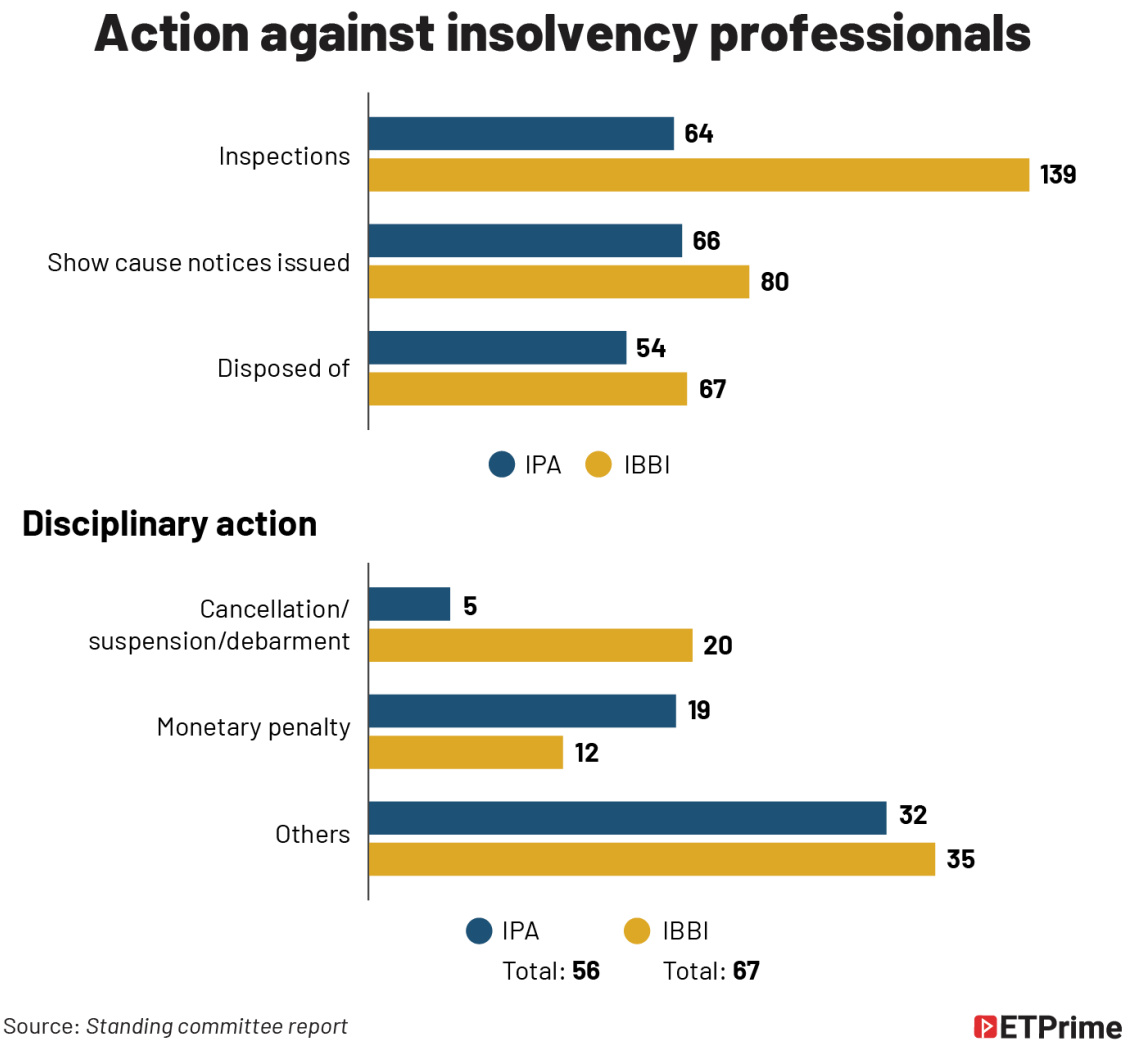
The IBC is a tool in the hands of stakeholders to be used in the right case at the right time in the right manner. They should use it in early days of stress when value of the firm is almost intact, and close the process quickly before value deteriorates further to minimise the possibility of liquidation or even avoid haircut in the resolution plan. The CoC (committee of creditors) needs to act like businessmen and explore limitless possibilities of resolution through a resolution plan. The IP must keep the firm as a going concern and the CoC and promoters must facilitate the IP to do so. The ecosystem should facilitate clawback of value lost in avoidance transactions and all participants must play by the rule book. Even, the manner of computation of haircut must change.

Also, there has been a lot of delay in the resolution process. As on June 30, 2021, 75% of the total cases under the IBC had been pending for more than 270 days. Can the IBBI do anything about this?
The IBC promises time-bound resolution and pegs it at 330 days, including litigation time, for conclusion of the CIRP. The outcome, as compared to pre-IBC days when it took more than four years, is extremely good. However, as compared to the legislative intent, it is not so good. There is huge scope to improve performance on this parameter.

An insolvency proceeding is like an orchestra wherein each constituent has a specific role. If there is any slip-up or inadequacy in the performance of any of the constituents, the process may not conclude in time. Delay arises from many sources: the promoters and management do not allow smooth takeover of the firm by the IP and do not cooperate with him in running business; the CoC does not take decisions promptly; the IP does not conduct the process with promptitude; many stakeholders file frivolous applications, wasting scarce judicial time; the adjudicating authority does not have adequate capacity to dispose of so many matters expeditiously, etc.

I understand that to address the judicial delays, the government is strengthening the NCLT infrastructure (both physical and human) on priority. It has appointed 18 new members in the NCLT recently. To address the delay, there is a need to further beef up administrative, technological, and research support for NCLT, penalise frivolous applications, limit the time for arguments, limit number of adjournments, adopt complete non-adversarial approach to matters, promote administrative process for simpler processes, and facilitate informal mechanism for resolution.

The IBBI is monitoring the conduct of market participants, particularly promoters and management, resolution applicants, and has been filing complaints against them in the special court in case of deviant behaviour. It is working on a guideline to regulate conduct of the CoCin consultation with stakeholders. Along with IPAs, it is undertaking several continuing education programmes for IPs and monitoring their conduct and penalising them in case of misconduct.



How far have we reached in forming the institutional framework for cross-border and group insolvency cases?

The Jet Airways and Videocon Industries caseshave highlighted the need for a regime that deals with situations where the assets and creditors are located outside India or the fate of one company is linked to that of other group companies.

The Insolvency Law Committee has suggested incorporation of UNCITRAL Model Law on cross-border insolvency into the code with certain modifications and variations. A committee of the Ministry of Corporate Affairs is working on subordinate legislation required to implement cross-border insolvency provisions. An IBBI working group has recommended a framework for group insolvency which is to be implemented in a phased manner.

Everyone, from the government to stakeholders, has been on a steep learning curve and addressing the immediate difficulties arising in implementation of the code. Their hands have always been full. In a sense, urgent matters have taken precedence over important ones. There is a sincere intent to enrich the code with value-added features such as cross-border insolvency and group insolvency and to make India a better place to do business.

The standing committee's report has pointed out a number of shortcomings in the IBC and has pitched for an overhaul of the law apart from citing delays in the resolution process and massive haircuts. The panel has recommended a benchmark for the quantum of haircuts. What are your views?
I do not think I can comment on the recommendations. There is a process to examine the recommendations and ultimately a view will be taken by the government.

How has been the stakeholder feedback so far on the pre-packaged resolutions?
It takes three-six months for the market to understand a new framework, compare it with other available options, and prepare itself to use it. A pre-packaged resolution requires prior understanding between the debtor and creditors before initiating the formal process. It envisages up to 90 days of informal preparatory work before the formal process begins.

It is, therefore, too early to expect the response. Nevertheless, the demand by market to expand its reach to large companies even before experiencing the framework, in practice, in the context of MSMEs, lays bare its huge potential.

As a matter of record, a few applications have been filed. One application relating to GCCL Infrastructure and Projects has been admitted.

How has been the progress so far with the proposed code of conduct for the committee of creditors? What was the trigger behind this proposal and how would it benefit the resolution process going forward?
The code provides for a creditor-in-control process for insolvency resolution of corporate persons wherein CoC, constituted primarily of all financial creditors (except related parties) of the corporate debtor, decides the fate of the corporate debtor and consequently of all its stakeholders. The commercial wisdom of the CoC is supreme and not justiciable.

It needs to play its role in accordance with the code. However, there have been instances wherein its conduct has not been above board, at times threatening integrity of the resolution process. In some cases, it has strayed into matters which do not fall into the commercial domain and has unduly influenced the resolution professional. Some such inadequacies in the working of CoC have been detailed in the recent discussion paper.

Given its wide powers and larger implications of its actions, it has become necessary to provide for matching accountability. The standing committee of finance, adjudicating authority, regulators, and stakeholders have suggested some form of regulation of conduct of CoC. In consultation with the Indian Banks' Association, the IBBI is working on the guidelines to stipulate the conduct expected from a CoC.

Power of withdrawals

(More recoveries were through withdrawal of proceedings than through resolution)

Cases dealt

32,547

Cases pending for consideration

13,170

	Number of companies	Liquidation value INR crore	Realisable value INR crore
Applications withdrawn before admission	17,631		545,483
Process commenced	4,487		
Process closed mid-way	1,085		
Process closed by resolution plan	365	113,012	211,635
Process closed by liquidation	1,318	49,783	NA
Ongoing process	1,719		

Source: *Standing committee report*

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Though there is a lot of information available on the IBBI website, the resolution plans of even large accounts are not available in the public domain. The stakeholders have to make do with incomplete press reports and other unreliable sources. Is there a scope for a disclosure framework for this?

A resolution plan may inter-alia include commercial details of the business, which are generally confidential in nature. However, details in respect of each resolution/liquidation process, each claim and each IP, are available in the public domain. Presently, there is a technical glitch for which full details are not available. This is getting sorted out soon.

There are some grievances among the insolvency professionals that the board has not adequately addressed their concerns or even acknowledged their representations. Could there be better communication with regulated entities?

It is unlikely that an insolvency professional (IP) has a grievance. He may be having difficulties in interpretation or application of a law in a particular situation. We have received a few mails seeking such interpretation. Since the IBBI is not the authority to interpret any law, it has refrained from providing an interpretation. It has, however, amended regulations wherever the difficulty required such amendment.

The IBBI also engages with IPs through several roundtables to take their inputs before framing regulations and to guide implementation of regulations after they are framed. For example, it conducted several roundtables on pre-packaged insolvency resolution process. IBBI and insolvency professional agencies (IPAs) organise several workshops and training programmes. I would urge IPs to take advantage of such programmes. It is not possible for the IBBI to interpret the law or provide customised solutions to a problem an IP may have.

Do you have any unfinished agendas during your tenure as the IBBI chairperson? What are the key areas you would like your successor to focus on?

We have just scratched the surface. As we have crossed a small mountain, a much bigger mountain has become visible. As we resolved the first order issues, much deeper issues have come to surface. They include: building capacity of the ecosystem; ensuring everyone plays by the rule book; enriching the processes with value-added features; simplifying the processes and operationalising provisions relating to individual insolvency; keeping firms resolvable; using the services of information utility to facilitate processes; automating resolution processes; institutional framework for valuation profession; developing robust and liquid market for distressed assets; best practices in different aspects; planning resources matching responsibilities of IBBI and so on. These tasks should form the agenda for a few successive chairpersons.