



Maximising value, not the haircut

Creditors must look beyond immediate recovery to the future value a resolution plan can create

The Supreme Court has described the Committee of Creditors (CoC) as the protagonist of insolvency resolution under the Insolvency and Bankruptcy Code (IBC), 2016. It decides the fate of a distressed corporate debtor (CD) — whether it should be rescued through a resolution plan or sent into liquidation. Whichever course it chooses, the objective is to resolve the stress while maximising the value of the assets of the CD.

The decision is commercial and ordinarily beyond judicial substitution. It is not amenable to arithmetic. A plan with the highest evaluation score, net present value, or upfront payment does not, by itself, determine the outcome. The decision rests on voting informed by commercial wisdom.

The IBC does not use the expression “commercial wisdom”. It is, however, now firmly embedded in IBC jurisprudence to describe a well-considered decision directed towards the statutory objective of maximising the value of the CD, though the CoC often seeks to maximise the outcome for creditors. These two forms of maximisation are not synonymous, though they are aligned to a large extent.

Creditors hold claims against the CD, ultimately linked to the value of the enterprise and its assets. If the CD is rescued, restored to health and made more productive, the pool from which creditors can derive value increases. Maximising the value of the CD should, therefore, maximise the value available to creditors.

The difference arises from the time horizon and the structure of the resolution plan. Creditors may remain economically connected with the enterprise through equity, continued credit, deferred or contingent consideration, or other arrangements. If they retain an interest in the future of the CD and the enterprise prospers, maximising the CD’s value and maximising their own value move together.

The position differs when creditors take their recovery upfront and walk away. They exit when the enterprise is at its weakest, exchanging participation in the future value for immediate realisation. Once they exit, they have little “skin in the game” in its post-resolution value creation. In choosing immediate recovery, they may compromise the future value of the CD and consequently their own value.

That distinguishes recovery and resolution. Recovery asks: What can be obtained from the enterprise in its present condition? Resolution asks: What can the enterprise become if its distress is addressed? They have different economic implications.

Recovery focuses primarily on distributing the value presently available. Resolution plan, by contrast, seeks to preserve a viable enterprise and create conditions for future value. A successful resolution can keep productive assets in use, preserve relationships with employees, suppliers and customers, attract fresh capital, change management or strategy, and address the causes of distress. Instead of distributing existing value, it enables the enterprise to create more.

This is why a resolution applicant is willing to invest. It sees value not merely in what remains, but in what can be created. Creditors should consider not only what they can obtain from the CD today, but what the enterprise can become tomorrow. If they remain economically connected with the enterprise, they can participate not only in the value preserved through the resolution plan but also in the additional value created by its revival.

Evidence from post-resolution outcomes shows that companies do revive and prosper. Operations can improve, capacity can be better utilised, customers

can return, fresh capital can be invested and enterprise value can increase. A creditor that has taken an upfront settlement and completely exited does not participate in that subsequent increase. It may, in effect, have left the gains from revival to the acquirer. This does not mean that creditors should always accept a lower upfront payment or always take equity. Nor should uncertain future returns automatically be preferred to certain present value. Time, risk, probability of success and certainty of payment are legitimate commercial considerations. But future value is not irrelevant because creditors have the power to take money out today.

There is a legitimate institutional reason why banks tend to prefer cash. Cash can be booked, provided for, and closed. Equity requires valuation, monitoring, patience, and eventual monetisation. A banker who accepts less cash today in return for equity tomorrow may have to justify that decision years later if the turnaround fails. A defensible immediate recovery can, therefore, appear safer than a potentially larger one in future. Yet the rush to realise dues upfront sits uneasily with the very reason financial creditors have been entrusted with the central role in insolvency resolution: Their ability to wait and realise their dues from the improved performance of a revived corporate debtor.

The challenge is to make value-maximising decisions defensible. CoCs could, for example, invite bids in both all-cash and cash-plus-upside formats and compare them on a properly risk-adjusted basis. Regulators could provide a clear framework for valuing and accounting for equity or contingent consideration received under an approved resolution plan. A reasoned decision to retain an interest in future value, supported by due diligence and documented assumptions about risk and probability, should be recognised as legitimate commercial judgement rather than treated with hindsight as imprudence.

This would distinguish between accepting uncertain value because it is genuinely superior after adjusting for risk, and accepting cash simply because it is easier to justify. The first is commercial wisdom. The second may be institutional risk aversion masquerading as commercial wisdom.

A resolution plan should, therefore, be judged not only by what creditors receive when it is approved, but also by what it enables thereafter: Whether the business survives, whether productive assets remain productive, whether fresh investment comes in, whether financial and operational weaknesses are repaired, and whether the enterprise is capable of creating value beyond the point at which it entered insolvency.

The CoC has a responsibility to exercise commercial wisdom consistently with the statutory objective. Maximising the value of the CD should maximise the value available to creditors. But when creditors choose to exit at the point of maximum distress, they may maximise neither the value of the CD nor their own value. They may simply be maximising their haircut.

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