

## Upgrade and Stabilize Insolvency and Banking Code

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### WHEN

a long-gestated reform becomes a perennial work-in-progress (WIP), it is time to call spade a spade. The list of WIP reforms is lengthening with Goods and Services tax (GST) being its show-piece. Rivalling GST is Insolvency and Banking Code (IBC) in terms of its impact on the economy.

A prolonged WIP creates uncertainty in the economy. It acts as a speed-breaker against revenue-generating capital investments by the private sector. A WIP thus acts as drag on entrepreneurship, economic growth and jobs creation.

Frequent amendments to a legislation underlying a major reform reflects poor drafting. It shows reluctance to incorporate ideas thrown up during the consultation process - both at pre-legislation and post draft bill for discussion stages.

Enacted in 2016, IBC has already been amended six times and requires a few more amendments. A major amendment required is to create a statutory framework for cross-border resolution of insolvency of companies that operate in more than one country.

IBC's implementation is pathetic. Parliamentary Standing Committee on Finance (PSC) has done a commendable job by turning torchlight on IBC's **"Pitfalls and Solutions"**.

In its 32nd report presented to Parliament this week, PSC has recommended:

**"the design and the implementation of the Code as it has evolved needs to be revisited, particularly in the light of its original aims and objects"**. It continued:

**"We therefore need a thorough evaluation of the extent of fulfilment of these aims and objects in the course of implementation of the Code over the years"**.

If one judges off-hand the outcome of IBC since its enforcement in May 2016 against objects and reasons stated in IBC Bill, 2015, the rating would be negative.

The Bill had claimed that its enactment would pave the way for resolution of insolvency in

**"time bound manner for maximization of value of assets" of loan defaulting entities. The Code would"**

**promote entrepreneurship, availability of credit and balance the interests of all the stakeholders including alteration in the priority of payment of government dues "**.

The Bill added:

**"An effective legal framework for timely resolution of insolvency and bankruptcy would support development of credit markets and encourage entrepreneurship"**.

As put by PSC,

**"the low (debt) recovery rates with haircuts as much as 95% and the delay in resolution process with more than 71% cases pending for more than 180 days clearly point towards a deviation from the original objectives of the Code"**. It has rightly called putting a **"benchmark for the quantum"** of haircut (loan sacrifices by lenders) comparable to global standards.

PSC deserves plaudits for seeking crucial reforms in the working of committee of creditors (CoC), Insolvency Professionals (IPs) and National Company Law Tribunal (NCLT).

The Government's contention that **"the commercial wisdom of CoC is supreme"** is strange and it thus has an overwhelming role in deciding fate of companies under the corporate insolvency resolution process (CIRP). If their collective wisdom was supreme, would the banks & financial institutions have doled out loans to companies without adequate due diligence and foresight?

No wonder then to find PSC seeing an **"urgent need to have a professional code of conduct for the CoC which will define and circumscribe their decisions, as these have larger implications for the efficacy of the code"**.

PSC has voiced apprehension about the competence of young IPs, without any experience, in handling the affairs of huge and complex corporations. As put by the Committee, **"there are numerous conduct issues"** with regards to IPs. Two regulators have taken disciplinary action against 123 IPs.

According to PSC, the main reason for time over-run in insolvency resolution process are the delays in approval of resolution plans by the NCLT. It found 71% of 13170 cases pending with NCLT for more than 180 days. The debt involved in these cases is Rs 9,00,000 crore.

NCLT takes considerable time to admit cases. During this time, a loan defaulting company remains in the control of the promoter. This enables owners to resort to value shifting, funds diversion and asset transfers.

PSC has recommended that NCLT should accept defaulters within 30 days and transfer control of their companies to resolution process within this timeframe.

The Government apathy in filling up vacancies has transformed NCLT into a lame-duck institution. As noted by PSC, **"the committee is deeply concerned to note that more than 50% of the sanctioned strength of NCLT is lying vacant and that "the issue of vacancy has plagued the tribunals for years"**.

Adding to unfilled vacant posts of staff in NCLT, as many as 278 posts of officers and other employees were vacant in NCLT benches, according to reply to Rajya Sabha question dated 9th March 2021.

PSC report contains other valuable recommendations too. A lot has been written and reported by experts on reforming IBC. We hope the Government would collate all valuable suggestions into a consultation paper on final amendments to IBC.

We would urge the Government to consider the need to provide for special resolution of companies that fall sick or turn loan defaulters due to policy flip-flops or judiciary striking down a policy such as 2G licencing and coal blocks allotment.

The PIL-induced Court interventions often lead to suspension of project work or temporary closure of factories. These, in turn, have profound impact on viability of the businesses.

In such cases, promoters just can't be blamed and deprived of management control of their dream projects. The national lockdown prior to emergence of first wave and due to state-wide lockdowns during the second wave are having profound impact on companies especially in the services sector. Lockdown was a policy decision and its IBC brunt should be borne jointly by the Centre and the States. Crackdown on wilful loan defaulters should not create collateral damage of enhancing aversion to take loans. The non-performing assets (NPAs) in financial services sector won't come down as long as there is laxity in the working of banks.

Lending frauds in banking sector are facilitated by unwarranted banking secrecy. This has a direct bearing on IBC. We hope Government would take a multi-dimensional view of loan defaults to reboot IBC.