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How filing for insolvency may get easier for banks with a new bankruptcy law

By [Joel Rebello](#) & [Atmadip Ray](#), ET Bureau | Updated: Dec 16, 2015, 12.03 PM IST [Post a Comment](#)

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If [General Motors](#) can continue selling its [Chevrolet](#) brand of cars even after filing for the biggest industrial bankruptcy in the world in 2008, why is that [Kingfisher Airlines](#) [[BSE 3.03%](#)] is not flying, nor are its bankers able to recover dues from it despite promoter [Vijay Mallya's](#) and group companies' loan guarantees? The difference may lie in how courts look at bankrupt companies, attitude of the borrowers and the lethargy of bankers.



All that is set to change, thanks to the proposed bankruptcy law under the recommendations of the TK Viswanathan Committee which is poised to end decades of gaming the [banking](#) system by unscrupulous promoters and the endless obstacles imposed by the courts in the name of providing discretionary relief. Also, [banks](#) will have little to offer as excuse if they don't go after the ones who missed payments.

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While the basis of any transaction in the world of business is the underlying contract between two parties and the failure to honour leads to compensation to those who are owed, the Indian financial system was on the other end of the spectrum. The state-bank dominated system and a benign as well as a corrupt legal system distorted the banking atmosphere making it profitable for companies to default.

"Currently, banks are at the mercy of large corporate borrowers in case of a default because borrowers can delay the proceedings," says Saurabh Tripathi, partner and director at BCG, a consultant. "Privately, bankers say that they are helpless in large loan cases. This (bankruptcy) law will provide certainty to investors and lenders and will be useful for banks after the lessons learnt from the rise in [NPAs](#) in the last few years."

After half-a-century of efforts and nine committees, [insolvency](#) in India may become easier with the TK Viswanathan Committee proposing a timeline of 180 days — extendable by 90 days — to deal with applications for resolving cases of insolvency. During this period, the management of the distressed firm or debtor could be placed in the hands of a [resolution](#) professional — a new class of professionals equipped to deal with such cases, who would be supervised by a proposed new regulator.



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Making it More Accountable

Bankruptcy Law Reform
Committee developed an 'Insolvency Code' for India covering all aspects of personal and business insolvency

Bankruptcy code aims to improve ease of doing business in India and ease of closing down companies

India is 137 out of 189 countries by World Bank's "Doing Business" ranking, which uses insolvency resolution as a key parameter

TK Viswanathan, former secretary general of Lok Sabha and former Union Law Secretary, headed the Bankruptcy Law Reform Committee

- Insolvency Code** will cover all forms of businesses (separate measures for MSMEs)
- Separate set** of resolution mechanism for banks and financial institutions. Recommended by Financial Sector Legislative Reforms Commission.
- Sick Industrial Companies Act, 1985** ("SICA") remains the only Central corporate rescue law in force in India till date. It applies to industrial companies only

Corporate debt restructuring & joint lender's forum are two non-statutory frameworks prescribed by the RBI to deal with stressed assets

Nearly ₹7.05-lakh crore worth of bank loans fall in the stressed category

compared with ₹5.91-lakh crore last year



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The average duration for unwinding a failed business in India takes some 4.3 years compared to the South Asian region's average of 2.6 years. In India, recovery value is limited merely to 25 per cent whereas in more efficient bankruptcy jurisdictions the recovery value is greater than 60 per cent in 1.8 years.

The World Bank's "Doing Business" ranking, which uses insolvency resolution as a key parameter, has placed India at 137 out of 189 countries. The Viswanathan Committee may be the best so far as it suggests scrapping layers and layers of bureaucracy which have been built since Independence. It also segregates the corporate and individual as well as partnership bankruptcies. It has also proposed a debt recovery tribunal for the individuals and the National Company Law Tribunal to deal with the corporates.

"The set time-frame of 180 days is a major advantage for resolutions because it puts the onus on the borrower to avoid liquidation by putting up an acceptable plan for revival before creditors," says Nikhil Shah, managing director at Alvarez & Marsal, a consultancy which specialises in credit restructuring.

At present, banks especially the one with government ownership are forced to carry the pain with the existing corporate debt restructuring system delaying the inevitable.

The gross non-performing assets for the government-owned lenders stood at 5.17 per cent as on March 2015 while their stressed assets ratio stood at 13.2 per cent, nearly 230 basis points more than that for the entire banking system. RBI Governor Raghuram Rajan, a former IMF chief economist, is cranking up the regulatory structure as bad and restructured loans threaten the banking system.

The stressed assets ratio (gross non-performing assets plus restructured standard advances to gross advances) for the system as a whole rose to 10.9 per cent at the end of March 2015 compared with 10 per cent in March last year. Nearly ₹7.05-lakh crore worth of bank loans now fall in the stressed category compared with Rs 5.91-lakh crore last year.

"Private sector banks could settle and exit some of the most celebrated NPAs in quick time while public sector banks are struggling with them," says State Bank of India chairman Arundhati Bhattacharya. "In a public sector set-up, there are certain processes that need to be followed, otherwise the Central Vigilance Commission would start hounding them. Public sector banks do not enjoy the flexibility that their private sector rivals do."

But the proposed law provides a level-playing field and enormous power to creditors that even government agencies such as the I-T department and the excise department will be placed a notch below unsecured creditors. That would also lessen the amount of litigation that government departments, especially the I-T department, bring about in most of the bankrupt cases.

Abhijit Joshi, founding partner at Veritas Legal, a law firm, says the draft insolvency and bankruptcy code make a distinction among financial creditors and operational creditors. They allow insolvency resolution to be triggered in the case of a single default and also prescribe penalties for false and frivolous triggers. "All these factors will help in making resolutions quicker," he says. The changes the code proposes will also help in making the debt recovery tribunal more effective.

We need a system that could ensure that every case is dealt the way Satyam Computer Systems was treated : a sale of viable business to Mahindra even after a financial fraud. There should be availability of talent to enable companies out of insolvency like the Insolvency Practitioners Association of the UK. Although the Viswanathan Committee says that associations of CAs and company secretaries could come up with a list of insolvency specialists, it may not be enough or it could create conflict of interests.

The proposed changes may open up opportunities for the economy to surge ahead, but the political impasse where no legislation is getting enacted may delay the process, but is unlikely to get into cold storage.

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