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LIQUIDATION FAR EXCEEDS COS RESCUED UNDER IBC

Relevant for: Indian Economy | Topic: Issues relating to Growth & Development - Public Finance, Taxation & Black Money incl. Government Budgeting

NEW DELHI : Unviable companies liquidated under the Insolvency and Bankruptcy Code (IBC) far outnumbered those rescued since the new bankruptcy framework came into force four years ago, indicating the challenges facing the economy.

Official data showed that almost in every quarter since January 2017, the number of businesses that were ordered to be liquidated was three to four times the companies that could find a fresh lease of life.

The highest number of liquidation orders of 155 came in the second quarter of FY20, against 33 resolution plans cleared by tribunals, data from the Insolvency and Bankruptcy Board of India (IBBI) showed. In the second quarter of FY21, 68 companies faced liquidation against 22 businesses stitching together revival plans.

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IBC’s goal is to salvage the maximum number of distressed firms, which experts said has helped, but the number of liquidation orders still remains high.

“The number of companies sent for liquidation could have been even higher but for the opportunities being given by the National Company Law Tribunal (NCLT) beyond 330 days to explore revival as is the ultimate goal of the IBC. The problem is that it will only result in kicking the can down the lane unless some inherent issues are addressed. One of the main reasons for more liquidation than resolution is the disqualification under section 29A of IBC of promoters, who happen to be the most obvious propounders of a resolution plan, from taking part in the bid process. In the Indian context of family-driven businesses, promoters play a crucial role in steering the company and in their absence, the corporate debtor is left to fend for itself," said Sumant Batra, managing partner of the law firm Kesar Dass B. and Associates.

IBC disqualifies promoters of defaulting companies from placing bids unless they pay up all overdue amounts. The idea is to check promoters from winning the company back at a discounted price while lenders take a haircut.

Inadequate number of buyers and the inability of businesses to remain viable are among reasons for the higher liquidation number, said Shardul Shroff, executive chairman, Shardul Amarchand Mangaldas and Co., a law firm. “The pre-pack scheme currently under discussions will help in reducing the number of liquidation orders. Also, the government could explore solutions like setting up a fund to support micro, small and medium enterprises in the resolution process," said Shroff.

Besides, the absence of a matured distressed asset market, lack of freedom for resolution professionals to proactively reach out to potential investors and stitch together a plan, general delays in attaining bid closure, the overall economic conditions including of tight liquidity and lenders’ overly defensive approach in taking a haircut are reasons for the high number of businesses going into liquidation, explained Batra.

India’s economy has been on a downward spin since the January-March period of 2018 when it expanded by 8.2%. As per official estimates, the economy is projected to contract by a record 7.7% in FY21 for the first time in 41 years with the services sector affected the worst by the coronavirus pandemic.

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