

Resetting the bar

India's Insolvency and Bankruptcy Code (IBC) got more teeth on Thursday after the president signed an ordinance that streamlines the process of restructuring bankrupt companies. The Code, which came into effect last year, now has provisions to prevent wilful defaulters from bidding for companies that are put up for sale under it. This means that business houses will not be able to reclaim assets on which a loan has been defaulted. The ordinance also bars promoters, whose firms are non-performing assets (NPAs) to banks for more than a year, from participating in the bidding process.

The IBC is a landmark in India's economic reforms. Before it was promulgated, reforms had focused on the setting up of businesses, rather than their closure. By putting in place a mechanism for the resolution of credit liabilities of insolvent companies, the Code has opened the door for the reallocation of capital to enterprises that are likely to make better use of it. The World Bank recognised the significance of the IBC in October when it cited the code as a major reason for India improving its ranking in the Ease of Doing Business Index. However, creditors had expressed concerns about promoters gaming the system to wrest back control of their defaulting companies. For instance, in the case of Synergies Dooray — the first case resolved under the IBC — creditors accused the promoters of the defaulting automotive-maker of buying out the company's bad loans. Before Thursday's ordinance, the Code tried to deal with such problems through a regulatory mechanism put in place by the Insolvency and Bankruptcy Board of India (IBBI). Earlier this month, the IBBI amended its regulations that made it incumbent on the board's professionals to take into account the credibility and credit worthiness of bidders, including promoters, while laying out the turnaround plan of a defaulting company. Though the thinking behind this regulation was the same as Thursday's ordinance — making sure that promoters don't regain their defaulting company at a discount — it was also felt that the measure would burden the IBBI's already-overstressed regulators, which have more than 300 insolvency cases before them. More importantly, the creditors feared that the curbs on bidding by promoters would not hold up in court. Thursday's ordinance takes care of such concerns.

In September, the rating agency CRISIL estimated stressed assets to be Rs 11.5 lakh crore, nearly 14 per cent of the total advances made by banks. Though the agency did not expect a substantial increase in such loans in the next year, it also stressed that faster recovery of stressed accounts "through the IBC is critical to improving the asset quality of banks". Thursday's amendments to the IBC will place the banks on a much surer footing while recovering such loans. They and the IBBI should now make certain that the new set of bidders have the track record to ensure the proper utilisation of public money.

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