What do amendments to IBC mean to promoters?

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Last week, India amended the Insolvency and Bankruptcy Code (IBC) 2016 through an ordinance that received the President's nod. Here's a lowdown:

What is bankruptcy? What is the IBC's intent?

A company is bankrupt if it is unable to repay debts to its creditors (banks, suppliers etc). The inability to repay debts by some Indian firms has resulted in a huge pile of non-performing assets for the banking system.

The Indian government had introduced the IBC as a method to tackle the issue. Under the Code, a resolution has to be found for the indebted company within 270 days. Otherwise, a liquidator is appointed. The company can also opt for voluntary liquidation by a special resolution in a general meeting.

How has IBC progressed? Why was the amendment needed?

According to Manish Aggarwal, partner and head — resolutions, special situations group, KPMG in India, the resolution to stressed assets picked up steam under IBC and investors started warming up to the huge opportunity. The question was whether existing sponsors / promoters of corporate debtors (ie the company with debt and under the insolvency proceedings) can directly or indirectly acquire stake in these firms post acceptance of a resolution plan which would have entailed substantial discount to outstanding loans of lenders.

He pointed out that the key questions were — can promoters seek a huge cut from lenders and be back in the business? Does this provide a level playing field to other prospective bidders?

Does this send the right political and economic signals? The government took note of all these concerns expressed by investors, and that's what led to the recent (amendment) ordinance.

What does the recent amendment do?

Nishit Dhruva, managing partner, MDP & Partners, a full-service law firm, said with the present amendment promoters/directors and guarantors, along with their related parties of the corporate debtor or company undergoing an insolvency resolution process, are prohibited or debarred from filing resolution plans.

This was needed to prevent the back-door entry of errant promoters into the company, thereby taking advantage of the haircuts and thus getting a premium for their own wrongdoings, he added.

What are the key elements of the amendment?

The amendment has inserted two new sections in the insolvency code — Section 29A, which provides for persons ineligible to be a Resolution Applicant; and Section 235A, which provides for punishment for contravention of the provisions where no specific penalty or punishment is provided.

Section 29A says those ineligible to be a Resolution Applicant include:

Wilful defaulters (ie, those associated with non-performing assets, or are habitually non-compliant and, therefore, are likely to be a risk to successful resolution of insolvency of a company);

Those whose accounts are classified as Non-Performing Assets (NPAs) for one year or more and are unable to settle overdue amounts including interest and charges relating to the account before submission of the Resolution Plan;

Those who have executed an enforceable guarantee in favour of a creditor, in respect of a corporate debtor undergoing a Corporate Insolvency Resolution Process or Liquidation Process under the Code and others connected to the above, such as promoters or those in management control of the Resolution Applicant, or those who will be promoters or in management control of corporate debtor during the implementation of the Plan, the holding company, subsidiary company, associate company or related party of the above persons.

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