

FIRM AND DECISIVE GOVERNMENT ACTION TAKEN TO PRESERVE VALUE AND ASSETS OF IL& FS

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Ministry of Finance

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IL&FS, incorporated in 1987, is a large Systemically Important Non-Deposit Accepting Core Investment Company (CIC-ND-SI). It has numerous infrastructure assets and has played a major role in infrastructure development and financing in the country. It has 169 group companies, as in 2017-2018, including subsidiaries, joint venture companies and associate entities. A series of defaults by IL&FS Group companies in August and September, 2018 on term-deposits, short-term deposits, inter-corporate deposits, commercial paper and non-convertible debentures and the rating downgrades in some and default on some other financial instruments has resulted into massive effect in the financial markets causing redemption pressure on the mutual funds, which held such financial instruments and has also adversely impacted the sentiments on the stock markets, money markets and debt markets. The redemption pressure on mutual funds has created a large systemic risk leading to quality papers being sold at steep discounts to meet the redemption demand. The debt market shocks got transferred to the equity market sparking sell off particularly in NBFC stocks and sectors linked with NBFC financing.

IL&FS Group, as per their latest Balance Sheet has infrastructure and financial assets exceeding Rs 115000 crore is presently facing tremendous debt pressure and struggling to service around Rs. 91000 crore in debt which is the outcome of its mismanaged borrowings in the past. The financial mismanagement of the IL&FS is apparent from its rapid debt built up and misrepresentation of true state of financial fragility, which is being reflected in unprecedented rating downgrade from highly rated to a default category. Considering the capital base of the Group, the leverage is very high. The IL&FS Group is involved in many infrastructure projects including through equity and debt financing. Any impairment in its ability to finance and support the infrastructure projects would be quite damaging to the overall infrastructure sector, financial markets and the economy, considering its systemically important nature. **The Government stands fully committed to ensure that needed liquidity is arranged for the IL& FS from the financial system so that no more defaults take place and the infrastructure projects are implemented smoothly.**

The IL&FS Group, especially its subsidiary companies, IL&FS Engineering and Construction Company Limited (IL&FS Engineering) and IL&FS Transportation Networks Ltd. had got into major problems beginning 2012. This led to massive delays in execution of projects and a number of projects had become stalled infrastructure projects even before 2014. This affected their financial performance and significantly increased the leveraging as delayed projects were kept afloat by more and more debt financing. IL&FS Engineering had a series of losses beginning 2011-12 and minimal profit started after 2015-16. IL&FS Transportation Network Ltd. witnessed significant erosion of profit starting from 2012-13 and the net debt also increased more than two times from Rs. 13939 crore to Rs. 29961 crore in 2017-18. Deterioration in the financial performance and substantial leveraging of the IL&FS Group started many years ago on account of stalled projects in infrastructure sector largely owing to wrong decisions and policy paralysis before 2014.

The restoration of confidence of the money, debt and capital markets, the banks and financial institutions in the credibility and financial solvency of the IL&FS Group is of utmost importance for the financial stability of capital and financial markets. There is an emergent need to immediately stop further financial defaults and also take measures to resolve defaulted dues to the claimants. This would require a combination of measures of asset sales, restructuring of some liabilities and fresh infusion of funds by the investors and lenders. The confidence of the financial market in the credibility of the IL&FS management and the company needs to be restored. There appears to be significant liquidity gap in the Company as estimated liabilities might not have any corresponding revenues / capital flows presently. In the circumstances, replacement of the existing management by the new management appeared to be most necessary and immediately required to be done for restoring that confidence and to avoid any suboptimal liquidation of assets.

The Government, after analysing the emerging situation of the IL&FS Group come to the conclusion that the governance and management change in IL&FS Group is very necessary for saving the Group from financial collapse, which required an immediate change in the existing Board and management and appointment of a new management. Continuance of the present Board had become prejudicial to the interests of the company and its members and this management was affecting public interest because of its adverse impact on financial stability and making capital markets so adversely affected. Therefore, the National Company Law Tribunal (NCLT) was approached today by the Government under section 241 read with 242 of the Companies Act, 2013 to order supersession of the present Board of Directors of the IL&FS and its substitution by the new Board of Directors.

The Government was compelled to take this extraordinary step under section 241(2) of the Companies Act, 2013 to apply to the Tribunal for an order to prevent further mismanagement in order to protect public interest. **The decision to supersede the existing board was taken after careful consideration of a report received from the Regional Director, Mumbai under the Ministry of Corporate, Affairs which clearly brought out serious corporate related deficiencies in the IL&FS holding company and its subsidiaries.** It was noted that the consolidated financial statement of IL&FS holding company and its subsidiaries, associates and joint ventures projected a picture through highly exaggerated depiction of non-current assets in the form of intangible assets amounting to over Rs. 20,000 crores. Besides, bulk of revenue was in the form of receivables, around 50%, which was locked up in litigation and arbitration. Added

to this, there has been a sharp increase in bank deposits held in lien, which rose by Rs. 1,681.59 crores in FY 2017-18. Overall, the company has negative cash flows from operations. Further the net outflow was Rs. 7,020 crores in 2017-18. From August 2018 the company has been making repeated defaults. It has been noted that there is deep-rooted mismatch in the debt-equity ratio because of excessive leveraging, which has put a question mark in its ability to continue as a going concern if allowed to continue in the hands of the present management. The high debt stress was clearly visible in the company and its main subsidiaries for the last so many years, but was camouflaged by misrepresentation of facts. **Besides, the fact that the company continued to pay dividends and huge managerial pay-outs regardless of looming liquidity crisis shows that the management had lost total credibility. There have also been serious complaints on some of the companies for which an SFIO investigation has been ordered into the affairs of IL&FS and its subsidiaries.**

The supersession of the existing Board and its replacement by a new Board of IL&FS is the necessary first step towards restoring the confidence of the financial market in the IL&FS Group. The Government is aware of the need to supplement this with several other measures which are required to be taken. Restoration of confidence of the financial market and to ensure solvency and orderly sale of the assets of the IL&FS Group would, inter alia, require time-bound sale of assets and realisation of receivables, fresh capital infusion, restructuring of business and ensuring continued access of the IL&FS Group to the financial market to meet its present and future financing needs. The Government is committed to ensuring the financial solvency of the IL&FS Group with a view to maintaining the financial stability in the country. **Towards this end, the Government is committed to ensure that ILFS Group receive much needed temporary liquidity support. It is hoped that financial institutions would be supportive for providing urgent liquidity. The Government would also take all necessary steps to ensure that the infrastructure and other productive sectors of the economy continue to get financial resources to maintain the growth momentum of the Indian Economy, the fastest growing economies in the world.**

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