

# Resolution of Educomp Infrastructure & School Management Ltd: A Case Study

*Educomp Infrastructure and School Management Ltd. (EISML), the Corporate Debtor (CD), was established in 2006 as a wholly owned subsidiary of the listed entity Educomp Solutions Ltd. (ESL) to set up and manage school infrastructure. Through nearly 20 wholly owned subsidiaries, EISML acquired land and constructed school buildings, largely financed by bank loans. The model primarily benefited 27 promoter-controlled trusts/societies operating schools across eight states, which paid the CD fixed and variable lease rentals along with support service fees.*

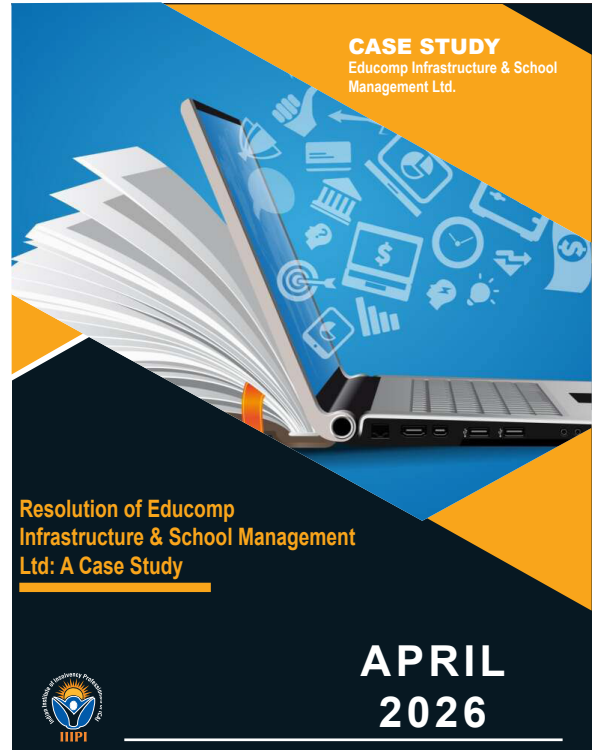
*After 2014, declining revenue flows from these trusts led to defaults on loans from eight banks. By April 2018, when EISML entered insolvency, it owned 62 properties, including 26 operational schools, and owed about ₹910 crore to its creditors. Despite the interlinked group structure, the CoC declined Group Insolvency and pursued the CIRP of the CD individually, encouraged by a strong Expression of Interest (EOI) response. However, the complex structure deterred most bidders, leaving only one Resolution Applicant, whose plan of ₹499.88 crore was approved by the CoC with 100% voting share. Finally, the CD was taken over by Jasrati Education Solutions Ltd.*

*In the present case study, Mr. Ashwini Mehra, the Resolution Professional (RP) of EISML, highlights the challenges encountered during the resolution process and the measures adopted to achieve a successful resolution of the CD. **Read on to know more...***



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## 1. Introduction

Educomp Infrastructure & School Management Ltd. (EISML), set up in 2006, is a closely held subsidiary of Educomp Solutions Ltd. (ESL), a listed Company (also admitted under insolvency). EISML, the Corporate Debtor (CD), developed and owned schools' infrastructure viz. land and buildings. At the time of admittance to insolvency in April 2018, the CD had a total of 62 properties at various locations spread across the country in seven states namely Bihar, Haryana, Karnataka, Madhya Pradesh, Tamil Nadu, Uttar Pradesh, and Maharashtra. These comprised of 26 operating schools, under 26 family-controlled Trusts/ Societies who managed the schools' operations, 12 closed/non-operating schools, 20 plots of vacant lands aggregating over 360 acres and four residential buildings. As per the business model, the CD received from the respective Trusts both pre-determined fixed lease rentals and variable lease rentals linked to a

percentage of each school's annual revenue. EISML also received service fees from the respective school Trusts on a per-student enrollment basis for, inter alia, support of the student curriculum, teacher training programs, and the school portal, which were managing the schools. These funds were received in a Trust and Retention (TRA) account of the lead lender and part thereof was utilized for payments towards the loans and interest thereon of the eight lending banks. The promoter was the MD of EISML, Chairman of ESL as also Managing Trustee/ Secretary of all the Trusts & a Society (barring two, where his father was the Managing Trustee). As per the Articles of the Trusts, the Managing Trustee could be replaced only by another immediate family member.

## 2. Reasons for Admittance to Insolvency

Over time, the CD engaged approximately 20 largely wholly owned subsidiaries to acquire land and construct school buildings in accordance with specified requirements. It raised loans aggregating ₹875 crores from eight banks for paying the subsidiaries as also for development and management of school infrastructure under several brand names at various locations across the country. The school properties and infrastructure were then leased to various trusts and a society for the operation and management of the schools. The respective school fees and other revenues were collected by these trusts, and the proceeds flowed back to the company. TRA account opened with the lead bank gradually dwindling from 2013 onwards; the aggregate revenue declined steadily from approximately ₹84 crores in FY2013-14 to ₹71 crores in FY2014-15, ₹47 crores in FY2015-16, ₹37 crores in FY2016-17, and ₹21 crores in FY2017-18. There had been unauthorized, unregistered downward refixing of lease rentals, in violation of the Master Agreements governing the loan covenants for conduct of the business by the CD, the Trusts, etc.

This was done without the written consent of the comity of lenders. Also, the fee income from various support services provided to the schools by EISML gradually stopped due to abrupt cancellation of service contracts and the franchisee business started getting diverted to another promoter owned entity from 2014

onwards. Part of the school revenues allegedly started flowing into other unauthorized bank accounts opened outside the TRA, resulting in the drying up of funds in the designated TRA account. Consequently, loan accounts with all banks turned non-performing. Despite attempts by banks to restructure the accounts, based on assurances from the promoter, under Corporate Debt Restructuring (CDR) and S4A schemes of Reserve Bank of India (RBI), there was no improvement in the position of accounts. Ultimately, the CD filed insolvency under Section 10 of the IBC 2016 and was admitted by the Adjudicating Authority (AA), National Company Law Tribunal (NCLT) Chandigarh<sup>1</sup>, on April 25, 2018. At the time of filing the application in early 2018, it owed over ₹900 crores to these banks and additionally Compulsory Convertible Preference Shares (CCPS) aggregating ₹300 crores. After the Interim Resolution Professional (IRP) demitted office soon after appointment due to health issues, the author was appointed as Resolution Professional (RP) in mid-June 2018.

***The TRA account opened with the lead bank began to dwindle from 2013 onwards, with aggregate revenue declining steadily from approximately ₹84 crores in FY2013-14 to ₹21 crores in FY2017-18.***

## 3. Claims Admitted

As on the date of admission to Corporate Insolvency Resolution Process (CIRP), the financial creditors had lodged claims of ₹1198.26 crores of which ₹904.94 crores were admitted by the RP. Besides, the operational creditors had also lodged claims of ₹6.81 crores of which ₹4.96 crores were admitted. Employees' claims of ₹0.13 crores were admitted to the extent of ₹0.11 crs. The following chart shows the claims admitted against the CD by the RP:

**Security Structure:** Apart from the mortgage of the

<sup>1</sup> *Educomp Infrastructure & School Management Ltd. vs. Andhra Bank*, CP (IB) No. 10, Chd. Hry. 18 with CA No. 87/ 2018 dated 25.04.2018.

## Case Study

### THE RESOLUTION PROFESSIONAL

**Table 1: Creditors and their dues**

Sr. No.	Name of Entity	Amount Due (₹ crores)
1	Axis Bank	227.71
2	State Bank of India	221.92
3	Punjab Natl. Bank	93.23
4	Yes Bank	117.98
5	Corporation Bank	44.30
6	Karnataka Bank	44.70
7	Andhra Bank	66.30
8	Bank of India	88.80
9	Others (OCs & Employees)	5.07
	<b>TOTAL</b>	<b>910.01</b>

individual properties in all cases barring one, the credit facilities were governed by a MSSA (Master Security & Support Agreement) dated May 3, 2014 entered into between the Trusts, Schools, Societies, EISML, subsidiaries, guarantors (i.e. ESL, Shantanu Prakash and Jagdish Prakash), the share pledgees (i.e. ESL, Educomp School Management Limited, Shantanu Prakash and Anjalee Prakash), Security Trustee and Axis Bank (as the Monitoring Institution). The MSSA provides for first charge over all fixed assets of the Trusts, Societies and subsidiaries, brands, intangible assets, current and non-current assets with certain exclusions in favour of the lenders.

**“The Transaction Audit revealed a whopping figure of around ₹905 crores in the realm of Avoidance Transactions or PUFÉ (Preferential, Undervalued, Fraudulent, and Extortionate) Transactions.”**

#### 4. Avoidance Transactions

The Transaction Audit revealed a whopping figure of around ₹905 crores in the realm of Avoidance Transactions or PUFÉ (Preferential, Undervalued, Fraudulent, and Extortionate) Transactions. Section 45 (undervalued) transactions were estimated to be ₹163.20 crores (four transactions overlapped with Section 66), and Section 66 transactions (fraudulent) were estimated to be ₹343.76 Crores. Approximately ₹561 crores of prima facie suspicious transactions were considered indeterminate due to lack of

conclusive data/records, hindered by the lack of access to the Accounting Platform. Till the conclusion of the CIRP, no substantive hearing on the Avoidance Application was conducted by the AA. At the stage of implementation of the Resolution Plan, the Monitoring Committee reached a consensus that the application would be pursued by the Successful Resolution Applicant (SRA) after implementation, with an agreed sharing arrangement of any recoveries with the financial creditors. Subsequently, the Monitoring Committee approved the transfer of the application from the RP to the SRA.

The Financial Creditors obtained a forensic audit report from the Transaction Auditor and based on the findings, most of the banks declared the CD and promoters as willful defaulters. The promoters' financial misdemeanors are the subject matter of an investigation by the Central Bureau of Investigation (CBI) based on a complaint filed by the State Bank of India (SBI) on behalf of other member banks. Even as the CIRP had commenced, Serious Fraud Investigation Office (SFIO) was already investigating the Group following the insolvency proceedings against ESL and one other company of the Group.

#### 5. Valuation of the CD

The valuation exercise was entrusted to two registered valuers to determine the Fair Value and Liquidation Value of the CD in accordance with Regulation 35 of the IBC. Their assessments are summarized below:

Thus, the average Fair Value of the CD was ₹957 cr. and Liquidation Value ₹462 cr. as on the date of commencement of CIRP. The average fair value

**Table 2: Valuation of the CD**

Sr. No.	Name	Fair Value (₹ in crores)	Liquidation Value (₹ in crores)
1	Valuer 1	900.48	437.47
2	(Valuer 2)	1013.69	487.3

(₹957 cr.) exceeded the admitted financial creditors' claims (₹910.01), as the loans were largely backed by real estate assets, which typically appreciate in value.

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### 6. Approval of Resolution Plan

The Expression of Interest (EOI) was invited from interested parties in mid-2018. A total of 21 EOIs were received, including several prominent players in primary and higher education; 14 were shortlisted as eligible bidders and granted access to the VDR. Gradually, all but three of the shortlisted entities exited for various reasons, primarily due to significant uncertainties arising from the organizational structure and legal mandates within the Educomp Group, which effectively impeded the transfer of control over the Trusts and their revenue streams to the SRA.

Consequently, access to the business cashflows would not flow to the SRA, making it a highly risky revenue model for the new owners/ successful bidders of EISML. Of the three who finally bid, one bidder was rejected as it failed to deposit the Earnest Money Deposit (EMD) and the other chose to step down after initial discussions with the CoC, leaving only one bidder. As regards the Plan submitted by the lone remaining bidder, there were initial hiccups in the approval process arising from the lenders' discomfort with the source of funding of the Plan and the inadequacy of the Plan amount. The bidder addressed these concerns making requisite improvements in the bid structure and amount. The revised Plan secured about 100 per cent approval of the CoC, and the bidder was declared as the Successful Resolution Applicant (SRA). The bid

aggregated ₹499.88 crores of which ₹363.88 crores was to be paid upfront in cash and the balance by issuance of ₹136 crores as 0% Compulsorily Redeemable Non-Preference Shares payable in four instalments from the 12<sup>th</sup> to the 20<sup>th</sup> year. The CoC approved the Resolution Plan with the requisite 100 per cent voting share in its meeting held in September 2019. The RP submitted the Resolution Plan to the NCLT in October 2019, and AA granted its approval<sup>2</sup> on December 14, 2020. Finally, the CD was taken over by Jasrati Education Solutions Ltd.

### 7. Challenges faced by RP

- At the commencement of the CIRP, all personnel of the Corporate Debtor had left employment, and only one junior official was placed in charge of handing over the records. This handover was carried out in a perfunctory manner, and the official also left soon thereafter. Consequently, given the paucity of funds with the Corporate Debtor, the RP appointed a junior graduate accountant in charge of day-to-day accounting operations, with oversight from the back office.
- There was a lack of access to the accounting software used by EISML, which remained under the direct control of its parent company, ESL; access for others had been blocked by its RP for security reasons.
- The CD had been engaging Haribhakti & Company, as its statutory auditor but they resigned after the audit of FY2015-16 and were replaced by a single person audit firm whose audits left many questions unanswered and who chose to discontinue audit after the last audit of FY2017-18.
- The Transaction Auditor's work was severely handicapped because of the lack of accounting and other financial records. The non-availability of access to past records on the Accounting Platform

<sup>2</sup>CA No. 898 / 2019 in CP IB No. 10/Chd/ Hry/ 2018 dated 14.12.2020.

added complexity to their exercise, consequently leaving a whopping amount of ₹561 crs. of possibly suspicious transactions indeterminate.

- e) A Section 19 Application under the IBC seeking cooperation from promoters of schools and Trusts in providing important information to help value maximization did not elicit any meaningful support from them. Additionally, the NCLT also ruled that their writ does not extend to the non-corporate bodies like schools and Trusts, therefore, they could not be directed by the NCLT to cooperate with the RP. However, the NCLT directed the Insolvency and Bankruptcy Board of India (IBBI) to initiate proceedings against the promoters and directors, which remains sub judice to date.

***The Whole Time Director of the CD engaged in filibustering before courts and other forums, including the Haryana Police, by filing complaints against the RP and the financial creditors.***

- f) The Whole Time Director (WTD) of the CD engaged in filibustering before courts and other forums, including the Haryana Police, by filing complaints against the RP and the financial creditors, and frequently adopted a disruptive approach during CoC meetings. This led to significant diversion of time and resources from the core CIRP process for all stakeholders.
- g) Substantial time was lost due to the advent of the COVID-19 pandemic, during which the SRA was unable to pursue implementation of the approved Resolution Plan. Subsequently, ostensibly due to the lack of a funds tie-up to deposit the plan proceeds, the SRA engaged in procrastination by alleging encroachments on land parcels and closed school properties. However, except for one, all 61 properties were found by teams of lenders and SRA representatives to be available for unfettered acquisition by the SRA. The SRA's challenge before the NCLAT in this regard was also rejected, and it was directed to implement

the plan forthwith. In the meantime, the SRA succeeded in tying up the requisite funds with an NBFC.

- h) Given the financial condition of the CD, the lenders were reluctant to provide financial support in the day-to-day running of the CD, which created friction with the back-office entity as also came in the way of appointing a Company Secretary to ensure secretarial compliances. As such, at the time of the Plan implementation in a very short time window to be completed within the FY2022-23 in line with financial creditors understandable expectations, the help of a professional secretarial agency was taken based on priority payment of their approved fees, in the form of unpaid CIRP cost, from the proceeds of the Resolution Plan.
- i) The lack of timely financial support from the financial creditors compounded the tensions arising from dealing with a recalcitrant SRA. Like other stakeholders, including the RP, the financial creditors could not discern any light at the end of the tunnel in the absence of confidence-building measures from the SRA and remain uncertain about how long their support toward CIRP costs would remain locked in.
- j) Although the Resolution Plan was approved in December 2020, the SRA appears to have faced difficulties in tying up the requisite funds for its implementation. The lack of financial support from the lenders created operational hurdles, resulting in mounting unpaid expenses and an inability to meet costs associated with verifying the allegations of land encroachments raised by the SRA, which were largely perceived as attempts to delay implementation of the Plan.

### 8. Case Prognosis and Postmortem

In the initial stages of EISML's formation, loans were raised to implement the business of building and managing school infrastructure at various locations across the country. At that time, operations functioned smoothly, and various stakeholders, including banks dealing with the group entities, were reassured that

they were effectively engaging with the group as a whole, led by the individual promoter.

It is common practice and perfectly reasonable for commercial ventures to operate through groups of entities and for each entity in the Group to have a separate legal personality. Separate entities are often set up to dissociate specific assets from general liabilities, the purpose often being to not only raise funding on more favorable conditions but also take advantage of statutory benefits made available by the legal characteristics particular Group entities.

When these businesses are solvent and operational, general perception is typically that they function as a unified Group in the eyes of customers, suppliers, creditors, etc. Nevertheless, as a normal credit risk measure, the lenders often seek guarantees or credit support from ultimate parent and the principal individual promoters, which were readily provided in the instant case. Formal divisions were ignored under the impression that they were dealing with the Group identified with the promoter. Consequently, a sense of complacency gradually set in with all agencies, including lenders, dealing with any of the group entities.

***Annual reports were allegedly manipulated by concealing losses and obscuring the true nature of transactions through intra-group entities, thereby creating a false sense of comfort among stakeholders, including lenders.***

However, as the case of EISML revealed, the use of the Group structure provided promoters and key personnel with opportunities to manipulate the corporate form and evade regulatory and fiduciary responsibilities. Annual reports were allegedly manipulated by concealing losses and obscuring the true nature of transactions through intra-group entities, thereby creating a false sense of comfort among stakeholders, including lenders. Assets appear to have been transferred within the enterprise without proper bookkeeping, and intra-group claims and payables remained indeterminate due

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to opaque record-keeping practices, board minutes, and accounting. The result was significant confusion regarding inter se liabilities and asset ownership, which hampered the Transaction Auditor's ability to classify a substantial volume of suspect transactions into the appropriate categories of PUFEE transactions.

While the Group Insolvency approach for 'substantive' consolidation would have otherwise been ideal in this case, somehow, despite the suggestion coming from an opinion of a well-regarded law firm, the financial creditors did not favor the approach at the material time. It is felt that this was possibly due to the overwhelming initial response to the request for EOIs and the lenders felt it better not to spread the canvas too much and focus on the approach adopted by proceeding against the CD only. Perhaps, in the minds of the financial creditors, any other approach would have resulted in further time delay.

## 9. Conclusion

The RP faced numerous challenges from the very outset of the CIRP. There was a severe shortage of funds, which constrained even routine operations. Members of the erstwhile Board were often uncooperative and, at times, disruptive. The existing personnel on the CD were largely unavailable, making it difficult to keep the business running. Creditors were hesitant to infuse additional cash for operations. The CD also had a large number of widely dispersed real estate units, making supervision and control difficult. There was no adequate secretarial support for statutory MCA (Ministry of Corporate Affairs) compliances. Further, the SRA remained recalcitrant, apparently due to delays in tying up finances for the Resolution Plan. Judicial delays at the NCLT level added to the difficulties. Despite these constraints, the RP successfully completed the CIRP and ensured that financial and other creditors received their dues under the Resolution Plan.