CoC Needs to be Fair towards all Stakeholders and Transparent in Discharge of its Responsibilities: Shri Sudhaker Shukla, WTM, IBBI

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Shri Sudhaker Shukla joined as a WTM of IBBI on 14th November 2019. He is currently looking after Research and Regulation Wing comprising Corporate Insolvency, Corporate Liquidation (including Voluntary Liquidation), Individual Insolvency and Individual Bankruptcy, Research & Publication, Data Management & Dissemination and Advocacy. In addition, he is also handling Human Resources, National Insolvency & Graduate Insolvency Programmes, Continuing Professional Education and Knowledge Management & Partnership divisions in the IBBI.

Shri Shukla served as a member of the Indian Economic Service (IES) for over 34 years in various capacities across Ministries and Departments of the Government of India. His last assignment was as Chief Economic Adviser in the Ministry of Rural Development. Earlier, he served as Adviser in African Development Bank. He had wide experience in dealing with various regulations.

In an Exclusive Interview with IIIPI for **The Resolution Professional**, Shri Shukla expressed his views on research, regulations and various other issues related to IBC Ecosystem. ***Read on to know more***....

IIIPI: IBC, 2016 has completed over five years of its implementation. Covid pandemic has acted as a disrupting force putting brake on many initiatives that were envisaged earlier. On the other hand, Covid has prompted many ameliorative measures as well. What were the key challenges that IBC regime has faced during the journey so far and how they were responded?

Shri Shukla: The introduction of IBC, 2016 (code) has been the most holistic and impactful insolvency resolution mechanism in India till date. The Code provided a time-bound framework for resolution of creditor situations in India. Beyond revival of firms and realisations for creditors, the behavioural change in debtor-creditor relationship prompting substantial recoveries for creditors outside the Code, while improving performance of firms have been some credible accomplishments which are captured well by significant leap in the ease of doing business rankings.

It is old saying foundation of success is laid through encountering tough challenges. IBC success story also had its fair share of challenges. To overcome them, the Code has witnessed several legislative quick fixes. The imperfect market conditions mature with time. The Hon'ble Supreme Court in the matter of *Swiss Ribbons Pvt. Ltd. & Anr. Vs. Union of India* held that: *"An economic law is essentially empiric. It evolves continuously through experimentation. To stay experimentation in things economic is a grave responsibility, and denial of the right to experiment is fraught with serious consequences to the nation."* The Code has so far witnessed six legislative interventions and 75 amendments to various regulations; which stand as testimony to a resolve for continuous search for improvement.

Further, the beneficiaries of earlier regime are continuously making serious attempts to latch on to favourable systems leading to intense legal scrutiny of every provision of the Code. This added to some cost and time over runs in some processes and difficulties in implementation. However, good part of the story is the evolving jurisprudence has confirmed all the important

legislative interventions made to tighten the regime to make the regime out of the reach of ineligible corporate persons.

Another challenge has been that at the time of IBC coming into force, the ecosystem associated with implementation of provisions were altogether absent. Situation has improved in leaps and bound. Despite Ecosystem being strengthened, extra-ordinary delays be at the admission stage or in carrying out the insolvency processes or in the implementation of resolution plan remains a major concern in moving forward. While as compared to pre-IBC days, timelines for resolution of stressed assets have shown improvement from 4.3 years earlier to an average of 400 days now, yet we are no way near to timelines as prescribed under the statute. It is important to have shorter time period for resolution as it is well evidenced fact that time take in resolution and realization of value are inversely related.

Success of insolvency proceedings is dependent on quality of professional services. At times lack of professional acumen on behalf of some insolvency professionals and valuers despite being regulated entity and also lack of code of conduct in respect of unregulated entities i.e. CoC has invited a few adverse commentaries from the courts. Though these numbers are exceedingly small, but they largely drive the market perception on the functioning of the insolvency regime in the country and this is needed to be avoided.

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Lastly, it will not be out of context that a major challenge to IBC has emerged recently in the form of force majeure situation posed by Covid Pandemic. With rise in stress levels and dearth of resolution applicants, a glut in the distressed asset market has been anticipated. This apart from raising the threshold limit of default to minimum one crore, led to one year suspension of Section 7, 9 and 10 of the Code. Indications are that NPA situation has not worsened during the pandemic period so far. Against projected figure of about 11%, actual GNPA in 2020-21 has recorded moderate number of 7.48%. Further, evidence suggests that NPA eventually translates into corporate stress but with a lag. These are early days to predict insolvency numbers, nevertheless, as pandemic is unfolding in waves, utmost vigil on emerging situation will be required.

IIIPI: The experience so far shows that liquidation cases far exceed the resolutions under IBC. Though legacy cases seem to the primary reason here, how do you visualize the framework to be more resolution-oriented than being focused on recovery or liquidation.

Shri Shukla: In the context of dealing with distressed assets, resolution not recovery is the first order priority under the Code. In *Swiss Ribbons Pvt. Ltd. & Anr. Vs. Union of India & Ors* the Apex Court has noted that the Preamble does not, in any manner, refer to liquidation, which is only availed of as a last resort if there is either no resolution plan or the resolution plans submitted are not up to the mark. Even in liquidation, the liquidator can sell the business of the corporate debtor as a going concern.

Nevertheless, the processes under the Code have yielded liquidation of 1349 companies against resolution of 394 CDs. Three-fourth of these companies were either sick or defunct when they entered insolvency proceedings. The companies rescued had assets valued at Rs. 1.46 lakh crore, while the firms refereed for liquidation had assets valued at Rs. 0.52 lakh crore which was just about 7.5 % of total admitted claims when they were admitted to CIRP. Thus, in value terms, about 75% of distressed assets have been rescued. Though it can be concluded that in terms of sheer numbers, while about 3/4th of cases are ending in liquidation, in terms of value rescued, contribution of liquidation cases is just about 25%.

The government, the central bank and the judiciary in India have also been very proactive in ironing out issues with respect to the insolvency code and making it more effective. The newly introduced pre-packaged insolvency resolution process will also help the resolution of stress for MSMEs going forward and thus improve the efficiency of the Code.

However, it is to highlight that liquidation versus resolution debate is misnomer to start with as numbers in each segment needed to be seen as outcome of market driven processes. Successful resolution depends on several factors, including firm specific factors like nature of business, sector specific factors and larger economic conditions. Equally important is the stage at which IBC process is initiated. Value preservation is easier and

maximisation higher through resolution when insolvency proceedings are initiated at the early stages of stress and when the business continues as a going concern. The IBC endeavours to maximise the value of the existing assets, not of the assets which do not exist. Therefore, the cases coming with a legacy of litigation or contest under earlier option and representing specific sectors like services sector, despite having technically devoid of any asset base are not expected to end in a meaningful resolution. In such cases of economic distress, liquidation may remain a preferred choice of the market, in times to come.

IIIPI: COCs are not regulated under IBC which at times causes differences with other stakeholders. How do you think self-regulation of COC could help improve the delivery?

Shri Shukla: The Hon'ble Supreme Court in the matter of Committee of Creditors of *Essar Steel India Limited Vs. Satish Kumar Gupta & Ors.* held that the insolvency resolution is ultimately in the hands of the majority vote of the CoC. It established the primacy of CoC by stating that it is the commercial wisdom of the CoC to decide as to whether or not to rehabilitate the CD by accepting a particular resolution plan.

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Under the Code, the CoC have a statutory duty to perform, and it discharges a public function. It must, therefore, apply the highest standards of duty of care. It must not only follow the due process, but also be fair towards all stakeholders and transparent in discharge of its responsibilities. Presently, the conduct and decision making of the CoC is not subject to any regulations, instructions, guidelines etc., however, the CoC must pursue upon the responsibilities and vested upon it by the Code. In that way, some form of self-regulation may be beneficial.

The Code has demarcated responsibilities of CoC and IP, while assigning certain responsibilities to them jointly. The CoC may neither encroach upon the role of IP and nor allow the IP to encroach upon its role. The CoC must have competent and empowered representatives of FCs. The representatives must attend the meetings, deliberate the maters, and take decisions in accordance with the provisions of the Code. This will prevent delay in concluding of the process and consequential depletion of value.

IIIPI: How can pre-pack framework for MSMEs alter the dispensation for different stakeholders especially lenders in the backdrop of pandemic?

Shri Shukla: MSMEs contribute significantly to gross domestic product and provide employment to a sizeable population. Further, as World Bank's study indicate MSMEs have been disproportionately affected by the pandemic. The COVID-19 pandemic has impacted their business operations and exposed many of them to financial stress. Resolution of their stress requires different treatment, due to the unique nature of their businesses and simpler corporate structures. Accordingly, PPIRP provides an efficient alternative insolvency resolution process under the Code for corporate MSMEs, that ensures quicker, cost-effective and value maximising outcomes. It is also least disruptive to the continuity of businesses.

As regards lenders, the process is based on mutual understanding and negotiation with the debtor in an informal setting which provides flexibility for the creditors. The process is quick and less costly which results in higher realisation for creditors. The chances of resolution are higher as the business continues to be a going concern, managed by the promoter, without any disruption in operation which prevents any erosion of value. The challenge mechanism ensures that there is value maximisation and also that the applicant gives his best efforts for resolution.

IIIPI: IPs, especially those joining afresh, often highlight concerns about not getting assignments. Many others getting assignments complain about not getting a reasonable minimum fee. Is there a need for broad-basing the profession by enhancing roles of new or small-sized IPs, for orderly development of profession?

Shri Shukla: A key supporting institution under the Code is insolvency profession. An insolvency professional (IP) exercises the powers of the Board of Directors of the firm under resolution, manages its operations as a going concern, and complies with applicable laws on behalf of the firm. He conducts the entire insolvency resolution process: he is the fulcrum of the process and the link between the Adjudicating Authority and stakeholders - debtor, creditors financial as well as operational, and resolution applicants. Thus, the Code casts a wide array of duties upon the insolvency professional.

Although there might be a large number of IPs, however, a large number of them decide not to take up insolvency practice and do not apply for AFA (Authorisation for assignment). It could be due to a variety of reasons like the insolvency practice is a full time practice rather than simply being an additional area of practice for the professional. Further, the insolvency profession like other professions is market oriented. The insolvency professionals would have to carve out a niche for themselves and make a mark in the market to get work. There are also young professionals coming into the market who have graduated from the Graduate Insolvency Programme.

However, newer avenues for work are opening for the professionals in the insolvency sphere. The newly introduced pre-pack process will provide opportunities to IPs regarding resolution for MSMEs. With the growth of insolvency landscape, the opportunities for the insolvency profession is also poised to grow. Further, with the roll out of provisions for individual insolvency and bankruptcy, the demand for services of IP will grow manyfold.

On the renumeration issue, Bankruptcy Law Reforms Committee (BLRC) opined that 'While the market is evolving, the Code tries to ensure that there is as much transparency about the behaviour and the performance of individual insolvency professionals that the professional, creditors and debtors are incentivised to behave optimally.....The Committee feels it is prudent to allow the market to develop and competition to drive charges of the RP rather than setting these in the Code, or in regulations."

With the goals marked by the preamble of the Code in place, it is felt that the next phase of the law will definitely be in the areas of group insolvency, cross-border insolvency, and fresh start process for individuals.

IIIPI: How do you visualize the IBC regime or distress resolution in next 3 to 5 years taking the shape in terms of law, systems, and processes?

Shri Shukla: In a limited span of 5 years, the Code has undergone numerous changes. With the goals marked by the preamble of the Code in place, it is felt that the next phase of the law will definitely be in the areas of group insolvency, cross-border insolvency, and fresh start process for individuals. These will require amendment to the law. After successful implementation of corporate insolvency, individual insolvency could be the next frontier. There will be challenges in implementing these provisions of the Code which surely will be addressed through stakeholders' consultations.

Some progress has already made in this direction. The Hon'ble Supreme Court has in the matter of *Lalit Kumar Jain Vs. Union of India & Ors*. upheld the Central Government notification dated 15th November 2019, which brought into force provisions relating to the personal guarantors (PGs) to CDs. This would complement the corporate insolvency regime and put personal guarantors and corporate guarantors on a level playing field. Further, the resolution of Jet Airways and Videocon Industries cases exemplified a need for a comprehensive cross-border insolvency group insolvency regime under the Code.