



REVITALIZING STRESSED ASSETS: INDUSTRY PRACTITIONERS PERSPECTIVE

PRESENTATION TO BANKRUPTCY LAW REFORM COMMITTEE (BLRC)

July 31, 2015

NORTH AMERICA EUROPE MIDDLE EAST LATIN AMERICA ASIA



AGENDA

- I. Findings of A&M survey, industry concerns and wish-list
- II. Revival – The preferred path
- III. Annexure



Objective of the study

To identify practical challenges in the existing bankruptcy, insolvency and stressed asset resolution mechanisms

To aggregate feedback on the proposed changes in the interim BLRC report from industry practitioners

To identify gaps, highlight best practices from other countries and suggest measures that are best suited for Indian environment



We met all the key stakeholders in the industry

Coverage statistics

- 31 industry practitioners across 18 organizations

- 39% banks (public, private and foreign)

- 22% special situation funds – domestic and overseas

- 16% asset reconstruction companies

- 22% law firms and investment banks / advisors

Methodology

- Primary interviews

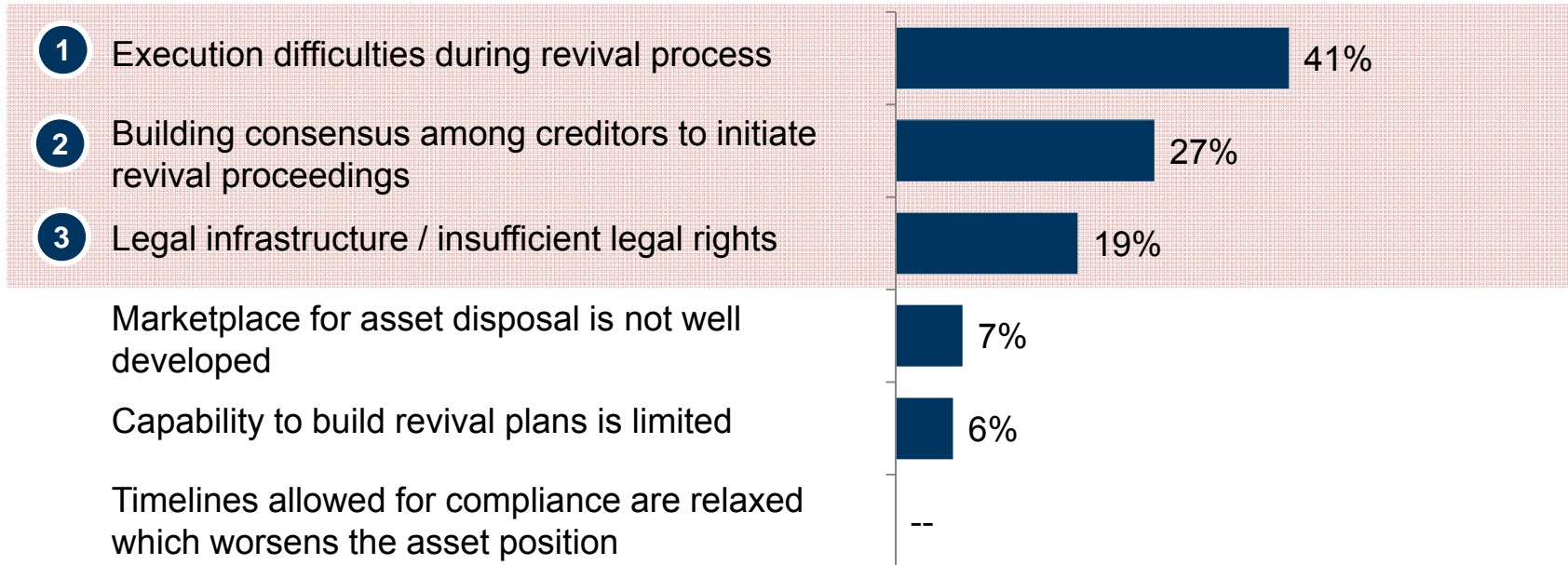
- Anonymous survey designed on the BLRC report



Execution during revival, building consensus among creditors and insufficient legal rights are top three challenges faced by industry (1/2)

Select top three challenges in the current set up with respect to revival of stressed assets

Weighted score, % of respondents



“Need a time bound restructuring process”

“Can’t wait for two years for lenders to come on the same page”

“Legal rights are only on paper”

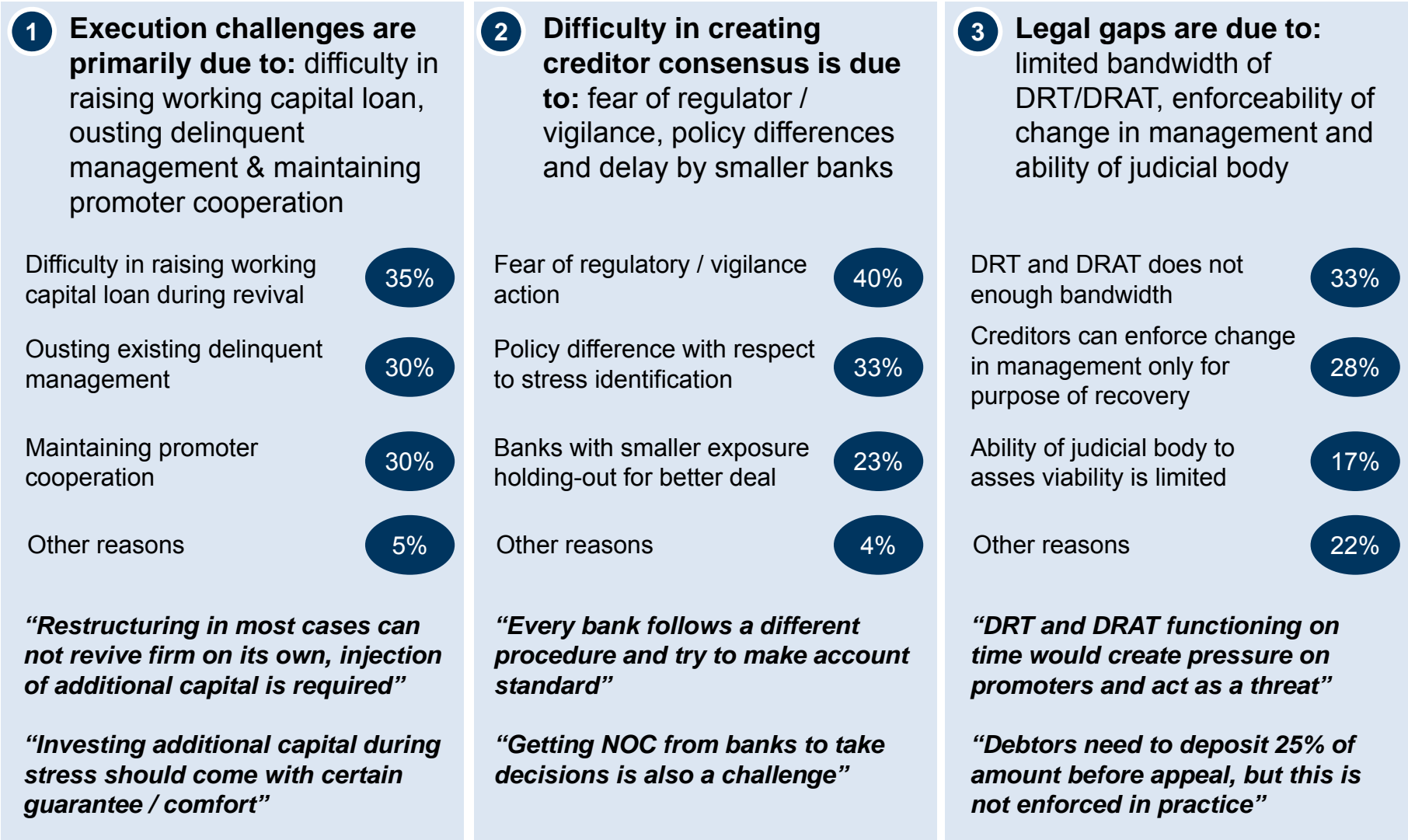
“We need to develop an independent body (administrator) who takes care of the asset, similar to what is there in the UK”



Execution during revival, building consensus among creditors and insufficient legal rights are top three challenges faced by industry (2/2)

Select top two reasons for gaps in respective areas

Weighted score, % of respondents





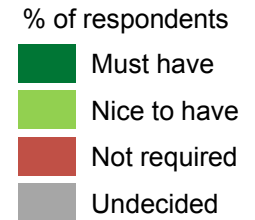
BLRC proposal has been successful in allaying many of the concerns of the industry (1/2)



Area	Proposed changes by BLRC	
Initiation of revival proceedings	Decision on rescue to be made within two months of filing of initial application	92% Must have, 8% Nice to have
	Allowing unsecured creditors to initiate rescue proceedings	38% Nice to have, 46% Not required, 15% Undecided
Building creditor consensus	Involvement of secured creditors in the appointment of Company Administrator during restructuring	100% Must have
	Ensure that consent of creditors who are not affected by a scheme is not taken	15% Must have, 23% Nice to have, 23% Not required, 31% Undecided



BLRC proposal has been successful in allaying many of the concerns of the industry (2/2)



Area	Proposed changes by BLRC	
Execution during revival procedure	Decreasing moratorium duration from 120 days to 30 days when debtor companies initiate rescue proceedings	46% (Nice to have), 31% (Not required), 23% (Undecided)
	Allowing the Company Administrator to take over the management or assets of the debtor company suo-moto	92% (Must have), 8% (Nice to have)
	Allow Company Administrator the power to raise both secured and unsecured loan during revival	38% (Must have), 38% (Nice to have), 8% (Not required), 15% (Undecided)
Legal infrastructure	Introduction for at least one bench of the NCLT in every state with a High Court	57% (Must have), 43% (Nice to have)
	Establishment of a statutory administrative mechanism for rehabilitation of distressed but viable MSMEs	14% (Must have), 57% (Nice to have), 29% (Not required)



Industry concerns and wish-list

- **Process needs to create a reasonable “fear” of an unfavorable outcome for borrowers who try to “game” the system**
 - Expedite action against wilful defaulters or perpetrators of fraud
 - Have financial incentives / penalties

- **Clarity and predictability of judicial / bankruptcy process needs to be high, in terms of:**
 - Interpretation of laws and guidelines
 - Enforcement of guidelines such as timelines for judgment etc.
 - Time taken to complete the process
 - Jurisdiction of competent authorities

- **Every new judicial system has faced the same issues such as lack of infrastructure, qualified personnel, speed, overreaching jurisdictions etc.**

- **Success of the new process hinges on the capability of people at various levels**
 - The capability cannot be similar to that of the current (average) Presiding Officers / Official Liquidators
 - There is limited scope to develop a “one size fits all” approach – need to take subjective decisions requiring assessment of alternatives
 - Need to create an ecosystem of qualified / certified agencies and authorities that can take commercial decisions and play the role of company administrators



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Key elements required for revival under Indian Insolvency Code (1/3)

- **Debtor should be required to initiate the insolvency proceedings by filing the application with the bankruptcy court, if in case the company can not meet its on-going obligations (“wrongful trading”);** in case the debtor fails to do it, necessary criminal / civil penalties should be applied to Company Directors and Management

- **Obligation to demonstrate the viability of business should lie with the debtor company**
 - Within **60 days** of initial application, Company Administrator should present the viability plan (liquidation vs. reorganization)
 - Debtor should be mandated to disclose all the obligations – secured and unsecured payments, employee related and statutory payments (“creditor obligations”) within 30 days on initiation of the proceedings
 - Debtor should disclose monthly financial statements within 45 days from the end of the month
 - Debtor should submit a plan of reorganization **within 180 days** of initial application and can be extended with the consent of bankruptcy court
 - Approval of the plan will require:
 - **Two-third majority** of secured creditors by value and fifty percent by volume
 - More than fifty percent of unsecured creditors by value; in case of non-agreement of unsecured class of creditors, “**cram-down**” provision should be available assuming the reorganization / revival plan is treating all the class of creditors “fairly and equitably”, following the absolute priority rule and prohibiting payment to the holders in a senior class more than the full value of their claims or interests



Key elements required for revival under Indian Insolvency Code (2/3)

- **Within the framework of NCLT, there should be a separate jurisdiction for handling bankruptcy cases**
 - Once the proceeding begins, only bankruptcy court should have full jurisdiction on all the cases related to the debtor and should be empowered to dispose all the matters

- **Automatic interim moratorium should be placed until bankruptcy court decides on the application of the moratorium; clear list of grounds should be laid down to guide bankruptcy court decision**

- **Company Administrator should be allowed to appoint auctioneer or by himself auction the assets (to be approved by bankruptcy court)**
 - Major benefit which should be provided by bankruptcy court is that debtor's assets are transferred to the purchaser free and clear of virtually all liens and claims
 - No related party and employees of the debtor company should be allowed to participate in the auction process



Key elements required for revival under Indian Insolvency Code (3/3)

- **Bankruptcy court should provide for protection to rescue financing**
 - Debtor should have the ability to pledge unencumbered assets to raise rescue financing
 - Any rescue financing should be approved by the bankruptcy court and may have a lien that has priority over secured creditors and a claim with superior priority to administrative expenses (including employee claims)
 - During revival, debtor has to meet all obligations relating to the operations of the business

- **SARFAESI should be repealed and any relevant clauses should become part of the Insolvency code**

- **Administration is an expensive process and there should be clear guidelines with respect to the priority of administrative fees**
 - Indemnity to administrators and third party agencies will reduce the entry barriers and allow more professional firms to enter the space



A&M suggestions to the “Open questions” (1/2)

- **Should secured creditors be allowed to initiate formal rescue proceedings on the ground of likelihood of insolvency?**
 - Secured creditors should be allowed to initiate the formal rescue proceedings but the debtor should have the right to object and demonstrate viability

- **Should unsecured creditors be allowed to initiate formal rescue proceedings on the ground of likelihood of insolvency?**
 - Unsecured lenders (debenture / bond-holders / NBFCs) should require a minimum of three parties to initiate an involuntary filing
 - Unsecured trade creditors should not be allowed to initiate formal rescue proceedings since the unsecured creditors always have a recourse of not supplying the materials

- **Should pre-packed schemes of rescue (with minimal involvement of the NCLT) be allowed as part of a scheme of debt restructuring?**
 - Yes, avoids unnecessary expenses and time



A&M suggestions to the “Open questions” (2/2)

- **Should the preferred status of the Crown over unsecured creditors under insolvency law be abolished? If so, what safeguards should be provided to mitigate the possibility of misuse of such benefit?**
 - No, it should not be abolished but the government should provide necessary documentation to prove the claim

- **What outcomes should be considered for reforming the personal insolvency regime in India?**
 - Should be treated in the same manner as debtor company

- **Should the proposed Insolvency Code provide for a separate insolvency processes for small businesses like voluntary auctions?**
 - Should be treated in the same manner as debtor company

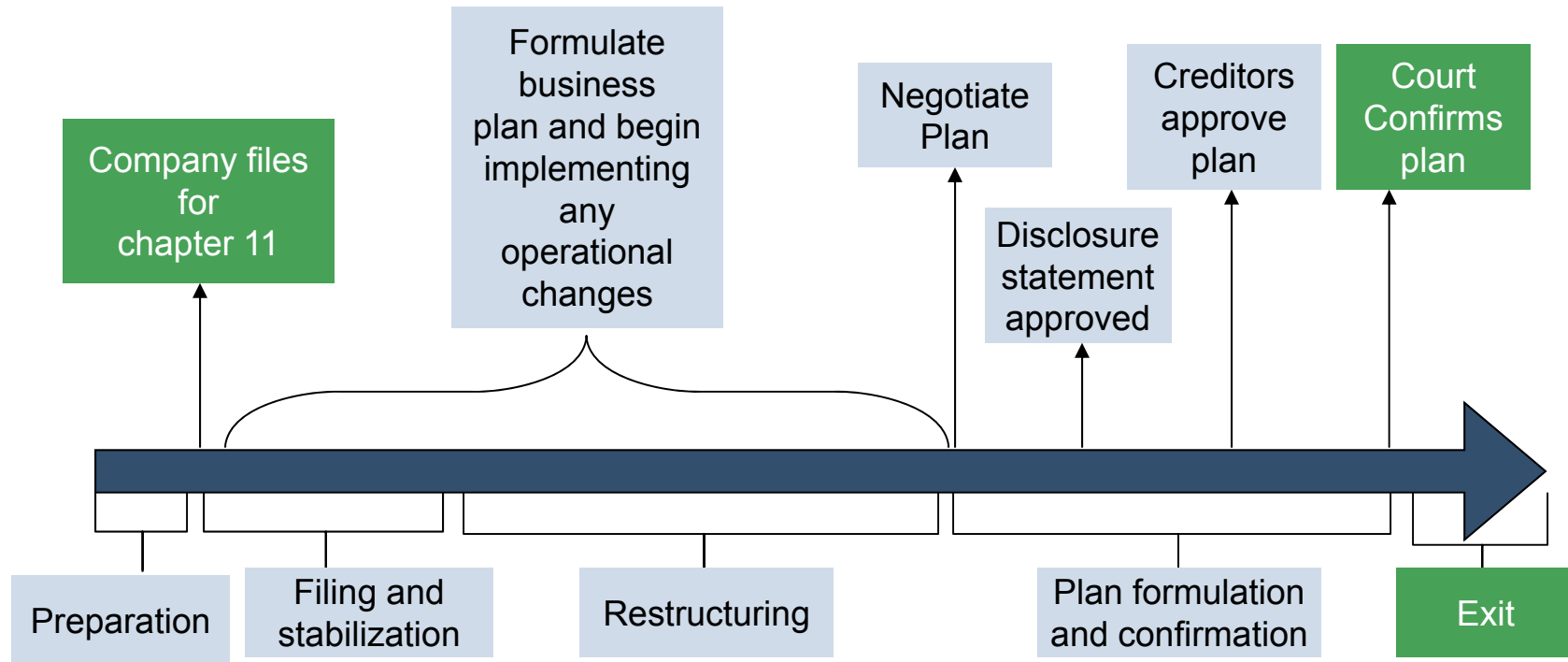


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Phases of traditional Chapter 11 case



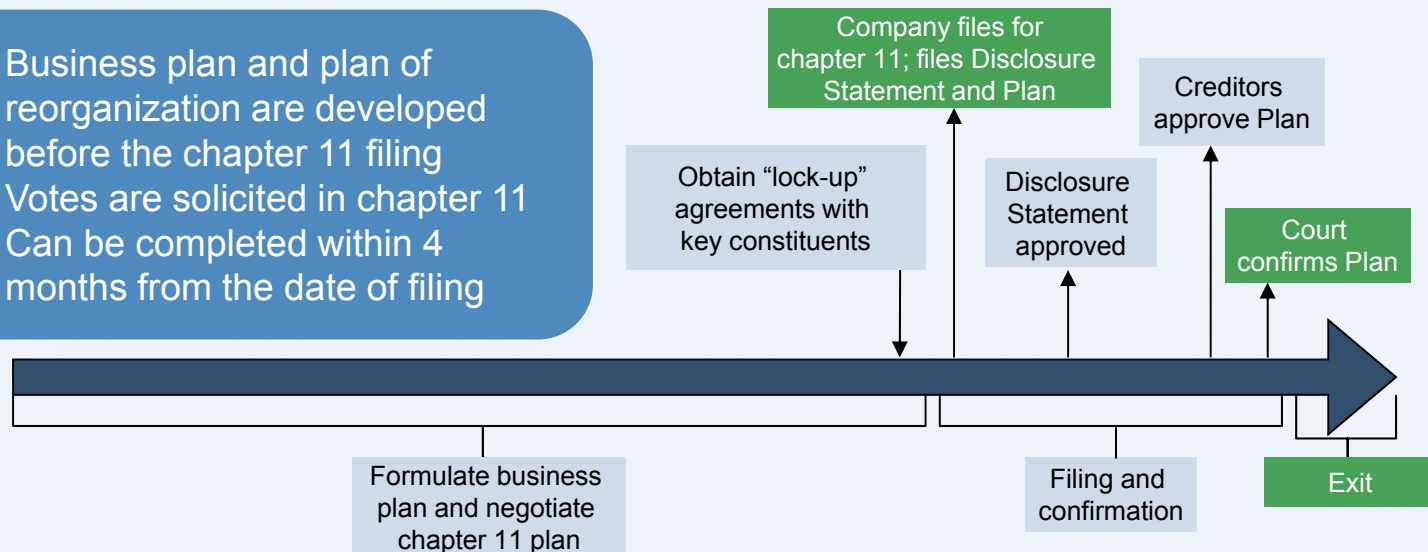
In a “traditional” chapter 11 case, the chapter 11 filing occurs first, an operational business plan is developed or finalized while in bankruptcy and then a chapter 11 plan of reorganization is negotiated.



Benefits of alternatives to traditional Chapter 11 case

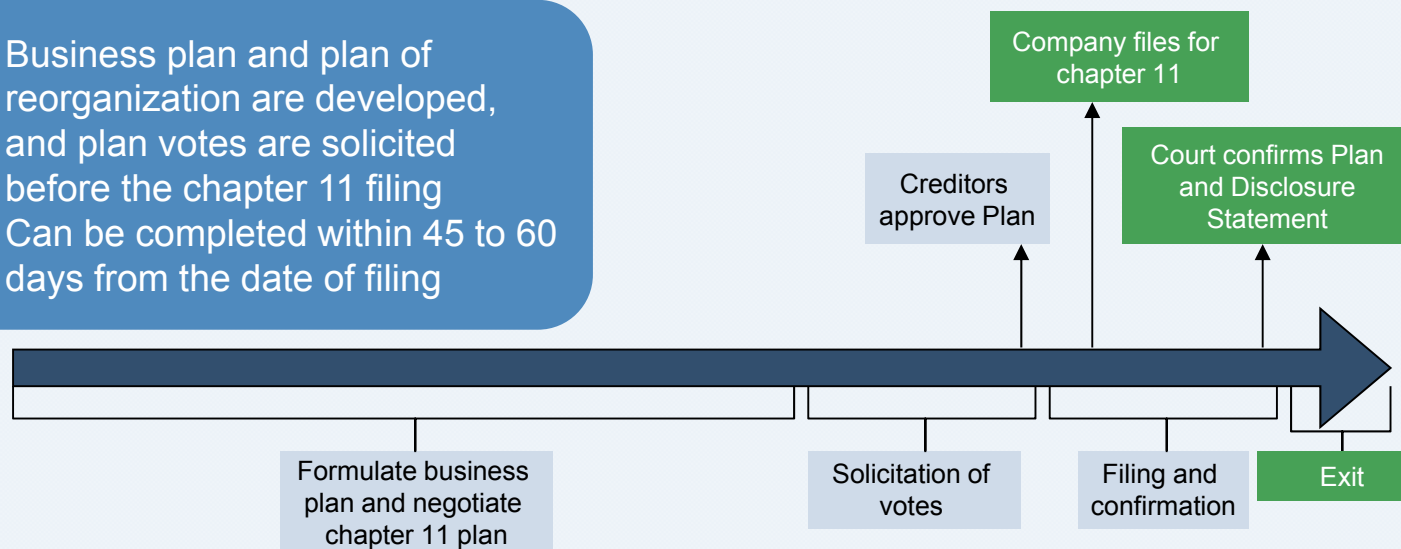
Pre arranged plan

- Business plan and plan of reorganization are developed before the chapter 11 filing
- Votes are solicited in chapter 11
- Can be completed within 4 months from the date of filing



Pre packaged plan

- Business plan and plan of reorganization are developed, and plan votes are solicited before the chapter 11 filing
- Can be completed within 45 to 60 days from the date of filing



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