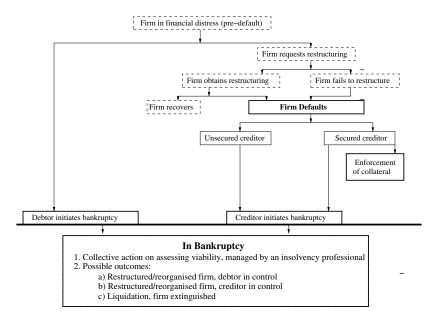
BLRC thinking about the Indian Bankruptcy Code

Susan Thomas

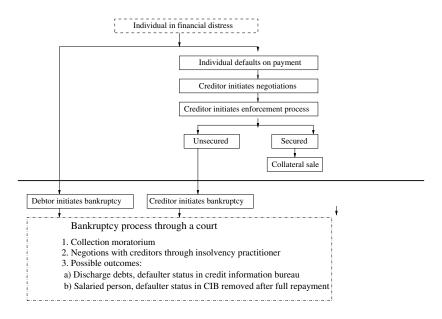
May 15, 2015

The case of corporate insolvency

Process flow of firms in stress



Not so different for individuals in stress



The economic problem of bankruptcy

- With a failure of repayment (default), a creditor will reconsider the long term viability of investment.
 - Viable: the problem is in the financial structure of the firm.
 → financial solution (restructuring, reorganisation)
 - ► Unviable: A problem in the economic model of the firm
 - \rightarrow firm is closed down.

The economic problem of bankruptcy

- With a failure of repayment (default), a creditor will reconsider the long term viability of investment.
 - Viable: the problem is in the financial structure of the firm.
 - $\rightarrow \text{financial solution (restructuring, reorganisation)}$
 - ► Unviable: A problem in the economic model of the firm → firm is closed down.
- In an environment with high information asymmetry
 - \rightarrow individual creditors hurry to enforce their contracts as quickly as possible.
 - \rightarrow higher stress of repayment on the firm.
- Add poor legal certainty,
 - → (individual) creditors actions escalate;
 - \rightarrow stress on the firm escalates.

What good bankruptcy law can do

- In a bad combination of high information asymmetry + poor legal certainty,
- Bankruptcy process can serve as calm period where,
- Viability is answered by
 - a collective decision of all parties debtor, creditors –
 - managed by an insolvency professional,
 - within the supervision of the court,
 - where the judge is not required to take a view on questions of business.

- The core problem of assessing viability is hard.
 - Collective decision delivers better outcomes on value maximisation.
 - \rightarrow involve the larger market in defining outcomes.
 - ► The final decision must be negotiated by creditors in a majority vote.
 - ► The legislature or the courts should not be asked to make this decision.

- The core problem of assessing viability is hard.
 - Collective decision delivers better outcomes on value maximisation.
 - \rightarrow involve the larger market in defining outcomes.
 - The final decision must be negotiated by creditors in a majority vote.
 - ► The legislature or the courts should not be asked to make this decision.
- All creditor rights must be respected in a formal bankrutpcy process.

- The core problem of assessing viability is hard.
 - Collective decision delivers better outcomes on value maximisation.
 - ightarrow involve the larger market in defining outcomes.
 - The final decision must be negotiated by creditors in a majority vote.
 - ► The legislature or the courts should not be asked to make this decision.
- All creditor rights must be respected in a formal bankrutpcy process.
- ▶ Delays ⇒ loss of value. Dilatory tactics by any party must result in penalties commensurate with resultant loss in value.

- The core problem of assessing viability is hard.
 - Collective decision delivers better outcomes on value maximisation.
 - \rightarrow involve the larger market in defining outcomes.
 - ► The final decision must be negotiated by creditors in a majority vote.
 - The legislature or the courts should not be asked to make this decision.
- All creditor rights must be respected in a formal bankrutpcy process.
- Delays

 loss of value. Dilatory tactics by any party must result in penalties commensurate with resultant loss in value.
- Courts are scarce public resources. Its use must be priced accordingly.

Efficiency measures: time to resolution, loss given default, cases filed to appeal outcomes.



The approach in the BLRC

The objective of the new bankruptcy framework should be to maximise economic value for all creditors to a firm. It seeks to:

- Ensure creditor rights, and priority of rights among creditors
 - helps business certainty.
- Establish a single law for all entities for insolvency resolution
 - helps legal clarity.
- Clarify role of the adjudicating authority and the role of the insolvency professional.
 - helps implementation.
- * Reduce information asymmetry in insolvency
 - helps implementation.
- * Reduce stalemate situations with well-defined 'cram-down' procedures
 - helps implementation.
- * Ensure swift and efficient liquidation
 - helps business certainty.
- * In either bankruptcy and liquidation, ensure criminal liability for fraud
 - disincentivise lying.



Process flow in bankruptcy

_1	
Day 0	Bankruptcy triggered. Court/interim IP validates claim. Case registered.
T	Period 1: to submit claims. Process to select an insolvency professional. (Fixed period = 15 days)
Day 30 -	On day 16, an Insolvency Professional is assigned, who is given authority by the court to * monitor the operations and management of the firm. * to replace management if fraud is detected at the firm. * to validate records of assets, presence of collateral, claims of liability, priority of liability * build up the information docket to invite bids for insolvency resolution.
Day 60	* organise interim financing if required.
Day 90	Period 2: to invite financial bids to resolve firm insolvency from the broad financial market. (Period: 60 days) Debtor can offer bids, where debtor can include minority shareholders. Creditors, either singly or as a subset, can offer bids. External financiers can offer bids.
Day 120	Period 3: to evaluate market bids and reach a consensus on the outcome of the bankruptcy (Period: 30 days)
Day 150	Creditors have the power of the final decision. Creditors are given weights in negotiation that is laid out in the law. The debtor can participate through an accepted resolution bid.
Day 180_	Last date for a binding contract with a resolution.
T	Bankruptcy resolution process stops automatically on Day 181.
	If there is a binding contract, the bankruptcy case is closed. Record of bankruptcy case will be retained for five years.
ļ	If there is no binding contract presented, the court liquidates the firm. Firm is renamed to Firm-in-Liquidation on Day 181 Management is taken over by IP Board is replaced with creditors The board selects a liquidator to manage the liquidation process. The court records all the steps in the liquidation process. The liquidator fee will be charged annually as a fraction of the proceeds from liquidation. The fraction will be a decreasing function of time; a higher fraction at times close to Day 181,

1 The bankruptcy process involves both debtor and creditors. Seen as 'fair' to both entrepreneur and financier.

- 1 The bankruptcy process involves both debtor and creditors. Seen as 'fair' to both entrepreneur and financier.
- 2 Within the process, the insolvency professional is the focal point of all information.
 - \rightarrow lowers information asymmetry in decisions.

- 1 The bankruptcy process involves both debtor and creditors. Seen as 'fair' to both entrepreneur and financier.
- 2 Within the process, the insolvency professional is the focal point of all information.
 - \rightarrow lowers information asymmetry in decisions.
- 3 Viability assessment runs parallel to the outcome.
 - \rightarrow faster path to resolution.

- 1 The bankruptcy process involves both debtor and creditors. Seen as 'fair' to both entrepreneur and financier.
- 2 Within the process, the insolvency professional is the focal point of all information.
 - \rightarrow lowers information asymmetry in decisions.
- 3 Viability assessment runs parallel to the outcome.
 - \rightarrow faster path to resolution.
- 4 Linear flow from assessment to resolution / liquidation.
 - \rightarrow higher clarity and certainty of processes for participants,
 - \rightarrow collective participation reduces the probability of appeals

1. One law to rule them all: repeal provisions that are legislative overlaps.

List of laws/provisions to repeal: CA2013, ESIRDLA2012, SARFAESI2002, RDDBFI1993, SICA1983, Presidency Towns Insolvency Act 1909, Provincial Insolvency Act 1929, *Idots*?

1. One law to rule them all: repeal provisions that are legislative overlaps.

List of laws/provisions to repeal: CA2013, ESIRDLA2012, SARFAESI2002, RDDBFI1993, SICA1983, Presidency Towns Insolvency Act 1909, Provincial Insolvency Act 1929, *Idots*?

Rules of trigger; rules of liquidation. Learning from other jurisdictions.

1. One law to rule them all: repeal provisions that are legislative overlaps.

List of laws/provisions to repeal: CA2013, ESIRDLA2012, SARFAESI2002, RDDBFI1993, SICA1983, Presidency Towns Insolvency Act 1909, Provincial Insolvency Act 1929, *Idots*?

- Rules of trigger; rules of liquidation. Learning from other jurisdictions.
- Bankruptcy information systems to validate * claims of liability;
 * ascertain assets and records of firm; * detect fraud in transactions for two years prior to trigger.

What exists? What needs to be created afresh? What processes to ensure efficacy during insolvency?

1. One law to rule them all: repeal provisions that are legislative overlaps.

List of laws/provisions to repeal: CA2013, ESIRDLA2012, SARFAESI2002, RDDBFI1993, SICA1983, Presidency Towns Insolvency Act 1909, Provincial Insolvency Act 1929, *Idots*?

- Rules of trigger; rules of liquidation. Learning from other jurisdictions.
- 3. **Bankruptcy information systems** to validate * claims of liability; * ascertain assets and records of firm; * detect fraud in transactions for two years prior to trigger.
 - What exists? What needs to be created afresh? What processes to ensure efficacy during insolvency?
- The role of the insolvency practitioner:
 Creation of regulator; guidelines for qualifications; access to information for resolution; monitoring performance; action against conflict of interest.

1. One law to rule them all: repeal provisions that are legislative overlaps.

List of laws/provisions to repeal: CA2013, ESIRDLA2012, SARFAESI2002, RDDBFI1993, SICA1983, Presidency Towns Insolvency Act 1909, Provincial Insolvency Act 1929, *Idots*?

- 2. Rules of trigger; rules of liquidation. Learning from other jurisdictions.
- 3. Bankruptcy information systems to validate * claims of liability; * ascertain assets and records of firm; * detect fraud in transactions for two years prior to trigger.

What exists? What needs to be created afresh? What processes to ensure efficacy during insolvency?

- 4. The role of the **insolvency practitioner**: Creation of regulator; guidelines for qualifications; access to information for resolution; monitoring performance; action against conflict of interest.
- The role of the adjudicating authority. Rules about the role; form, processes and structure of the court.

Next steps for the workplan

Overall workplan of BLRC

- 1. What has been done so far: An interim report is on the MOF website, led by Vidhi Centre for Legal Policy.
- 2. Volume 0 of the report: A collection of papers, also released as IGIDR FRG Working Papers.
- 3. Volume 1: An argument for design of the bankruptcy code leading up to drafting instructions.
- 4. Volume 2: The draft Indian Bankruptcy Code.

Late June: A conference in Goa with a draft Volume 1 in hand, refine it, and then turn it into code.

Research papers that are presently under preparation

- 1. The evolution of corporate bankruptcy in India, Anjali Sharma and Susan Thomas
- 2. Debt recovery and insolvency resolution proceedings in India: case review, Aparna Ravi and Susan Thomas. Presented last time.
- 3. Comparing corporate bankruptcy law: India, U.K., Singapore, Anjali Sharma and Rajeswari Sengupta
- 4. Comparing individual insolvency process: India, Australia, Canada, Renuka Sane and Susan Thomas
- 5. Information infrastructure for the bankruptcy process, Ajay Shah and Susan Thomas. Presented last time.
- 6. *Issues around land as collateral in insolvency*, K. P. Krishnan, Venkatesh Panchapagesan, and Madalasa Venkataraman
- 7. Building an insolvency professional industry in India, Anirudh Burman, M. S. Sahoo, Shubho Roy
- 8. Adjudication infrastructure for the bankruptcy proceeding, Anirudh Burman, Pratik Dutta, Shubho Roy.



Table of contents of volume 1 of the report

- Review of bankruptcy process in India today (both firms and individuals)
- 2. Information infrastructure for improved functioning of the credit market and of the bankruptcy process
- 3. Creating the profession of insolvency practitioners
- 4. Obtaining modern adjudication infrastructure
- 5. Designing the bankruptcy process
- 6. Designing the liquidation process

Presentations for today

- Learning from other jurisdictions
 - Corporate insolvency law in the U.K. and Singapore: Anjali Sharma, Rajeswari Sengupta
 - Individual insolvency in Australia: Renuka Sane
- Bankruptcy Information systems
 - Issues around land as collateral in insolvency: K. P. Krishnan, Venkatesh Panchapagesan, Madalasa Venkataraman
- The role of the insolvency professional
 - Role and rules for the insolvency professional: *Anirudh Burman, M. S. Sahoo, Shubho Roy*
- Processes, form and structure of the bankruptcy court
 - A court for efficient bankruptcy proceeding: Anirudh Burman, Pratik Dutta, Shubho Roy
 - Learning from the FSAT Task Force: Pratik Dutta

Thank you

susant@igidr.ac.in
http://www.ifrogs.org