

Restructuring & Insolvency

India's insolvency scheme evolves on pre-packs

A Chapter 11-style plan will help to encourage investor participation for distressed assets but is clouded with implementation risks

By **Karry Lai**

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The Insolvency and Bankruptcy Board of India is proposing changes to the country's Insolvency and Bankruptcy Code (IBC) to introduce a pre-packaged insolvency resolution process (PPIRP). Lawyers in India are optimistic that the proposed scheme will speed up the insolvency process but see potential implementation issues.

The aim of a pre-pack is to provide speedier resolutions for insolvencies. It enables debtors and creditors to approach the National Company Law Tribunals (NCLTs) with a resolution plan. Once a NCLT approves the plan it becomes binding on all stakeholders.

Ajay Shaw, partner at DSK Legal, said: "The PRIRP is intended to minimise court supervision and provide the flexibility stakeholders need to conclude a resolution in an expeditious manner."

He believes that the pre-pack scheme will encourage more participation by investors for distressed assets in India.

"Investors will be able to strike a deal with the creditors or promoters of a corporate debtor in stress with a level of certainty and the ability to ringfence the overall liabilities going forward," he added.

Avijit Banerjee, CEO at Argon Capital Advisors, agreed and said: "It's a win-win situation for both debtors and creditors since the time taken for resolution would be far less than a formal insolvency procedure."

Investors can directly negotiate with the promoters or management of stressed companies and reach a viable resolution or plan without going through a lengthier process under the IBC, according to Niloufer Lam, partner at ZBA Partners.

"This may make it quicker and the crux of commercial issues can be determined and resolved," she said. "In India, promoters hold the key of a company and investor confidence will grow if promoters directly negotiate and provide fair and transparent information to investors."

In a pre-pack, resolution doesn't necessarily mean a sale, so if an investor wants to invest in a distressed business, it may get in touch with the company for negotiation of the pre-pack or come through a Swiss challenge mechanism for bidding.

Meenal Maheshwari, legal counsel at Essar, said: "If the investor chooses to use a Swiss challenge, the issue is that the investor's way of looking at the resolution may be different from that of the buyer so pricing may not be comparable."

However, she said that if investors choose to participate in the pre-pack, they have to keep an eye out for distressed companies before it is publicly known that they are stressed.

Compared to the existing process in the IBC where resolution plans are invited through a time bound public process, the proposed scheme offers more flexibility.

Rajeev Vidhani, partner at Khaitan & Co, said: "Under the proposed scheme, creditors may choose to run a private and confidential process to invite bids or resolution plans from promoters."

He added that since a pre-pack remains away from public view until the formal process starts, it minimises stigma and reputation loss to a stressed business.

In addition to taking less time compared to the corporate insolvency resolution process under the IBC, the overall cost is also reduced, which is better for a company reeling under financial stress.

“The business disruption cost is also reduced as the management remains with the existing promoters during the pre-pack,” said Vidhani. “This ensures continuity of the business and avoids loss of customers, employees and vendors by reducing uncertainty.”

See also: [India's suspension of insolvency proceedings brings risks](#)

Areas of concern

Lawyers in India believe that there are a number of potential implementation problems for debtors and creditors to keep in mind.

One disadvantage of a pre-pack, according to Shaw, is that it could be a tool for the corporate debtor and the creditors to restructure the debt to postpone the problem.

Vidhani pointed out that as the entire process of a pre-pack is heavily reliant on the cooperation of the management of the corporate debtor and a substantial part of the process is opaque.

“This is in stark contrast to the objective behind a creditor in control model of the IBC, which mandates handing over of management of the corporate debtor to a resolution professional instead of leaving in the hands of those who were responsible for the stress in the corporate debtor,” said Vidhani.

Banerjee said that the concern is on the clarity of the valuation process and what pre-agreed value needs to be reached to strike a deal.

“This is one key criterion that may or may not cut a deal between the parties and may force them to go through the formal resolution procedure which would prolong the recover process,” he said.

While efficiency may be a key goal of the pre-pack, it could be a lofty goal in some cases.

“Getting the resolution plan accepted by the lenders is a process unto itself and quick resolution- oriented decision making by the lenders will be a key factor,” said Shaw.

Shaw added that the process of getting the resolution plan approved by the NCLT is saddled with the risk of litigation so it is imperative that the courts do not allow frivolous litigation on issues that are well settled under the law.

As the consent from operational creditors is not required to start the pre-pack process, Meenal said that resistance may lead to challenges in court.

According to Lam, there is a drawback of relying heavily on the NCLT for approval of the resolution plan. “The NCLTs are already overburdened and it will be a herculean task to handle pre-packs, insolvency and liquidation processes under IBC,” she said.

However, she added that enhancement in the bench capacity and infrastructure of NCLTs is being considered, which if implemented, will be a boost for pre-packs and insolvency processes.

The other challenge that Lam expects is completion of the entire pre-pack process within 90 days and approval within 30 days. “Undoubtedly the timelines are well intentioned, they could, however, be slightly ambitious at this stage,” she said.

A comparative view

Compared to other jurisdictions with pre-pack schemes, such as the UK and US, India's proposed regime is slightly different.

“In the UK, the pre-pack sale option enables the sale of a business by the administrator without court intervention or creditors sanction,” said Shaw. “The prepack proposed in India is intended to be a hybrid of informal and formal mechanisms.”

In the US, pre-pack bankruptcy proceedings are based on an agreement on the terms of the plan with the creditors and the corporate debtor. Once it receives the required votes in favour, the corporate debtor files for a Chapter 11 petition.

Shaw said India's proposed scheme is similar to the US' but resolution plans need to be implemented within the contours of the IBC.

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