R&I India

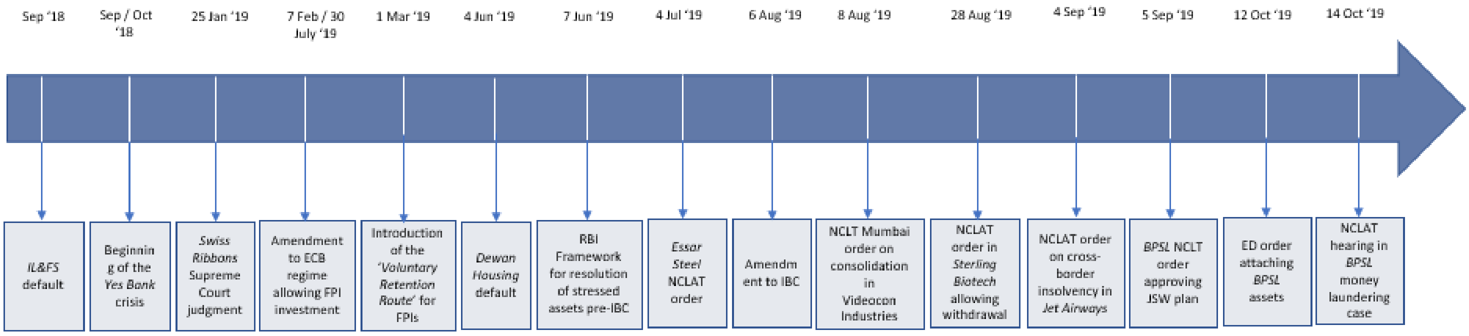
INSOLVENCY LAW UPDATE | IBC -THE LAST 12 MONTHS

October 2019

INTRODUCTION

Over the last 12 months, the market has witnessed myriad developments in relation to the Insolvency and Bankruptcy Code 2016 ("**IBC**"), the deterioration of the financial services sector in India and the compression of credit from traditional banking sources and continued high levels of interest in distressed investments in India by international investors. Consequently, market practice, case law and regulatory change have been moving at great pace and this note summarizes the main developments over the last 12 months.

A timeline of key events in the last 12 months is below.



1. SUMMARY OF MAIN DEVELOPMENTS OVER THE LAST 12 MONTHS

The most significant developments in the distressed debt space over the last 12 months are as follows:

- Despite multiple cases and amendments of law, the law on treatment of financial creditors and operational creditors and treatment of secured creditors remains in flux. The market is eagerly awaiting the Supreme Court's determination on this, which it is hoped, will clarify these key principles once and for all.
- Indian exchange control regulations have been liberalized to allow international funds to refinance Indian distressed debt. Although the rules permit direct acquisition and trading of secondary bonds, a task force of the Reserve Bank of India ("**RBI**") recommended further relaxations to permit direct acquisition and secondary market trading of loans by international investors. Therefore, it is possible that there may be some further easing of the regulations over time.
- Partly because of the litigated nature of the IBC's insolvency process and the timelines imposed on banks in India by the RBI to resolve distressed situations, there has been significant interest in pre-IBC restructurings, known as "one-time settlement" ("**OTS**") transactions. Although the IBC does not expressly

contemplate "pre-pack" transactions, market participants have been attempting to structure pre-agreed transactions through various techniques.

- Indian regulators have recognised the lack of a comprehensive framework for substantive consolidation and cross-border insolvency in India and have proposed a draft framework. In the interim, Indian courts appear to have already set the ground rules in the case of *Videocon* and *Jet Airways*.
- There has been a surge in withdrawal cases under the IBC, which has raised questions with regard to the sanctity of Section 29A (which was added to prevent backdoor entries by errant promoters).
- There has been significant interest from international investors in distressed debt and special situations opportunities in India, especially in the financial services and road infrastructure sector (in relation to the infrastructure sector, relating to the monetization of claims and OTS transactions).

2. LIBERALISATION OF EXCHNAGE CONTROL NORMS

2.1 Increased market access for FPIs

In 2018, the RBI introduced certain concentration and exposure norms, which limited the exposure that international funds with foreign portfolio investor ("**FPI**") registration could have to debt instruments issued by Indian companies known as non-convertible debentures ("**NCDs**"). Reacting to market feedback on the restrictive nature of these rules, the RBI has introduced some regulatory easing in 2019. This has taken the form of a new route for FPI investment in NCDs, known as the 'voluntary retention route', which does away with the concentration norms (which restrict FPIs from investing more than 50% in a single issue of bonds and restrict exposure in a single company or its related group to 20% of its entire bond portfolio). However, under this route, the FPIs need to remain invested for a minimum of 3 years.

The principal exchange controls restricting the ability of international investors to lend to Indian companies, the external commercial borrowing ("**ECB**") regime, was also amended to provide for greater flexibility. The changes allow FPIs to invest through the ECB route, especially in distressed debt. Earlier this year, the RBI had permitted international investors to refinance the Rupee debt of companies undergoing the corporate insolvency resolution process ("**CIRP**") under the IBC, subject to receipt of RBI approval. With the rise in pre-IBC restructurings, the RBI amended the ECB framework to allow international investors (including FPIs) to refinance Rupee debt (classified as a non-performing asset or SMA-2[1]) of borrower companies engaged in the manufacturing and infrastructure sector, provided that the purpose of the original loan was to fund capital expenditure.

Whilst these changes were introduced with the aim of facilitating direct secondary debt trading by international investors, a few issues remain. First, the amendments in relation to pre-IBC refinancing applies only to limited sectors (i.e. manufacturing and infrastructure) thereby excluding other sectors with high levels of distress. Second, and more importantly, the resultant ECB is required to comply with the all-in-cost cap (450 basis point spread over the benchmark rate) and requirements on the minimum maturity periods applicable to ECBs. In other words, the ability to directly acquire secondary Indian debt is limited to situations where this Indian debt is ECB compliant.

***Comment**: Although it is encouraging that the RBI has opened a window for direct secondary trading of distressed loans, the applicability conditions, in particular, the reference to the cost of debt of the transferred loan being capped and the*

[1] Where the debt has remained unpaid between 61 to 90 days.

> *imposition of ECB minimum maturity requirements, may limit the universe of loans capable of such transfer. For loans that are capable of secondary transfer, if the coupon is capped, international funds will look to generate sufficient returns on their capital through acquisition of the debt at a discount and then seek recovery through the OTS at a higher level.*

2.2 Question marks over the future of the ARC model

The traditional way for international funds to invest in secondary distressed debt in India is to acquire security receipts ("**SRs**") issued by asset reconstruction companies ("**ARCs**"), who acquire portfolios of non-performing loans. This model has been criticized for creating inefficiencies and also because the ARCs are both principal and agent (as the ARCs need to hold 15% of SRs).

Also, the capital constraints that many ARCs face create issues in larger transactions, around the financing of their 15% SR holding requirement. Some leveraged solutions have emerged, but they involve lending that is unsecured by the 15% holding requirement (although there may be other forms of security).

The RBI appears to have recognized these issues. In addition to the amendments to the ECB regime allowing direct secondary debt trading by foreign investors, the RBI has recently published a report on the development of the secondary market for corporate loans (the "**RBI Report**"). The RBI Report has, with a view to deepen the corporate loan market, recommended that that in addition to ARCs, other investors such as FPIs, pension funds, mutual funds and insurance companies be permitted to invest and trade in corporate loans.

This proposal, if implemented, will encourage competition amongst investors, manage asset-liability mismatches of banks by facilitating liquidity and will result in better price discovery. That said, implementation of this proposal will require a number of laws to be amended, including extending relaxations provided under the existing securitization framework (such as exemption from mandatory open offer and framework for preferential allotment for public listed companies) to FPIs and other investors.

> ***Comment****: The changes proposed by the RBI, if implemented, will constitute a welcome measure and will ease the current "choke points" in the market. Investors should therefore "watch this space" for future developments.*

3. RECENT AMENDMENTS AND ISSUES THAT REMAIN UNDER THE IBC

3.1 Treatment of financial creditors vs. operational creditors and secured and unsecured financial creditors

The law on the treatment of financial creditors and operational creditors under a resolution plan is currently in a state of flux. A number of decisions in late 2018 and early 2019 stated that dues owed to operational creditors must get "*at least similar*" treatment as compared to financial creditors.[2] The Supreme Court of India, in January 2019,[3] recognized the distinction between financial and operational creditors, but fell short of expressly stating that operational and financial creditors are not similarly situated.

However, in a recent decision,[4] the National Company Law Appellate Tribunal ("**NCLAT**") placed financial creditors and operational creditors on the same footing for distribution of proceeds and ruled that the committee of creditors had no role in deciding such distribution. This is a decision that has been widely criticized for

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2 *Binani Industries Limited v Bank of Baroda & Anr,* NCLAT, 14 November 2018; *Tata Steel Limited* v *Liberty House Group Pte Ltd & Ors,* NCLAT, 4 February 2019.

3 *Swiss Ribbons Pvt Ltd* v *Union of India*, Supreme Court of India, 25 January 2019.

4 *In re Essar Steel India Limited*, National Company Law Appellate Tribunal, 4 July 2019.

its broader impact on the market and for not considering fundamental principles relating to credit and security. Therefore, the matter was appealed before the Supreme Court of India.

In addition to the judicial challenge, the Government appears to have recognized the impact of the NCLAT judgement in *Essar Steel* and introduced amendments in August 2019 partially rolling back the NCLAT decision on equality of treatment of financial and operational creditors and brought back the concept of operational creditors and dissenting financial creditors receiving at least their liquidation value. The amendment also clarified that the distribution of proceeds must be "*fair and equitable*" to such creditors.

Soon after the amendment to the IBC, the NCLAT[5] directed the resolution applicant of Rave Scans Private Limited to modify its plan to ensure that a secured dissenting creditor (Hero Fincorp) was paid the same as other similarly placed secured creditors. The NCLAT noted that while the recently amended IBC allows a resolution applicant to provide at least liquidation value to the dissenting creditor, a corresponding amendment had not been made to the regulations under the IBC (which does not allow discrimination between secured financial creditors on the ground of a dissenting vote).

In any event, the Supreme Court is considering both the NCLAT decision in *Essar Steel* and the validity of the recent amendments to the IBC and has ordered that status quo be maintained. The matter is listed for hearing on 15 October 2019 and we anticipate that a judgment will follow in November.

> ***Comment**: The market is keenly following this matter and the hope is that the Supreme Court will definitively rule on the treatment of financial and operational creditors and secured and unsecured financial creditors under CIRP once and for all in this judgment.*

3.2 Lack of certainty of bids and role of promoters

Whilst recovery of stressed loans has improved from 26% to 48% since the advent of the IBC, and one concern in relation the insolvency process is the lack of certainty of bids. This can be attributed to a number of factors such as court orders for re-commencement of CIRP to avoid liquidation (*Jaypee Infratech Limited*), non-implementation / withdrawal of resolution plan by bidders (*Amtek Auto Limited, Ruchi Soya Industries, Orchid Pharma Limited, Metalyst Forging Limited*) and withdrawal from the insolvency process on account of settlement offers by promoters (*Sterling Biotech, SBM Paper Mills*).

Re-commencement or withdrawal of CIRP disrupts the process and is likely to have far-reaching effects on investors, especially with respect to their investment outlook for India. The withdrawal right introduced in the IBC last year is a curious feature of Indian law and does not sit easily with the fact that insolvency is a collective process to avoid a "*race to the bottom*". Not surprisingly, the introduction of this provision has not been without its fair share of legal challenges.

Although the legal validity of the provision has been upheld by the Supreme Court in *Swiss Ribbons*, another recent case law has brought forth the dangers inherent in this provision. Recently, the NCLAT allowed the erstwhile promoters of *Sterling Biotech*[6] to regain control over the company by accepting a settlement offer and held that the withdrawal provisions under the IBC pertain to a different subject matter from Section 29A of the IBC (which was added to prevent backdoor entries

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5 *Hero Fincorp Ltd* v *Rave Scans Pvt Ltd & Ors*, NCLAT, 17 September 2019.

6 *Andhra Bank* v *Sterling Biotech Ltd (through the Liquidator)*, NCLAT, 28 August 2019.

by errant promoters) and ineligibility under the latter will not disallow withdrawal of CIRP.

> ***Comment:*** *The decision in the case of Sterling Biotech is likely to have far reaching consequences. It has not only rendered Section 29A of the IBC effectively obsolete but has also opened floodgates for promoters categorized as willful defaulters to regain control of the companies.*

3.3 IBC overrides money laundering law?

The IBC imposes a moratorium on initiation and continuance of suits or proceedings against a corporate debtor during CIRP. However, with conflicting judgements having been passed by Indian courts, unless the Supreme Court finally settles the issue, a judicial grey area continues to remain with regard to the overriding effect of the moratorium under IBC on attachment proceedings under the Prevention of Money Laundering Act, 2002 ("**PMLA**").

The NCLAT[7] and Delhi High Court[8] have ruled that the moratorium under the IBC does not apply to proceedings under the PMLA as PMLA, which relates to penal action for 'proceeds of crime', operates in a different field from the IBC and cannot be overridden by the latter. On the other hand, in a recent decision by the Appellate Tribunal for PMLA,[9] the tribunal, while recognising that the objectives of the IBC and PMLA are different, ordered release of the properties belonging to PMT Machines, a subsidiary of debt-laden Sterling Biotech, which were attached by the Enforcement Directorate ("**ED**"), on the grounds that the attached properties were not purchased from 'proceeds of crime'.

On-going proceedings under PMLA pose several practical challenges during implementation of a resolution plan. One such issue is being faced by JSW (the successful resolution applicant of Bhushan Power & Steel Limited) where JSW has sought immunity from prosecution under PMLA on account of pre-existing criminal proceedings against the debtor company and its erstwhile promoters for alleged siphoning off funds. The ED provisionally attached assets of Bhushan Power & Steel Limited worth INR 4,025 crores. This causes concerns because: (a) bona-fide third party bidders, who make an acquisition through a public and transparent IBC process are adversely affected; and (b) creditors of the corporate debtor, who have no involvement in any wrong-doing are also affected.

Although there is due process under the PMLA and certain reliefs may be possible there, the matter has been litigated, challenging this attachment order. This litigation has been supported by the Ministry of Corporate Affairs ("**MCA**") of the Government of India. The ED's attachment order was stayed by the NCLAT on 14 October 2019 and the ED has been asked to appear before the NCLAT in the next hearing on 25 October 2019.

The court is yet to deliver an order on this issue and it is possible that the matter ultimately needs to go up to the Supreme Court to reach resolution, but lenders may draw some comfort from the MCA's stance on this (which could result in amendments to the law) and also the Supreme Court's decision in 2017 in the case of *Tech Mahindra*.[10] Market participants are hopeful that the criminal liabilities of erstwhile promoters and directors will not be inhered by an incoming investor.

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7 *Varrsana Ispat Limited* v *Deputy Director, Directorate of Enforcement*, NCLAT, 2 May 2019; *Rotomac Global Private Limited* v *Deputy Director, Directorate of Enforcement*, NCLAT, 2 July 2019

8 *Deputy Director, Directorate of Enforcement Delhi* v. *Axis Bank & Ors,* Delhi High Court, 2 April 2019.

9 *M/s PMT Machines Ltd* v *Deputy Director, Directorate of Enforcement Delhi,* Appellate Tribunal for SAFEMA, FEMA, PMLA, NDPS & PBPT Act, New Delhi, 16 September 2019.

10 *Joint Director, Directorate of Enforcement & Ors* v *Tech Mahindra Limited*, Supreme Court of India, 8 December 2017.

Comment: *The matter of the primacy of the IBC v. anti-bribery and money laundering law represents a policy issue that the IBC needed to resolve at some point. Therefore, although concerning (and although the impact is very significant upon the distressed landscape), had the issue not arisen in this context, it would have inevitably faced judicial scrutiny in the future. International investors can draw comfort from the MCA's position to date and case law and it is possible that changes to law may provide further assistance to innocent lenders or bidders.*

However, whereas all the interest has been in the IBC context, parties need to consider what this means for pre-IBC restructurings. To date, the various exemptions in the IBC process have not been extended to OTS transactions. Therefore, international investors should diligence these matters carefully before investing and build in protections to secure recoveries from other sources. In any event, even OTS transactions will benefit from the same line of case law supporting the position of innocent third parties and so international investors may ultimately need to draw comfort from that.

3.4 Permissibility of "*loan-to-own*" structures

The IBC recognises the concept of bidding by financial creditors (because the IBC permits them to also serve on the committee of creditors), this is perhaps not as broad as the concept of credit bidding as generally understood in western jurisdictions. The jurisprudence on this aspect is yet to evolve, but earlier this year, the National Company Law Tribunal ("**NCLT**") in the case of *In Re Bharati Defence and Infrastructure Limited*[11] discussed potential issues in "*loan-to-own*" structures.

In the *Bharti Defence* case, the bid by Edelweiss ARC was challenged on the grounds that on account of being the majority creditor, there was conflict of interest on the part of Edelweiss. While the NCLT Mumbai did not specifically rule on the issue of "*loan-to-own*", it observed that Edelweiss intended to initially run the company with the help of professionals and later sell the company to an investor, which went against the core principle of the IBC of ensuring continuity of the corporate debtor as a going concern.

Comment: *The Bharti Defence case involved some particular circumstances, so can be distinguished, but financial investors bidding will need to carefully demonstrate a long-term plan to turn around the corporate debtor, should they decide to bid.*

4. RECENT TRENDS UNDER THE IBC

4.1 Substantive consolidation – A "judge-made" law

Unlike its western counterparts, the IBC, in its current form, does not recognize the concept of substantive consolidation, primarily on the grounds of the basic corporate law principle of 'separate legal identity'. Given the rise in group wide insolvencies in India and the need to streamline the process and maximise value for creditors, the Insolvency and Bankruptcy Board of India has constituted a committee to examine the feasibility of substantive consolidation.

In the interim, Indian courts appear to have already set out the ground rules for substantive consolidation. In the first of its kind order, the NCLT Mumbai[12] directed substantive consolidation of 13 insolvent Videocon group companies based on the following considerations: (a) inter-dependence of the companies; (b) common control, directors, assets and liabilities; and (c) commonality of creditors. A similar

[11] *Mr Dhinal Shah, Resolution Professional and Edelweiss Asset Reconstruction Company Ltd* v *Bharati Defence and Infrastructure Ltd*, NCLT, Mumbai, 14 January 2019.

[12] *State Bank of India & Ors* v *Videocon Industries Limited & Ors*, NCLT Mumbai, 8 August 2019.

view was taken by the NCLAT in September 2019[13] where it permitted consolidation of IBC proceedings against 5 out of the 9 companies in the Adel group on the grounds that parcels of land held by each of the companies were combined and development agreements were executed on that basis.

Whilst substantive consolidation will permit easier resolution of complex group structures, resolve looming issues of information asymmetry and "*double dipping*" by financial creditors, market participants should be wary of the challenges that are associated with this.

For instance, group consolidations could become the victims of a "*too big to fail*" conundrum, as the IBC still does not contain an express mechanism for asset sales, in the absence of which, the entire group would necessarily need to be sold to a successful resolution applicant, and takers for this may be few. Further, lenders will need to build in adequate protections in their financing documents to ensure that their interests are not adversely impacted the event of a consolidation.

> ***Comment:*** *One key concern with regard to the decision of the NCLT Mumbai is its potential retrospective application to lending transactions in India. Its implementation without the introduction of more phased policy change may mean that lenders with bespoke pieces of the debt stack in complex groups with significant inter-linkages may now unwittingly be exposed to substantive consolidation and thereby lose their loan value and voting rights in the committee of creditors, which they would otherwise expect to retain if the borrower alone had been put into insolvency.*

4.2 Cross-border insolvency

The IBC contains limited provisions with respect to cross-border insolvency which deal with entering into agreements with other countries for enforcing provisions of the IBC. The government has recognized the lack of a comprehensive framework for cross-border insolvency matters and has issued draft guidelines on this.

While the final framework with respect to cross-border insolvency is awaited, the question on consolidation of insolvency proceedings against *Jet Airways* in India and Holland arose. While the NCLT[14] refused to accept the order passed by the Dutch court on the grounds that the IBC provisions on cross-border insolvency are yet to be notified, on an appeal, the NCLAT[15] stayed the order of the NCLT and ordered that: (a) a joint insolvency process should be conducted; and (b) the Dutch administrator and the resolution professional should cooperate with each other and an agreement should be entered into recording the terms of such cooperation.

Based on the directions of the NCLAT, a '*cross border insolvency protocol*' was submitted and approved by the court where it was agreed that the Dutch administrator will be eligible to participate in the meetings of the creditors as an observer, but shall not have any voting rights. Curiously, this was a request made by the Dutch administrator itself and the NCLAT did not discuss the rationale for allowing this. The NCLAT order also does not discuss the mechanics of conducting a joint insolvency process and the value attribution between the Dutch and other creditors, but given that the cross-border insolvency regime is still in its nascent stages, such "*teething*" issues are inevitable.

4.3 Liquidation – the last resort?

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13 *Edelweiss Asset Reconstruction Company Limited* v *Superlative Infrastructure Pvt Ltd*, NCLAT, 20 September 2019.

14 *State Bank of India* v *Jet Airways (India) Limited*, NCLT Mumbai, 20 June 2019.

15 *Jet Airways (India) Limited (Offshore Regional Hub)* v *State Bank of India*, NCLAT, 12 July 2019 and 4 September 2019.

As a policy matter, the IBC clearly provides for the compulsory liquidation of corporate debtors if the corporate insolvency resolution process does not deliver results in a time bound period. This was deliberately designed to incentivise positive insolvency outcomes.

However, the judiciary appears to treat insolvency as the last resort. Apart from its willingness to permit re-bidding in certain cases, there have been cases where the insolvency courts have permitted the liquidator to initiate a scheme of arrangement under the Companies Act, 2013 ("**CA 2013**") to sanction a scheme between the corporate debtor and its creditors, and where applicable, its members.[16] The IBC and the rules were recently amended to recognise that schemes of arrangement may be given effect to after an order for liquidation has been passed.

Comment: *The directions passed by insolvency courts to implement a scheme of arrangement under the CA 2013 are fact specific and do not apply to all on-going liquidation cases. The real issue is not the enabling nature of these cases, because similar provisions also exist in other jurisdictions such as the UK and Singapore, but in how they are used. If they are used to delay liquidation, then the impact will be unfortunate. On the other hand, if they are intended merely to facilitate the liquidator realising value for creditors, then the impact may be more benign.*

5. RESOLUTION OUTSIDE IBC

5.1 Introduction of a new regulatory inter-creditor agreement

The initial version of the RBI's circular on resolution of stressed assets was struck down by the Supreme Court of India[17] in April 2019 as it required banks to mandatorily initiate insolvency proceedings against debtors where pre-insolvency restructuring efforts failed to be achieved in a time bound manner. The RBI re-published the guidelines on 7 June 2019 ("**RBI Pre-IBC Circular**") with suitable amendments to comply with the Supreme Court directions and a new regulatory inter-creditor agreement ("**Regulatory ICA**") has been prescribed.

In contrast to the previous version of the inter-creditor agreement, the Regulatory ICA is meant to serve only as a template (and can be modified, on a case to case basis) and is to be mandatorily signed by scheduled commercial banks, specified all-India financial institutions, NBFCs and ARCs ("**Specified Lenders**"). All key decisions (including resolution plan approval) require the consent of the lenders (75% in value and 60% in number).

Although the Regulatory ICA does not bind international investors, they can choose to accede to it by signing a deed of accession in the format prescribed and benefit in the restructuring discussions and process.[18] That said, if international investors do not sign up to the Regulatory ICA, the cram down provisions will not apply to them. Investors have seen this dichotomy as an opportunity to structure their investments and leverage their position.

This has particular significance in the financial services sector as discussed further in paragraph 6 below.

5.2 Pre-packaged deals

Pre-packaged reorganisations in the way that it is classically understood in the US or the UK is not explicitly recognised under the IBC. While the government is

16 *S C Sekaran* v *Amit Gupta*, NCLAT, *29 January 2019; Y Shivram Prasad* v *S Dhanapal*, NCLAT, 27 February 2019; *Ajay Agarwal* v *Ashok Magnetic*, NCLAT, 22 February 2019; *Rajesh Balasubramanian* v *Everon Castings Pvt Ltd*, NCLAT, 25 February 2019; *Daiyan Ahmed Azmi* v *Rekha Kantilal Shah, Liquidator*, NCLAT, 20 March 2019.

17 *Dharani Sugars and Chemicals Limited* v. *Union of India and Ors.*, Supreme Court of India, 2 April 2019.

18 There is still some ambiguity whether FPIs will qualify as "financial institutions".

working towards publishing formal guidelines, market players have already devised structures to facilitate pre-negotiated plans under the Indian legal framework.

Debt aggregation is a key step before any pre-packaged reorganisation plan can be implemented, which is often achieved through ARCs (although this might change if the recommendations in the RBI Report are implemented). Lenders then use different techniques to drive through a pre-agreed restructuring plan.

Some key considerations while structuring pre-packs include:

- the ability to bind the various stakeholders;
- achieving a cram-down;
- S.29A and related party issues;
- the availability of statutory exemptions to various regulations and tax provisions; and
- the techniques to implement this and the timing of these processes.

> ***Comment:*** *There are a number of complex considerations involved and parties will need to plan for sufficient structuring time in any structured pre-pack process. Also, to manage expectations, the structural solutions are unlikely to be "perfect" and are likely to represent pragmatic solutions to structure an outcome in the absence of an explicit regulatory enabling regime.*

5.3 Rise in OTS deals

Since the beginning of the year, the market has witnessed an increase in proposals for OTS with banks. Government statistics[19] suggest that until June 2019, a total of 101 insolvency cases have been withdrawn primarily on the grounds of settlement with creditors.

OTS can be implemented both within the purview of the IBC or outside it (pursuant to the RBI Pre-IBC Circular), although role of the debtor company and shareholders is excluded in the IBC process.

With many insolvency cases mired in litigation, banks have been increasingly opting for loan settlement offers from defaulting firms by withdrawal from the formal insolvency process. Promoters of defaulting companies also appear to be in favour of OTS as this gives them the opportunity to re-gain control of their companies.

In order to avoid higher provisioning (on account of litigation related delays), banks have been accepting OTS offers even if it comes at the cost of a deeper haircut. For instance, press reports suggest that banks have agreed to take a haircut of 65% in case of Sterling Biotech and 85% in Alok Industries.

> ***Comment:*** *With the latest amendment to the IBC capping the resolution process (including litigation) to 330 days, the market is yet to see if banks continue to prefer OTS deals to the formal resolution process under the IBC. The outcome of the Bhushan case, with regard to potential ED risk, may also have some bearing on the future of OTS transactions, particularly if the law evolves in a manner that provides comfort in IBC situations in respect of ED attachment risk but not in OTS transactions.*

6. INSOLVENCY IN THE FINANICAL SERVICES SECTOR

The last year has witnessed a surge in defaults by financial service providers in India and perhaps owing to an unintended legal gap, there currently exists no framework for initiating insolvency against financial institutions. The IBC specifically excludes its applicability to financial services providers and a specialized legislation called

[19] Quarterly Newsletter of the Insolvency and Bankruptcy Board of India, April – June 2019, Vol. 11.

the Financial Resolution and Deposit Insurance Bill, 2017 was withdrawn by the parliament before it became law.

This legal vacuum, although unhelpful, has not left creditors without remedies. For instance, in the case of IL&FS, where it was alleged that the affairs of the company were being conducted in a manner prejudicial to public interest, the NCLT ordered suspension of the board of directors and declared a moratorium against IL&FS and its subsidiaries. Although outside the ambit of the IBC, the resolution of the IL&FS group is being conducted in a manner similar to that of the IBC with NCLT overseeing its implementation.

With respect to restructuring alternatives in the financial services sector, opportunities continue to exist under the RBI Pre-IBC Circular as well as a consensual restructuring, which as discussed above, can be implemented through a court approved scheme under the CA 2013. Many international funds and bulge bracket buyout firms are exploring the opportunity to infuse equity capital or mezzanine debt or use structured financial instruments to ensure the much-required capital investment in this sector.

Comment: *The government appears aware of the legal gap here and various press reports suggest that it is contemplating legislative changes to provide a legal regime to cover the financial services sector. That may involve the application of a variation of the current IBC provisions to financial services entities, but international investors will need to watch this space. Until then, restructurings in this sector will be very dependent on securing lender consents.*

7. INVESTMENTS IN THE ROAD SECTOR – OPPORTUNITY IN CRISIS

Despite overall financial stress in the infrastructure sector, investments in the road sector has picked up pace in the past year with deals worth approximately USD 1.8 billion being announced within this year. Foreign investors find it more attractive to invest in operating road projects since toll road assets have progressive revenue, which enhances the returns over the concession period. In addition, a significant portion of the annuity road assets are projects with the National Highways Authority of India ("**NHAI**") as the counter-party, thus leading to significantly lower credit risk.

In most cases, the real value in road assets lies in the claims owed to the project SPVs from the NHAI and there are various routes through which foreign investors have sought to monetise this. However, investors considering claims-based strategies should carefully diligence the value of the claims to assess and the likely timelines for the arbitration and appeals process. OTS transactions in this sector involve a different set of considerations, but again, an understanding of the legal remedies available to various parties and the need for NHAI consent is critical.

Comment: *Irrespective of the nature of investment in this sector, having a clear litigation strategy and good dispute related advice at the outset is critical.*

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