ICRA
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INSOLVENCY AND BANKRUPTCY CODE

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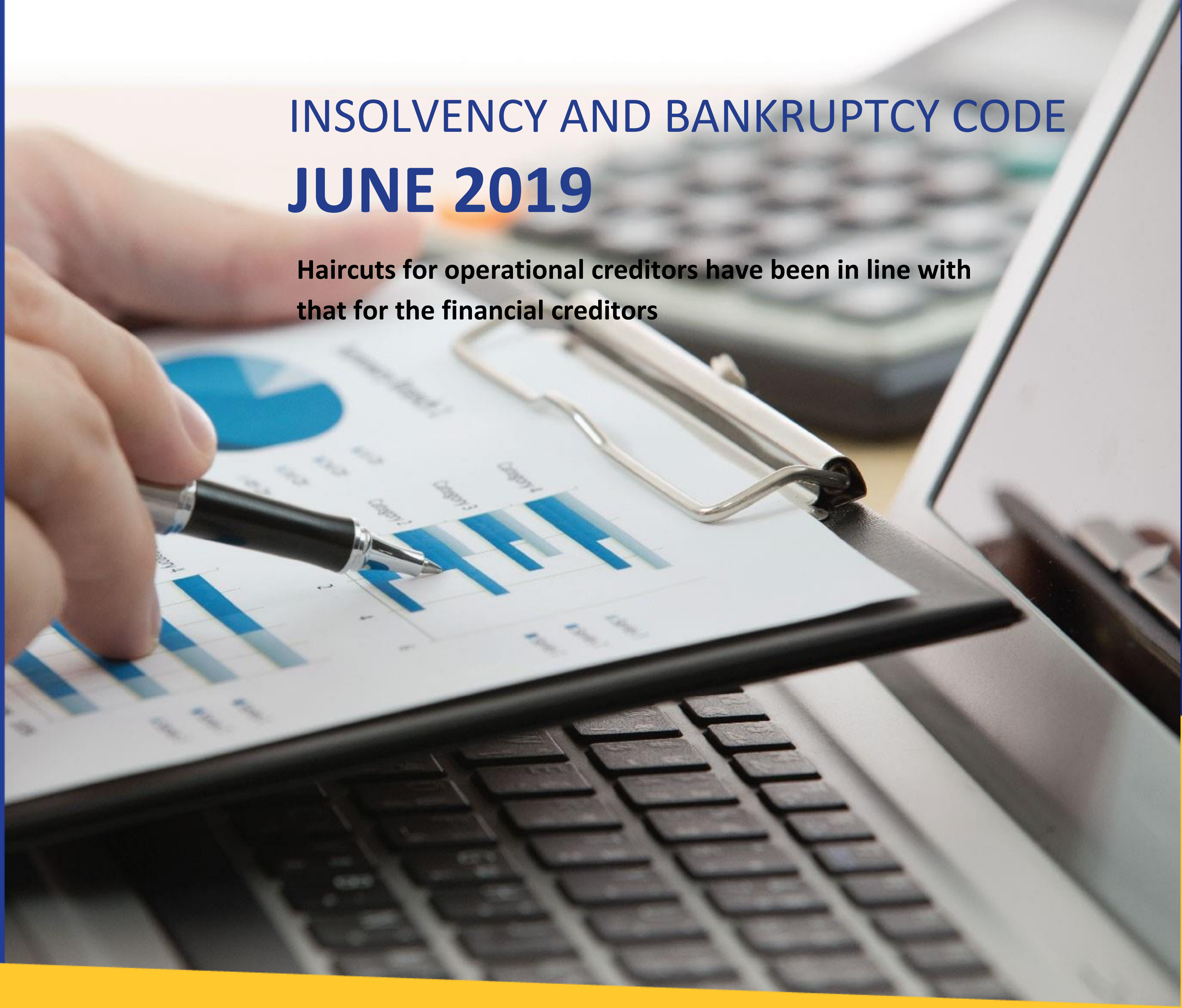
Haircuts for operational creditors have been in line with that for the financial creditors



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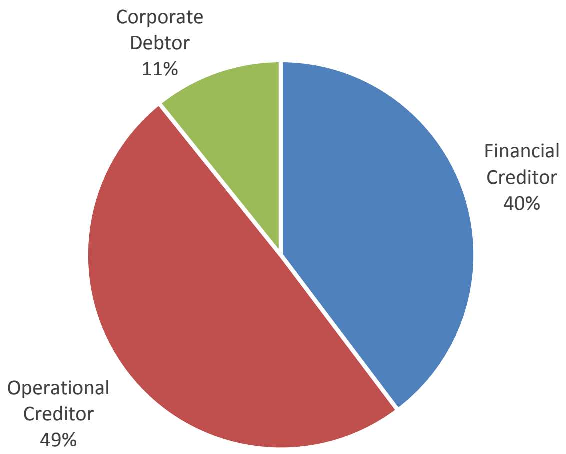
Operational creditors remain instrumental in referring defaulting corporate debtors to the NCLT

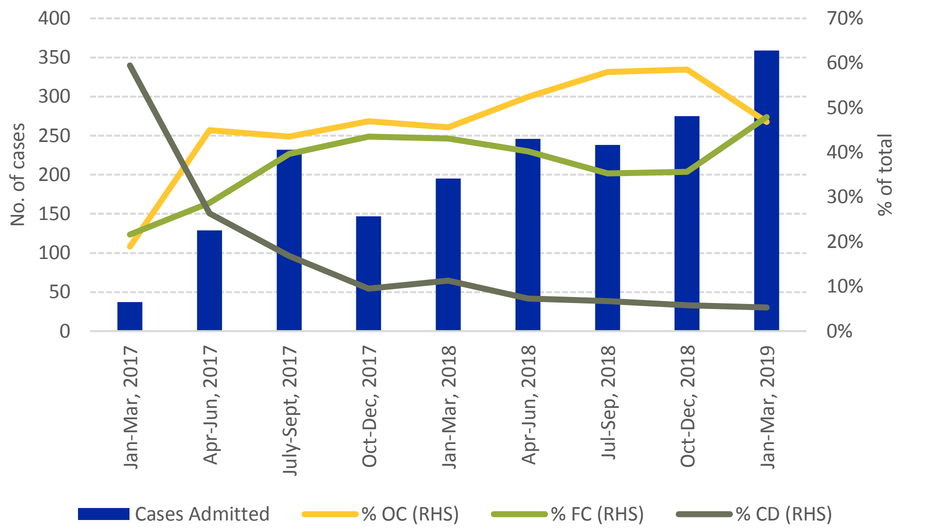
One of the biggest successes of the introduction of the Insolvency and Bankruptcy Code (IBC) has been the power given to the operational creditors to take a defaulting corporate debtor to the National Company Law Tribunal (NCLT). For a non-payment of as low as Rs 1 lakh, the operational creditor can initiate the corporate insolvency resolution process (CIRP) for a corporate debtor by referring it to the NCLT. The operational creditors have been using this power proactively and effectively. Of the 1,858 corporate debtors referred to the NCLT upto March 31, 2019, 920 cases (i.e. 49%) have been referred by the operational creditors (refer *Exhibit 1*). Despite the delays being witnessed in the application being accepted by the NCLT and then the delays in the CIRP itself, the operational creditors have continued to show confidence in the process and remained at the forefront of pushing corporate debtors to the NCLT. As seen from *Exhibit 2*, the operational creditors have almost consistently been the biggest reason for the cases being admitted by the NCLT ever since the introduction of the IBC.

EXHIBIT 1. Break-up of different creditors initiating CIRP (upto Mar 31, 2019)



Source: IBBI, ICRA Research

EXHIBIT 2. Quarter-wise trend of CIRP admissions by the NCLT and break-up of initiating parties

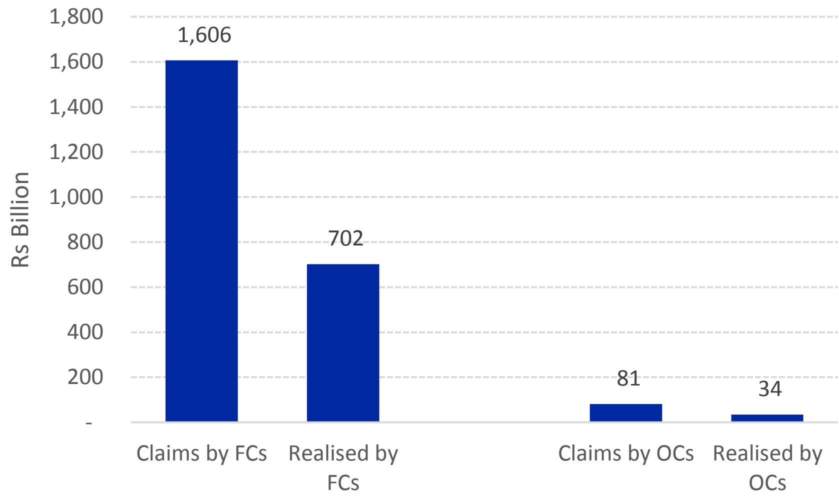


Source: IBBI, ICRA Research; OC: Operational Creditor; FC: Financial Creditor; CD: Corporate Debtor

Haircuts for operational creditors through IBC have been in line with that for financial creditors; CoC should continue to factor in the demands of operational creditors when evaluating resolution plans

As per the IBC, the operational creditors do not form part of the Committee of Creditors (CoC) and thus have limited influence on the resolution plans being evaluated and approved by the CoC which consists only of financial creditors[1]. Nonetheless, ICRA observes that the haircuts the operational creditors have been required to take so far are not materially different than the haircuts taken by the financial creditors. ICRA has looked at data from 92 CIRPs that have yielded a resolution upto March 31, 2019[2]. Of these 92 CIRPs, the operational creditors would realise about 42% of the total claims of Rs. 81.4 billion. For the same CIRPs, the financial creditors would realise 44% of the total claims of Rs. 1,606 billion (refer *Exhibit 3*). In absolute terms though, the loss to the financial creditors has been significantly higher compared to the operational creditors.

EXHIBIT 3. Comparison of realised amounts by FCs and OCs for CIRPs upto March 31, 2019



Source: IBBI, ICRA Research

ICRA believes that the reason the operational creditors have not suffered significantly higher haircuts is on account of the criticality of certain creditors to the core operations of the corporate debtors. As a result, the resolution applicants have ensured that relationships with such creditors are maintained. Among certain large size corporates, realisation by the operational creditors has been much higher than the average realisations such as that seen in the resolutions of Bhushan Steel Limited (81% of claims received by operational creditors) and Binani Cement Limited (86%). However, operational creditors have felt aggrieved in certain other instances, such as in the resolution of Electrosteel Steels Limited (nil) and Alok Industries Limited (5%). At present, the extent of funds to be paid out to the operational creditors as part of the resolution plan of Essar Steel Limited is under dispute, highlighting the difficulty in satisfying all the parties especially when the operational creditors do not have a say in the selection of the resolution plan.

ICRA believes that introducing operational creditors in the CoC would increase the operational challenges of concluding the CIRPs in a timely manner which now itself are getting stretched beyond the mandated time period. Nevertheless, the financial creditors who are part of the CoC have a responsibility to ensure that the operational creditors receive a fair share of their claims so as to maintain their own financial health. A short-sighted vision of the financial creditors to enhance their own realisation from the resolution applicant could impact the sustainability of the businesses of the operational creditors which would thus have a bearing on the going-concern status of the corporate debtor itself in the long run.

[1] Excluding real estate entities where the flat owners have been allowed to be part of the CoC
[2] It excludes 4 cases where the resolution plans were not implemented and the cases were again referred to the NCLT and 1 case viz. Essar Steel Limited where the distribution of funds has not been finalised

ANNEXURE

EXHIBIT 4. Haircut for operational creditors for top 10 corporate debtors (where CIRPs have yielded a resolution plan)

Corporate Debtor	Operational Creditor Claims (Rs billion)	Claims realised (Rs billion)	% haircut
Bhushan Steel Limited	14.8	12.0	19%
Alok Industries Limited	11.8	0.6	95%
Electrosteel Steels Limited	7.8	0.0	100%
Binani Cements Limited	7.3	6.3	14%
Jyoti Structures Limited	6.5	2.7	58%
Kalyanpur Cements Limited	5.0	2.5	50%
Monnet Ispat & Energy Limited	4.6	0.3	95%
Raj Oil Mills Limited	3.7	0.1	98%
Adhunik Metaliks Limited	2.8	0.3	88%
Burn Standard Company Limited	2.4	2.4	0%

Source: IBBI, ICRA research

ABOUT ICRA

ICRA Limited (formerly Investment Information and Credit Rating Agency of India Limited) was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

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- Assist the regulators in promoting transparency in the financial markets;
- Provide intermediaries with a tool to improve efficiency in the funds raising process.

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