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Opinion

WEDNESDAY, SEPTEMBER 6, 2017

INDIA-CHINA THAW

PM Narendra Modi

Met President Xi Jinping. We held fruitful talks on bilateral relations between India and China.

Home-owners could derail entire NCLT process

One solution is to put them at same level as banks, but this means they too need to take big haircuts if need be

JUST WHEN IT seemed the Supreme Court (SC) had given the insolvency process a big boost through the Innoventive Industries judgment last week, the stay on the judgment of the Allahabad bench of the National Company Law Tribunal (NCLT)—at the behest of buyers who had not got their flats from Jaypee Infratech—threatens to derail the process. And, from the point of view of the home-buyers, if the SC stay in the Jaypee-IDBI Bank case looked like a victory, the case has taken a fresh turn with IDBI Bank asking the apex court to restore insolvency proceedings which had been ordered by the Allahabad bench. From the point of view of the lenders, it is a lot easier to try and recover dues via the Insolvency and Bankruptcy (I&B) Code, 2016. Once an insolvency petition has been admitted, no other suits can be filed against the company—in other words, no existing litigation can obstruct the path of the lenders. Indeed, the authority of the IBC is total because it prevents the debtor from transferring, or encumbering or disposing of any assets or any legal rights. As such, the Allahabad bench's order prohibits any action to foreclose, recover or enforce any security interest created by the corporate debtor—Jaypee Infra—in respect of its property.

However, from the perspective of home-owners, initiating insolvency proceedings leaves them with little or no recourse to the money they have paid the company. They are technically not financial creditors and legal experts say they cannot claim to be creditors of any sort since the money they have paid is simply an advance and not a loan. While there is a lot of pressure on SC to take a view on humanitarian grounds and not allow insolvency proceedings, this will be a setback not merely for the financial lenders—in this case, IDBI Bank—but also for the NCLT and the IBC. To be sure, the Jaypee case is very different from the other corporate cases like those of an Essar Steel or an Alok Industries in that a large number of individuals are involved in this case. However, should the SC overrule the NCLT order, it would give corporate defaulters the room to challenge such orders in the future, making it difficult for banks to recover their dues, running into several lakh crore rupees. As it is, several companies have already raised objections to the insolvency proceedings, though almost all of these have been overruled by the NCLT benches. So it is critical the authority of the NCLT benches is not undermined.

Giving home-owners the status of financial creditors would set a bad precedent; it would allow other stakeholders to claim a similar status, derailing the insolvency process. At the same time, given their numbers, it is important that home-buyers get back their money or the apartment they had purchased. The best way out, as a senior executive of SBI suggested, would be for home-buyers to agree to share the pain by taking haircuts. What is most important is a quick resolution of the problem; for instance, the projects could be sold to other developers who could complete them. Litigating endlessly will help neither the lenders nor the wannabe home-owners.

Lessons on Teachers' Day

Too few teachers, too little freedom, too little teaching

ON THE EVE of Teachers' Day came a sad commentary, the AAP government in Delhi withdrew its proposal to appoint some 9,000 teachers. As per data tabled in the Lok Sabha, nearly 18% positions for teachers in government-run primary schools and 15% positions in secondary schools need filling urgently—in other words, we are short of one million teachers. The states with poor literacy levels have the worst shortages—nearly 70% of the posts for teachers in secondary schools in Jharkhand are vacant. This is made worse by teacher absenteeism of around 19-20%—some studies contend, though, this is because teachers have a lot of non-teaching work as well—and very poor quality of teaching, compounded by the fact that the adverse pupil-teacher ratio puts a strain on the already creaky system.

There has, of late, been some improvement in outcomes in government schools but this is far from enough. The proportion of Class 3 students who could read at least a Class 1-level text has increased from 40.2% in 2014 to 42.5% in 2016, as per ASER 2016, and the proportion of children who can read a Class 2-level text has gone up from 23.6% to 25.2%. Once you take into account the relative expenditure in government-run and private-sector schools, however, the gaps become starker. As per an Accountability Initiative study, the average public expenditure per government school student in 20 states in 2011-12 was ₹14,356 versus ₹6,257 spent per student in private unaided schools. Yamini Aiyar of the Centre for Policy Research, writing in the ASER 2016 report, highlights how learning outcomes have so far not been a focus of governments budgeting for education. Against such a backdrop, unless the government starts linking its spending to learning outcomes, a colossal amount of public money will continue to be wasted.

Things aren't much better in the case of tertiary education. Gross enrolment ratios are up from 11% in FY13 to 24.5% in FY16, but the quality of teaching is clear from the fact that less than a handful of Indian universities ever figure in any global top-500 list in comparison with China's growing numbers. The problem is compounded by inefficient higher education regulation—regulators like UGC/AICTE continue to stifle universities and institutions. After having promised a radical overhaul, including bringing in foreign competition, the government seems to be having second thoughts. That's a lot of lessons on Teachers' Day, both for the teachers as well as for those that hire them.

RagiSOLUTION

Karnataka pushing ragi over paddy and cane is well-intentioned, but the state must incentivise the millet

TO MITIGATE THE effects of the drought Karnataka is reeling under, the state government is forcing farmers in the Cauvery command area to opt for ragi or other millets cultivation over their preference for paddy or sugarcane. It might seem illiberal of the government to dictate crop choice in the manner it is doing, but the move is a good one for the long-term water security of the state. Managing water scarcity has become seminal for the state that is at the threshold of its fourth consecutive drought year. Against such a backdrop, pushing drought-tolerant millets over water-intensive crops like sugarcane and paddy makes eminent sense. To stabilise farm income and have enough fodder stock, the state has stopped the sale of paddy sees in many districts and imposed caps on availability in districts like Mysuru and Chamrajnagar. The states has only made 37,662 quintals of paddy seed available by kharif 2017 as compared with 134,315 quintals last year. To be sure, the farmer can still procure paddy seeds from his peers or from private seed sellers. But, the hope is that the state government, with ₹150 crore invested in seed subsidies, buybacks and promotions to position ragi not just as a drought-tolerant but also a nutritional crop, the millet will resonate with the farmers.

As a *Mint* report notes, getting entire districts to switch to millets has been a mammoth ask—the state had to procure 11,000 quintals of ragi, over and above the kharif season availability of 34,000 quintals. Other drought tolerant and less water requiring crops—maize, pulses and oilseeds—are also being introduced into the mix. With farmers already unhappy with the caps on release of Cauvery—thanks to the legal wrangle over water-sharing with Tamil Nadu—selling ragi cultivation is a hard proposition. Farmers claim that the returns from paddy and sugarcane are much higher—area under ragi had already fallen from 7.87 lakh hectares in 2010-11 to 6.77 lakh ha in 2015-16. While pushing ragi seems like a just solution, the fact is that forcing farmers to swallow the crop is not going to work; the state must look at incentivising it and possibly even making it a part of the public distribution system.

GDP GROWTH

EXPECTATIONS THAT GROWTH WILL REVERT TO 7%-PLUS LOOK IMPLAUSIBLE. AN OPTIMISTIC SCENARIO IS THAT THE PATH AHEAD IS L-SHAPED: GROWTH MAY HOVER IN THE 6-6.5% REGION

The economy's L-shaped recovery?

RENU KOHLI

New Delhi based economist

TWO DISTINCT FEATURES mark the three years of NDA government: sustained market buoyancy boosted by 7%-plus growth; and analysts chasing a mirage that this growth will raise corporate earnings. It remains a mystery as to why such high growth did not buoy corporate earnings, which only underscores the many difficulties in interpreting India's macro numbers in recent years. Nonetheless, many analysts continue to exhibit optimism even amidst a sharp growth deceleration to below 6% in the past two quarters. They strongly believe that growth will rebound no sooner the economy is through with short-term pain inflicted by demonetisation and the transition to GST implementation.

How realistic is such optimism? Recall that not so long ago, a V-shaped rebound was predicted in the first quarter of 2016-17 as the shock impact of demonetisation wore off. With April-June 2017 growth sliding to 5.7%, expectations of an upturn have now merely been rolled over into the next quarter or at best, second half of the year. Why is that? Because most assume India's potential growth rate to be closer to 8%; the GST and other reforms could raise it further. With inflation staying low, a quick cyclical recovery should therefore be the natural way forward, which is fairly consistent with any macroeconomic diagnostics.

But such optimism evades the hard question: What led to the deceleration that predates demonetisation? Why would growth fall off in a period when exports were rising and agriculture rebounded with a normal monsoon after two years of drought? Many analysts had already flagged that the extraordinary benefit from favourable terms-of-trade would come to an end—the IMF estimated such gains to be 2.5% of GDP—and also that the boost to manufacturing GVA from lower input prices would gradually subside. Therefore, the slowdown was not entirely unanticipated. But from a macroeconomic perspective, it is critical to assess if the short-term gains contributed to raising the economy's potential growth.

Recall that in the period before the terms of trade bounty, India's potential growth rate was estimated at about 6.75% by the IMF (Country Report No. 15/61: pg 29, March 2015) and 6% by RBI (Macroeconomic & Monetary Developments 2014-15, Update: pg 3, para II.2, April 2014). It had considerably fallen from its pre-crisis peak of 8% due to a trend decline in total factor productivity growth. But as growth accelerated beyond 7% from 2014-15, most analysts revised their potential growth estimates closer to, or even higher than 8%, based on econometric estimates that carry an end-point bias. These higher potential output growth estimates also appeared consistent with the persistent negative output gap and falling inflation.

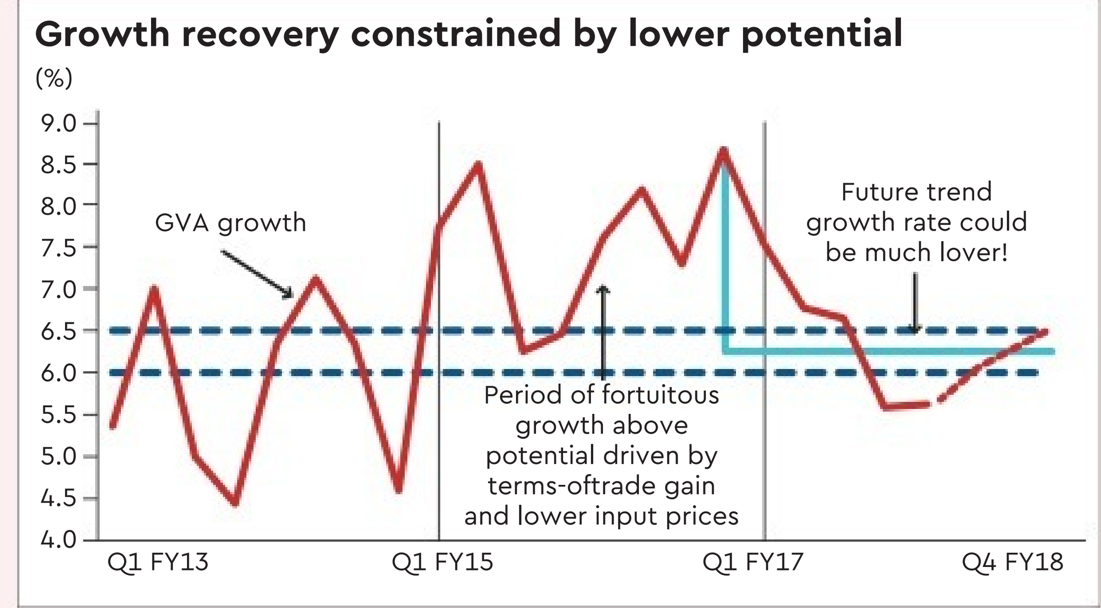
But such a narrative cannot evade the more fundamental concern: If the investment rate was steadily falling throughout and there was no visible sign of productivity gains—microeconomics tells us that persistently lower capacity utilisation results in higher unit costs—then how rational was it to assume an increase in potential growth?

The alternative and more consistent macro framework may be that the potential growth slowdown persisted while growth driven largely by consumption demand rose above potential (positive output gap) thus slowing down the decline in inflation. This may also explain why core inflation remained sticky in this period in spite of both fiscal and monetary stance remaining contractionary. Once the terms-of-trade effects began to peter out, both output and inflation fell sharply. While potential output may possibly have further weakened due to the prolonged investment decline, it is certainly unlikely to have risen beyond 2014 levels, 6-6.5%. The remarkable feature of the period is that despite a series of small, medium and big reforms, investments failed to spark back to life. There are strong indications the slowdown in potential growth persisted.

How does that impact the future growth path? Reforms could help, but fruits from the just-instituted GST system are still in the distance. At this point, lead indicators are much worse than last year: Industrial production shows a discrete drop to 0.2% this April-June from 7% last year. A six-month contraction in durable goods' production persists; it plunged to -0.9% in the recent quarter from 8% in April-June 2016, betraying the slump in consumer demand. Capital goods grew -4% in the period against a comparative 13% last year. The slack in industrial capacity is unchanged from 2014-15, an average 2 percentage points lower compared to average use in 2012-13. The weakness and shrinkage in non-food credit growth, broad based across segments, is well documented. Personal loans including housing, have slowed.

In fact, at this point most growth drivers are either weak or absent. Investment demand shows no signs of return and NPA resolution is at a very early stage. Exports are faltering while imports are rising. More importantly, private consumption on which rest all hopes of an upturn, is beginning to slow as personal incomes decelerate. In an environment of low inflation and high indirect taxation, the revival of private consumer spending will depend upon the trade-off, i.e., how much the increase in real incomes or more buying power from lower inflation outweighs the dampening effects of regressive taxation. Finally, government capex could also slow down with emergence of fiscal stress at central and state levels from increased revenue expenditures, especially from state salary revisions, subsidies, farm loan waivers, and so on. Weaker growth also lowers tax revenues, causing further strain.

Thus, an optimistic scenario may be that the growth path ahead is L-shaped instead of a V or a U: Growth may hover in the 6-6.5% region (see accompanying graphic). Lower potential output growth will also impose policy constraints, i.e. restrain the government from relaxing the fiscal stance or RBI from further monetary easing, unless growth persists below potential for a few more quarters.



Are taxis the new banks?

Ride-sharing companies are getting into financial services—competition should reduce the cost of joining the digital economy

ADAM MINTER

Bloomberg

IN SOUTHEAST ASIA, mobile banking is taking on a whole new meaning. Last week, Grab, one of the region's top ride-hailing companies, announced that users of its app can start sending credits—used to pay for rides—to each other. By the end of the year, they will be able to use those credits at more than 1,000 restaurants and retailers. If all goes well, Grab will one day be known as an e-payment platform that just happens to offer a taxi service.

That's a radical evolution, but hardly illogical. As many as 2 billion people lack access to traditional financial services worldwide. Most are concentrated in developing countries with cash-based economies, where banks have long resisted offering services such as loans, checking accounts and credit cards. As incomes in these countries rise, technology is helping entrepreneurs leapfrog old ways of doing business. In particular, mobile phones have enabled a parallel financial system to evolve, with some intriguing results.

The trend began in Kenya. In 2007, Safaricom Ltd. introduced M-Pesa, a service that allowed users to move money via text message. In short order, M-Pesa evolved into a full-fledged payment-and-banking system that runs on the region's dominant feature phones. In 2016, M-Pesa processed 6 billion transactions for 30 million customers in 10 countries. Africa now has more "mobile money" accounts than it has bank accounts.

In Asia, the transformation has been just as dramatic. China's leading e-commerce and social-media services—Alibaba and WeChat—have created payment platforms that are so ubiquitous that cash has all but disappeared in some places. In 2016, people in China made about $5.5 trillion in e-payments. In India, about a fifth of the population now uses such payments, mostly through start-ups such as Paytm E-commerce Pvt.

Southeast Asia is the next frontier and, in some ways, the most interesting. With 640 million people, and growing access to the internet and mobile phones, it is certainly fertile ground for financial start-ups. Over the past three years, they have started to emerge from a surprising source: the innovative local ride-hailing industry. That'd be an unusual business model in places where credit cards and bank accounts are common—Uber Technologies Inc., for one, would have little incentive to try something similar in the US.

But in countries such as Indonesia, where only 36% of people have a bank account, and fewer than 5% have a credit card, it is a great way to lure users and lock them into a convenient payments platform. The more than 200,000 drivers who work for Go-Jek, Indonesia's leading ride-sharing service, can use their e-wallets to store their earnings or spend them on other services. Customers can use the wallets to pay for everything from food delivery to massages to house-cleaning.

In more affluent Singapore, Grab has much the same idea, expanding the use of its e-wallet to small businesses such as coffee shops, hawkers and wet markets. By allowing vendors to accept money without the hassle or expense of renting a payment terminal, and giving customers the convenience of paying with an app they are already comfortable with, it may have a significant advantage. Its ability to collect vast amounts of data from users—combining location and travelling habits with purchase histories, say—could become a game-changer. It is no surprise that the company wants to move into insurance and lending.

> It is great news for consumers, particularly those left out of the traditional financial-services market. Competition should reduce the cost of joining the digital economy, make tasks like paying bills easier, force banks to pay attention to lower-income customers

Taxi companies going to war with banks for the chance to offer e-payments would have sounded implausible just a few years ago. Today, it is great news for consumers, particularly those left out of the traditional financial-services market. Competition should reduce the cost of joining the digital economy, make tasks like paying bills easier, force banks to pay attention to lower-income customers, and put pressure on credit card companies to lower fees and penalties. In Singapore and elsewhere, banks are rallying to set up their own e-payments standards. They may be in for a wild ride.

LETTERS TO THE EDITOR

Good that SC batted for NCLT process

Apropos of the editorial "SC boost for NCLT" (*FE*, September 5), the SC's dismissal of the appeal of Innoventive Industries is a landmark judgment as it will set a clear direction that corporates cannot take the law for a ride by using theatrical drama in courtrooms, thus slowing down proceedings and hampering overall economic growth. It has been years since the banks have been saddled with bad loans, and an end is nowhere in sight. The green shoots of lending are far away given the myriad laws and rules and the proceedings which are often stalled time and again by these promoters with vested interests. Like South Korea, India should also start hiving out parts of these defaulting companies and sell them for profit. These Indian *chaebol* need to learn their lesson. Hope that SC's ruling sets a clear precedent for all and ensures that NCLT proceedings speed up.

— Gaurav Gupta, Hyderabad

IPL media rights

The BCCI has been left laughing all the way to the bank after Star India bagged the coveted Indian Premier League (IPL) media rights for a whopping ₹16,347.50 crore for the next five years. The mind-boggling deal, which will run from 2018 to 2022 is almost double the amount that Sony paid for a decade-long IPL broadcast rights (₹8,200 crores) from 2008 to 2017. The huge amount is an affirmation of the game's popularity. The BCCI must now plough all the moolah back into the game and develop infrastructure in *mofussil* areas. Cricket is our number one sport, despite the administrative crisis it is facing at the moment.

— NJ Ravi Chander, Bengaluru

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TEJINDER NARANG
Grain trades expert

Pros and cons of importing two million tonnes of sugar

Right now, international prices are supportive and thus imports with viable duty can soften domestic values

ON AUGUST 29, the government impliedly confirmed tightness in sugar stocks by limiting inventories of mills by the end of September and October, with specified percentage as 21% and 8% of total sweetener available with them in sugar season 2016-17. Maharashtra mills were requested to commence early production, immediately after Diwali—but they have expressed their inability due to the absence of required labour strength and low recovery issues. Now, millers from Uttar Pradesh are promising to start mills promptly after Diwali. Industry has further suggested that transport subsidy be given to mills in Uttar Pradesh and Maharashtra for despatches to Karnataka and Tamil Nadu to obviate imports.

All this activity is meant to ensure that sugar prices in local markets do not flare up beyond the existing wholesale price of ₹40 per kg versus the same prices of ₹26 per kg in 2015 (see chart). Retail values are ₹43-45 per kg versus ₹28-29 per kg in 2015.

The government has been considering additional imports of sugar, especially for the mills in South India, to contain demand pressures after the import of the first tranche of 0.5 million tonnes (MT) of raw sugar in April-June 2017. The article by Harish Damodaran in *The Indian Express* ("A tough balancing act: The new bitter North-South divide in India's sugar industry," August 24; *https://goo.gl/stqMfH*) stated that "cane-starved southern mills want duty-free raw sugar imports, which the industry particularly in UP is bound to resist." He called this North-South divide. Duty hike in July 2017 from 40% to 50% was done to completely rule out the possibility of cheaper imports (that would cost ₹27-28 per kg without duty, ex-mill). Thus, local prices have ruled firmer.

Irrespective of the North-South divide, let this issue be considered upon data available on record. The issues are, one, whether additional imports are justified and, two, what has been the price behaviour of sugar in the last two years.

Sugar stocks

Are the carry-over stocks of 4 MT sufficient when the next year's anticipated output is 25 MT and consumption is also about 24-25 MT? The thumb rule is that a country should have a minimum three months of stocks of annual consumption. If India's annual usage is 24-25 MT, we need at least 6 MT carry in or import of 2 MT (6-4) next year for ensuring three months' stocks.

The other empirical formula is the "stock to use" ratio be higher than 20%, say at least 25%, if prices are required to be moderated. Currently, the carry in stock/use ratio is 4/25x100=16% that will make values more bullish. If sugar prices are required to be tapered down somewhat, 24% stock/use ratio can be attained by 6 MT carry in (or 6/25x100). In both cases, the logical answer is the same—import of 2 MT next year. The stock/use ratios have been 32% to 42% in the previous years (see chart). Psychologically, lower inventories lead to ideas of stockpiling and speculation for better returns.

For example, the Food Corporation of India uses a similar matrix while determining wheat stocks. As of April 1—beginning of the marketing year—the minimum inventory level is fixed at 7.5 MT and the usage in public distribution system (PDS) is 30 MT—this gives a stock/use ratio of 25%.

Prices

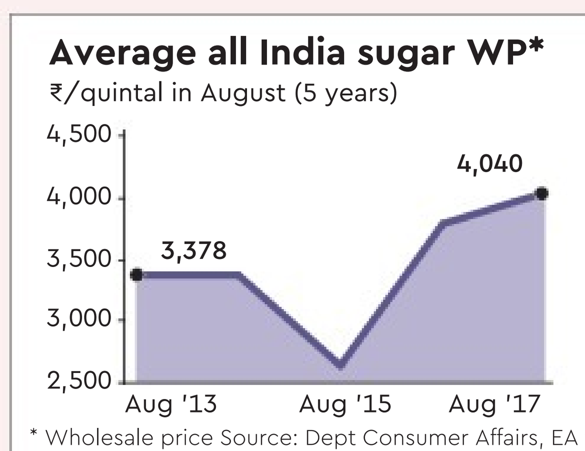
Policy profiles of the last two years have aided higher prices of sugar that have helped both farmers and mills. This, indeed, is welcome. If imports are completely blocked by high duty, sugar values would ascend further to the detriment of consumer.

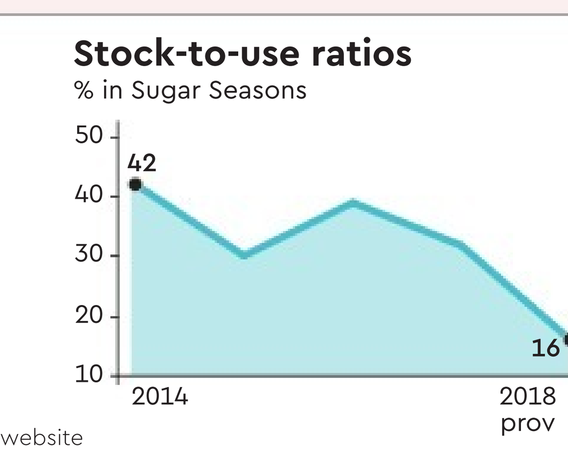
If the matter is assessed on the basis of sugar inflation of 39% in 2016-17 and 8.44% as of July in the financial year 2017-18 (Economic Advisor report date August 14, 2017), then there is a case of relaxing terms of import for 2 MT of sugar to moderate prices.

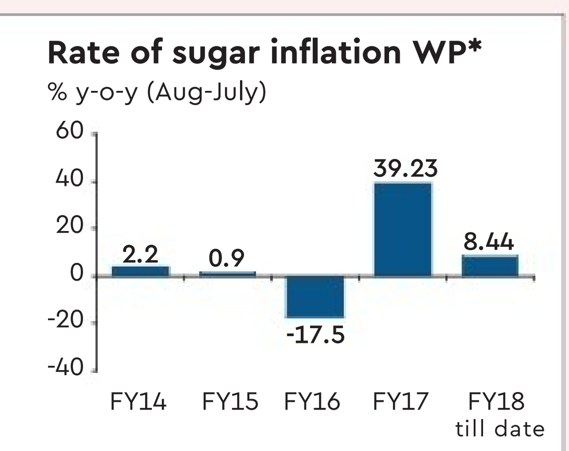
The basis of the current retail prices of ₹43-45 per kg is the fair and remunerative price (FRP) of sugarcane of ₹230 per quintal of 2016-17. When FRP is ₹255 per quintal in sugar season 2017-18, which is 11% higher, and given the fact other matrix remain unaltered, sugar retail values may also elevate pro rata.

The plea of the stakeholders that the price of Indian sugar has to be much higher than international prices because of FRP and state advised price (SAP) etc is logical up to a point, but not under the current domestic scenario. Continued choking of imports is bound to inject inefficiency in the industry because profits are secured under closed market mechanism.

It is well admitted that the cost of production of sugarcane in India is higher by about 30% compared to other competing origins—and this percentage can be rechecked. If true, then duty protection beyond this point may be reviewed. This will ensure that the principle of comparative advantage is not abandoned or deserted, which is fundamental to national and international trade. Right now, international prices are supportive and thus imports with viable duty can soften domestic values. The government needs to take a call on moderation of sugar prices, act in the interest of all the stakeholders and avoid sugar inflation to double-digit levels, when wholesale national inflation is just 1.8%. Facilitating minimum imports of 2 MT is the sole prerogative of the authorities.







* Wholesale price Source: Dept Consumer Affairs, EA website

InfraTweets

VINAYAK CHATTERJEE
Chairman, Feedback Infra
Twitter handle: @Infra_VinayakCh

Shipyard IPO on a high

Make In India: Success of Cochin Shipyard IPO leads to renewed energy & enthusiasm to build larger ships incl LNG carriers. Good luck!

● Shipyard IPO gets massive response
The issue got oversubscribed 76 times, receiving bids for 258.25 crore equity shares against IPO size of 3.39 crore shares. A state-run company, Cochin Shipyard, had targeted to raise up to ₹1,468 crore through its share sale offer.

2 steps forward on City-gas: (1) Accorded 'public utility' status (2) Gas pipelines to be made mandatory in all new buildings design

● Stepping on the gas on city gas
Public utility status means easier approvals & clearances, and puts city gas distribution (CGD) under Essential Commodities Act. NITI Aayog batted for extending the CGD network to 326 cities by 2022 through changes in bidding or regulatory practices of Petroleum and Natural Gas Regulatory Board.

Smart: To challenge road trpt, Rlys gears up for door-to-door service. RoadRailer unit tested—a combo of trailer on road & wagon on rail

● Roadrailer put on track
A greenfield RoadRailer manufacturing unit in Nashik has been in production since 2011. Kirloskar Pneumatic Co Ltd has developed RoadRailer terminals at Chennai and Palwal (Haryana), and will deploy two dedicated RoadRailer rakes.

Sensible: The pan-India tariff for suburban trains may soon be replaced with decentralised powers enabling local competitive benchmarking

● Suburban tariff to get decentralised
A Railway panel had suggested different fare structures for peak and off-peak services, with competitive tariffs. It will also allow the introduction of specific services to capture a greater share of the local market.

Boarding Pass: New E-way bill from Oct 1. All non-exempt goods > Rs 50,000 to be pre-registered online before moving for sale beyond 10 km

● E-way bill introduced
The permit in the electronic format can be generated by the registered suppliers or recipients or the transporter. SMS-based generation and cancellation may be allowed. However, many goods have been kept out of its ambit.

No need to wait for new Jewar Airport in Gr Noida to get operational. Hindon Air Force base in Ghaziabad getting readied for regional flights

● RCS take wings at Hindon air base
Part of the Hindon Air Force base is to be converted into a civilian enclave. As per the agreement between the GMR-run DIAL and the AAI, there can be no civilian airport operations within 150 km of IGI; therefore, DIAL's nod is crucial.

Tangedco auction ~ lowest wind power rate = Rs 3.42/unit. Amidst many complications, silver lining is reduces mkt risk of Discoms not buying

● Lowest renewable tariff discovered
ReGen Power Tech Company made the bid for a capacity of 200MW. The price now is 4 paise lower than that quoted in the Union renewable power ministry's wind power tender bid.

New Metro Policy mandates "5km on either side of station" linkages for passengers; brings focus back on cycle tracks & e-rickshaw lanes

● No metro without last-mile connectivity
States proposing new metro projects must indicate in project report investments to be made for last-mile connectivity through feeder services, non-motorised transport infra, etc.

A weekly selection of the author's tweets

INSOLVENCY CODE

From pro-debtor to pro-creditor

The SC judgment in the *Innoventive* case arms the NCLT process by upholding the right of the creditor as paramount

ABIR ROY
Partner, Lakshmikumaran & Sridharan

ENTRENCHED MANAGEMENTS ARE no longer allowed to continue in management if they cannot pay their debts"—the most unequivocal and incontrovertible finding of the Supreme Court of India, in its first substantial ruling under the Insolvency and Bankruptcy Code in the case of *Innoventive Industries Ltd vs ICICI Bank*.

Keeping in mind the history of the Code and the legislative intent, the Court has noted that managements are not allowed to continue if debts are not being paid. The decision takes note of the legislative history, and notes that the Bankruptcy Law Reforms Committee of November 2015 held that a limited liability company is a contract between equity and debt; if debt obligations are met, equity owners have complete control and creditors have no say in the running of business—when default happens, control is transferred to the creditors.

The Court further notes that time is of critical essence in the scheme of the Code, and the intent of the Code is to see whether corporate debtors can be put back on their feet to stave off liquidation. The Court has made elaborate observations on the scheme of the Code and notes that the management is divested off its powers in case of an initiation of insolvency proceedings; the said management powers are given to a professional agency to continue the business as a going concern and draw up a resolution plan. Once the resolution plan is drawn up, the management is handed over so that the corporate debtor can pay its debts and get back on its feet. Conversely, if the resolution plan is not drawn up within a maximum period of 270 days as permitted under the Code, liquidation would commence. The underlying theme of the Code is to bring defaulter companies back to the commercial fold or get them to face liquidation. To ensure that the defaulter companies can continue their commercial activities, the Code also provides wide powers to the resolution professionals related to raising finances, creating security interests, etc, subject to the approval of the committee of creditors. It is noteworthy that under the Code, the committee of creditors comprises all financial creditors.

The Code provides for two categories of creditors: financial and operational creditor, and the Supreme Court has noted that there is a difference in the manner the insolvency proceedings are initiated at the instance of a financial creditor and an operational creditor. For financial creditors, in case of a default by a corporate debtor, the role of the adjudicating authority is limited to merely seeing the records of the information utility or other evidence produced by the financial creditor to satisfy itself that a default has occurred. The only defence for a corporate debtor, at this stage, is to point out that the default has not occurred, in the sense that the debt is not due. The Court has further noted that debt may not be due if it is not payable in law or in fact. Thus, the adjudicating authority may therefore only reject an application on the defence taken by the corporate debtor that the debt was not due. The observations of the Supreme Court for initiation of insolvency proceedings for the financial creditor is significant considering the recent efforts taken by RBI to expedite the NPA resolution process.

Conversely, an operational creditor must first send a demand notice of unpaid debt to the corporate debtor. The corporate debtor has time till 10 days from the receipt of the demand notice to bring to the attention of the operational creditor the existence of a dispute or a record of the pendency of a suit or arbitration proceedings which existed at the time of the demand notice. The moment there is existence of a dispute, the operational creditor is out of the scheme of the Code.

The Court has further unequivocally noted that due to the *non obstante* clause contained in the Code, any rights accruing to the corporate debtor under any law cannot come in the way of the Code. Thus, the Court is clear that the Code is to bring defaulter companies back to the commercial fold or liquidate them, and any other law which unsettles the scheme of the Code will be considered repugnant.

The judgment of the Supreme Court further amplifies the legislative intent behind the Code. The aim of the Code should not be seen from a myopic perspective of recovery of money, but should be thought of as a well-thought-out Code. It lays down that resolution of the corporate debt is paramount, failing which the borrowing company must face liquidation. The judgment is forward-looking, and if properly implemented, will pave the way for effective implementation through strict adherence of timelines.

ILLUSTRATION: ROHNIT PHORE