

Reserve Bank of India backs finance ministry on debt recast plan

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The RBI told the Supreme Court that the inter-creditor agreement (ICA) aimed at helping debt defaulters avoid bankruptcy proceedings requires the approval of 66% of lenders and not all of them, backing the plan that had been drawn up at the behest of the finance ministry.

Rakesh Dwivedi, senior advocate appearing on behalf of the RBI, clarified that after execution of ICA, all lenders in a consortium don't have to approve it.

The RBI also told the SC that banks could have continued with various resolution processes that were being discussed before February 12 last year, when a circular issued by the regulator had scrapped such mechanisms.

This seems to contrast with the RBI's previous stand in cases in the Allahabad and Madras high courts. In a case filed by Infrastructure Leasing & Financial Services in the Madras High Court last year, the RBI had argued that if a restructuring scheme had not been implemented before February 12, 2018, then it became null and void. Governor Shaktikanta Das had said last month that "there is no proposal on the table seeking modifications to the February 12 circular".

The RBI didn't reply to queries.

The Centre said it was seeking to resolve the financial woes that ail the power sector and took a firm stand on excluding stressed plants from the RBI circular.

Solicitor general Tushar Mehta argued that if this requires striking down the circular, then so be it. In the Allahabad High Court case, the government had said that such entities should not be categorised as stressed in 90 days and that the deadline of 180 days to resolve a bad loan be extended to 270 days. The ICA comes into play during the 180-day period and the 66% threshold is meant to ensure that smaller lenders don't stall such plans.

The circular provided flexibility to lenders to undertake any restructuring scheme and in fact did not limit them to the earlier schemes allowed by the RBI, said Dwivedi, senior advocate appearing on behalf of the central bank. It's not clear whether any such schemes can now be revived.

The bench comprising Justices Rohinton F Nariman and Vineet Saran reserved judgment on the matter on Thursday while asking all parties to make written submissions within 10 days. The matter has been heard daily since March 6.

The SC halted insolvency proceedings on September 11 last year against defaulters in the power, sugar, shipping and textile sectors by staying the RBI circular. It directed parties to maintain status quo while transferring about a dozen cases on the matter in various lower courts to itself. The petitions were then segregated into two buckets — those challenging the constitutional validity of insolvency proceedings and those challenging RBI's circular on stressed assets.

The February 12, 2018, circular had directed lenders to refer any loan account over Rs 2,000 crore to the bankruptcy process if it wasn't resolved within 180 days of default. It also underscored the IBC's status as the cornerstone of India's bad-loan resolution framework, scrapping all previous mechanisms, such as corporate debt restructuring, strategic debt restructuring and the scheme for sustainable structuring of stressed assets.

The circular also imposed a one-day default rule — a company is treated as a defaulter even if it misses one day of the repayment schedule. This is said to have rattled borrowers and annoyed many within the government, leading to a clamour that it be diluted. The circular had been one of the key measures the regulator took under the governorship of Das' predecessor Urjit Patel, who quit before his term was over amid a dispute with the government over various issues including autonomy.

Dwivedi, however, maintained the RBI's stand against exempting the power sector from the circular.

He said the banks should look into individual cases rather than seeking a blanket special dispensation for the entire sector. He said banks have not been able to resolve projects despite getting time since the last Supreme Court order on September 11 last year, when it had stayed the RBI circular. Dwivedi also submitted that initiation of insolvency proceedings under the Insolvency and Bankruptcy Code (IBC) was not a penal measure but aimed at resolving stress in the banking system.

The notification had been legally challenged, with several borrowers and especially the Association of Power Producers terming it impractical and too harsh. The central bank has previously defended the circular, saying it would improve the "trust between counterparties in a transaction." The circular compelled lenders to identify stress in the loan accounts without delay, it said.

"It lays down broad principles that should be followed in the resolution of stressed assets, with clearly defined rules for ensuring credible outcomes," RBI had said in its Trend and Progress Report late last year. The rules are aimed at encouraging the prompt repayment of loans and preventing deliberate delays by borrowers that have the ability to repay by the due date, it said.

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