Inclusion of pre-packs in IBC

Why in news?

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There has been a speculation recently about the introduction of pre-packs in the Indian insolvency regime.

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What is a pre-pack?

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- Pre-pack is a description for an insolvency regime that involves both formal and informal processes.
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- Under that, a plan for restructuring the debtor company is solicited in advance of commencement of a formal insolvency procedure.
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- The distressed company and its creditors negotiate and conclude a plan to restructure the debtor company.
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- Advisors or insolvency practitioners are engaged to find investors and assist in consulting creditors, negotiating the plan, and seek the support of major creditors and ensure that the plan is legally compliant.
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- The plan must be agreed upon by financial creditors holding 66% of the debt of a corporate debtor.
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- If approved, insolvency proceedings may be initiated under the IBC to get the resolution plan formally approved by the committee of creditors and confirmed by the NCLT.
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- The plan approved by the NCLT will become binding on creditors, members of the company, guarantors, employees and other stakeholders.
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What are its advantages?

- Restructuring plan can be negotiated and agreed to while the business of debtor continues uninterrupted.
- Other benefits include –

1. Lower costs
2. Faster approval and implementation of restructuring plan
3. Protection for and retention of employees
4. Maximisation of return to creditors
5. Maximise value realised in sale
6. Minimise risks associated with trading and preservation of value.
7. Reduces possibility of litigation and delays

- The promoter and management of debtor will have greater incentives to cooperate as it will allow them to <u>negotiate directly</u> with creditors and investors to achieve a plan.
- This will maximise the value of assets of debtor while balancing the interest of all stakeholders.
- Pre-packs can significantly reduce the time-frame, since obtaining approval of financial creditors can be achieved before commencement of insolvency process.
- These very financial creditors, when assembled as committee of creditors, can swiftly approve the plan when presented by the insolvency professional under the IBC.

What was the related amendment made?

- Amendments to the insolvency law (as part of the Companies Act 2013) approved by the Parliament were inspired from pre-packs.
- The amendment required the debtor to file, together with application of commencement of insolvency, an implicitly pre-negotiated plan.
- Once the plan was submitted, the debtor was allowed to remain in possession under the oversight of an independent insolvency professional appointed as chairman of the board of directors.
- This prevented disruption in cases where there was no trust deficit between the creditor and the debtor.
- If no pre-negotiated plan was submitted, the debtor was to be displaced and make way for an independent insolvency professional who would run the enterprise and invite plans from the market.
- However, the amendment was not notified by the central government and correspondingly the Bankruptcy Law Reforms Committee (BLRC) was set up.

What should be done?

- A secured creditor is generally a bank or other asset-based lender that holds a fixed or floating charge over business assets, whereas operational creditors are suppliers of goods or services to a defaulting company.
- Pre-packs are perceived to be <u>favourable to secured creditors</u>.
- Operational creditors and statutory dues holders may feel left out of negotiations and advisors may be conflicted.
- However, safeguards can be built to address these concerns by making the process of <u>negotiation inclusive</u>.
- Thus, IBC framework needs an amendment to make way for a pre-negotiated plan conforming to the laws currently in force.

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Source: Financial Express

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