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Supreme Court Order on RBI's 'February 12 circular'

Why in news?

The Supreme Court, in its recent order, has struck down the Reserve Bank of India's 'February 12 circular'.

What was the February 12 circular?

- The RBI circular issued on February 12, 2018 is essentially a revised framework for the resolution of stressed assets.
- The circular went into effect on the same day that it was issued.
- All existing schemes for stressed asset resolution were withdrawn with immediate effect, which included the -
    i. Framework for Revitalising Distressed Assets
    ii. Corporate Debt Restructuring Scheme
    iii. Flexible Structuring of Existing Long Term Project Loans
    iv. Strategic Debt Restructuring Scheme (SDR)
    v. Change in Ownership outside SDR
    vi. Scheme for Sustainable Structuring of Stressed Assets (S4A)
- All these schemes allowed more lenient terms of resolution than the February 12 circular.
- As per the circular, banks were required to immediately start working on a resolution plan for accounts over Rs 2,000 crore.
- It prescribes insolvency proceedings under the Insolvency and Bankruptcy Code (IBC), for a debt servicing default beyond 180 days.
- Also, banks have to recognise loans as non-performing even if the repayment was delayed by just one day.
- Not adhering to the timelines in the circular would attract stringent supervisory and enforcement actions.
- The RBI argued that the circular had been issued in the public interest, with a view to ensure the timely resolution of stressed assets.
- It was intended to stop the "evergreening" of bad loans.

What were the concerns?

- Several companies from the power and shipping sectors had challenged the circular.

- They had argued that the time given by the RBI was not enough to tackle bad debt.
- Power producers contended that the RBI’s ‘one-size-fits-all’ approach was impractical as the sector had to confront many external factors.
- These included the unavailability of coal and gas, and problems arising out of state governments' failure to honour power purchase agreements. Click here to know more.
- These factors were beyond its control, and so made an early revival difficult for them.
- The total debt impacted by the circular stands at Rs 3.8 lakh crore across 70 large borrowers.
- These include Rs 2 lakh crore across 34 borrowers in the power sector alone.
- As of March 31, 2018, 92% of this debt had been classified as non-performing, and banks have made provisions of over 25-40% on these accounts.
- The government too had asked the RBI to make sector-specific relaxations in the timeline for the implementation of the circular.

What is the Supreme Court's present order?

- The Supreme Court held the February 12 circular “ultra vires as a whole”.
- This means that the RBI had gone beyond its powers and thus the circular is “of no effect in law”.
- The order provides immediate relief to companies that have defaulted in repayments, especially those in power, shipping and sugar sectors.

What is the possible drawback?

- The circular had significantly tightened stressed loan recognition and resolution for large borrowers.
- Now, banks will have the choice of devising resolution plans or going to the National Company Law Tribunal under the IBC.
- So the urgency that the RBI’s rules had introduced in the system could be impacted.
- In effect, the verdict could delay the process of stressed assets resolution which had just taken pace.

Source: Indian Express

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