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24th June, 2022

CORPORATE RESTRUCTURING AND INSOLVENCY: NAVIGATING THROUGH THE PANDEMIC AND BEYOND

Introduction

- 1 Incredible change has happened as companies have hurdled through the pandemic and made important decisions to come out of the losses that many businesses have faced. In the current period, various forces now determine how a company structures itself including changed customer behaviours, the uncertainty, regulatory factors, etc.
- 2 With the aim of pandemic recovery, corporates have resorted to crisis management tactics which includes reshaping the organization. Such resort is not merely to deal with the losses but also to improve business performance.
- 3 In the background of the material changes brought about due to the pandemic, this article deals with the impact of the same on corporate restructuring and insolvency and what lies ahead on that front.

Corporate Restructuring meaning

- 1 Corporate restructuring refers to an act by which a company decides to modify its business substantially by restructuring the capital structure, operations, debts and finances. The company deploys a strategy to alter the business in the proposed manner in an expectation of better results which may lead to changes in composition and diversify the business.
- 2 Restructuring may include amalgamations, mergers, acquisitions, arrangements, etc. A corporate restructures its company primarily for greater profitability and competitive advantage.
- 3 Insolvency refers to a situation where a company fails to acknowledge its debts and becomes financially incapable to pay off the money owed to the creditors.
- 4 Both restructuring and insolvency and methods essentially arise out of financial difficulties of a corporate entity. However, the aid of corporate restructuring is taken to ensure that the company can be maintained as a going concern rather than being pushed into liquidation.
- 5 The difference between restructuring and insolvency is that insolvency of a company is mandated by a court

- while restructuring may or may not be affected on court directions.
- 6. The Insolvency and Bankruptcy Code, 2016 (IBC) provides for the procedure for declaration of a corporate as an insolvent. It also provides that once insolvency resolution process has been allowed, the Resolution Professional may take decision as to the restructuring or liquidation of the company.
- 7. Such procedures are to be approved and admitted by (Supreme Court of England & Wales) the National Company Law Tribunal (NCLT)

The impact of COVID-19

- 1. In the wake of the pandemic ever since March, 2020 all courts including the NCLT shut down their functioning and the insolvency proceedings came to a halt. Various companies that were already under debts became seriously hit, especially micro, medium and small enterprises.
- 2. Studies have recognized this widespread and deep nature of defaults that heightened during the pandemicas "debt overhang". It has also been argued that the debt overhang has had a negative impact on investments by businesses and has also substantially saturated growth.
- 3. To address the issue of large number of defaults, on 24th March 2020, vide Notification no. SO 1205 E, the pecuniary limit for filing insolvency proceedings against debtors was increased from Rs. 1 lakh to Rs. 1 crore meaning that in case of default below the amount of Rs. 1 crore, no proceedings could be initiated against corporate debtors under the IBC.
- 4. In case of pre-packaged insolvency resolution process (when the creditors and debtors work on an informal plan before applying for insolvency), the minimum amount of default has been raised to Rs. 10 lakh under which no insolvency resolution process can be initiated. (Notification No. S.O. 1543 (E) of 9th April, 2021)
- 5. In response to the economic distress, the legislature introduced the Insolvency and Bankruptcy Code



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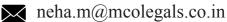


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- (Amendment) Ordinance, 2020 by virtue of which the filing of fresh insolvency proceedings before the NCLT in relation to debt or default that arose during the pandemic was suspended initially for a period of 6 months and then extended further for additional 6 month bringing the total to 1 year. The suspension was lifted in March, 2021.
- 6. Section 40C has been inserted under the IBC which specifies that the period of lockdown shall not form part of the time-lines specified under the Code for the purpose of the different stages of the Corporate Insolvency Resolution Process.
- 7. The legislature had also clarified that such reliefs shall not apply to proceedings initiated before 25th March, 2020, i.e., before the lockdown. *In Foseco India Limited v. Om Boseco Rail Products Limited*, NCLT, Kolkata also clarified that the notifications shall not have a retrospective effect.
- 8. Thus the numerous decisions taken by the legislature and the Ministry clearly shows that companies received policy and legislative support during the financial crisis imposed by the pandemic.

Navigating through the distress

- 1. An interesting study on corporate restructuring was released wherein it stressed on understanding the kind of restructuring a company may need to undergo based on the kind of crunches it has faced.
- 2. When the distress has been primarily in relation to revenues, the answer may be found in a refresh of marketing strategies or redesigning the standards.
- 3. When the effect has been severe, changes in supply chain or rebalancing financial and tax conditions may be required.
- 4. However, when the strain has reached beyond a limit and also beyond the pandemic, significant changes in capital structure, reconnection with the shareholders and an overall reconstruction may be required.
- 5. For instance, amidst the Amazon-Future-Reliance battle, Future Retail restructured its secured financial debt under RBI's August 6, 2020, Circular for Resolution Framework for COVID-related stress.

Conclusion

- 1. There have not been instances of sudden rise in the filing of applications ever since the suspension was uplifted. The IBBI chief had also argued during the suspension of proceedings that corporates would not wait for suspension but rather adopt several other measures available under statutory provisions, corporate arrangements and RBI directives for resolution of stressed assets. Thus, the pandemic has not as of now shown long lasting effect on the insolvency proceedings.
- 2. Thus, the pandemic may have affected business severely with increased instances of default, however the suspension did provide a relief to corporates to stand back on their own two feet. The corporate restructuring and insolvency process has also not undergone majorchanges and continue in a similar manner as it was prior to the pandemic.
- 3 Additionally, the increase in pre-packaged deals may be seen to be on the rise owing to its ample benefits including reduced costs and time while it also substantially reduces issues of regulatory and compliance barriers.
- 4 In view of the increased pecuniary jurisdiction of NCLT for accepting insolvency proceedings, parties have also resorted to the Out of Court Settlement (OCS) system. Even during pendency of proceedings, there are multiple stages available to a party during which they make seek to opt the OCS to avoid litigation costs and hurdles which are also time consuming.
- 5 The new forms of debt resolution mechanisms as discussed may be adopted by parties as an answer to the rising number of cases of defaults.
- 6 Yet, corporate restructuring and insolvency mechanisms are still the most sought after mechanisms owing to certainty and high ratio of debt recovery that has been achieved thereunder. (The Finance Minister in 2021 assured that debt recovery under the IBC was close to 45%).
- 7 However, it has to be ensured that such methods can be also applied to banks that are already suffering the poor recovery rateseven since before the pandemic.