

ESIL - Corporate Insolvency Resolution Process – Challenges and Learnings

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Overview: Essar Steel India Limited

Company Overview

- An integrated steel producer with an installed steel making capacity of 9.6 MTPA
 - In top 4 steel manufacturers in India and is the largest integrated steel manufacturer in Western India
- Manufacturing operations are strategically located in Western India in close proximity to the major steel market
- Product portfolio includes hot rolled, cold rolled, galvanised and colour coated coils, plates, pipes, etc.
- 7 service centres in various parts of India

Facilities Overview

- Manufacturing facilities primarily comprise:
 - Beneficiation (Odisha and Chhattisgarh) and pelletization plants (Odisha and Andhra Pradesh)
 - Integrated steel complex situated in Hazira, Gujarat Downstream capability hub located in Pune

Power, ports, shipping are owned by separate legal entities which are not owned by ESIL

Various Risk Buckets resulting in loss of value, litigations, delayed resolution



Managing as 'Going Concern'

1 - Control of bank accounts and collections

2 - Focus on liquidity

3 - Pre-payment checks
- Prioritization of payments – critical v. urgent
- Tagging/recovery by banks during CIRP not permitted
- Opening of LCs/BGs, Bill discounting, etc.

4 - Normal capex

5 - Interim Finance

Various Risks/Potential Litigations emanate from

- 1
 - Differing objectives of various stakeholders, Non-cooperation from certain members – Build consensus

- 2
 - Compliances issues

- 3
 - Time bound process
 - Limited Information availability

- 4
 - Operational issues – may impact ‘Going Concern’ : First few months critical

- 5
 - Related Parties issues
 - Protection & Preservation of assets

- 6
 - Claims of creditors – Amount, disputes, payment etc.

- 7
 - Ongoing and new litigations by Creditors

- 8
 - Resolution Plan related from Resolution Applicants (RFP, 29A) etc

Resolution Professional – Framework

1 - Objective – Non adversarial, non arbitrariness, transparent

2 - RP as Facilitator

- When in doubt, please disclose

3 - Take professional advice

- Consult and inform CoC, use provisions under IBC to approach AA for direction

4 - Provide opportunity to aggrieved party, follow 'Principle of Natural Justice'

5 - Reasoned decisions

Clarity of Role of IRP/RP – Various Relevant Orders

- ESIL SC Order Oct 4, 2018 : RP not required to take any decision, but merely to ensure that the Res Plans submitted are complete in all respect before they are placed before CoC
- RP to only “examine” and “confirm” that each Res Plan conforms to Sec 30(2)
- RP only required to give a prima facie opinion to the CoC on 29A eligibility – supplemented by Swiss Ribbons SC order
- RP only to provide his prima facie opinion to CoC that a law has not been contravened
- Binani NCLAT Order - Approval of the ‘Resolution Plan’ is in the domain of the ‘CoC’ and not that of ‘RP’ and, therefore, if the ‘Resolution Plan’ provides for the mandatory contents and is in accordance with the ‘I&B Code’ even if in case a ‘Resolution Plan’ does not provide for full satisfaction of claims of ‘OCs’, in absence of any power of the ‘RP’ to reject such ‘Resolution Plan’, ‘RP’ cannot be blamed
- Swiss Ribbons SC Order- RP a facilitator of the Resolution Process, whose administrative functions are overseen by CoC and by AA
- Swiss Ribbons SC Order- RPs have no adjudicatory (quasi-judicial) powers unlike Liquidators whose determination of claim is a decision

Verification of Claims – Various Relevant Orders 1/3

- Verification – Completeness of documentation
- RP has not been vested with the power of adjudicating the claim such issues can be dealt with and decided by a competent court/authority.
- In case of dispute, RP to disclose the dispute and include the same in IM (ESIL – Orissa Slurry NCLT Order)
- Sec 5(7) and 5(20) of IBC – creditors include to whom debt has been **legally** assigned
- All assignments to be legally reviewed as same will impact constitution of CoC and amount of claims
- Fortune Pharma Order- if the assignor is a related party then the assignee shall also be treated in the same status as 'related party' vis-à-vis to the impugned debt
- Pankaj Yadav v. SBI dated 07.08.2018 NCLAT Order- Rights of assignee are no better than those of assignor. Rights and disadvantages also go along with such assignment
- Related party FC does not have right to be part of CoC and therefore can't vote

Verification of Claims – Various Relevant Orders 2/3

NCLT- Para 8 – claim not admitted by the Resolution Professional due to non-payment of requisite stamp duty and for non-completing the statutory formalities for not without furnishing the proof of making payment of requisite stamp duty as per the Indian Stamp act. Hence, such agreement cannot be looked into as evidence nor can it be treated as valid claim

SC Dated November 15, 2019 – Para 99 -the Resolution professional has rejected the claim of the Appellant on the grounds of non-availability of duly stamped agreements in support of their claims and the failure to furnish proof of making payment of requisite stamp duty as per Indian Stamp Act despite repeated reminders sent

Verification of Claims – Various Relevant Orders 3/3

- Various disputed claims by operational creditors (~INR 14,000 crore) were admitted by NCLAT in its judgment dated July 4, 2019 and NCLT had asked resolution professional to register these claims.

Supreme Court held (para 102) that the resolution professional was correct in only admitting the claim at a notional value of INR 1 due to the pendency of disputes with regard to these claims

- Supreme Court (para 98) held that rightly rejected by NCLAT in view of the fact that said claim was filed after the completion of the CIRP period. However, the NCLAT's judgment inasmuch as it left it open for the Appellant to pursue the matter in terms of Section 60(6) is set aside
- Role of RP – Reiterated earlier role, further on basis of claims admitted, negotiations can take place between RA and CoC for payment (para 27)

Legal Advisors to RP – Very Critical Role

- 1 - Multi-disciplinary skills – Banking docs, litigations, contracts, etc.

- 2 - Experience in running sale process, due diligence, etc.
- Documents – Simple, no ambiguity (RFP etc)

- 3 - Pro-active, prompt advice/opinion rather than reactive one with focus on reduced litigation
- Regular reviews with team

- 4 - Up to date with various precedents resulting in quicker decision making

- 5 - Independent /No conflict

Challenges to the Resolution Process

Challenges & Difficulties faced

- Res Plan being challenged at various stages – Late bids, 29A eligibility, distribution, etc
- Myriad litigations thereby moving away from resolution and resultant delays in resolution due to cross-allegations by the rival resolution applicants
- SC held that an RA has no vested right that his resolution plan be considered by the CoC, in light of which no challenge can be preferred before the NCLT by a Resolution Applicant, at a stage where (a) the Res Plan has been turned down by the RP for non-compliance of Sec 30(2) of the Code or (b) a Res Plan as presented by RP is not approved by CoC. A challenge can be preferred once a Res Plan is approved by the NCLT, before the NCLAT and thereafter the SC.
- K Sashidhar SC Order dated 05.02.2019: If CoC approves the resolution plan by requisite percentage of voting share, it is imperative for the RP to submit the same to the NCLT

Rights of suspended Board of Directors

- Board members (comprising promoters also) invited to all CoC meetings
- SC in the case of Ruchi Soya held that the scheme of the Code makes it clear that the directors, though not members of the CoC, have a right to participate in every meeting of the COC
- Further, as vitally interested parties, they have right to receive copies of the Res Plan presented to the CoC

Litigations against RP

Letter issued by IBBI to RPs stating that while conducting CIRP, an IP is an officer of the Court and discharges a statutory public function.

Further, any hindrance in the working of the CIRP will amount to contempt of court (Ref NCLT Order in Shivam Water, Jan 2019)

Sec 233- Protection of action taken in good faith

Code has restricted jurisdiction of the civil courts by Sec 63 and Sec 231

Reg 39(7) - No proceeding to be initiated against RP for any action of the CD, prior to the insolvency commencement date

Litigation against RP - 1

Claim Related

One of FC, who filed claim with RP and whose claim had been accepted, continued its legal suit in London and got decree against ESIL during CIRP.

RP filed violation of Sec 14 moratorium application in NCLT.

FC challenged the appointment of RP in NCLT submitting that the same was not in accordance of the provisions of the Code. Further, desired to take amount admitted as per decree

Before NCLT, counsel of FC agreed not to proceed to with execution of the decree during the moratorium period and application was disposed of.

NCLT also did not find any illegality in the appointment of RP

Litigation against RP - 2

Payment Related

PDCs issued by CD as security interest were being encashed by a beneficiary. It is well settled now that recovery or enforcement of any security interest is prohibited during moratorium period.

Sec 17(1)(d) read with Sec 23 of IBC require FI/banks maintaining account of CD to act on the instructions of RP.

Beneficiary issued Sec 138 notice to suspended Board and 'RP'

NCLT directed that no coercive action to be taken against RP as RP is an Officer of the Court

Criminal proceedings can not be started against RP for discharging his duties (No proceeding can be initiated against RP other than as per provisions of Code)

Alchemist Order, Shah Bros NCLAT & SC Orders - SC decision awaited

NCLT held that Beneficiary not to proceed in view of SC stay

Extract from SC order dated October 4, 2018

Para 88

The Resolution Professional, after looking at this affidavit, correctly noted that statements of such a nature would not have been made by a truly independent trustee of a discretionary trust, which demonstrates that the trustee was under the complete control of promoters, This in turn indicates that Prisma Trust is one more smokescreen in the chain of control, which would conceal the fact

IBC Amendment Act, 2019

- NCLAT Order which modified the distribution of amounts and all creditors were treated at par, increased admitted amounts of OCs, creditors to continue proceedings after conclusion of CIRP, guarantees stood discharged
- Appeals filed in SC challenging various aspects of NCLAT order
- While appeals were pending before SC, IBC Amendment was passed in a short time.

Landmark Supreme Court Judgments

- 1 - ArcelorMittal (Oct 2018): Interpretation of Sec 29 A – Role of RP and CoC

 - 2 - K Sashidhar v. IOB – AA have limited scope to suggest or recommend but can't make judicial review of CoC's commercial decision
 - AA were to only review 'fairness and equitability' of a resolution plan

 - 3 - Swiss Ribbon v. Union of India – ruled FCs have higher pecking order and claims of OCs to yield to those of FCs, RP only a facilitator

 - 4 - Binani Cement – Plan by CoC providing for payment of dues of OCs, CoC received much needed credibility

 - 5 - Pioneer Urban Land and Infrastructure Limited vs. Union of India – Economic legislation
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Supreme Court Judgment November 15, 2019

Landmark ruling by the Supreme Court paved the way for ArcelorMittal to finally acquire debt-laden Essar Steel after almost 2 years of an intense legal tussle.

The ruling brought finality on the insolvency resolution process and strengthens the IBC by defining roles and responsibilities of key stakeholders ie Resolution Professional, Resolution Applicant, Committee of Creditors (CoC), Adjudicating Authority (AA).

Disregard of security would have made secured lending unattractive

Respite to bidders in respect of claims

This should aid in speedy resolution of other matters. Importantly, one can expect greater interest and engagement by foreign investors as the ruling brings much needed clarity.

Key Principles laid down by SC

-Commercial decision of CoC paramount (P 36,38,40), who has to determine 'feasibility & viability' of a plan factoring all aspects (P 40), including manner of distribution amongst creditors(P 89)- Rationale for only FCs handling affairs of CD as per BLRC

-AA has only 'limited judicial review' over CoC decision (P43), to ensure going concern, maximising value of CD, stakeholders' interest has been taken care of(P 46)

-Allocating Nil value to OCs basis liquidation value would amount to not balancing interest of all stakeholders (P 46)

-AA can send back plan to CoC only if CoC has not acted within defined parameters, but not on the basis merits of commercial decision (P 46)

Key Principles laid down by SC

- Secured & unsecured creditors need not be treated equally or paid pro rata ((P 54-57)
- Code itself differentiates within FCs and OCs.
- Plan may provide for extinguishment of subrogation right of guarantor (P 66)
- No new claims can be filed which have not been considered by RP (P 67)
- Corporate Debtor- Clean Slate (para 66,67)

Clarified that re-agitation of undecided claims cannot be permitted and a SRA can't suddenly be faced with "undecided" claims as this would amount to **hydra head popping** up which would throw into uncertainty on amount payable by SRA

Key Principles laid down by SC

- Sec 53 priority irrelevant for plan (P 80) but CoC may consider the same (P 92)
- Distribution of profit during CIRP will not go towards payment of debt of any creditor (P68)
- CoC has no fiduciary duty to any group of creditors (P 93) and consequently refused to interfere with the financial allocation by the CoC
- RP decision to admit disputed claims at a notional value (P 102) upheld
- Sub-committees of CoC

While the CoC can delegate its administrative powers or power of negotiation with the resolution applicants to a smaller committee, such acts, in the ultimate analysis, would be required to be approved and ratified by the CoC

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