SC's Stay on RBI's Circular

Why in news?

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- The Supreme Court has ordered a stay on the implementation of RBI's February 12 circular dealing with insolvency proceedings. Click here to know more on the issue.
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What is the case on?

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- The RBI's circular is part of a revised RBI framework for resolution of stressed assets in the economy.
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- It mandates insolvency proceedings under the new Insolvency and Bankruptcy Code (IBC) for a debt servicing default beyond 180 days.
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- It also asks banks to recognise loans as non-performing even if repayment was delayed by just one day.
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- Power firms have argued that the provision was unfair.
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- It's because their debt repayment capacity was directly linked to revenue from power distribution companies.
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- It is also depended on the availability of coal, a natural resource closely regulated by the State.
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- The Allahabad High Court thus earlier refused to grant relief to troubled power companies facing action from the RBI.
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- But the SC has now ordered that insolvency proceedings should not commence against the defaulting power companies.
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What is the SC's rationale?

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- The current insolvency resolution process has its own flaws, despite the benefits.
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- Lenders could realistically expect to recover less than a tenth of their dues if stressed assets are to be liquidated.
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- It's because the IBC overemphasises on speedy resolution than the recovery of maximum value from stressed assets.
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- Power companies thus argue that their assets could yield better returns if resolved completely outside the IBC's purview.
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- With SC's order, the distressed power companies and many other firms in shipping, sugar and textile sectors would be relieved.
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- The decision is also helpful for the banks as they would have time for the recognition of bad loan losses.
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What are the concerns?

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- **Intervention** - The troubles of power companies can be traced to structural issues such as the -
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i. absence of meaningful price reforms
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ii. unreliable fuel supply
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iii. unsustainable finances of public sector power distribution companies
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- So banks are unlikely to make much money out of the stressed assets until these structural problems are addressed.
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- Certainly, policymakers, and not courts, would have to take charge and resolve these issues.
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- So the Court’s decision to intervene will do very little good in the long run to either stressed power companies or their lenders.
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- **IBC** - The decision will transfer all pleas seeking exception from RBI's circular to the court itself.
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- This has come as the biggest challenge against the Insolvency and Bankruptcy Code (IBC) yet.
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- Postponement of next hearing and the resultant delay undermines the new bankruptcy regime's feature of resolution within a strict time frame.
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- It is thus likely to cause significant uncertainty in the resolution of stressed assets.
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- It would also undermine investor confidence in the bankruptcy process.
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Source: The Hindu

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