

Financial Institution Insolvency in India, Creditors' Rights, and Securitization

October 31, 2019

Developments in the insolvency and restructuring space in India continue to attract attention, most recently, with the decision of the Bombay High Court on 10 October 2019 in a matter relating to Dewan Housing Finance Corporation (DHFC), which could have implications more broadly for India's securitization market.

DHFC's problems began earlier this year when it defaulted on payments due under bonds issued by it. Its problems were aggravated by the fact that India's new and much lauded insolvency law, the Insolvency and Bankruptcy Code 2016, does not apply to financial companies such as DHFC with the result that the only real route out for the likes of DHFC and their creditors is a consensual process.¹ A few months later, the DHFC saga took on a broader significance. On 10 October, the Bombay High Court, in an application by an investment manager for certain mutual funds that hold bonds DHFC has defaulted on, ordered that no payments were to be made by DHFC, including to investors holding units of securitized receivables, from its receivables, including such securitized receivables, in preference to the holders of bonds on which DHFC had defaulted.

If you have any questions concerning this memorandum, please reach out to your regular firm contact or the following authors

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¹ There are two provisos to that statement. First, theoretically, the creditors could try and implement a scheme of arrangement, although it's not clear there is a long enough runway to practically implement such a plan. Second, banks and certain financial institutions are required, by rules enforced by India's central bank, the Reserve Bank of India, to agree a resolution plan for defaulting debtors (such as DHFC) and sign up to an inter-creditor agreement (ICA) within a short time period following default or face additional provisioning. Under the ICA, decisions taken by lenders representing 75% by value and 60% by number bind all lenders, but asset managers and international funds are not required to sign the ICA and may take whatever action they consider appropriate to enforce their rights.

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Does this decision mean the true sale of receivables in securitization transactions in India isn't that true after all? Will investors in securitized receivables in India be exposed to the credit risk of the seller simply because it becomes the collection agent? Does it then, sound the death knell for India's securitization market? Many may say it does, but a little closer analysis suggests all is not lost – not yet, at least. We would be happy to discuss with you our take on the decision, the unique factual matrix in which it was made, and the broader political and economic context in India, all of which suggest that the decision may not be as severe as it seems. We continue to consider these questions across situations, given Indian law does not yet provide for a comprehensive regime to address the insolvency and restructuring of financial institutions.

Please feel free to reach out to Lisa Schweitzer, who has extensive experience advising clients on bankruptcy and insolvency matters across jurisdictions, and Nallini Puri, who has an in-depth understanding of the Indian market, if you would like further information on the issues raised by the DHFC decision, the Indian bankruptcy resolution framework, or on emerging markets more generally.

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