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INSOLVENCY

Employees can do what defaulting promoters can't — bid for their bankrupt firm. But owning a business is different from working for it.

The rising number of attempts by employee groups and unions raises hope of a new segment of bidders emerging from insolvency resolutions. While global examples are encouraging, concerns over business acumen linger.



Muskan Khan • 4 Feb 2019

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Courtesy of NCLT

Recently, the Supreme Court upheld the provisions of Section 29(A) of the Insolvency and Bankruptcy Code (IBC), which bars defaulting promoters from bidding for their troubled companies. However, there is no law that can stop employees, another set of stakeholders with detailed knowledge of the company, to take over. In its first two years, the insolvency regime has seen employees – either as a union, trust, or in collaboration with institutional investors – making attempts to take control of the company. ET Prime digs deeper to find out how these bids could give insolvency resolution a new dimension. Employees stand behind bankrupt firms. Insolvency proceedings of Reid and Taylor India (RTIL) is the latest case in point. Employees have showed interest in running the bankrupt suit maker. The employees' union came up with an “interested” bidder, CFM Asset Restructuring Company, after Hong Kong-based SPGP failed to deposit the earnest money at the last moment. However, CFM on Thursday backed out at the National Company Law Tribunal (NCLT), Mumbai, saying it was no longer interested in submitting a resolution plan for the company's revival. Indian Gas (IGL), a Delhi-based company, has now been asked to bid for the resolution process. The last-moment entry of CFM to back the employees' association of RTIL and the extra time given for the

Finquest, a major creditor to Reid & Taylor with an exposure of ₹2 crore, did not agree with the committee of creditors' decision to consider the union's move. During a hearing on January 29, it argued that the bid had come after the stipulated period of 270 days, and another resolution plan was just a way to divert attention. NCLAT, however, was of the view that there were chances of bringing the company back to life in the time granted for the resolution plan. It further clarified that the primary motive of the insolvency law is revival and not liquidation. NCLT, Mumbai has now allowed the entry of IGL as the new bidder and asked it to pay a non-refundable ₹2 crore on February 5. IGL is yet to appear before NCLAT to explain its bona fide and interest in the resolution process. Kumar Kartikay, advocate and the representative of employees' association of RTIL, dismisses the notion that employees are not capable of managing the affairs of a company. "The employees know the company better than the owners of the company. They work 24x7 and if the owners have failed to manage the company, why not give us (employees) a chance? Let us try." The bidder will infuse the capital and the association will bring in the relevant expertise, he adds. A senior executive, who has spent over 16 years with RTIL, feels indebted to the company. "It's our responsibility (not to let it die). We (executives) will anyways find another job, but 1000-plus workers will be on the streets. So, we should definitely think about it as an organisation and must try to protect it". Funding is problem, but he is banking on the brand. "Our brand is still No. 2 in the market. If that was not the case, then we could definitely have gone for liquidation". Roofit Industries is another case in point where workers wanted to bid for the bankrupt company. Its union, the Gummidipoondi Roofit Employees' Welfare Association, went to NCLT for approval, which rejected the proposal due to partial bidding of assets of the bankrupt company. "Same employee association is now trying to buy the same unit in liquidation," says Jitender Kumar Jain, an advocate and the resolution professional (RP) at Roofit Industries. He is, however, not allowed to share the complete details until the issues get finalised. Similarly, the employees' unions of Delhi-based Clutch Auto submitted a resolution plan for the company. But they did not pass muster as a group, as the proposal couldn't meet the minimum net-

of Alok Industries, one of the big 12 insolvency cases, the Alok Employees Benefit and Welfare Trust has written to lenders, including Dena Bank, Central Bank of India, IDBI Bank, Union Bank of India, and LIC of India, who voted against a resolution plan submitted by the Reliance Industries–JM Finance ARC combine. Similarly, in the matters of Jyoti Structures, which is among the Big 12, a group of 800 employees had moved the NCLAT to put the plan to liquidate the company on hold. They wanted the proposal by investor Sharad Sanghi reconsidered. Global examples India can learn from Employees of distressed companies can draw inspiration from global success stories. Weirton Steel in the US is one of the major successful employees' buyout (EBO) in 1984 supported by the Independent Steel Workers Union. USD200 million was raised to purchase the company after a labour-cost reduction of 30%, including a 20% wage cut for 8,500 employees. In 1994, the employees of Good Stuff Food Company, Los Angeles, teamed up with American Capital Strategies (ACS) and purchased their company out of bankruptcy. ACS is an investment banking firm that specialises in helping unionised workers buy their companies. Tower Colliery buyout in Wales, the UK, was another successful EBO, where its workers were granted the status of preferred bidder and the buyout was eventually approved. Between the 1970s and 1980s, the Marcora Law in Italy had set up a legal framework, which included banks and technical-support organisations, to help workers purchase insolvent companies. A similar initiative, Sociedades Laborales, took place in Spain in the 1980s. Are employees capable of running a company? The house is divided There are no such success stories in India. But employees are trying to have their say and are slowly getting there, according to senior officials involved in insolvency proceedings. They say the attempts of the employees are an encouraging sign. "Employees taking over distressed companies is good for the regime. If one or two of these attempts succeed, more will come," says an official. He drew a parallel with the Janata Party regime of 1977–1980. People identified with the regime so much that they thought of it as their own and punched above their weight to make it work. "As an employee, if I am finding value in the company when everyone else has washed their hands off, then I will work doubly hard to make it work," says an

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very important stakeholders in a company. Ideally section 29(OK brought in to keep the errant promoters out, should not hit the plans from the employee. In any case, after checking its applicability, unions and employees should be allowed and encouraged to submit a [resolution] plan,” says Sanjeev Ahuja, founding director of Ensemble Resolution Professionals. Lack of access to financial information and management skills could be a handicap. According to Shalu Khanna, partner at Luthra & Luthra Restructuring and Insolvency Advisors, these employees’ unions have no say in the resolution process, as they are not included in the committee of financial creditors. They also don’t have access to financial information of the company. “Though these unions are important for the company, they don’t have the necessary financial, operational, and managerial expertise to handle the affairs of the company, as this is a difficult job even for a full-fledged team of professionals,” Khanna says. “However, this has to be analysed case by case and there could always be exceptions.” Jain of Roofit highlights another problem. “Who is funding them?” he asks, adding, “Banks do not fund such acquisitions. Bankers and regulations have nothing to favour them (employees). There is no law to favour them, nor is there a perception to favour them, and nor do they have the capabilities.” Even if the employees overcome the funding problem and get an institution to back them like in the case of Reid & Taylor, concerns about their capability to manage the affairs of the company remain. “Employee-driven entities lack the experience of the process of insolvency resolution and trust of lenders, who are ultimately to approve the resolution plan,” explains Karan Gandhi of Transactions and Insolvency Resolution. “Creditors in insolvency are keen on the offers where maximum upfront payment is being made by the resolution applicant.” This practice, he feels, is against employee-driven resolution plans, which are generally interested in running the company, and repayment to the creditors is back-ended. “Not all employees are from lower levels. This chunk also includes many white-collar people,” counters Kartikay, the lawyer of the Reid & Taylor employees’ association, suggesting the union has enough bandwidth of about 100 people to turnaround the struggling suit maker. The bottom line: an opportunity fraught with risks There are also concerns around the

sponsoring such employees' associations just to protect their s OK

association is capable of running a business, he says. Such concerns underline the need for having a robust due-diligence process. Recent regulations by the Insolvency and Bankruptcy Board of India have brought in the requirement for "performance security" for winning bidders after the Amtek case, where the winning bidder failed to honour its obligation. The onus is also on the resolution professional and the committee of creditors to ensure that bids are genuine. Ahuja of Ensemble Resolution Professionals says such bids should be supported through some benefits or incentives. "Initially nobody had an idea that this (employees bidding for the troubled company) could be an option. The intent is right, and they do struggle a bit, but they should be a strong contender. All this will evolve over a period for sure," he adds. Khanna of Luthra & Luthra suggests it would be better for the employees to come in at the liquidation stage rather than at the resolution stage. "In such a situation, when there is no resolution applicant [with all the resources available] coming forward with the resolution plan for survival of the company, the job at hand for such [employee] union may be very difficult. In our view, in case the employees' unions are confident of their plan to revive the company, a better course would be to make a buyout offer in the liquidation process for taking over the asset". The buyout attempts by employees and the judicial process thereafter would be educative and help pave the way for future deals, feel lawyers. "This would be a phenomenon, which will be looked at more as we move forward," concludes Ahuja. (With inputs from N Sundaresha Subramanian) (Graphic by Abdul Shafiq)

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