

Stressed Assets of Road & Highways Sector and its Resolution— Industry Perspective



Insolvency and Bankruptcy Code (IBC)-2016 is a game changer but, however, there are other ways also for solution to the problem of stressed assets across all the sectors. Although many companies of Steel sector have been referred to NCLT and are undergoing insolvency proceedings, however, the resolution of stressed assets in sectors such as Roads and Highways cannot be solely done through the IBC process alone because not all cases in the Roads and Highways sector have asset value. The finance professionals, particularly Chartered Accountants, who are well-acquainted with this situation in Road and Highways sector, are best fit to advise and effect positive resolution both through IBC-2016 or otherwise. Read on to know more...

Industries where the underlying assets do not hold much value will not find much resolution either through the IBC or outside the Code. The IBC may work well for commodity-based industries, but may not render swift and desired results for those industries where there is substantial

involvement of promoters, their experience, their pre-qualification, Public Private Partnership (PPP) or Engineering, Procurement and Construction (EPC) projects.

Particularly with respect to PPP or EPC Projects, the underlying assets and strengths of EPC Contractors in terms of pre-qualification criterion on which the projects are allotted to them goes into drain, the moment insolvency proceedings are initiated against them. Further the clients, which had trust in the capabilities of the Company till now, start invoking their Performance Bank Guarantees. It immediately instigates bankers to raise the alarm bells, who not only start adjusting



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their margin money and existing securities against invoked Bank Guarantees but also stop further financing to all the group companies under the same management. That way, it brings cascading impact on the company, group companies under the same management and to a larger extent on the entire sector.

Model Concessionaire Agreements in PPP Projects or EPC contracts in Highways Sector provide for clauses which enable their clients to terminate project agreements upon commencement of insolvency proceedings. It creates uneasiness among key personnel and they often decide not to continue their engagement with these companies. Large-scale exodus of key personnel severely impacts the execution of on-going projects, which in turn result in termination of contracts by NHAI.

Insolvency and Bankruptcy Code provides procedure when the Concessionaire or Contractor becomes insolvent. NHAI has taken many steps to bring the concessionaire out from financial stress: Few of them are as under:

1. Hybrid Annuity Project

Due to limitation of finance and increasing incidence of financial stress in case of BOT (Toll) projects and liquidity problem in BOT (Annuity) projects since the banks/financial institutions were not coming forward for big exposure, Ministry of Roads Transport and Highways, came out with a new model i.e. Hybrid Annuity Model in which grant up to 40% of the Bid Project Cost is contributed by NHAI. It has resolved the problem of time overrun which was hitherto happening in BOT (Annuity) projects due to non-availability of finance. Further it has also resolved the problem of financial stress which is present in BOT (Toll) projects due to non-happening of expected growth in traffic or due to availability of competitive Roads and Highways and thereby affecting the revenue.

2. Substitution

The Lenders' Representative, on behalf of Senior Lenders, may exercise the right to substitute the Concessionaire pursuant to the agreement for substitution of the Concessionaire (the "**Substitution Agreement**") to be entered into amongst the Concessionaire, the Authority and the Lenders' Representative, on behalf of Senior Lenders, substantially in the form set forth for this purpose..

Upon substitution of the Concessionaire under and in accordance with the Substitution Agreement, the Nominated Company substituting the Concessionaire is deemed to be the Concessionaire under the Agreement and enjoys all rights and is responsible for all obligations of the Concessionaire under the Agreement as if it were the Concessionaire; provided that where the Concessionaire is in breach of the Agreement on the date of such substitution, the Authority shall by notice grant a Cure Period of 120 (one hundred and twenty) days to the Concessionaire for curing such breach.

3. Harmonious Substitution

Where NHAI or Senior Lenders have reasons to apprehend, in their considerate opinion that the concessionaire is likely to face financial distress and is likely to default in the compliance of the terms of the Concession, then instead of substitution, which can happen only when actual default occurs, can go for harmonious substitution. This method is a treatment on the occurrence of symptom, much before appearance of complete disease or stress onto the project. Even the Concessionaire can make a representation to the Lenders Representative, with a copy to NHAI.

In this method, selection of the Substitute and the valuation of the equity of the Concessionaire would be determined not only by Lender(s) but by both Concessionaire and Lenders and hence chances of litigation/dispute gets reduced to minimum.

4. Securitization

With a view to ameliorate the shortage of equity and improve liquidity of the prospective bidders/under construction project bidder, NHAI has decided to grant permission to the Concessionaire of existing and operational BOT Projects which have revenue significantly higher than to repayment obligations, to raise subordinate loan on the strength of future surplus cash flows of operational BOT Roads and Highways projects up to the 30% of the Total Project Cost. However, repayment of such subordinate loan shall be the last priority.

5. Premium Deferment

BOT projects, which have been allotted on premium/negative grant, are being allowed to defer the payment of premium if there is a subsistence

revenue shortfall so as to maintain the liquidity in the project. However, the same is on payment of Interest basis.

6. 100 % Equity Disinvestment

100% equity disinvestment is allowed by the concessionaire which have been allotted project after following due financial/tendering procedure by the NHAI once the project is completed and 2 years have elapsed. However during construction of the project and up to 2 years after the project is complete, selected bidder/ Consortium Members, together with its/their Associates, should not allow to decrease its/their share in the total Equity to decline below 51%.

7. Refinancing/Restructuring of Loan

100% refinancing/restructuring of loan is being allowed by NHAI if the future liability of NHAI on termination of the project does not increase.

8. NOC for Additional Loan

NHAI is liberal in providing No Objection for availing additional loan by the Concessionaire with the only condition that the debt servicing and repayment of such loan shall be the last priority in waterfall mechanism.

9. Release of 75% of the Arbitral Awards to Concessionaire

To provide liquidity, NHAI is releasing 75% amount of the Arbitral Awards, even when an appeal is filed before High Court on furnishing of Bank Guarantee.

If Insolvency has become inevitable

The steps narrated above were taken to bring the Concessionaire out of financial distress. But in spite of the efforts, if it becomes inevitable for the Concessionaire to become insolvent, Model Concessionaire Agreement provides mechanism of termination of Contract. Brief summary of the procedure for termination of the Concession Agreement and there upon payment of terminal dues by NHAI is as under:

Clause of the Model Concession Agreement dealing with termination provides that in the event that any of the defaults specified below have occurred, and the Concessionaire fails to cure the default within the Cure Period as specified in the agreement, the Concessionaire shall be deemed to be in default of

this Agreement. The defaults referred to herein, *inter alia*, shall include the following:

- upon occurrence of a Financial Default, the Lenders' Representative has, by notice required the Authority to undertake Suspension or Termination, as the case may be, in accordance with the Substitution Agreement and the Concessionaire fails to cure the default within the Cure Period specified hereinabove;
- the Concessionaire is adjudged bankrupt or insolvent, or if a trustee or receiver is appointed for the Concessionaire or for the whole or material part of its assets that has a material bearing on the Project;
- the Concessionaire has been, or is in the process of being liquidated, dissolved, wound-up, amalgamated or reconstituted in a manner that would cause, in the reasonable opinion of the Authority, a Material Adverse Effect;

Termination Payment by NHAI in case insolvency has become inevitable:

Model Concession Agreement provides the method of calculation of termination payment by NHAI, which is as under:

Event of termination	Termination payment	
Authority event of default	Debt Due + 150 % of Adjusted Equity	
Concessionaire event of default	90% of Debt Due	
Force Majeure Event	If termination is on account of Non-Political Event	90% of the debt due
	If termination is on account of Indirect Political Event	Debt Due+110% Adjusted Equity
	If termination is on account of Political Event	Debt Due + 150 % of Adjusted Equity

However, the proceeds of Termination payment as calculated on above basis; shall have to be made in accordance with the IBC code and Regulations effective in this regard. ■