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MANAGING BANKRUPTCY

It's time India introduces an efficient mechanism to deal with personal bankruptcy cases, which will only abound as the EMI culture spreads.

MANU KAUSHIK

THE WORST THING about losing a job—and more so during a downturn—is getting a handle on the EMIs. No working mechanism to deal with personal insolvencies and bankruptcies exists even though EMIs have replaced MRPs for most big consumables. In fact, the big question of dealing with EMIs is just hanging above the heads of each of the steadily growing army of fired men and women. They are at a complete loss on how to get banks to keep their loans alive and restructure the repayment schedules. Banks, on the other hand, have no sure means of segregating the non-willful from willful defaulters. The net result: growing bad loans for banks and hassles—and needless shame—for the hapless pink-slipped.

Take the example of Ranjeet Chawla (name changed), till recently a Senior VP with a Delhi-based real estate company. After doing his MBA in 1995, he joined as an assistant sales manager. Ambitious and hardworking, Chawla rose through the ranks quickly. His compensation, too, grew manifold—his last salary was Rs 60 lakh per annum.

In 2005, Chawla bought a house. The value of the flat was Rs 85 lakh; so he decided to take a loan of Rs 70 lakh and paid



DEALING WITH BANKRUPTCY

Personal bankruptcy procedures need a major overhaul in India.

- Mechanisms for early detection of personal bankruptcy are imperative
- Special bankruptcy courts with trained judges required
- Need to expedite resolution of insolvency proceedings
- Stipulate guidelines to segregate willful default from non-willful default on loans
- Moratoriums on EMIs should be granted through pre-specified or negotiable clauses

the rest from his pocket. Soon after, he got a luxury sedan financed, which increased his liabilities by another Rs 7 lakh.

Then Chawla's troubles began. In December 2008, his company, like most real estate companies, began retrenching and handed him the pink slip. Today, clearing the debt against his name is a daunting prospect for Chawla. After paying up EMIs to the tune of Rs 28 lakh and Rs 4 lakh on home loan and car loan respectively, his total debt outstanding is around Rs 45 lakh. "One option for me is to request the bank for a 6-7 month moratorium on the EMI payments. If the bank wants, they can charge me a higher rate of interest during this period," he says adding that there have been instances in other countries where banks have used such practices based on the good credit history of their customers. "None of that has come to India as yet, though we have imported the mortgage culture," he adds.

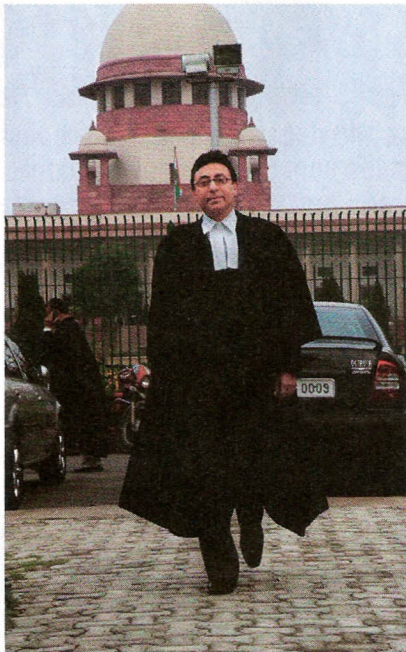
In India, people like Chawla miss out on another option: filing for a personal bankruptcy. The objective of the exercise is to give individuals a "fresh financial start" by discharging many of their debts—this is done by liquidating assets of debtors and giving it to the creditors who are first in line for repayment. Any debts that remain are cancelled.

Of course, while bankruptcy can relieve you of debts, there's a price to pay. Once you file a bankruptcy, you can't borrow money from the banks in future to start your own business as you have already been blacklisted.

In the West, it's commonplace for individuals to invoke the personal bankruptcy provisions. Indeed, in the US, recessionary conditions have led to a surge in bankruptcy filings in 2008. The American Bankruptcy Institute said overall consumer filings rose to 1.06 million in 2008, compared with 8,01,840 during 2007. It's a relatively unheard and misunderstood concept in India, though. Blame it on social conditioning and effete laws. Says Sumant Batra, Managing Partner, Kesar Dass B. & Associates: "In India, bankruptcy has a social stigma attached to it. If you take a look at the West, you'll find that bankruptcy filings are common there." Simply put, invoking a personal insolvency in a court helps a person to settle all his/her dues against creditors amicably.

Ineffective laws, too, are a major hindrance. In India, generally, the personal insolvencies are typically resolved out of court by the traditional methods such as restructuring of loan or waiving the interest due or settling for partial repayment. This is largely due to the complexity of the legal framework.

It's not like there aren't any bankruptcy laws. There are two Acts—Provisional Insolvency Act, 1920 and Presidency Towns Insolvency Act, 1908—that specifically deal with personal bankruptcy. However, these laws were enacted at a time when the



SHEKHAR GHOSH

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Sumant Batra/ Managing Partner, Kesar Dass B. & Associates

personal credit markets were not evolved. "Today, the country is experiencing a massive growth of retail loans, housing loans and credit card



RACHIT GOSWAMI

"The country is experiencing massive growth of retail, housing loans and credit card users. More effective procedures and laws are required."

Harsh Roongta/ CEO, Apnaloan.com

users. More effective procedures and laws are required," says Harsh Roongta, CEO, Apnaloan.com.

So, what needs to be done? To begin with, experts say, the government should take the lead in setting up special bankruptcy courts with judges trained specifically to deal with issues related to personal bankruptcy. Then, there is the need to dispose of cases quickly. "It's both tedious and time-consuming procedure. Typically, it takes 4-5 years before everything comes to an end," says Roongta.

Another important step forward would be the introduction of clear cut guidelines and procedures to distinguish between willful and non-willful defaulters. So far, the use of personal bankruptcy law has

been made for all the wrong reasons. Instead of being used in the bona fide circumstances such as job loss or critical illness in the family, most of the personal insolvency cases are filed by high-profile individuals who can pay, but misuse the law to wriggle out of their commitments. Says Batra: "Right now, a court appointed receiver takes the call on the merits of the case. Since professionals are not involved, it often leaves scope for the misuse of the provisions of the law by unscrupulous elements. This has to change."

The existing laws also need to be modified. "With the EMI culture spreading, defaults will only rise in future, particularly in a slowing economy. It's not a crime if you fail to pay your EMIs; you just need an insolvency mechanism so that they benefit both the creditor and the debtor," says Batra. It's about time an inability to pay EMIs, arising out of a job loss, is handled with as little fuss as is the eligibility to pay, prior to the sanction of loans. ■