

INFRASTRUCTURE LEASING & FINANCIAL SERVICES

Learn IL&FS Lessons?



Sugata Ghosh

The pipe-smoking Ravi Parthasarathy, who ran Infrastructure Leasing & Financial Services (IL&FS) as his fiefdom, was never an easy man to like. He subjugated managers, fooled generations of lenders, bullied journalists and made directors dance to his tune.

Even if the central agencies fail to prove he was ever bribed, B-school curriculum will probably add a chapter on how a sharp, abrasive man could spin a maze of over 300 companies to borrow from banks, mutual funds and pension pools — which had no reason to lend — to ensure a fat salary and lavish lifestyle for himself and his army of meek, loyal managers. It's a story about how an executive head enjoyed unbridled powers, cultivated the men who matter, and dealt with politicians across parties, while shareholders behaved like absentee landlords.

A year after his house of cards collapsed, Parthasarathy is battling cancer, while the IL&FS story is caught between a new board struggling to sell assets and multiple court cases, which unfold as enforcement sleuths pick up the debris. The questions now are: how long will the new board take to pay off investors? Will they be able to? And, in the drive to fix the guilty, will recovery take a back seat?

The old unsolved riddles continue to hang over a scam that resembles Satyam, but is only more colourful and complex. The greatest mystery is why RBI never stopped IL&FS from borrowing even after knowing that the group's non-banking financial company (NBFC) I-Fin was breaking all the rules. Was there a handful of very senior RBI officials who gave IL&FS a long rope? Even after 2013 when the consolidated balance-sheet was published, why did no one — particularly bankers who financed

IL&FS companies — raise eyebrows? Why did IL&FS shareholders having nominees on the board never pull up Parthasarathy?

There will be no answers to some of these questions, and the disgraced managers will be slowly forgotten, relegated as characters in a sordid corporate drama. But there are lessons that go beyond the headlines on arrests, investigation and money laundering. If we forget them, chances are there will be another IL&FS — a company that originated from a white paper on infrastructure development in the 1980s, bagged a World Bank loan backed by a sovereign guarantee, used its ownership structure to position itself as a top-rated quasi-government entity that was simply 'too big to fail', and then succumbed to greed and ambition.

What's there for GoI, stakeholders and regulators in the IL&FS fiasco? One of the most prosaic messages is the absence of a bankable model for infrastructure in India. If we don't have long-term funds to finance long-gestation projects like roads, ports and airports, and as long as infrastructure companies borrow and continuously roll over cheaper short-term borrowings to built large projects, it will remain a touch-and-go for them.

IL&FS modus operandi was simple: aggressively bag new projects, borrow to fund them, divert the money to repay lenders to earlier projects. The music stopped when State-owned shareholders refused to chip in with

more equity to bridge the gaps. IL&FS may have been a full-blown scam. But the truth is most infrastructure projects are languishing, thanks to their abysmal cash-flow and a non-existent market for long-term debts.

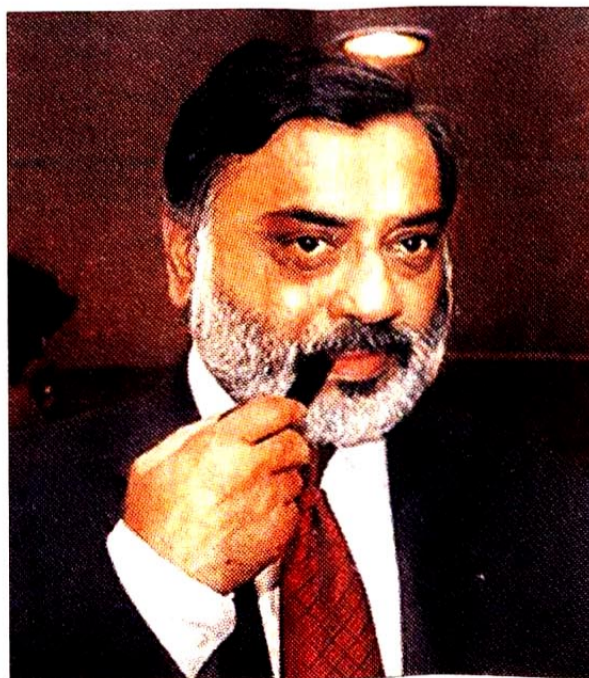
Scores of infrastructure companies are in dispute with the tax department, which has questioned whether these companies can apply a special rate of depreciation allowed by GoI. It's a make-or-break situation for these firms with GoI leaving the incentive for infra projects to the interpretation of the taxman.

The misuse of I-Fin by IL&FS should make RBI rethink whether business groups should own and control NBFCs. The temptation to divert the funds of the NBFC to group entities is irresistible. Recently, a top auditor, while announcing its resignation, hinted at such a fraud in a large company. Layering its transactions to keep auditors happy, I-Fin lent money to contractors who, in turn, lent to the group's infrastructure arm, IL&FS Transportation Networks Ltd (ITNL). These contractors, which acted as conduits, were assured that loans from I-Fin will not have to be repaid till ITNL pays them back.

Indeed, ITNL, with 22 road and 10 power projects, was the bane of IL&FS. The company, which was unable to revisit the equity market after its listing, went on a spree to bag projects and used the circuitous route to dip into I-Fin's funds. As long as it could, ITNL didn't default.

And I-Fin's independent directors were satisfied as long as it got back the money lent. They never asked why such loans were given at all in the first place. Their behaviour raises a bigger question: should management pick independent directors? Like credit-rating agencies and auditors, it's time for independent directors and regulators to explain.

Many ills underlie the IL&FS saga. Fixing these are as urgent as punishing the scamsters. Make no mistake. Infrastructure is an ageless, alluring story that involves big money, prestige and votes. If it isn't set right, some day another Ravi Parthasarathy will play around it.



Piped dreams: Parthasarathy

FILE PHOTO

sugata.ghosh@timesgroup.com