IJCRT.ORG ISSN : 2320-2882

INTERNATIONAL JOURNAL OF CREATIVE RESEARCH THOUGHTS (IJCRT)
An International Open Access, Peer-reviewed, Refereed Journal

EVOLUTION OF DEBT RECOVERY REGIMES AND THEIR EVALUATION IN ADDRESSING NPAs.

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Abstract: The wide spread of non-performing assets ("NPAs") in the Indian banking and finance sector can be due to many reasons. In the view of neo-classical economy, non-payment of loans are mostly due financial and economical difficulty of the company. It is believed that NPAs can be minimised by 'proper implementation of banking laws and enforcing punishments and strengthening the assessment of credit risk' through various mechanisms. To curb the menace of NPAs legislature has passed many laws. Though this paper, I will try to examine the role and effectiveness of these Debt recovery regimes/laws in tackling NPAs in India. in this paper, I will try to examine the Insolvency and Bankruptcy Code, 2016. I shall also try to examine the various legislation passed by Parliament and their performances in tackling NPAs in current regime. I shall also touch upon the issues relating to recovery and asset reconstruction under the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 ("SARFAESI Act") and also examine the current status of this Act. Further, I shall also evaluate the functioning of the Debt Recovery tribunals (DRT) under the Recovery of Debts Due to Banks and Financial Institutions Act, 1993 ("RDDBI Act") and examine how far they have been able to tackle the issues of NPAs.

INTRODUCTION:

This bond doth give thee here no jot of blood; The word expressly are "a pound of flesh."
The Merchant of Venice Act 4, scene 1, 304–307 "The pound of flesh which I demand of him is dearly bought; 'tis mine, and I will have it" Shylock, The Merchant of the Venice.

This quote is an argument made by Portia in the Merchant of Venice in order to save Antonia from the moneylender Shylock. This succinctly portrays the how insolvency was perceived in the Medieval age, one had to part with a pound of flesh as Antonio was bound by the bond where such promise was made to a Jewish moneylender Shylock who owed Antonio money.

The history of borrowings are probably as old as the history of human civilization. When the individual applies for credit, he enters some kind of agreement. If there are no repayments, the debtor breaks the contract that is considered fundamental in every economy. The treatment of people who have become insolvent can thus give us an indication of how those who failed or could not fulfil their borrowings contract has been considered from the point of view of the legislators. Already in Classical Antiquity, different systems were created to address the issues with insolvencies. Bondage, corporal punishment and debtors' prisons were used[1].

Insolvency laws in India have its origin in the English laws. There was a requirement for the legal frameworks to deal with insolvency initially in the all 3 Presidency towns of Madras, Bombay and Calcutta. There were different laws in existence before the enactment of the Insolvency and Bankruptcy Code 2016 like Presidency Towns Insolvency Act, 1909 and Provincial Insolvency Act, 1920, both Act dealt with insolvencies of firms and the individuals.

The banking industry is critical to the growth of any economy. The pace of economic development is determined by the bank's role. As a result, the banking sector's stability is critical to an economy's growth. Any bank's main duty is to lend money to diverse sectors such as agriculture, industry, personal and housing, and others in order to put the money to good use. Banks have become more cautious in providing advances in recent years for a variety of reasons NPAs.

Financial institutions have never been more determined to ensure timely resuscitation and subsequent decrease of nonperforming assets than they are now. It's important to remember that recovery management, whether for new loans or old debts, is critical to NPA management. This management approach must begin throughout the loan application process. Two ways are used to effectively control recovery and NPA. The first is concerned with stopping a default and forming an NPA, while the second is concerned with handling loan defaults. The principles of banking reform were revolutionary, instilling a sense of urgency in banking staff and sending them a message that it was either perform or die. The prudential rule has forced the banks to look into the asset value.

Strong banking sector is vital for healthy financial system. One in all of the leading important and key parts compete by banks are that of loaning businesses. It is commonly inspired due to it's the result of fund being transferred from the systems to creative function that conjointly outcome into monetary processes. As there are unit execs and cons of all, steady is with loan business that carry credit risks that arise from the letdown of receivers to please its written contract obligation either throughout the course of managing with or on prospect obligations. The breakdown of the banks could have connected in nursing unfavorable effect on various segments. Non playing asset area unit one in each of the key consideration for Indian banking companies. NPAs reflect the act of banking and finance companies.

EVOLUTION OF DEBT RECOVERY REGIMES:

The entries relating to winding up of corporation is under the Union List[2]. The Parliament enacted the Companies Act ,1956. The Companies Act,1956 Act governed all the aspect of the functioning of companies, including their winding up[3].

The High Courts constituted the adjudicating authority for winding up related matters under the same law. Creditors with unpaid dues above a defined threshold could petition the court for winding up a company. Winding up was preceded by liquidation, a process managed by an official Liquidator, appointed by the High Court[4].

Most of the corporate insolvencies were delt by the Companies Act, 1956. However, In 1980, an expert panel was set up to recommend legislative and administrative remedies to the issues of industrial sickness and their grievances. As the outcome of this, the Sick Industrial Companies Act (SICA) was enacted and passed in 1985 with the aim of identifying "sickness" in an industrial company and reviving/restructuring these companies. The Act was supported by the setting up of the new legal forum, the Board of Industrial and Financial Reconstruction[5].

The RBI has instituted a slew of "Restructuring schemes" in order to 'revitalise stress assets in the economy'. These schemes span from the SICA era to RDDBFI and SARFAESI to finally IBC, 2016. The Corporate Debt Restructuring (issued vide RBI Notification[6] in 2001) to ensure the timely and transparent mechanisms for restructuring of the corporate debt of viable corporate entities affected by internal or external factors, outside the purview of BIFR, DRT and other legal proceeding. CDR will apply only to multiple banking account/consortium accounts with outstanding exposure of Rs. Twenty crores and above

[1] Karl Gratzer and Dieter Stiefel (eds.),History of Insolvency and Bankruptcy from an International Perspective
[2] Schedule VII to the Indian Constitution
[3] Part VII of the Act, covering Sections 425–56o, Companies Act, 1956
[4] Rajeswari Sengupta, Anjali Sharma, Susan Thomas (2o16), "Evolution of the insolvency framework for non- financial firms in India"
[5] Ibid.
[6] RBI Notification vide: BP.BC. 15 /21.o4.114/2ooo-o1

with the banks and financial institutions. Similarly, the Flexible financing scheme or the 5:25 Scheme, for infrastructure projects allowed banks to extend long term loans of 20-25 years to match the cash flow of the infra. projects, while offering refinance every five years. The SDR Schemes was introduced by RBI vide Notification[7] in 2015, under this scheme, banks who have given loans to a corporate borrowers get the right to convert the full or part of their loans into equity shares in the loan taken companies, thus help banks recover their loans by taking control of the distressed listed companies/entities.
The Reserve Bank of India guideline titled 'Framework for Revitalizing Distressed Economy' (2014) provided for the Joint Lender's Forum (JLF). It is a dedicated grouping of lender banks that is formed to speed up decisions when an asset (loan) of more Rs 100 crore or more turns out to be a stressed-assets. Subsequently, in 2015 the Strategic Debt Restructuring (SDR) was introduced in order to facilitate banks to recover their loans by taking control of the distressed listed entities.

The Recovery of Debt Due to Banks and Financial Institutions, 1993 (RDDBFI Act)[8] was enacted on the recommendations of Narsimham Committee. Debt Recovery Tribunals were set up for speedy adjudication of matters pertaining to the recovery of dues. Subsequently, SARFAESI Act, 2002 was brought in with the intention to expedite the recovery of debts that becomes due or defaults made on the debts respectively. These legislations provide recovery mechanism by setting up a Debt Recovery Tribunal. SARFAESI marks the departure from RDB Act by allowing "Secured Creditors" the right to take over possession of the assets of the "Borrower" without any judicial intervention under section 13(4). It is pertinent to note that these legislations acknowledge the rights of only Banks and Financial Institution or their consortiums. The RDB was highly DRT driven process delaying the recovery process due to very high litigation rate.
To overcome the limitations of the earlier insolvency resolution frameworks, the Banking Law Reforms Committee (BLRC) was constituted in October, 2014, under the chairmanship of Mr. T.K. Viswanathan. In November 2015, the BLRC gave its report with its recommending, asking for making transformational changes to be made in the law relating to insolvency and bankruptcy (BLRC Report). The BLRC Report recommended a complete institutional overhaul, inter alia, proposing the constitution of the regulator (which eventually became the Insolvency and Bankruptcy Board of India), information utilities, insolvency professional agencies and insolvency professionals. Most importantly, taking into account the need of the times as well as the statutory framework in place in other developed countries, the BLRC proposed that we should shift from a "debtor-in- possession" to the "creditor-in-control" model.
In a remarkable departure from the previous two legislations IBC, 2016 does not merely aim for recovery but also "resolution and rehabilitation" to ensure that the Corporate Debtor remains going concern.

CONTRIBUTION OF INSOLVENCY AND BANKRUPTCY CODE, 2016 TO BUSINESS RESCUE:

The IBC, 2016 has been successful in addressing the issues of NPAs, to some extent. However, IBC, 2016 is at nascent stage and it requires to strengthen the organizational strengthening and creating checks and balances at the different layers of stakeholders. The IBC, 2016 has been successful in bringing all the laws and acts related to insolvencies and bankruptcy under one roof, and that was the whole purpose of the Code. It is also pertinent to mention that other previous legislations too tried to address the issue of NPAs and other aspects of NPAs. However, these enactments had become redundant with times, and moreover, due to multiplicity of laws, it created confusion and took more than required time to settle the issue of NPAs, judiciary. The IBC has been successful in bringing all the laws related to NPAs together and settle matters expeditiously.
IBC is at nascent stage and it can't be compared to previous debt recovery regimes. However, IBC is being tauted as the one of the biggest economic reforms in last decade. It has helped in early exit and easy exit of companies and at the same time, it has also been successful in bringing FDIs and investments in the country. It shall be too early to give verdict, whether IBC has been successful in addressing the issues of NPAs and recovery of debts, but it is in right direction.
The average rate of recovery under the erstwhile regime of SICA, CDR, SDR etc. was around 15%, in fact the SARFAESI Act, 2002 also couldn't deal with the issues of mounting NPA and subsequent defaults. The ARC mechanism of securitisation has not been able to take-off to the extent it was intended. The IBC in 2016 provided a consolidated framework to deal with insolvencies with the preamble of the

[7] Review of Prudential Guidelines - Revitalising Stressed Assets in the Economy RBI/2o15-16/33o
[8] High Level Committee on the Financial System (Narasimham Committee I, 1991)

code stating the intention to rescue and rehabilitate the business rather than mere recovery. The code had provided a single pipeline to investor and resolution applicant alike to bid for the company and get a resolution plan approved. The role of the IBC could be defined with the following numbers,
Recovery is incidental yet the recovery has been around 45% which earlier stood at 15% under the SARFAESI and the SDR/S4A regime. This is among the highest recovery in the options available. The Code has rescued 250 Corporate Debtors till June 2020 with a recovery of around Rs. 1.03 Lakh.
Thus, the IBC is tackling the "twin balance-sheet problem", developing a robust corporate bond market, improving the credit environment and, consequently, providing a fillip to India's competitiveness as the business destination, the new code was designed to introduce the Eight High Level Committee on the Financial System (Narasimham Committee I, 1991) streamlined, two-step corporate insolvency processes which, among other things, prevented "value destruction in corporate distress". The aim to protect the integrity of the process and ensure revival, promoters responsible for driving the enterprise into indebtedness in the first place are kept at arm's length. An important step in this direction has been taken with the insertion of the new Section 29A preceded by an ordinance, which view the promoter of a corporate debtor with suspicion, and bars such promoters from submitting the resolution plans. Apart from preventing promoters from assuming control by offering to pay off creditors, the National Company Law Tribunal should exercise caution to prevent the corporate debtor itself from subverting the IBC process by entering into out-of-court settlement, as this would amount to allowing the corporate debtor to illegally assume management powers that are vested in the Resolution Professional. One of the fundamental underlying principles of insolvency laws the world over is that, on initiation of the insolvency processes, the corporate debtors ceases to be the beneficial owner of its own asset and the promoter of management. It is seen that about 53% of the CIRPs9[9], which were closed, yielded orders for liquidation, as compared to 134% ending up with a resolution plan. The contribution of IBC can also be seen in the fact that around 70% of these cases which ended in liquidation were earlier in BIFR or defunct companies. The economic value of most of them were already eroded yet the CIRP to gain value out of it thereby helping the economy grow as well as rescue viable businesses.

ROLE OF IBC, 2016 IN TACKLING NPAs:

The "Three Arms "of the State has to function in tandem in order to make successful any piece of legislation. The IBC being an economic legislation requires even more cohesion and synchronization as a lot of experimentation is required and the Executive requires enough elbow room as the Supreme Court in Swiss Ribbons had observed "Judicial hands-off qua economic legislation". Let us briefly examine the recent past of NPA and consequent insolvency. The post-2007 phase saw a spike in the gross non-performing assets owing to reckless lending and push by government to lend in order to stimulate growth. While it is nobody's case that such stimulus should not have been injected, however, it is now widely agreed that the stimulus was over-stretched marked by banker making errors in judgment both due to optimism as well as design. The murky business was finally unearthed by the Asset Quality Review by the RBI in 2015-16, which ascertained the NPA level had risen to a whopping 11 percent, some 1o Lakh crore in quantum.
The Economic Survey 2016-17 succinctly expounded on the NPA or 'twin-balance-sheet' issue and the *Chakravyuha challenge*[10] as one of the prime factors for it. We will use these concepts in the following paragraphs. The above graph signifies how the NPAs have risen over the years especially post 2014 which is attributed to the AQR. The remedy of the situation is provided by the Insolvency Code which has to be seen in light of both Horizontal and Vertical Cooperation.

[9] Quarterly Newsletter of IBBI, April-June 2020.
[10] The Chakravyuha Challenge of the Indian Economy, Economic Survey 2o16-17

CONCLUSION:

India's Fiscal federalism is the cornerstone of the Centre-State relations[11]. The relationship has been outlined in the Constitution under Chapter XI and the Fiscal Federalism is government by a Constitutional body the Finance Commission[12]. Fiscal federalism was strengthened significantly when the 14th Finance Commission increased the share of the states in the divisible pools of central taxes from 32 per cent to the 42 per cent. Although central grants to states Swiss Ribbons Case saw compensatory cuts, the shift empowers the state to manage their revenue and expenditures independently, thereby giving states more autonomy and elbow room to spend.

The efficiency of IBC is dependent on the functioning of the NCLTs, Now, it is imperative of the State governments to maintain the staffing and upkeep of these Tribunals. It is also seen that many of the NCLT infrastructure is supported by State Government employees, therefore a symbiotic relationship between the States and the Centre is a must.

The relationship between the State and the Judiciary is a pertinent one a balance has to be struck between the two as separation of power is a must while one also has to see that there is enough synchrony between these two organs of the State. The implementation of IBC is conditional on how effective and fast the courts are and are they adhering to the timelines given in the Code. Recovery is incidental yet the recovery has been around 45% which earlier stood at 15% under the SARFAESI and the SDR/S4A regime. This is among the highest recovery in the options available. The Code has rescued 250 Corporate Debtors till June 2020 with a recovery of around Rs. 1.03 Lakh.

[11] Articles 245-255 of the Indian Constitution
[12] Article 28o of the Indian Constitution