

Will Insolvency and Bankruptcy Code fix the Bank NPA issue?

The Insolvency and Bankruptcy Code (IBC) marks the first time the government and RBI are truly on the same page for effective resolution of NPAs

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The coming months will show us the early trends in actual resolutions under the Insolvency and Bankruptcy Code (IBC). Photo: Pradeep Gaur/Mint

Even as the Insolvency and Bankruptcy Code (IBC) was completing its first year of existence, the cat was set among the pigeons with the promulgation of an ordinance restricting the promoters' ability to bid for their stressed assets. Much has since been said, both for and against this. Arguments have ranged from the ordinance going against the preamble of the IBC, which stipulates the need to maximize value by making the assets available to the largest number of bidders, to suggesting that the ordinance was timely in preventing bids from those quarters which had failed to utilize the assets viably. Some also suggested a middle path of framing a differentiated set of rules for bidding for promoters and others. A critique of the code, anticipating the direction of its evolution from the present stage, is, therefore, called for.

“Capitalism without Bankruptcy is like Catholicism without Hell,” said Frank Borman, renowned astronaut and erstwhile chairman of a failed US airline. As such, the institutions established by the state should promote freedom to start a

business (entry), to run the business (level playing field) and to exit/discontinue the business. The reforms of the 1990s focused on freedom of entry (dismantling the licence-quota raj) and then, from the beginning of this century, the focus shifted to freedom of continuing business. The third leg, which is freedom to exit, has now been provided in the shape of the IBC, to provide a mechanism to stressed businesses to resolve insolvency in an orderly manner.

All past efforts in the direction of the third leg have fallen far short of expectations due to poor implementation and the legal loopholes available for defaulters. According to the World Bank, the average time taken for completion of the bankruptcy process is 4.3 years in India, whereas Singapore, Finland and the US take just 0.5-1.5 years. Also, the recovery percentage in India is as low as 26%, whereas this ranges from 78-92% in the developed world.

The IBC seeks strict time-bound initiation of corrective action even at the stage of the very first default either to the bank or to the business counter parties. By ensuring certainty and clarity in all aspects of the process, the code hopes to achieve speedy resolution, higher recoveries and, in course of time, encourage lenders to go in for higher levels of debt financing.

The IBC seeks to consolidate scattered and unstructured jurisprudence on insolvency prevalent in various Acts, like the Presidency Towns Insolvency Act, 1909, Sick Industrial Companies Act, 1985, Limited Liability Partnership Act, 2008, Companies Act, 2013, etc. A committee has been formed recently under the chairmanship of the secretary, Union ministry of corporate affairs, for a comprehensive review of the IBC, including cross-border insolvency, development and regulation of information utilities and instances of insolvencies in group companies. There is, anyway, bound to be a whirlwind of judicial pronouncements on various interpretational issues that should result in the development of robust IBC jurisprudence in the days to come.

On the positive side, we are witnessing that debtors are now reconciling with the 'creditor in control' scenario, with the committee of creditors (CoC) becoming all-powerful in the resolution process. It is, therefore, incumbent on this CoC to be fair to all stakeholders in the stressed company. After all, a company is an amalgam of stakeholders and its corporate governance norms are expected to maximize the value of its assets and balance the interests of all entities linked to the company. The IBC supports this by generally preferring resolution over liquidation.

The success of the IBC is dependent on the alacrity with which the government, courts, tribunals and Insolvency and Bankruptcy Board of India (IBBI) respond to early-stage issues arising in their domain, post implementation.

However, the role played by debtors and creditors during implementation will also be critical to its success. At the centre of it all is the insolvency professional (IP). Today, there are over 1,200 IPs certified by the IBBI, most with virtually no experience of being in the hot seat of a resolution professional. They are expected to take all steps to keep the company as a going concern and display utmost integrity, impartiality and independence in their day-to-day conduct. IPs need to possess the skills and acumen to balance commercial reality with the legal requirements to preserve the entitlements of all stakeholders.

It is the first time that the government and Reserve Bank of India are on the same page for effective resolution of the problem of bad debt and improving overall financial discipline in the way business is conducted in India. A number of features of the IBC and the pronouncements of various high courts and Supreme Court motivate us to look at this latest effort in a positive manner. The coming months will show us the early trends in actual resolutions under the code. Hopefully, it will prove to be a game changer in the interest of the Indian economy's health and long-term growth. As Nelson Mandela said, "I never lose; I either win or I learn." The jury is still out on the IBC even though the World Bank has acknowledged the effort. Let's hope all involved entities implement the lessons they learn along the way for cracking this debilitating problem of non-performing assets and financial indiscipline facing the country.