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**DAILY EDITORIAL
ANALYSIS**

TOPIC

**RECASTING INSOLVENCY
RESOLUTION**

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RECASTING INSOLVENCY RESOLUTION

Context

- The **Insolvency and Bankruptcy Code (IBC)**, introduced in 2016, was designed to **streamline India's insolvency processes**, aiming for timely resolutions and maximization of asset value.
 - ♦ However, as the law has matured, **certain issues have emerged** that demand attention, particularly regarding institutional capacity and procedural efficiency.

Historical Background of IBC, 2016

- IBC is the umbrella legislation for insolvency resolution of **all entities in India—both corporate and individuals**. It aims to overhaul the corporate distress resolution regime in India.
- **Need of IBC:**
 - ♦ Rise in India's Non-Performing Assets (NPAs) and debt defaults;
 - ♦ **To consolidate previously available laws** to create a time-bound mechanism with a **creditor-in-control model** as opposed to the **debtor-in-possession system**.
 - ♦ **Limited applicability and restrictions** of existing loan recovery mechanisms such as:
 - *Recovery of Debts Due to Banks and Financial Institutions Act (1993);*
 - *Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act (SARFAESI) 2002;*
 - *Lok Adalats;*
 - *Debt Recovery Tribunals (DRTs);*

Key Features of IBC 2016

- **Resolution of Insolvency:** IBC lays down **separate insolvency resolution procedures** for companies, individuals, and partnership firms.
 - ♦ It allows both creditors and debtors to initiate the insolvency resolution process.
 - ♦ **Time-Bound Resolution:** The resolution process **must be completed within 180 days**, which can be **extended by 90 days if necessary**.
- **Regulator of Insolvency:** The **Insolvency and Bankruptcy Board of India (IBBI)** oversees the insolvency proceedings and regulates entities registered with it.
 - ♦ The Board consists of representatives from the Ministry of Law and Justice, Ministry of Finance, and the Reserve Bank of India (RBI).
- **Adjudicating Authorities: National Company Law Tribunal (NCLT)** handles insolvency resolution for companies and limited liability partnerships.
 - ♦ **Debt Recovery Tribunal (DRT)** oversees insolvency resolution for individuals and partnership firms.
- **Two-Step Process for Corporate Insolvency:**
 - ♦ **First Step: Insolvency Resolution Process (IRP)**, where creditors assess the feasibility of continuing the debtor's business.
 - ♦ **Second Step: liquidation**, if revival attempts fail, where the debtor's assets are distributed among creditors.
- **Licensed Insolvency Professionals:** They manage the insolvency process and control the debtor's assets during the process.
 - ♦ They play a crucial role in drafting resolution plans and ensuring compliance with the Code.
- **Priority of Claims:** IBC establishes a clear hierarchy of claims, ensuring that secured creditors are paid first, followed by unsecured creditors and operational creditors.
- **Promoting Corporate Governance:** By providing a structured and transparent process for insolvency resolution, the IBC promotes corporate governance and accountability among corporate entities.

Key Challenges

- **Institutional Challenges:** The effective implementation of the IBC hinges on the performance of the **National Company Law Tribunal (NCLT)** and its **appellate body, the National Company Law Appellate Tribunal (NCLAT)**.
 - ♦ These tribunals face the **dual burden** of handling **corporate insolvencies** under the **IBC** and cases under the **Companies Act**.
 - ♦ It suffers from what might be termed 'temporal disjunction'.

Do You Know?

- **National Company Law Tribunal (NCLT)** was conceived in 1999 based on the **Eradi Committee's** recommendations and operationalized in 2016
- Its structure reflects the economic realities of a bygone era, leaving it ill-equipped to meet contemporary demands.

- **Procedural Delays:** The NCLT has become a bottleneck for insolvency resolutions and corporate transactions such as **mergers and amalgamations**.
 - ♦ With a sanctioned strength of 63 members, many of whom divide their time across multiple benches, the NCLT struggles to handle the caseload efficiently.
- **Delays in Resolution:** According to the **Insolvency and Bankruptcy Board of India (IBBI)**, the average time for insolvency resolutions increased to 716 days in FY2023-24, up from 654 days in FY2022-23, surpassing the stipulated **330-day timeframe**.
 - ♦ It often stretches much longer due to **litigation, inefficiencies, and lack of preparedness** among stakeholders.
 - ♦ Asset value often deteriorates during the prolonged resolution process, reducing creditor recoveries.
- **Declining Recovery Rates:** Recovery rates under the IBC have reportedly dropped from **43% in March 2019 to 32% by September 2023**, raising concerns about the process's effectiveness.

Other Key Concerns

- **Quality of Institutional Capacity:** The current method of appointment ignores the need for domain experience.
 - ♦ Members often lack the domain knowledge required to appreciate the nuanced complexities involved in high-stakes insolvency matters.
- **Bureaucratic Labyrinth:** There is no effective system in place before the NCLTs for urgent listings.
 - ♦ The staff of the Registry is given wide powers to list or not to list a particular matter that further complicates the resolution process.
- **Underdeveloped Credit Ecosystem:** The lack of robust credit information systems and distressed asset markets constrains resolution effectiveness.

Proposed Amendments and Stakeholder Engagement

- **Insolvency and Bankruptcy Board of India (IBBI)** has proposed amendments to the **Corporate Insolvency Resolution Process** regulations.
 - ♦ **Key suggestions** include requiring registered valuers to submit comprehensive valuation reports for the entire corporate debtor, rather than separate asset class valuations. It aims to enhance efficiency and transparency.
- **Exploring Mediation as an Alternative:** IBBI's expert committee has recommended incorporating mediation as an **Alternative Dispute Resolution** method under the IBC.
 - ♦ It seeks to expedite resolutions and reduce the burden on judicial institutions by allowing parties to **voluntarily opt for out-of-court settlements**.

- ◆ The committee suggests establishing a specialized mediation framework tailored to insolvency cases, which could operate within the existing IBC structure.

Other Suggested Reforms

- **Facilitating Pre-Packaged Insolvency:** Frameworks for **micro, small, and medium enterprises (MSMEs)** have shown promise in speeding up resolutions.
 - ◆ Expanding this mechanism to other sectors could further reduce delays and costs.
- **Promoting a Resolution-Centric Approach:** The framework must prioritize resolution over liquidation.
 - ◆ Greater emphasis on innovative restructuring strategies and incentives for bidders to keep businesses operational is essential.
- **Sustainability Integration:** Incorporating **Environmental, Social, and Governance (ESG) criteria** into insolvency resolutions can ensure long-term sustainability and align with global best practices.
- **Other reforms** like *streamlining litigation* by clearer guidelines, *strengthening institutional capacity* of NCLT and *operational efficiency, and encouraging professionalism*.

Global Best Practices

- The dynamic global economic environment necessitates rethinking insolvency frameworks to adapt to new challenges, such as cross-border insolvency, digital economy disruptions, and the need for sustainability.
 - ◆ Adopting the **UNCITRAL Model Law on Cross-Border Insolvency** can ensure cooperation and coordination in cases involving assets or creditors in multiple jurisdictions.
- Lessons can be drawn from mature **jurisdictions like the USA and United Kingdom**, which emphasize flexibility, pre-packaged insolvency plans, and **debtor-in-possession (DIP)** financing.

Conclusion and Way Forward

- Insolvency resolution is not just about recovering dues but also about preserving economic value and fostering a culture of responsible borrowing and lending.
 - ◆ By recasting the IBC to address its current limitations, India can further consolidate its position as a business-friendly and resilient economy.
- A robust insolvency resolution framework is essential for strengthening credit markets, boosting investor confidence, and fostering a healthier financial ecosystem.
 - ◆ With targeted reforms, the IBC can continue to be a cornerstone of India's economic growth story.

Source: TH



Mains Practice Question

Analyze the current framework of the Insolvency and Bankruptcy Code, 2016 in India. Discuss the key challenges faced in its implementation and propose recommendations for recasting the insolvency resolution process to achieve its objectives more effectively.