



Indian Economy

Seven Years of the Insolvency and Bankruptcy Code

Tags:

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For Prelims: Insolvency and Bankruptcy Code (IBC), National Company Law Tribunal, Insolvency, Bankruptcy

For Mains: Challenges faced by the IBC, Indian Economy and issues relating to planning, mobilization of resources, growth, development and employment.

Why in News?

The Insolvency and Bankruptcy Code (IBC), **introduced in 2016**, has been a transformative tool in resolving **stressed assets and improving the credit culture** in India.

- However, a recent report by CRISIL Rating highlights certain challenges that are impacting the success of the IBC as it completes seven years.

Note

- CRISIL Rating is a subsidiary of CRISIL Limited, a leading credit rating agency in India.
- It is a full-service rating agency that rates the entire range of debt instruments, from manufacturing companies to financial institutions.

What's Hampering the IBC's Success?

- **Falling Recovery Rates:**

- Recovery rates have witnessed a significant **decline from 43% to 32%** between March 2019 and September 2023.
 - The recovery rate is the percentage of the admitted claims that the creditors recover from the resolution or liquidation of the corporate debtor under the IBC.
- **Root Causes:**
 - **Limited Judicial Bench Strength:** The IBC resolution process is impeded by a **shortage of judges**, resulting in a **deceleration of case processing**. This, in turn, contributes to prolonged resolution times.
 - **Delays in Default Identification:** Time-consuming processes for identifying and acknowledging defaults contribute to reduced recovery rates. It hampers the **timely initiation of resolution proceedings**, contributing to reduced recovery rates.
- **Impact:**
 - Diminution in asset values.
 - Sub-optimal recoveries, affecting creditors and stakeholders.

- **Increased Resolution Time:**

- The average resolution time has surged from **324 to 653 days**, well beyond the stipulated 330 days.
- Resolution time is the duration between the admission of the insolvency application and the approval of the resolution plan or the order of

liquidation by the National Company Law Tribunal (NCLT).

- **Root Causes:**

- **Prolonged Pre-IBC Admission**

- Stage:** Significant delays in this stage, **lasting 650 days in fiscal 2022 (up from about 450 days in fiscal 2019).**

- **Impact:**

- Slower resolution processes.
 - Suppression of recovery rates due to delays in initiating proceedings.

What is the Insolvency and Bankruptcy Code (IBC), 2016?

- **About:**

- The IBC, 2016 is the **bankruptcy law of India** that consolidates and amends the **existing laws relating to insolvency and bankruptcy** of corporate persons, partnership firms, and individuals.

- Insolvency is a state where the **liabilities** of an individual or an organization **exceeds its asset** and that entity is unable to raise enough cash to meet its obligations or debts as they become due for payment.
 - Bankruptcy is when a person or company is **legally declared incapable of paying their due and payable bills.**

- The IBC aims to provide a time-bound and creditor-driven process for insolvency resolution and to improve the credit culture and business environment in the country.
 - IBC resolves claims involving insolvent companies. This was intended to tackle the bad

loan problems that were affecting the banking system.

- **Regulating Authority:**

- The Insolvency and Bankruptcy Board of India (IBBI) was established under the Insolvency and Bankruptcy Code, 2016.
- It is a statutory body, responsible for making and implementing rules and regulations for insolvency and bankruptcy resolution of corporate persons, partnership firms, and individuals in India.
- The IBBI has 10 members, representing the Ministry of Finance, the Ministry of Corporate Affairs, and the Reserve Bank of India.
- Adjudicating Authority:
- National Company Law Tribunal (NCLT)
 - has jurisdiction over companies, other limited liability entities.
 - **Debt Recovery Tribunal (DRT)** has jurisdiction over individuals and partnership firms other than Limited Liability Partnerships.

- **Amendments in the IBC:**

- The IBC has undergone significant amendments in the past 12 months to address emerging challenges and enhance its effectiveness.
 - These amendments include the approval for the sale of assets or resolution plans on a segregated basis, an increase in the number of **NCLT benches to 16**, and extended timelines for filing claims.
 - Sector-specific amendments, provisions for the audit of corporate debtors, and modifications in Form G2 have been introduced to address unique challenges.

- **Achievements:**

- Since its inception in 2016, **IBC has resolved Rs. 3.16 lakh crore** of debt stuck in 808 cases in seven years, according to CRISIL.
- It has resolved a significant amount of stressed assets with **better recovery rates** compared to previous mechanisms like the Debt Recovery Tribunal, the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 and Lok Adalat.
- IBC has achieved higher recovery rates, with creditors realizing 32% of admitted claims on average and 169% of the liquidation value.
 - In contrast, other mechanisms had recovery rates ranging from 5-20%.
- IBC's deterrent effect is evident as borrowers, fearing the loss of companies, have proactively settled over Rs. 9 lakh crore in **debt before cases entered the insolvency process.**
 - This highlights a significant behavioral change among borrowers, showcasing the efficacy of the Insolvency and Bankruptcy Code in encouraging timely settlements.

How Can the IBC Overcome Challenges?

- CRISIL Rating suggested a **CDE approach** to enhance the IBC's performance, where C stands for Capacity augmentation, D for Digitalisation and E for Expansion of pre-pack resolutions to large corporates.
- Capacity augmentation involves **enhancing the infrastructure and human resources** of key institutions like the NCLT, responsible for IBC implementation.

- This aims to boost case throughput, mitigating the backlog of 13,000 cases in different stages of resolution.
- Digitalisation refers to creating a digital platform for **connecting all the stakeholders** involved in the IBC process.
 - This will help eliminate data asymmetry, enhance transparency, and facilitate faster decision-making.
- Expansion of the pre-packaged insolvency resolution process (PPIRP) to large corporates will help in preventing value erosion due to time.

UPSC Civil Services Examination, Previous Year Question (PYQ)

Prelims

Q. Which of the following statements best describes the term 'Scheme for Sustainable Structuring of Stressed Assets (S4A)', recently seen in the news? (2017)

- (a) It is a procedure for considering ecological costs of developmental schemes formulated by the Government.
- (b) It is a scheme of RBI for reworking the financial structure of big corporate entities facing genuine difficulties.
- (c) It is a disinvestment plan of the Government regarding Central Public Sector Undertakings.
- (d) It is an important provision in 'The Insolvency and Bankruptcy Code' recently implemented by the Government.

Ans: (b)