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ON THE ROADS OF RECOVERY: HOW FAR TO GO?

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Abstract: *There are ample researches on Indian banks grappling with the issue of Non-Performing Assets (NPAs).There are equal numbers of supporting literature on pre-emptive measures which needs to be taken to avoid bundling up of these stressed assets. The present study, however, is an effort to evaluate the various remedial measures introduced by regulators to recover the non-performing assets due on defaulting borrowers.*

This document has three sections in all. The first section gives a brief environment amidst which, the recovery related reforms were enacted. The second section introduces the recovery mechanisms brought into force since independence. The third section evaluates the performance of the recovery mechanisms with respect to Gross Non Performing Asset ratio. This section also talks about the reason of variations in the recoveries through various channels. The study finally summarises with recommendations and suggestions which could help recovery system to be more effective individually and collectively.

INTRODUCTION

It is important for an economy to keep the banking sector de-stressed from the load of carrying unwarranted non-performing assets. The statistics empirically show, that whenever there were escalations in sub-standard assets, credit expansion in the economy has taken a hit (Rajan, 2014). The reason for the occurrence of this pattern is the tendency of banks becoming risk aversive. They tend to restrict credit disbursements, especially towards sectors showing any sign of stress. This trend has been more prominent in the industrial sector, especially with respect to the core industries. Acknowledging this, the government and regulators have been building up the mechanisms to insulate the banking sector from adopting risk aversive tendencies by curbing the issue of non-performing assets (NPAs).

THE OBJECTIVE OF THIS STUDY THUS IS TO:-

- To study the background of rising NPAs and reasons of introduction of recovery channels.

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- To study the various Indian Recovery Mechanisms introduced so far (SICA 1985, RDDBFI-1993, SARFEASI-2002 and IBC-2016).
- To evaluate the efficacy of DRTs, SARFEASI (with ARCs) and IBC-2016.

SECTION-1 : BACKGROUND

Prior 1990s, the major focus of the government was to manage, consolidate and stabilise the economy. This was done by controlling the core industries and nationalising the financial institutions by the then government. This era saw a tight and regulated environment (Sahoo, 2017b). The objective was towards social control and thus the focus was directed towards breaking the nexus between few giant corporate houses and existing private banks (Assocham & E&Y, 2016). In addition to this, efforts were also to extend the credit towards the long-time ignored agriculture sector and introducing the environment of 'inclusion of all' allowing everyone to invest and contribute (Kapur & Ramamurti, 2002).

Till early 2000 much focus of the reforms introduced, were on encouraging and giving a boost to the growth of industrial sector. The free entry and congenial environment incentivised coming up of budding of promising companies, but along with it came inefficient, incapable 'Zombie entities'(Sahoo, 2017a). Zombie entities further led to mushrooming of unwarranted defaults. The story of escalating NPAs did start with these entities, but there were other participants who had a major role as well. Banks to start with, had their share of contribution towards rising NPAs.

By the time govt did away with the controlled and regulated regime, the banks were more or less working in a protective environment. The regulated era barely needed the banks to work towards building an efficient disbursement mechanism. The deregulated regime empowered the banking sector to extend credit as they desired. Entry of new private sector banks, post reforms instilled competitive pressure among public sector banks to survive. An upsurge in credit demand, in the post reform era, banks actively indulged in exuberant lending with slack behaviour in credit appraisals, disbursements, monitoring and lack of technological advancement (Reserve Bank of India, 2007).

There was a third angle attached to this problem. The reforms hence introduced were focused towards encouraging the companies to enter and participate in the free market environment. However, there was no mechanism built for a company to exit if it wishes to. The issue related to entities failing to perform and thus defaulting were not addressed effectively. The absence of legal, institutional and ineffective regulatory framework was what added to the already brewing problem.

With the advent of free market environment, inexperience of the banking sector under the deregulated environment and the absence of effective regulatory mechanism and a legal framework, it became unavoidable to establish a robust

mechanism so as to help the system keep up with the dynamic financial reforms and the prevailing commercial practises.

SECTION-2 : RECOVERY MECHANISMS

The Companies Act 1956 and SICA 1985, enacted prior 1990s, more or less were brought up in a socially controlled and a regulated environment. The economic objective during this period was to encourage the budding companies to settle and survive (Kapur & Ramamurti, 2002). In case of a company failing to perform, efforts were more towards rehabilitation instead of liquidations even when circumstances demanded so.

Companies Act 1956, though not a recovery mechanism, catered to liquidate or winding up of the company in the absence of any mechanism (Rathinam & Raja, 2010). Liquidations initiated by creditors proved to be a tedious and time consuming process. The procedure under this Act had a lot many loop holes which pushed and delayed the resolution process, eventually devaluating the company in question.

SICA 1985

SICA 1985 was the first Act which was meant to address the issue of rehabilitation and liquidation among so called 'Sick industries'. The cases referred to BIFR- the adjudicating authority under SICA, was required to examine the feasibility of the company in question (Bhagwati, Khan, & Bogathi, 2017). This Act, however totally failed to address the issues of liquidations of non-viable units since the govt at this time was in the mode of stabilising and encouraging the industries (Jaitley, 2019). In line with the objectives of the government, BIFR remained focused only on rehabilitations. There are ample evidences that the High Courts which acted as adjudicating authorities in non-viable cases, very often referred the cases back to BIFR for rehabilitation claiming it to be in the public interest'. This led to enormous loss to creditors in terms of time and value of stressed assets with a very high opportunity cost (Branch & Khizer, 2016)traces its roots back to colonial rule. That framework has undergone a number of amendments over the past 200 years, creating a plethora of overlapping and sometimes conflicting articles. The latest attempt at reconciliation of these various Acts was made under the Companies Act, 2013. This paper drives through the land mark amendments in the history of India, leading to the current bankruptcy framework. Each Act is discussed based on the requirements, procedures and outcomes post enactment. Also, the major pros and cons of the different Acts are identified, and a critical analysis is presented of the latest Act, Companies Act, 2013. Moreover, the provisions of Chapter 7 and Chapter 11 of the U.S Bankruptcy Framework are compared against the provisions of these Acts. The paper then presents a diluted, easy to understand, step by step procedure of the current bankruptcy framework.

Followed by a case analysis of a recent prominent Bankruptcy, to elicit the issues in the current framework. In conclusion, a list of recommendations is presented, to improve the Bankruptcy Framework in India.",”author”:[{“dropping-particle”:””,”-family”:”Branch”,”given”:”Ben”,”non-dropping-particle”:””,”parse-names”:false,”-suffix”:””},{“dropping-particle”:””,”family”:”Khizer”,”given”:”Abdul”,”non-dropping-particle”:””,”parse-names”:false,”suffix”:””}],”container-title”:”International Review of Financial Analysis”,”id”:”ITEM-1”,”issue”:”March 2004”,”issued”:{“-date-parts”:[[“2016”]]},”page”:”1-6”,”publisher”:”Elsevier B.V.”,”title”:”Bankruptcy practice in India”,”type”:”article-journal”,”volume”:”47”},”uris”:[“http://www.mendeley.com/documents/?uuid=e788cfae-0b46-4b2c-945e-aee125848264”]}],”mendeley”:{“formattedCitation”:”(Branch & Khizer, 2016.

Due to the absence of effective recovery mechanism, banks were riddled with delays in disposal of default cases, leading to heavy losses in the value of stressed assets. Too much interference by the government for compliance of social objectives by banks, and overburdened judiciary had led to an alarming deterioration in the status of NPAs. These problems led banks to adopt sub-optimal decisions in order to hide the actual NPAs status (Kang & Nayar, 2003)such as import substitution, industrial licensing, and limited private ownership, fostered a breed of inefficient and uncompetitive companies. Deregulation, foreign competition and financial reform led many financially unviable firms to consider exit or restructuring options. However, the existing legal, political and social system did not provide the appropriate framework for efficient and equitable resolution of insolvency cases, thus dramatically slowing the pace of the much needed industrial restructuring. This paper shows that there is no single comprehensive and integrated policy on corporate bankruptcy in India comparable with the bankruptcy code in the US. Instead, there are a number of legislative acts and special provisions, which provide procedural guidance on the liquidation or reorganisation process and there is an involvement of different agencies, having overlapping jurisdiction, which creates systemic delays and complexities in the process. In so far as the objective of a well functioning bankruptcy system is to promote economic efficiency by maximising the total value of assets, the Indian system fails, as under this system, liquidation or reorganisation is extremely time and resource costly; the system does not encourage optimal valuation outcomes; and creates incentives for managers or stockholders to take actions that generate private benefits at the expense of firm value. The paper evaluates the existing corporate bank-ruptcy system; and the incentives and biases it has created, given the Indian socio-political context and economic goals. It assesses the new Companies (Second Amendment. The GNPA ratio during 1997 was as high as 15.4 (muniappan 2004).

LOK ADALAT-1987

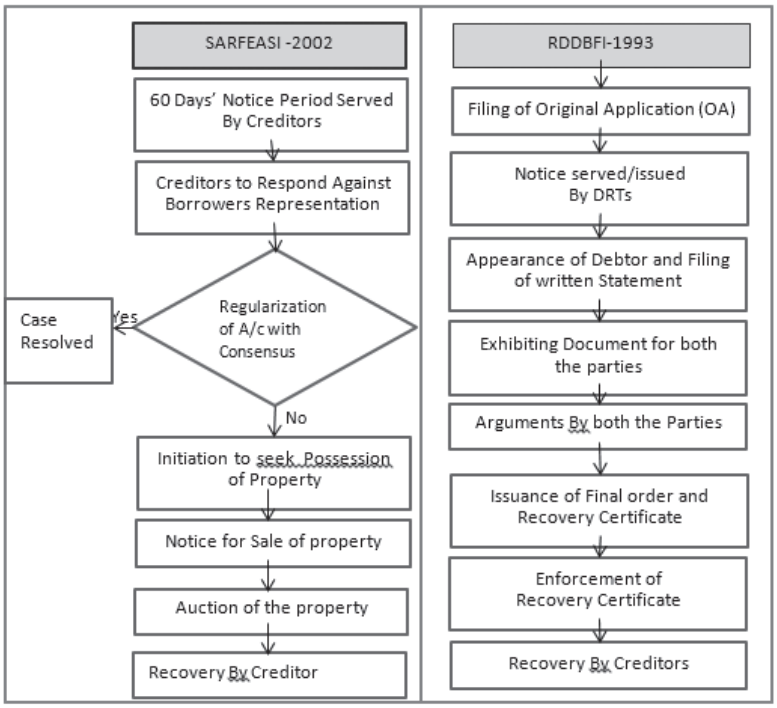
In 1987, Lok Adalats got introduced under Legal Services Authorities Act. It en-

abled a process of voluntary arbitration and reconciliation between the debtor and creditors.. The limitation in processing of this measure, however, was that the pecuniary jurisdiction of Lok Adalat was limited to Rs 10 Lakh only (later increased to 20 lakhs). Because of such small amount being referred to Lok Adalat and a mandatory requirement of concurrence of both the parties, this channel didn't prove to be successful in terms of the total amount recovered (Muniappan, 2004).

RDDBFI-1993

By 1993 another act under RDDBFI got introduced. This act was a result of financial reforms introduced in 1990. The enactment of this Act majorly was to limit the extraordinary delays in the disposal of recovery related matters lying with already burdened civil courts (Roy, 2017). The Act established special Tribunals called the Debt Recovery Tribunal (DRTs) to adjudicate matters pertaining to Banks/ Financial institutions involving Rs 10 Lakhs or more (Kang & Nayar, 2003)such as import substitution, industrial licensing, and limited private ownership, fostered a breed of inefficient and uncompetitive companies. Deregulation, foreign competition and financial reform led many financially unviable firms to consider exit or restructuring options. However, the existing legal, political and social system did not provide the appropriate framework for efficient and equitable resolution of insolvency cases, thus dramatically slowing the pace of the much needed industrial restructuring. This paper shows that there is no single comprehensive and integrated policy on corporate bankruptcy in India comparable with the bankruptcy code in the US. Instead, there are a number of legislative acts and special provisions, which provide procedural guidance on the liquidation or reorganisation process and there is an involvement of different agencies, having overlapping jurisdiction, which creates systemic delays and complexities in the process. In so far as the objective of a well functioning bankruptcy system is to promote economic efficiency by maximising the total value of assets, the Indian system fails, as under this system, liquidation or reorganisation is extremely time and resource costly; the system does not encourage optimal valuation outcomes; and creates incentives for managers or stockholders to take actions that generate private benefits at the expense of firm value. The paper evaluates the existing corporate bank-ruptcy system; and the incentives and biases it has created, given the Indian socio-political context and economic goals. It assesses the new Companies (Second Amendment. The DRTs were better skilled, equipped and empowered as compared to the Civil Courts .They proved to be an effective mechanism compared to the earlier ones but soon after they got caught in the web of pendency and delay in judgements. Contradictions in judgments and litigations were also common in cases filed under DRTs (Roy, 2017), (Kapur & Ramamurti, 2002). By Sep 2001, the number of pending cases had risen to alarming 33,049, holding an amount of Rs 42,988.84 crores (Muniappan, 2004)

WORKING OF SARFEASI & DRTs



[1] Bare Act Lok Adalat 2018

SARFEASI ACT 2002

SARFEASI Act, introduced in 2002, empowered the creditors to seek the recovery without involvement of courts (Act, 2002). The Act empowered the secured creditors to seek recovery under SARFEASI Act through Securitization, Asset Reconstruction and Enforcement of Securities. The Securitisation of Assets was done through issuing of security receipts to qualified institutional buyers through ARCs route, Asset Reconstruction by revamping the management or restructuring payment schedule and enforcing the security by taking possession or sale of property[1]. This Act helped the establishment of Asset Reconstruction Companies (ARCs) which were empowered to buy bad assets from the banks against Security Receipts (SRs) (Bhagwati et al., 2017). It helped reduce the length of time from 10-15 years to 2 years (Kang & Nayar, 2003)such as import substitution, industrial licensing, and limited private ownership, fostered a breed of inefficient and uncompetitive companies. Deregulation, foreign competition and financial reform led many financially unviable firms to consider exit or restructuring options. However, the existing legal, political and social system did not provide the appropriate framework for

efficient and equitable resolution of insolvency cases, thus dramatically slowing the pace of the much needed industrial restructuring. This paper shows that there is no single comprehensive and integrated policy on corporate bankruptcy in India comparable with the bankruptcy code in the US. Instead, there are a number of legislative acts and special provisions, which provide procedural guidance on the liquidation or reorganisation process and there is an involvement of different agencies, having overlapping jurisdiction, which creates systemic delays and complexities in the process. In so far as the objective of a well functioning bankruptcy system is to promote economic efficiency by maximising the total value of assets, the Indian system fails, as under this system, liquidation or reorganisation is extremely time and resource costly; the system does not encourage optimal valuation outcomes; and creates incentives for managers or stockholders to take actions that generate private benefits at the expense of firm value. The paper evaluates the existing corporate bank-ruptcy system; and the incentives and biases it has created, given the Indian socio-political context and economic goals. It assesses the new Companies (Second Amendment.The SARFEASI Act, though improved the recovery environment, it still was saddled with kinds of challenges which were common to previous mechanisms. Time delays, devaluation and deterioration of the assets were some common recovery problems (Bhagwati et al., 2017). Besides this, possessions of secured assets by lender banks were proving to be a tough job due to systematic and bureaucratic pressures. Even if the banks managed the possession of assets in question, the banks still found it difficult to dispose it off through auction (Ghosh, 2018).

SCHEME OF CORPORATE DEBT RESTRUCTURING (CDR)

Besides these Acts, Scheme of Corporate Debt Restructuring (CDR) was also introduced in Aug 2001. CDR was framed to restructure the debts amounting to 100 million or more (Muniappan, 2004). CDRs could not contribute much in mitigating NPAs in the long term. There were two reasons for this, one, the effectiveness of this scheme got countered by existing volatility in the economy and the other, that, banks most often used this scheme to disguise the NPAs by ever greening the accounts than addressing the issues in genuine cases (RBI speech). The ineffectiveness of CDR could be seen in 2016 wherein out of 633 cases referred to CDR, as much as 530 cases were approved with only 97 cases of successful exits (Rao & Jessica, 2017). Thus, not serving the purpose, it was discontinued with the enactment of IBC in 2016.

The major limitations of the prevailing schemes to curtail non-performing assets were undue delays, absence of strong backup for creditors with no legal bindings on borrowers, the prevalence of multiple regulatory authority and cross overlapping along with misinterpretation of rules and provision in the recovery mechanism (Bhojani et al., 2018; Branch & Khizer, 2016; Kang & Nayar, 2003; Rajeswari &

Anjali, 2016; Ravi, 2015; Roy, 2017; Sengupta, Sharma, & Thomas, 2016)traces its roots back to colonial rule. That framework has undergone a number of amendments over the past 200 years, creating a plethora of overlapping and sometimes conflicting articles. The latest attempt at reconciliation of these various Acts was made under the Companies Act, 2013. This paper drives through the land mark amendments in the history of India, leading to the current bankruptcy framework. Each Act is discussed based on the requirements, procedures and outcomes post enactment. Also, the major pros and cons of the different Acts are identified, and a critical analysis is presented of the latest Act, Companies Act, 2013. Moreover, the provisions of Chapter 7 and Chapter 11 of the U.S Bankruptcy Framework are compared against the provisions of these Acts. The paper then presents a diluted, easy to understand, step by step procedure of the current bankruptcy framework. Followed by a case analysis of a recent prominent Bankruptcy, to elicit the issues in the current framework. In conclusion, a list of recommendations is presented, to improve the Bankruptcy Framework in India.","author":[{"dropping-particle":"","family":"Branch","given":"Ben","non-dropping-particle":"","parse-names":false,"suffix":""},{"dropping-particle":"","family":"Khizer","given":"Abdul","non-dropping-particle":"","parse-names":false,"suffix":""}],"container-title":"International Review of Financial Analysis","id":"ITEM-2","issue":"March 2004","issued":{"date-parts":[["2016"]]},"page":"1-6","publisher":"Elsevier B.V.","title":"Bankruptcy practice in India","type":"article-journal","volume":"47"},"uris":["http://www.mendeley.com/documents/?uuid=e788cfae-0b46-4b2c-945e-aee125848264"]},{"id":"ITEM-3","itemData":{"author":[{"dropping-particle":"","family":"Rajeswari","given":"Sengupta","non-dropping-particle":"","parse-names":false,"suffix":""},{"dropping-particle":"","family":"Anjali","given":"Sharma","non-dropping-particle":"","parse-names":false,"suffix":""}],"container-title":"MPRA","id":"ITEM-3","issue":"11543","issued":{"date-parts":[["2016"]]},"title":"Corporate Insolvency Resolution In India:Lessons from a cross country comparision","type":"article-journal"},"uris":["http://www.mendeley.com/documents/?uuid=e3aac87a-c7b3-4c3f-96e7-b074207029a1"]},{"id":"ITEM-4","itemData":{"ISBN":"9780821389836","author":[{"dropping-particle":"","family":"Bhojani","given":"H","non-dropping-particle":"","parse-names":false,"suffix":""},{"dropping-particle":"","family":"Kumar","given":"Dhananjay","non-dropping-particle":"","parse-names":false,"suffix":""},{"dropping-particle":"","family":"Mukherjee","given":"Debanshu","non-dropping-particle":"","parse-names":false,"suffix":""},{"dropping-particle":"","family":"Paterson","given":"Sarah","non-dropping-particle":"","parse-names":false,"suffix":""},{"dropping-particle":"","family":"Qu","given":"Charles Zhen","non-dropping-particle":"","parse-names":false,"suffix":""},{"dropping-particle":"","family":"Rao","given":"Pramod","non-dropping-particle":"","parse-names":false,"suffix":""},{"dropping-particle":"","family":"Ravi","given":"Aparna","non-dropping-particle":"","parse-names":false,"suffix":""},{"dropping-particle":"","family":"Segal","given":"Nick","non-dropping-particle":"","parse-names":-

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IBC -2016

Enacted on May 2016, IBC became operational on Dec 2016. IBC was framed with the intention of building an environment which could improve the credit culture and recovery management in the economy (Rajeswari & Anjali, 2016).

The IBC Framework has Insolvency & Bankruptcy Board of India (IBBI) as the regulator to supervise the whole process within the ambit of Insolvency and Bankruptcy Code,.National Company Law Tribunals

(NCLTs) and DRTs are assigned to be the adjudicating authorities. Insolvency Professionals, Information Utilities and Valuers act as service providers.

Role of NCLTs in the IBC mechanism is to adjudicate the impartial compliance of the proceedings. Insolvency Professionals oversee the management and proceedings of the case, while Information Utility and Valuers supplement the relevant information required during the whole proceedings.

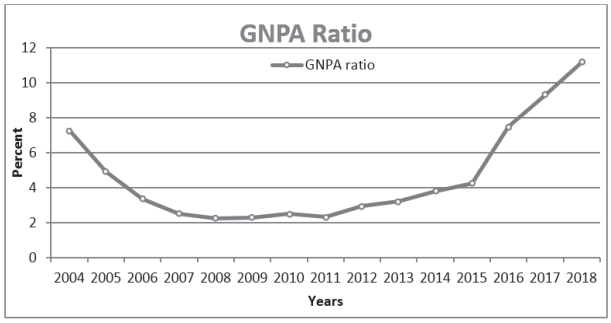
Cases filed by financial creditors, operational creditors or corporate debtors have 180 / 270 days' timeline for its resolution. The resolution plan may reorganise (including sale to other corporates/investors), restructure or it may even change the ownership of the company in distress (Ghosh, 2018). In case the resolution plan doesn't get materialised the case is subjected to liquidation.

SECTION-3 : PERFORMANCE OF RECOVERY MECHANISMS

The recovery mechanisms introduced from time to time to support the banking system have delivered mixed results. The reason of mixed results have been attributed to bank specific, recovery tool specific, and the contagion effect due to global volatility (Quote). To analyse the performance of existing recovery channels, the period between 2004 - 2018 has been divided into three phases.

FIRST PHASE (2004-08)

Year 2004-08 was a period of stable economic environment. The banks during this phase registered less slippages in NPAs with higher provisioning and high write-offs helped contain NPAs to a large extent (Trend and progress). The GNPA ratio which was 7.26% in 2004, witnessed a downward fall reaching to 2.26% by 2008. Thus GNPA witnessed a relatively slow growth from Rs 5,15,567 million to Rs 5,66,060 million by 2008.

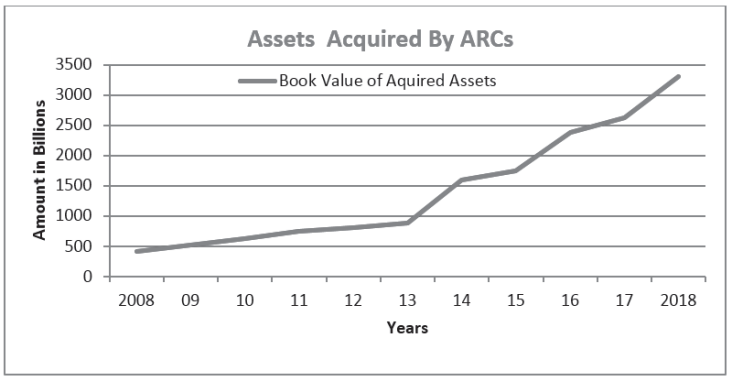


Source: Trends and progress 2004-18,RBI

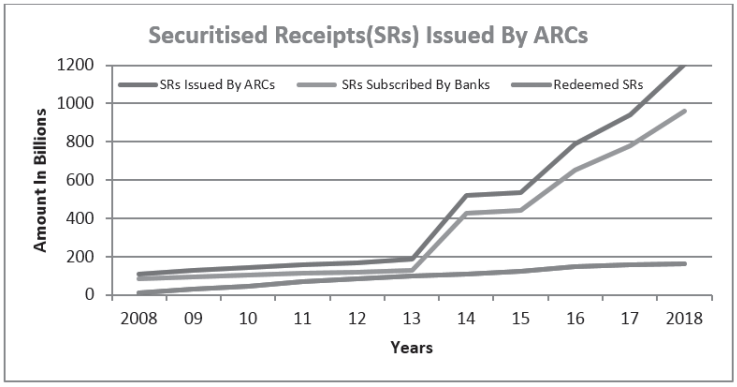
As per trend and progress 2006-07, the performance of recovery channels, especially that of SARFEASI and DRTS, were found to be satisfactory.

In 2006, the DRTs were the most effective as recovery tool. A significant amount of Rs 47 billion was recovered out of Rs 63 billion, achieving as much as 75% of the total amount claimed under this recovery tool. The average recovery from Lok Adalats, SARFEASI and DRTs taken together also rose to 49%.

During the said period the banks had also started using the ARC Channel, thereby transferring NPA risk to ARCs. In line with the stable economic environment and relative impressive recoveries, year 2006-07 witnessed the establishment of three additional ARCs, totalling up to six. The first major success of ARCs happened with the sale of 559 cases by 31 Banks having a Book Value of Rs 21,126 Crores (Trend and progress 2006).



Source: Trends and progress 2004-18,RBI

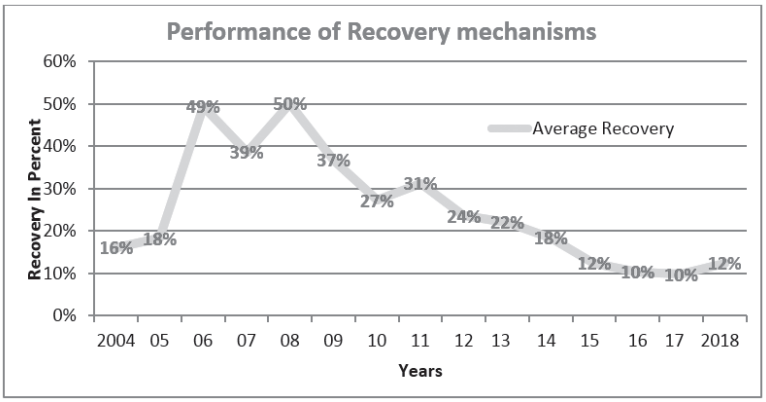


Source: www.arcindia.co.in

The total asset acquired by ARCs by 2006-07 increased to Rs 28,544 crores. The restructuring also helped in restricting the NPA escalation. The said period witnessed a comfortable trend in Banking Industry in terms of growth in advances vis a vis percentage of substandard assets/ NPAs and the comparative recovery effected through the available recovery mechanism.

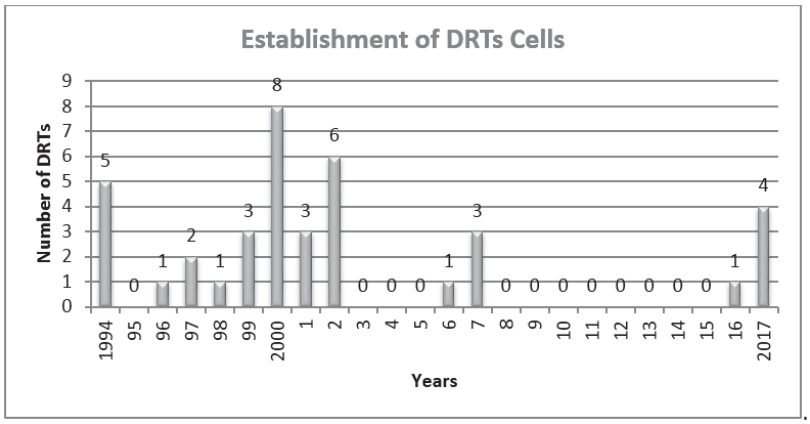
SECOND PHASE (2008-09 TO 2013-14)

Post 2007 GNPA ratio started signalling an upward trend. The GNPA ratio which was as low as 2.26% in 2008 rose to 3.83 by 2014. The over indulgence in credit disbursement by banks in the past, started showing its side effects in terms of rising NPAs. The impact of economic meltdown and absence of debt related waivers also had a share in this unwarranted hike. The prevailing performance stress in industries also got transferred on to banks in the form of increasing defaults. According to Financial Stability Report June 2014, 5 core industries namely infrastructure, mining, textiles, iron & steel and aviation contributed to as much as 52% of the total stressed advances which is considerably high. (FSR) Average performance in recovery mechanism Lok Adalat, DRTs and SARFEASI taken together saw an alarming dip from 50% in 2008 to 37%, 27%, 31% and 24%, 22%, 18% by 2012 respectively.



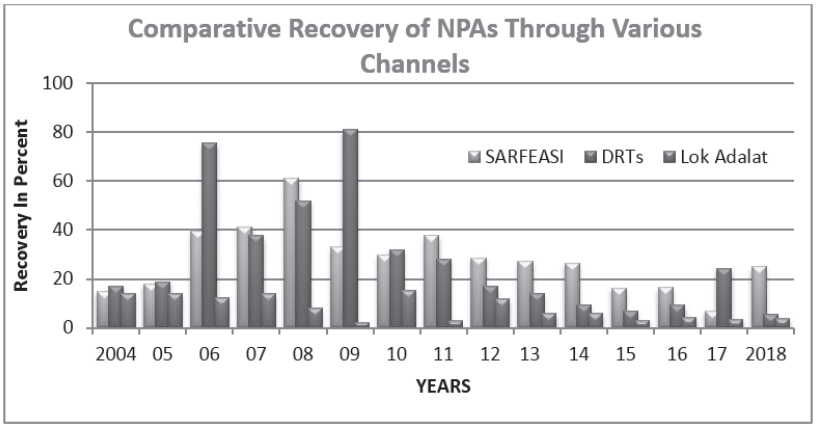
Source: Trends and progress 2004-18,RBI

Till 2014, performance of all mechanisms taken together were experiencing a downward slope. DRTs though were relatively better till 2009 with a record 81% recovery; they followed the same downward pattern as that of all other mechanisms. The percentage recovery by DRTs was recorded to be 32%, 28%,17%,14% and 10% by 2014. The poor recovery performance of DRTS can also be correlated to the growth pattern of DRTs cell



Source: www.drt.gov.in

The data indicates that there was practically zero addition of DRT cells between 2008-2015. The number of cases filed on the other hand rose unabatedly to as much as 1,01,658 between the said period. This contributed to a downward trend in the recovery behaviour of DRTs in a major way. Looking at the data pertaining to recovery through DRTs, the number of cases filed in 2008 were 1,86,535 which rose to 5,48,308 in 2009. This meant an incremental filing of an additional 3,61,773 cases within a span of 1 year. This overburdening of DRTs was bound to get reflected in its performance in coming years.



Source: www.rbi.org.in

Recovery through SARFEASI Act also showed steadier fall registering 30% recovery in 2010. The figures changed to 38%, 29%, 27% and 27% by 2014. The downward behaviour in the mechanisms was attributed to infrastructural ineffi-

ciencies, lack of clarity in interpretation and inabilities to understand the corporate working by adjudicating authorities. Performance of Private Sector Banks during this phase recorded a better recovery even after having a higher GNPA. This further raised a question on the **internal recovery management system** in Public Sector Banks.

The reduction of NPAs through ARCs route didn't witness any proportionate increase with respect to rising NPAs. The reason was conflicting interests among ARCs and Banks. The banks till this period were more keen on settling the ARC transactions on cash basis whereas ARCs were keen on the settlement through Security Receipts redeemable only after five years or more. Along with this, the ARCs were trying to come up with ways and means to increase their profitability. To further this objective, ARCs introduced a 'senior class of Security Receipts' which had a prior preference during redemptions. The ARCs also managed a sustainable income with an annual management fee and an assured return in case of waterfall distribution.

To develop this route, the RBI, has been issuing guidelines to incentivise the banks encouraging them to adopt ARC route. In this respect, the RBI, from 24th Feb 2014 onwards relaxed the provisioning norms for banks. It also helped banks interact with specialised ARC officials (Bhagwati et al., 2017).

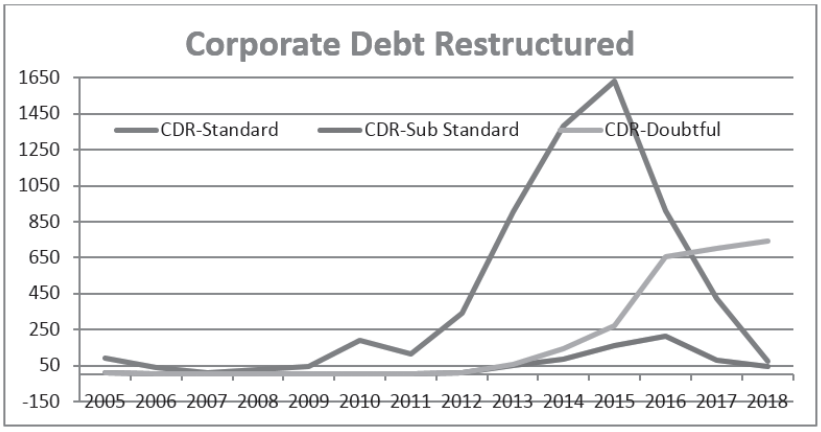
The SC/RCs Regulatory Framework Guidelines, introduced in 2014, also made the ARCs more accountable. This was done by increasing the in-house stake of ARCs, to be increased from 5% (in 2006) to 15%. The annual management fee charged by ARCs also witnessed certain changes during the said period ((RBI (2014), (Regulatory framework for SCs/RCs – Certain amendments)).

Other than the above mentioned changes, regulators also introduced certain measures which were thought to help banks ease with the NPAs burden. In this context, RBI issued fresh instructions to the banks to identify early signals of stress assets under Special Mention Accounts (SMAs) and made it compulsory to disseminate loan related information to 'Central Repository of Information on Large Credits'(CRILIC) (Assocham & E&Y, 2016; Bhagwati et al., 2017).

Thus this phase witnessed significant steps taken by the regulatory authority to improve recovery. Asset Quality Review (AQR) was also one of them.

THIRD PHASE(2014-15 TO 2017-18)

In this phase, RBI further introduced restructuring schemes, namely SDR, S4A, 5/25 during 2014-15. As a result banks resorted to substantial debt restructuring.



Source: www.rbi.org.in

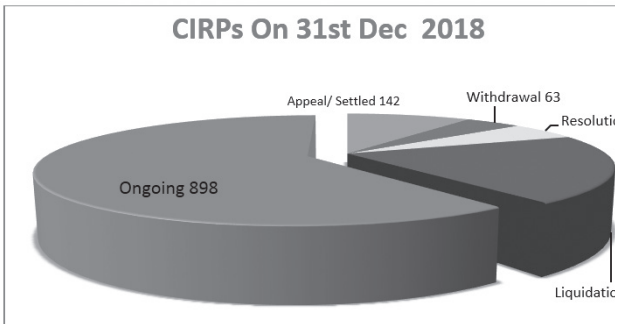
In 2014-15, the loans subjected to restructuring and corporate debt restructured was registered to be a total of Rs 3,175 and Rs 2,067 billion respectively.

The phase beyond 2015 did not improve the recovery status of the banks. Banks were severely into high impaired stress and inadequately capitalised banks. The regulators tried to manage the problem with establishing more DRTs in the recovery system. With the addition of five more DRTs in 2016- 2017, it increased to 38 by 2018. Amendments in RDDBFI also helped provide more teeth to the adjudicating authorities in order to help them adhere to the time line envisaged for disposal of the cases. Average recovery from (Lok Adalats, DRTs and SARFEASI) was still as low as 9%,10%,12% and 11% between 2015 to 2018. DRTs registered a fall in recovery of 7%, 9%, 24% and 5% during 2015-18. The SARFEASI contributed 16%, 16%, 7% and 25% during the same period.

This phase saw the restricting conditions like the ARC's initial capital requirements, 15% stake in each transaction and negatively affected management fee due to RBI guidelines discouraged the ARCs performance (Bhagwati et al., 2017). The only times the banks registered an upsurge in using ARC route was during the times banks experienced extraordinary stress due to NPAs. The recovery in terms of redemption, however always had a below average performance .(Reserve Bank of India, 2015)

It has also observed that because of either absence or practical problems in the relevant laws, ARCs could never be motivated to restructure the stressed entities which were sold to them (Bhagwati et al., 2017).

By the end of second quarter, IBC armed with 13 NCLTs[2] and 2287 Insolvency Professionals took off with an impressive start with resolving as many as 568 cases with 302 on the basis of liquidation and 79 under resolution Plan.

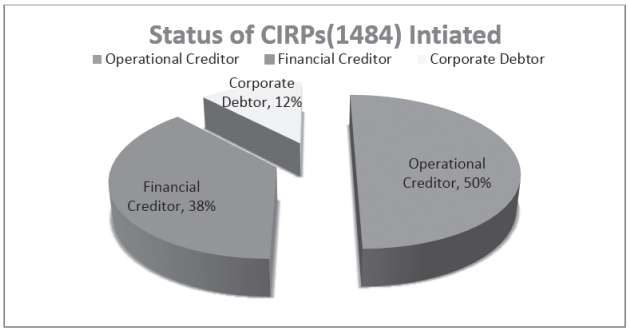


Source: www.ibbi.gov.in

Among the 302 cases under liquidation 70% have been defunct or old cases carry forwarded from BIFR referred cases (IBBI, 2018).

It has been just two years since its inception; IBC is being looked upon as panacea of all ills (E&y2016). There are certain advantages which IBC has been able to equip the system with. Firstly, it has created an environment of deterring the borrowers to default(Jaitley, 2018). The Borrowers themselves are trying to resolve the cases at pre-litigative stage to avoid their case being admitted under NCLT(Chatterjee, Sreyan; Shaikh, Gausia; Zaveri, 2017). According to the finance minister Mr Arun Jaitely, the these cases could manage to recover over two Lakhs crores without registering themselves under NCLT. A mechanism in the role of being a deterrent is something which the earlier mechanisms were not able to adopt.

Secondly, the code has empowered the existing creditors and has expended the list by entitling the operational creditors to pursue before NCLTs. Entitling to file the claims under NCLT, the new mechanism, assisted unsecured creditors to file as many as 742 out of 1484 cases referred so far. This makes 50% of the total number of cases admitted(IBBI, 2018).



Source: www.ibbi.gov.in

Thirdly the IBC brought a paradigm shift by transferring the control from debtors in possession to creditors in control (Tandon, 2019). This is also the reason why the debtors are trying to resolve the stress before the cases being registered under NCLT.

There are, however, certain grounds which IBC seems to be faltering on. One is that the time adherence seems to be on jittery ground.

Time Status of CIRPs	Resolved beyond 270 days	Total Cases
Resolved cases	60	82
Ongoing Cases	275	898

Source: Newsletter IBBI 2016-18

Looking at 1484 cases admitted by Dec 2018, as many as 335 cases have exceeded the prescribed timeline.

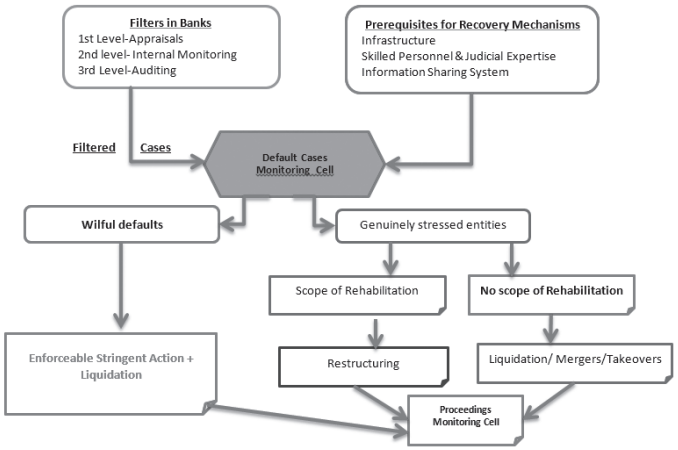
Secondly, the NCLTs are indicating seemingly overburdened and IPs seem to have been facing difficulties on ground of their inexperience and non-cooperative stance of defaulting entities(Patel, 2017).

Thirdly, there seems a strong bias towards the liquidation of cases than on resolution wherein only 79cases have been successfully closed under resolution plan against 302 cases closed under Liquidation. The concern is not of such gravity if we deduct the old BIFR/ Defunct cases, the figure still is alarmingly high(IBBI, 2018)

It is important to cater these insufficiencies to make sure they don't fall in the same line as other mechanisms.

RECOMMENDATIONS

The recovery mechanisms cannot work in isolation. They need to be assisted with an auxiliary support system. It has to have



Source: Authors viewpoint

1. Preliminary support of banks having borrowing entities undergo three filtering mechanisms with appraisals, monitoring and auditing system set in place.
2. The recovery mechanism must be supported by adequate infrastructural facilities, skilled personnel and judicially expertise to handle the business and finance related cases. The system must also be supplemented with a robust information dissemination system, which would act as a storehouse of information for the creditors, regulator and adjudicating authority.
3. The system must have the capability to identify wilful and genuine stressed accounts. A recovery system must also be empowered with enforceability which would help create an environment of productive credit culture.

CONCLUSION

The Lok Adalat, SARFEASI and DRTs have proved to assist in recoveries during the times when the banking sector was registering very high NPAs. There have been times when one mechanism, not being effective, has been taken over by another mechanism, as in the case of SARFEASI registering as much as 70% of the recovery when DRTs could manage only 26% in 2014. The effectiveness of these mechanisms, however, have been marred with confusions and complications within each mechanism and among their respective Acts.

Cross overlapping of rights and obligation of creditors and debtors under different jurisdiction and Acts, lack of clarity in rules and regulations led to delays and destruction of the economic value of assets. In addition to these insufficiencies in the infrastructure, lack of business and financial expertise with the adjudicating authorities has aggravated the problem.

IBC seen to be a unique and single forum did create an environment for credit expansion and productive credit culture, proving a deterrent for borrowing entities to default. IBC still is an evolving mechanism. It at present is affected with delays in the resolution and recovery. Lack of hands-on experience by insolvency professionals, infrastructural issues and ongoing amendments in IBC is something which the regulators need to pay more attention to.

It is important to understand that any mechanism cannot work in isolation. It has to be supported by appropriate regulations, amendments, robust judicial expertise and infrastructure and a strong will to resolve the case among the stakeholders.

NOTES

1. Bare Act Lok Adalat 2018
2. SARFEASI Bare Act 2018
3. Two more NCLTs have been approved for Madhya Pradesh and Arunachal

Pradesh -ET 8th March 2019

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