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Role of Insolvency and Bankruptcy Code 2016 in Sustaining Indian Economy

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Abstract

There are numerous overlapping laws in India that deal with financial loss and insolvency of both organisations and individuals. Under the current legal and institutional framework, lenders are unable to collect or restructure defaulted assets in a timely and effective manner, imposing an undue strain on the Indian credit system. The framework intended to combine a time-bound and scientific approach to insolvency resolution with the goal of maximising value for all stakeholders and balancing knowledge asymmetry, while also protecting the interests of all parties involved. In 2000, the amount of Non-Performing Assets (NPAs) grew rapidly. Banks made indiscriminate loans between 2008 and 2014, resulting in a high number of NPAs, as revealed by Asset Quality Reviews of the Reserve Bank of India (RBI), causing the government to act immediately. A Committee was formed, and its report, in which the IBC was recommended, was delivered in 2015. Following that, a bill was introduced in the Lok Sabha and referred to a Parliamentary Joint Committee for examination. On May 5, 2016, the Indian Broadcasting Corporation (IBC) was approved by both Houses of Parliament and received presidential assent on May 28, 2016. Indian insolvency rules have their origins in English law. Sections 23 and 24 of the Government of India Act 1800 established the first laws governing insolvency. In 1828, India passed a statute establishing the first expressly tailored insolvency legislation. This act was extended to include the Presidency towns of Bombay, Madras, and Calcutta. A few years later, the Indian Insolvency Act 1848 was introduced, which established a division between traders and non-traders. The High Courts were given jurisdiction over insolvency, with the High Courts' jurisdiction confined to presidential towns. This statute, known as the Presidency Towns Insolvency Act 1909, was enacted in 1909. Due to the absence of legislation governing insolvency in non-presidency areas before to 1907, the Provincial Insolvency Act was enacted in 1907 and was eventually succeeded by the Provincial Insolvency Act 1920, which is in force today.

Keywords: NPA, IBC Incorporation

Introduction

Insolvency is described as a legal entity's inability to pay all of its debts on any given day. It is the state or scenario of having “more than total assets available to pay those bills”, even if those assets have been mortgaged or sold to pay those debts. Insolvency arises as a result of a variety of situations, including

cash mismanagement, inflation in cash expenses, and a lack of cash flow, to mention a few.[1] The discovery of insolvency is crucial because creditors are authorized and entitled to exercise specific rights against an insolvent individual or organization upon notification of their insolvency. For instance, an insolvent party's liquidation assets may be utilized to satisfy any remaining debts owing to creditors. Prior to commencing the liquidation process, it is customary for the bankrupt entity to meet with creditors to attempt to work out a more favorable payment plan.

Bankruptcy is not synonymous with insolvency in every way. In technical terms, bankruptcy occurs when a judge determines that a person or corporation is bankrupt and issues legal directions on how to proceed. Bankruptcy, for the purposes of this definition, refers to a court-ordered determination of insolvency followed by legal orders intended to resolve the insolvency. When a debtor is unable to meet his or her ongoing obligations, the legal term is insolvency. Bankruptcy is a legal man oeuvre that enables an insolvent bankrupt to obtain relief from financial obligations.[2]

Effective capital transfer from inefficient to efficient firms will be a critical driver of India's economic resurgence in the coming years. Despite the severity of the coronavirus epidemic, In India, there are a plethora of overlapping laws that deal with financial loss and insolvency of both businesses and individuals. Lenders are unable to collect or restructure defaulted assets in a timely and effective manner under the current legal and institutional framework, putting undue burden on the Indian credit system. The framework intended to combine a time-bound and scientific approach to insolvency resolution with the goal of maximising value for all stakeholders and balancing knowledge asymmetry, while also protecting the interests of all parties involved.[3]

In 2000, the amount of NPAs grew rapidly. Banks made indiscriminate loans between 2008 and 2014, resulting in a high number of NPAs, as revealed by the RBI's Asset Quality Reviews, causing the government to act immediately. A Committee was formed, and its report, in which the IBC was recommended, was delivered in 2015.[4] Following that, a bill was introduced in the Lok Sabha and referred to a Parliamentary Joint Committee for examination. On May 5, 2016, the IBC was approved by both Houses of Parliament and received presidential assent on May 28, 2016.

India’s Economic Slowdown and Why the IBC Matters

According to official figures, the economic shock caused by the COVID-19-induced lockdown resulted in a 23.9% decline in India's Gross Domestic Product (GDP) in the first quarter of 2021. According to government estimates, GDP is expected to decline by 7.7% between 2020 and 2021.[5] While growth is expected to accelerate significantly in 2021, certain structural flaws in the economy must be addressed if the economy is to continue on a high growth trajectory for the foreseeable future. Among these issues is

1 A. Ogus, “Regulation: Legal Form and Economic Theory”, 1994.

2 A.V. Pavlova, “The Organizational and Legal Mechanism of Control of the Insolvency and Bankruptcy Institution as an Economic Growth Factor”, Studies on Russian Economic Development, Pleiades Publishing Ltd., 2008.

3 Balleisen Edward, “Vulture Capitalism In Antebellum America: The 1841 Federal Bankruptcy Act And The Exploitation Of Financial Distress”. Business History Review, Spring 1996, 473-516.

4 Belcher Alice, “Corporate Rescue”, Sweet & Maxwell, 1997.

5 World Bank, “Resolution of Financial Distress : An International Perspective on the Design of Bankruptcy Laws”, 2001, Bankruptcy Laws: Basic Economic Principles, Joseph E. Stiglitz.

the difficulty in resolving bankrupt businesses, which has resulted in an increase in the financial industry's NPAs. The fact that this has been a problem for over a decade has only exacerbated it. By September 2021, the RBI anticipates that gross NPAs in Indian banks will reach 13.5%. Solving the problem of NPA is critical to reviving the economy's credit growth.[6]

"The Indian economy had already begun to deteriorate prior to the shutdown, and the lockdown has strained the resilience of numerous Indian businesses as well as the country's financial infrastructure".

According to the Bureau of Economic Analysis, GDP growth slowed from 8.2% in 2016–17 to 5% in 2019–20. Despite government capital injections, NPAs represented 9.5% of total bank assets in 2019. Between 2011–12 and 2017–18, personal consumption expenditures per capita fell by an average of 3.7%.

While both "structural" and "cyclical explanations" have been advanced for the slowdown, economists Arvind Subramaniam and Josh Felman argue that "the slowdown is the result of long-standing macroeconomic issues that have not been resolved since the 2008 financial crisis, and thus is both cyclical and structural in nature". For the last decade, there has been a race between stimulus and stress. "Multiple doses of stimulus have kept the economy afloat, allowing for the resolution of the Twin Balance Sheet crisis as the economy recovers". However, because the majority of the legacy TBS problem remains unresolved, a second wave of problems has emerged - and stimulus funds have already run out."

The IBC's Incorporation

The Indian government recently established a new bankruptcy law that, among other things, makes it easier to close down failed businesses and collect debts in our country. As a result, I've sought to summarise how the "Insolvency and Bankruptcy Code", 2016, could help India become a more business-friendly country in the coming years.[7]

Numerous committee reports, "the most significant of which is the November 2015 report of the Bankruptcy Law Reforms Committee 326 were evaluated prior to the Insolvency and Bankruptcy Code, 2016, being adopted following careful consideration and in compliance with the code". The following is the code's statement of objects and justifications: There is no single statute in our country that governs insolvency and bankruptcy. Numerous statutes, including the Sick Industrial Companies (Special Provisions) Act (1985), the Recovery of Debt Due to Banks and Financial Institutions Act (1993), the Securitisation, Reconstruction of Financial Assets, and Enforcement of Security Interest Act (2002), and the Companies Act (2013), contain provisions governing business insolvency and bankruptcy in India. Along with the establishment of many forums, including the Board of Industrial and Financial Reconstruction (BIFR), the Debt Recovery Tribunal (DRT), and the National Company Law Tribunal (NCLT), these statutes also require the establishment of Appellate Tribunals for each of these forums.

[6] Janet P. Near, Marcia P. Miceli, "Organizational Dissidence: The case of Whistle blowing", Journal of Business Ethics, February 1985, pp. 1.

[7] Kumar V., "Major Issues In Non-Performing Assets Of Commercial Banks In India", International Journal of Applied Financial Management Perspectives", 2013, 2(3), 527.

"The High Courts are responsible for corporate liquidation. Individual bankruptcy and insolvency are governed by the Presidency Towns Insolvency Act of 1909 and the Provincial Insolvency Act of 1920", respectively, and are adjudicated by the courts. The current framework for insolvency and bankruptcy is weak, ineffective, and results in unduly lengthy adjudication times; as a result, the proposed legislation is necessary.[8]

Key Issues and Analysis of the Insolvency and Bankruptcy Code, 2016

A number of new firms will need to be formed in order to archive time-bound insolvency resolution. Additionally, given the dismal status of DRT pendency and disposal rates, their existing capacity may be unable to perform this additional task in the future. To achieve the code's objectives, a considerable overhaul of DRT infrastructure will be necessary, both in terms of physical facilities and human resources.[9]

The board will develop IPAs to control the functioning of IPs, which will be monitored and maintained by the board. Rather than enabling IPs and/or IPAs to self-regulate, the board has been charged with the responsibility of regulating their performance and establishing performance standards for these entities. In the vast majority of insolvency/liquidation cases, the government will be a party interested in collecting outstanding statutory dues owing by various government departments around the country. As a result, it will be more difficult for insolvency practitioners (whose entry and leave from the insolvency profession are governed by the government through the Board) to operate objectively[10].

A sizable number of qualified and skilled insolvency experts will be required to ensure the code's successful implementation. When it comes to building a large pool of insolvency professionals and the institutional structure that will generate and govern them, a strong anchor and a well-defined strategy are essential. Not only will such insolvency specialists need to understand the intricate distinctions and contrasts between various components of restructuring and liquidation, but they will also need to be able to manage the firm's affairs during the process.[11] Almost definitely, this endeavour will need a large investment of time, finances, and skill. Additionally, efforts should be made to ensure that such professionals are available throughout India, rather than just in high-profile cases in economic and commercial centres.

Impact of IBC on Indian Markets

> "It is not the strongest of the species that survives, nor the most intelligent, but the one most responsive to change."
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> - Charles Darwin

[8] Nidugala G.K., Pant A., "Lessons from NPA s crisis in Indian banks", Journal of Public Affairs, 2017, 17(4), e1672.
[9] Sengupta R., Sharma A., "Corporate Insolvency Resolution in India: Lessons from a cross-country comparison", 2016.
[10] Sethi M., Krishnakumar D., "Equity market reaction to regulatory reforms: a case study of Indian banks", Journal of Financial Regulation and Compliance, 2020.
[11] Tandon D., Tandon N.,. "Drifts in Banking Business and Deepening Losses Amidst the Insolvency and Bankruptcy Code, 2016", Business Governance and Society, Palgrave Macmillan, Cham, 2019, 143-160.

Charles Darwin's ideology, which encourages constant change for the sake of survival, is fit for both economic and ecological order. Economic stability is maintained by the careful calibration of macroeconomic policies and economic legislation that adjust to changing market dynamics and market conditions. Economic growth and prosperity-promoting government interventions, such as macroeconomic policy, are clearly the most visible sorts of government interventions. In the short run, policy debates are usually centred on these overt fiscal and monetary interventions meant to correct market failures and restore equilibrium. However, there is an increasing recognition that economic legislations, particularly those that set the quality of business regulations and act as 'enablers' of economic activity, are critical organs that contribute to the economy's strength, stability, and steady growth. These 'enablers' of economic progress contribute to the abolition of 'various kinds of unfreedoms (exclusion from opportunities)' that prevent people from exercising "their reasoned agency" in situations when these unfreedoms restrict their ability to exercise "their reasoned agency".[12]

One of these unfreedoms is the absence of an institutional and legal structure that enables firms to exit in the case of an honest business failure. To close this gap, a jurisdiction's insolvency and bankruptcy laws are employed.[13]

Insolvency and bankruptcy legislation's objective for insolvent entities is to ensure an orderly process for their reorganization or liquidation while also protecting creditors' interests. For instance, if a business becomes unviable as a result of economic collapse and is unable to be resurrected, it establishes a legal framework for its liquidation. On the other hand, it establishes a legal foundation for business dissolution. As an alternative, in the event of a financial failure of the firm, which implies that the firm is still operational, albeit in a stressed state, the process provides for a resolution mechanism through which the business can be resurrected in an entirely different form with a completely new or revamped management team.[14]

Conclusion

Deficiency in the Present Insolvency Regime

Deficiency in NCLT

It has been seen that the ordinary time essential to wind up an association subject to court-mentioned liquidation is over 10 years. The high court judge allotted to association cases can't sit reliably and consequently can't commit the significant investment critical to rapidly manage issues including the winding up of undertakings. The suggestion to draw in the Company Law Board (CLB) with legitimate ability to rehearse court ward was excused at this point in light of the CLB's shortfall of people, seats using any and all means of the extraordinary court regions, and establishment to deal with the assortment of methodology related with wrapping up issues. The continuous delays intrinsic in SICA (Sick Industrial Companies Act) rebuilding and multiplication frameworks are weakened generally by unfathomable maltreatment of the rules regulating the suspension of legal techniques, the recording of

[12] Tandon D., Tandon N., "Drifts in Banking Business and Deepening Losses Amidst the Insolvency and Bankruptcy Code, 2016", Business Governance and Society, Palgrave Macmillan, Cham., 2019, 143-160.

[13] Sengupta R., Sharma A. "Corporate Insolvency Resolution in India: Lessons from a cross-country comparison", 2016.

[14] Reserve Bank of India, "Resolution of Stressed Assets—Revised Framework", RBI/2017-18/131, Mumbai, 2018. https://www.rbi.org.in/scripts/BS_CircularIndexDisplay.aspx?Id=11218

suit, and the execution of legitimately restricting commitments. The Eradi Committee proposed a National Tribunal for business inquiries in 2000 considering the High Courts' shortfall of time, the CLBs' spoiling system, and the endemic deferrals at the Board for Industrial and Financial Reconstruction (BIFR).

The committee's proposition transformed into a reality in 2016 with the improvement of the NCLT.

The NCLT will hear and conclude any cases arising under the Companies Act, 2013. Additionally, it will hear cases brought before it under the Insolvency and Bankruptcy Code. The NCLT will be blamed for the commitment of moving all approaching cases from the High Courts, the CLB, the Debt Recovery Tribunal (DRT), and the BIFR to the as of late settled board. The NCLT is a singular substance that integrates the components of the CLB, BIFR and DRT. In any case, will it be prepared for conveying?

Legitimate counsels and various reasons for living voiced antagonism about what's to come. The CLB uncovered 4000 cases, however the BIFR declared 2000. There are 5,200 cases approaching under the watchful eye of the Supreme Court. DRTs were locked in with 15,000 occasions. This is the gigantic weight that the NCLT, which has 11 seats, the greatest of which is in New Delhi, would have to bear. The NCLT's introduction has been upsetting without anyone else. Tragically, the NCLT is pained by the bothers and issues experienced by the Company Law Board (CLB).

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