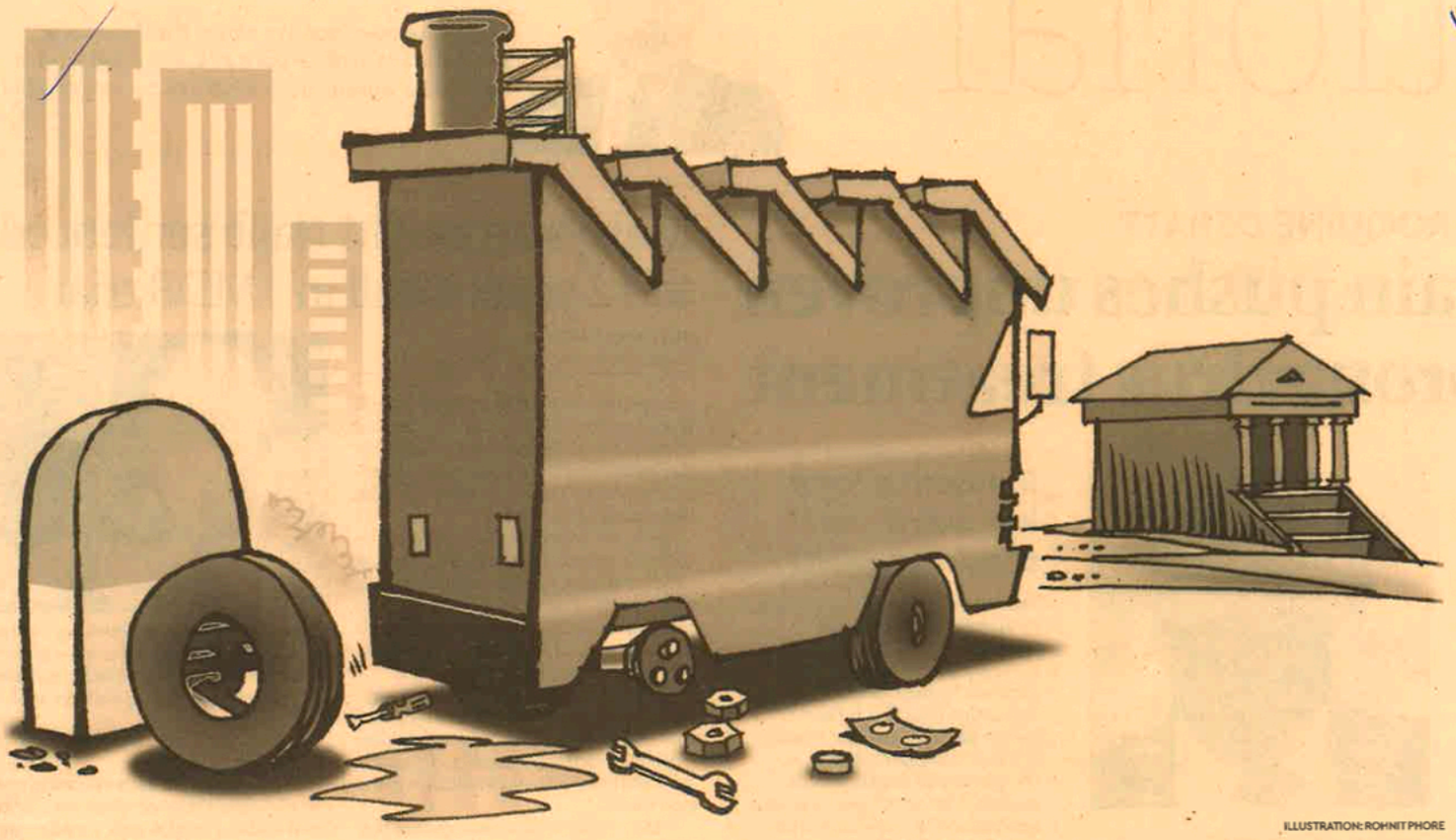

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● DISPUTE OVER RESOLUTION

# Urjit Patel's criticism of IBC changes is flawed

**The expectations from the IBC have not been fully met because it is not a panacea. But it has certainly made a difference by discernibly improving recovery**

FORMER RESERVE BANK OF India Governor Urjit Patel in his new book, *Overdraft: Saving the Indian Saver,* has severely criticised the government for diluting the Insolvency and Bankruptcy Code (IBC) and the powers of RBI. In fact, he went on to claim that this dilution made the insolvency regime "vulnerable and brittle". It had also delayed the process, helping many defaulters escape the bankruptcy court. The February 2018 circular, issued when Patel was Governor, had forced banks to classify borrowers as defaulters immediately and had brought several large defaulters to the National Company Law Tribunal (NCLT).

The amended sections 5 (12), 5 (15), 7, 11, 14, 16(1), 21 (2), 23 (1), 29 (A), 227, 239, 240 of IBC, 2016 and insertion of new section 32A were sought to realise objects of code, protect corporate debtors, prevent ill-thought triggering of bankruptcy proceedings and to further ease of doing business.

Patel's observations are fascinating reading. However, a comprehensive and objective analysis of the overall macroeconomic situation based on the data from RBI, World Bank, and Economic Survey clearly substantiate the thesis that Patel's arguments are flawed and not borne out by facts. Simply put, the resolution under IBC has been substantially higher as compared to other processes, as is indicated by data and analysis from sources, such as RBI reports, Economic Survey, and the World Bank's *Ease of Doing Business Report.* The report on *Trend and Progress of Banking in India 2018-19* clearly brings out that the amount recovered as a percentage of the amount involved in FY18 and FY19 has been much higher for IBC at 49.6% and 42.5%, respectively, as compared to Lok Adalats, DRTs etc. Further, most of the money recovered in case of Lok Adalats, DRTs etc. went towards legal expenses, such expenses formed a smaller proportion in the case of big-ticket IBC cases.

Similarly, the *Economic Survey* for FY20 demonstrated that the realisations under the IBC for financial creditors and time involved in this process was lesser than those under other available avenues for resolving distressed assets.

As per the *Ease of Doing Business Report 2020,* which assessed 190 economies over 10 parameters, India's overall ranking improved by 14 places to 63rd position among 190 countries. What is particularly significant is that in the 'resolving insolvency' parameter, India jumped 56 places to 52 this year from 108 last year. This success is strikingly reflected in the fact that the overall recovery rate for creditors jumped from 26.5 to 71.6 cents on the dollar and the time taken for resolving insolvency came down significantly from 4.3 years to 1.6 years.

Patel has blamed the striking down of the February 2018 circular. But it has to be realised that the February 2018 circular, which gave defaulting companies 180 days to agree on a resolution plan with lenders or be taken to the bankruptcy court to recover the debt of ₹2,000 crore and above, was quashed by order of the Supreme Court. A bench of Justice Rohinton Fali Nariman and Justice Vineet Saran pronounced the judgement saying that "we have declared the RBI circular *ultra vires*".

The order came as a relief to companies in stressed sectors, which had blamed extraneous reasons, such as, regulatory controls that capped prices. They had claimed that the circular treated them like wilful defaulters and narrowed the window within which a bad loan was to be resolved from 270 days as per the IBC to 180 days (plus a grace period of 15 days). The rationale behind the circular was that the revised framework would establish an ecosystem where NPAs would not only get recognised based on time but also see faster resolutions. The bankers were critical of the almost instant recognition of stress and the crippling rise in provisioning requirements and the devastating impact on profits and profitability. The industry was against the circular because of the timeline involved, and the possibility of losing control. While the ostensible objective was to reduce defaults and delinquencies and strengthen the banking sector over the long haul, this measure caused widespread pain and suffering in the short-term.

The sweeping nature of the February 2018 circular was also reflected in its imposition of a one-day default rule-a company was treated as a defaulter even if it missed one day of the repayment schedule. While this provision may have a strong theoretical basis, it was widely perceived to be unrealistic and had, therefore, caused concern and consternation among almost the entire development spectrum, viz, borrowers, banks and financial institutions and the government. Hence, the striking down the February 2018 circular was widely welcomed.

Even if it is hypothetically assumed that the February 2018 circular had a sound legal basis, Patel does not spell out options in the light of the Supreme Court judgement. Further, Patel may claim that the February 2018 circular, in its original *avatar*, may have a greater deterrent effect, but in view of its stringent provisions, it was vehemently criticised by multiple sections of the society.

Indeed, the expectations from the IBC have not been fully met because it is not a panacea. But it certainly made a difference to the ground realities and discernibly improved the recovery ethics and the overall ecosystem of recovery. We are required to strike a balance between the ideal and the practical and go for the second-best solutions. I am afraid that despite his wealth of qualifications and knowledge, Patel's actual field level banking experience in India, especially rural banking, MSME, etc. is not all that rich. Hence, Patel perhaps fails to appreciate the need to explore second-best solutions.