The Indian Insolvency and Bankruptcy Bill: Sixty Years in the Making

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Abstract

This research paper provides an analysis of the development of Bankruptcy and Insolvency laws in the post-independence period in India. Evolution of the regulatory framework and significant changes in regulations are temporally analysed in the context of political realities. The paper identifies critical shortcomings in individual laws and discusses the lack of harmonisation. The role of a weak framework for insolvency and bankruptcy in promoting a bank-oriented economy is discussed. The paper summarizes,using empirical data, the impact of inefficient and inadequate insolvency framework on resolution timelines and recovery rate. Author analyses the recently passed Insolvency and Bankruptcy Bill and concludesthat the Bill in its current form encourages liquidation at the cost of financial restructuring. An opinion is expressed that the Bill fails to provide adequate representation to all stakeholders. The paper highlights a lack of clarity in the Bill regarding appointment of executants. Certain other lacunae in the Bill impeding its overall effectiveness are also identified. The author draws upon cross-country experiences to suggest remedial measures that address impediments in the successful implementation of the Bill.

Keywords: Indian Insolvency and Bankruptcy Bill, Bankruptcy law reforms, SARFAESI Act, DRT, Harmonisation, Forum shopping, Bank-oriented economy.

1. Introduction

In an environment where the present NDA government in India has failed to get key bills approved in the Upper House of Parliament, it is saddening to note that the government has lost an opportunity in the recently passed Insolvency and Bankruptcy Bill (the "Bill"). This Bill was one of a small number of legislations where the government was able to build political consensus and muster enough votes to ensure safe passage.

This paper provides an analysis of Indian Bankruptcy and Insolvency laws in the post-independence period, identifies critical shortcomings in individual laws, summarizes the impact of inefficient and inadequate insolvency framework on resolution outcomes in the past, and identifies critical shortcomings that remain in the new Bill. The paper is structured as follows. In section 2, I analyse constitutional locus for insolvency and bankruptcy, comment upon economic and political circumstances that existed from 1947-2000 affecting evolution of governance framework, and analyse the changes in insolvency and bankruptcy laws after Indian independence till the year 2015. Section 3 summarizes select empirical data on bankruptcy resolution timelines and procedural delays under different regulatory frameworks. In section 4, I posit my concerns with the new Bill. I conclude this paper in section 5 recommending amendments to the recent Bill and highlighting key expectations of different stakeholders.

2. Historical developments in regulatory and legal framework

As the first step towards understanding the eventual effectiveness of the new Bill, it is imperative to analyse the legislative history and understand past efficacy of bankruptcy and insolvency frameworks in India. Bankruptcy and insolvency are not synonyms - rather bankruptcy is an outcome of being insolvent. In plain English, insolvency means inability to pay a debt. A concise legal definition of insolvency is insufficiency (of an individual or a corporate) to discharge all enforceable debts. Bankruptcy, on the other hand, is a legal process for resolving insolvency. It is a legal declaration of an individual or a corporate, averring its inability to pay a debt that is due as of today, triggering a resolution process in accordance with jurisdiction's regulatory framework.

Insolvency and Bankruptcy is entry covered in the seventh schedule under concurrent list in the Indian Constitution, allowing both State and Central Governments to develop the legislative framework. The concurrent list is a vital element of the Indian

Constitution in ensuring the robustness of federalism. Both Parliament and the State Legislatures have the authority to legislate on the matters covered in the concurrent list. Dual control on certain subject matters was first envisaged in The Government of India Act, 1935. The constitutional position in India on concurrent power for the States and Union in dealing with insolvency and bankruptcy is similar to United States (Sarkaria et al, 1988). In the United States, insolvency laws are generally the subject matter of the State but once a bankruptcy process is initiated to resolve insolvency, only federal laws are applicable (Goldberg, 1927 and Ponoroff, 2015). However, in India, there is no state legislative history regarding either insolvency or bankruptcy in the post-independence period and the subject matter was left entirely to Parliament. Article 19 (1)(g) of the Constitution of India provides freedom to undertake any industrial activity but such freedom can be restricted by the State using other adjunct clauses, article 19 (6) . The government has created both entry and exit restrictions, and has imposed various conditions that need to be fulfilled prior to the dissolution of trade or business.

In the initial years after independence (1947-1980), government policy was focused on reducing disparity across sections of society. Consequently, India adopted a distinctly redistributive model of economics. Government's focus was on labour-intensive industrialization sponsored by the public sector enterprises. Foreign capital investment was discouraged and government's control on the key sectors was considered essential. The legal provisions outlined in the Industries Development and Regulation Act, 1951 formed the basis of 'who can produce what'. The draconian state laws and requirement of state license for industrial production severely restrained the development of a free market economy. In the absence of free markets, A limited number of private sector enterprises, enjoyed virtual monopoly and were inefficient users of available resources. This inefficient allocation of capital and labour resulted in a situation where many units were making losses and their net worth was significantly eroded. Early signs of resentment amongst intellectuals on the efficacy of the socialist democratic setup and the need for an alternative economic policy framework started appearing since 1960. They demanded opportunities of promotion, uninfluenced by pull and favouritism, and the abolition of private monopoly to achieve true economic freedom (Mehta, 1964). Industrial production was significantly reduced in both state and private enterprises, and workmen were laid off. By early 1980s, the government started prioritizing economic growth at the cost of redistribution (Sen, 2009). Kohli (2012) assigns this complex political shift to several underlying political realities including a growing realization that redistributive possibilities were increasingly limited, the negative impact that radical rhetoric had had on the corporate sector's willingness to invest, and low industrial growth during the 1970s. In the 1990s, severely impacted by a 'Balance of Payment' crisis, India embarked on a path of economic liberalization. Gradual reforms were introduced in foreign direct investment and the labour sector. India has been continuing on the said path since then.

Historical developments in the regulatory and legal framework for dealing with insolvency and bankruptcy have been significantly influenced by the socio-political milieu and evolving economic realities. The key developments in Indian regulatory and legal framework across the three distinct developmental phases are summarized below.

2.1 Evolution of regulatory framework and subsequent developments between 1947 and 1990

Till the year 1985, the legal framework for dealing with corporate insolvency and bankruptcy consisted of only one law - The Companies Act, 1956. The Companies Act was based on recommendations of Bhabha Committee that was set up in the year 1950 and submitted its report in the year 1952. Personal bankruptcy was adjudicated by two archaic laws - The Presidency Towns Insolvency Act, 1909 and The Provisional Insolvency Act, 1920. The former relates to individuals residing in the erstwhile presidency towns of Calcutta, Bombay and Madras. The latter covers all other individuals. Section 425 of the Companies Act provided a base framework for involuntary dissolution (compulsory winding up as defined in the Act) as well as voluntary dissolution. Various other sections including Sections 433, 443, 444, 455, 463, 466, 481' and 488 contained detailed procedures for the resolution process. Despite several sections addressing the resolution process, the original Act of 1956 was incapable of dealing with corporate insolvencies. The Act failed to provide any provision either for the inclusion of insolvency cost or for super- priority of insolvency cost. It relegated most matters to courts, which in turn, relegated the due process to an official liquidator, generally a legal professional appointed by the court with an extremely limited understanding of the company's business. Inexperienced liquidators, with limited knowledge of technology, auction theory, organizational behaviour and financial engineering, affected prolonged resolution timelines and suboptimal recovery for the benefit of creditors and workmen. The prospect of subpar recovery in a very distant future dissuaded affected parties from initiating dissolution proceedings under Companies Act (Patwari, 2014). The power to adjudicate on merits of dissolution was assigned solely to the judiciary (jurisdictional High Courts) by Companies Act but the courts were not provided with any legislative framework to assess merits. Lack of a supporting legislative framework resulted in a deranged legal process with each High Court interpreting individual cases differently and promulgating orders, often contrary to another High Court.

In the 1980s, industrial sickness was reaching alarming propositions in many parts of India, accompanied by massive downsizing (Sen, 2009). Government's effort towards the interim management of sick industrial units and nationalizing sick industries proved futile. Workmen's dues were mounting, loan recovery was anaemic and unemployment was going up. The provisions of Companies Act 1956 were proving inadequate as explained earlier. It was in this context that the first legislative action to deal with insolvency and bankruptcy was promulgated in the form of The Sick Industrial Companies Act, 1985 ("SICA"). SICA was an end product of reports by various committees appointed by the Government and the Reserve Bank of India since 1975. These included Tandon Committee of 1975, Rai Committee of 1976 and Tiwari Committee of 1981. Under SICA, a sick industry was defined as an industrial company with five years of history whose net worth is zero or negative, having 50 or more workers and established in accordance with Industrial and Dispute Act, 1951. SICA allowed companies to make a reference to a quasi-judicial body called Board for Industrial and Financial Reconstruction ("BIFR"). BIFR adjudicated the reference in the presence of the company and creditors. An appellate authority was also instituted in the form of Appellate Authority for Industrial and Financial Reconstruction ("AAIFR"). For the first time, SICA allowed companies in distress to propose a restructuring package in the form of Draft Rehabilitation Scheme under the aegis of an operating agency. Unfortunately, SICA had several shortcomings, and abuse of Section 22 of SICA is often highlighted as an example of the inherent deficiency in its provisions. Section 22 allowed companies to seek a bar on proceedings for execution, arbitration, recovery suits, enforcement of security interest etc. and was often misused by unscrupulous promoters. Further, delay in completion of the inquiry and delay in sanctioning of the scheme, and inadequacy of powers vested with BIFR and AAIFR to expedite the process, made matters worse (Ravi, 2015).

2.2 Developments after 1990 till 2010

The reform process for legal framework related to insolvency and bankruptcy in the 1990s started with the introduction of The Recovery of Debts Due to Banks and Financial Institutions Act, 1993 ("RDDBI"). RDDBI Act was influenced by the findings of the Goswami Committee that was working on proposed improvements to the regulatory framework for insolvency and bankruptcy. SICA was proving to be a bottleneck for creditors in recovering dues from promoters with spurious designs and financial institutions were facing inordinate delays in securing a final decree from courts on civil suits. Goswami Committee report in its preamble ruefully said, "There are sick companies, sick banks, ailing financial institutions and unpaid workers. But there are hardly any sick promoters. Therein lies the heart of the matter." In order to expedite the recovery process, RDDBI was enacted with provisions allowing Banks to file an application before a specially constituted Debt Recovery Tribunal ("DRT") asking for a 'Certificate of Recovery'. Certificate of Recovery had the same effect and standing as a Decree of a Civil Court. RDDBI Act failed to make any improvements in the muddled insolvency landscape, primarily due to the fact that SICA had precedence over RDDBI. If a case was pending before BIFR, DRTs were incapable of issuing a certificate of recovery. In addition, DRTs lacked powers for considering rehabilitation or dissolution and were therefore a venue of the last choice with promoters who blatantly indulged in 'Forum Shopping' to suit their personal interests. Finally, DRTs were found to be overburdened with a large number of pending cases (Unny, 2011). Considering these impediments and with the intent to expedite resolution of non-performing assets, the Government introduced a new legislation called The Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act (SARFAESI) in 2002. The SARFAESI Act provided a legal mechanism for expedited recovery of secured assets through empowering Banks and Financial Institutions to recover their non-performing assets without intervention of the court. Though SARFAESI did expedite the recovery process to some extent, its effect was limited to secured assets. In addition, similar to RDDBI, SARFAESI lacked any powers or provisions for considering restructuring and reorganization. Lastly, there were multiple instances where SARFAESI and RDDBI exercised parallel jurisdictions, leading to a complete confusion on primacy (Kang et al, 2004) and 'Forum Shopping'. The constitutionality of SARFAESI and certain definitions contained therein were challenged vigorously by debtors and the challenges were resolved to finality much later in 2014 by the Supreme Court.

Around the same time when SARFAESI Act was introduced, Reserve Bank of India introduced a Corporate Debt Restructuring Scheme ("CDR Scheme") that provided broad guidelines for debt restructuring by Banks. The CDR Scheme, first introduced in 2001, was amended multiple times over the next fifteen years and became a working document rather than a statute. In parallel, various committees were evaluating true efficacy of company laws and suggesting amendments to effectively tackle insolvency and bankruptcy. The first comprehensive report in this regard was presented by Sachar Committee in the year 1987 that resulted in a major amendment to Company Act in 1988. The government introduced two additional amendments in 1993 and 1997, but failed to achieve the majority required for passage of these amendments. In 2000, Eradi Committee submitted its report for amendments in the Companies Act to address insolvency situations. The Company Act was amended in 2002 incorporating some of its recommendations. This was followed by Chandra Committee report in 2002 and Irani Committee report in 2005 that resulted in another amendment in 2006. The incremental nature of improvements, significant changes in other regulations that impact Company Act without an amendment to Company Act, and slow implementation of changes enacted by amendments have resulted in slow progress of reforms.

2.3 Developments after 2010

It was clear by the year 2010 that a single, comprehensive framework is needed to effectively tackle delay in insolvency and bankruptcy proceedings. The process for a comprehensive bankruptcy reform was initiated with the setting up of Financial Sector Legislative Reforms Commission, led by Justice Srikrishna in 2011. In 2014, the Ministry of Finance instituted the Bankruptcy Legislative Reforms Committee, led by T. K. Viswanathan. The Viswanathan committee submitted a two-volume report in 2015. The economic rationale and design features of a new legislative framework were covered in the first volume and the draft bill was laid out in the second volume. A modified version of this bill, incorporating public comments, was tabled in Parliament in late 2015. After the bill was tabled, a Joint Parliamentary Committee was set up and the Joint Parliamentary Committee submitted its report which included a new draft of the law that was passed in the form of the current Bill.

In summary, the legal and regulatory framework for dealing with insolvency and bankruptcy situations was grossly inadequate from 1947 until the recent introduction of the new Bill. There were interventions made by the Government during this period, but these interventions failed to bring the desired results due to the existence of multiple laws and lack of harmonisation of various regulations. An inadequate environment for dealing with insolvency resulted in the development of a bank-oriented economy in India. The reliance of firms on other market-based funding options was extremely limited in India unlike developed countries (Samuel, 1996). Capital markets were wary of the ever-changing regulatory regime, the impact of new laws on the recovery of debt and enforceability of security interests. Hence, there was extremely limited participation of private players in the corporate debt space and lending activity was largely controlled by Public Sector Banks. Absence of free market competition in the corporate debt market resulted in massive mispricing of individual debtor risk which has culminated in the form of high NPAs (Citation 1 - redacted).

3. Empirical Analysis

As explained in Section 2, the first act dealing with insolvency and bankruptcy was SICA which referred companies to BIFR. An analysis of BIFR data since

1987 shows a decreasing trend in new cases. In the first year for which data is available from BIFR, 311 companies were referred to BIFR. From an empirical analysis conducted at a five-year interval and for a 29 year period, it is seen that the number of companies being referred to BIFR peaked in 2002, the count of such companies being 559. By 2005, the number of companies seeking reference to BIFR came down to approximately 80 companies per year (see Table 1). The data clearly establishes that abuse of BIFR provisions came down significantly after the introduction of SARFAESI Act. Data also validates that the introduction of RDDBI Act had no impact on the attractiveness and misuse of the BIFR forum. Data available from Eradi Committee findings clearly highlights the lack of success of SICA. The success rate of companies referred to BIFR was only 19%. In addition, 65 cases out of total 962 cases referred to BIFR between 1987 and 1990 were pending for more than 10 years as of June 2000 (see Table 2). The ineffective Company Act caused inordinate delays in winding up a company. The data based on all pending cases as of March 1999 shows that 33% of cases were pending for more than 15 years (see Table 3). The cases referred to DRT under RDBBI Act suffered a similar fate. The recovery percentage of cases adjudicated by DRT was an abysmal 16% and approximately 70,000 cases were pending with DRT as of March 2014 (see Table 4). The recovery percentage of insolvency cases administered through SARFAESI Act was marginally better at 25%, based on an empirical study conducted over a three- year period (see Table 5). The findings from the empirical study clearly establish the inefficacy of the then extant legal and regulatory framework, including SICA Act, Companies Act, RDDBI Act and SARFAESI Act. The average time to resolve an insolvency proceeding in India, 4.3 years, was far higher than the time taken in developed economies (see Table 6). In fact, in a World Bank study, India ranked 186th on the list of 200 nations where data was available (see Table 7). All the above data points validate the hypothesis that the legal and regulatory framework for addressing insolvency and bankruptcy were grossly ineffective during the study period.

4. Concerns with the current Bill

It was imperative in such a background that a comprehensive and effective single framework is promulgated, safeguarding the interests of all stakeholders. The current insolvency Bill, despite its long drafting history, falls woefully short on the following six counts.

4.1 Liquidation Preference

The new Bill has a marked preference to liquidations versus reorganization, thereby defeating the stated objective of maximizing asset value. The Bill mandates that a specialized personnel should be appointed to manage insolvency resolution process completes this exercise within 180 days. The timeframe of six months (or nine months including an extension) is grossly inadequate to prepare a robust revival plan that is agreed upon by a super-majority of creditors. Even in developed economies like the United States, with experience of tackling economic, harmonisation and legislative challenges involved in the bankruptcy process for over thirty years, an eighteen months period is provided to evaluate the viability of corporate restructuring and reorganization. Such an arbitrarily decided resolution period of six months, without any consideration to the size of a firm, its recent financial performance, asset coverage, the number of creditor claims or severity of default, will lead to hastily arranged liquidation proceedings, resulting in significant impairment of intrinsic enterprise value.

It is also important to consider that the Indian economy is still largely a 'bank-oriented economy' rather than a 'market-oriented economy', and a large amount of corporate debt is owned by Banks. In a market-oriented economy, creditors often have the option to participate in the liquidation process, thus ensuring optimal price discovery and arresting transfer of value. It is extremely unlikely, given the current regulatory and accounting environment for banks, that banks will be able to bid for liquidated assets. In a fire-sale liquidation process, the value will be appropriated by vulture firms from Banks (and ultimately taxpayers). Aghion et al. (1992) question the conclusion that a competitive auction will inevitably lead a firm to be sold at the highest price. They posit that auctions work well if raising cash for bids is easy and there is plenty of competition among several well-informed bidders. However, even in the most advanced Western economies, these conditions will often not be met, and they believe that such conditions are even less likely to be satisfied in developing economies like Eastern Europe. If research findings of Aghion et al., hold true, Public Sector Banks, unsecured creditors, workmen and minority shareholders will suffer the most in liquidation via cash-auction approach.

4.2 Limited or No Representation to Key Stakeholders

Workmen and operational creditors do not enjoy the same status as financial creditors in the new Bill. In the event of an alleged default, the financial creditor can initiate insolvency proceedings without intimation to the debtor. In a similar instance, an operational creditor is required to deliver a demand notice and a corporate debtor can stall the insolvency proceeding by merely disputing the veracity of such claim. It is almost certain that a debtor will dispute the legitimacy of a claim when facing the spectre of insolvency proceedings, and consequently operational creditors (typically micro and small enterprises lacking financial and legal wherewithal) will continue to suffer inordinate delays in the recovery process.

Workmen have no representation in the insolvency resolution process and are at the mercy of a creditors committee with disparate interests. Workmen dues are prioritized only for a period of twenty-four months. Wages and dues of contract workers are prioritized for an even smaller period of twelve months. The Bill assumes that financial creditors, who may very well be secured creditors with sufficient asset cover and no risk exposure, are the only appropriate decision makers for creditors committee. This inaccurate assumption may lead to adverse consequences for workmen. The challenge faced by displaced workmen, particularly those who have attained a certain age and will find reskilling challenging, has not received any consideration in the Bill. Graham et al. (2013), using data from the Census Bureau's Longitudinal Employer Household Dynamics Program, suggest that one year after bankruptcy, the magnitude of the decline in annual wages is 30% of pre-bankruptcy wages. The principle of equity would mandate that a weaker stakeholder is offered more protection by law than a stronger stakeholder, but the Bill embodies a contrary rationale.

The Bill envisages an extremely limited role of the Government in ensuring a fair and orderly resolution process. In the United States, the U.S. trustee plays a major role in monitoring the progress of a bankruptcy case and supervising its administration. The confidence of market participants in the integrity and transparency of the bankruptcy process is extremely essential for a well-functioning equity and debt capital market. La Porta et al. (1997), in their seminal work on inter-linkage between law and capital structure, have underlined the importance of shareholder and creditor rights in influencing the development of financial systems and establishing funding preferences for a country. Undue favouritism shown by laws, to either creditor or equity participant, can artificially skew the financing preferences and raise the overall cost of capital for businesses. Finally, limited participation of union and state governments in the bankruptcy process and creditors committee is even more questionable when their claims from the liquidation estate are prioritized below claims of unsecured creditors. Recent cases in India provide enough evidence that defaulting firms often fail to remit their statutory dues and taxes for an extended period prior to default. The absence of active government participation in creditors committee will definitely hamper the ability to recover the maximum possible amount for taxpayers' benefit.

4.3 Qualifications for Key Executants Envisaged by Bill

The key executants to manage insolvency process as envisaged in the Bill are an Insolvency Resolution Professional ("IPR") and a Liquidator. IPR is responsible for managing the company, appointing and coordinating creditors committee proceedings, entering into contracts on the behalf of the company, securing interim financing for the company and completing many other critical tasks with substantial financial and strategic implications. It is glaring therefore that the Bill does not specify minimum qualifications necessary for the appointment of Insolvency Resolution Professional ("IPR"). The lack of minimum qualifications or past experience becomes critically important as IPRs can be nominated by either a creditor or a corporate debtor. Lack of clarity on qualifications necessary for IPR appointment may lead to the appointment of IPRs with vested interests or IPRs who are in cahoots with the creditor or corporate defaulter. Since IPRs assume the role of management at the commencement of insolvency proceedings, it is absolutely essential that IPRs have character and qualifications that ensure impartial attention to the interest of all stakeholders and not only the financial creditors or corporate debtor. Claessens and Clapper (2002) suggest that in a market-based economy, creditors benefit more from the aspects of bankruptcy law aiming to overcome collective action problems among creditors. They also suggest that there may be more scope for conflicts between the role of banks as creditors and equity holders in a bank-based system. Their research findings support my case for the appointment of an able and impartial IPR to ensure an impartial and efficient bankruptcy resolution process.

The Bill does not mandate any past experience or minimum recovery criteria for appointment as Liquidator. A capable liquidator can make the correct decisions regarding quantum of asset sale (bulk sale or smaller packages), sale strategy (private versus public), auction technique and bidding mechanism (English Auction versus Dutch Auction, fixed versus moving bid increments) etc. and maximize proceeds for the liquidation estate. Liquidator's experience and expertise in managing complex liquidation process by structuring appropriate disposal strategy is critical for the success of the bankruptcy process.

4.4 Minimum Threshold for Default Amount

The Bill does not specify any minimum threshold for defaulted debt, either as a percentage of total debt or otherwise. This can result in a situation where a financial creditor commences insolvency proceedings even if less than one percentage of total obligations of the corporate are in default. It is also disconcerting to note that the Bill allows a financial creditor to commence insolvency proceedings even if the debtor is making regular payment on his debt, but has defaulted on the debt availed from another creditor. This incongruity is particularly problematic in instances where the debtor has secured a waiver from the creditor who is directly impacted by the debt default. It is customary to have a minimum threshold clause in debt covenants along with a cure period provision in cross-default situations. The Bill in its current form allows debtors to override such provisions and create nuisance value of catastrophic magnitude for the debtor and its shareholders. A debtor against whom insolvency proceedings have publicly commenced will face massive challenges in running its enterprise in 'ordinary course'. The firm's ability to secure any new financing will be impaired, its ability to secure goods and services from suppliers will be curtailed, the morale of employees will be adversely impacted, prospective buyers will delay or cancel their planned purchase, and the loss of goodwill in the marketplace will have prolonged repercussions. Eckbo and Thorburn (2009) rightly opine that a poorly designed code exacerbates rather than attenuates costly conflicts among security-holders, and risks destroying company value by misallocating control over corporate resources. Considering such grave consequences, it is shocking to note that the Bill fails to include a minimum threshold amount.

4.5 Disclosure of Interest and Intent of committee members and other executants

The Bill does not mandate that creditors forming part of creditors committee and IPR disclose their interests and intent to other committee members and debtor. Bankruptcy laws in many developed nations demand full disclosure of all instances that may give rise to actual or potential conflicts of interest. The fact that committee members may have a conflict of interest can result in lack of adequate representation of all stakeholders. Committee members with conflicted interest may dominate the committee proceedings and entertain high-risk strategies at the cost of other stakeholders. Harner and Griffin (2011), based on their study of 296 chaptereleven bankruptcy cases in the United States, suggested that cases with single creditor committee are more likely to result in a plan of liquidation. These cases were also more likely to provide distributions of less than fifty percent of claim value to unsecured creditors.

4.6 Fraudulent Asset Conveyance

The Bill fails to adequately address fraudulent conveyance of assets and does not bring cross-border assets of defaulters within its ambit. The "look back" period for fraudulent conveyance is limited to one year for unrelated parties and two years for related parties. Keeping in mind our recent experience with wilful default in case of more than 3000 accounts (see Table 8), clearly establishing the premise that business failures and bankruptcies are often planned events In India, a longer look back period is needed. Liquidator and Trustee have neither been mandated nor empowered to look for cross-border assets of defaulting parties, thereby impeding full recovery potential for stakeholders.

5. Conclusion

Bankruptcy Law is an important tool for a well-functioning society and an ideal bankruptcy process must provide justice to all stakeholders. Distribution of claims needs to be impartial for all stakeholders including creditors, workmen, taxpayer and the debtor. A hasty liquidation of an enterprise with long-term economic viability, especially when liabilities exceed assets, will lead to losses for both secured creditors and unsecured creditors. Reorganization in such instances can generate future cash-flows that will inure creditors, protect workmen employment, and generate tax revenue for the government. At the same time, creditors need to be protected from sinister designs of fraudulent promoters that often 'plan' bankruptcy at the outset and blatantly indulge in asset stripping. A balanced regulatory and legal framework for dealing with insolvency and bankruptcy will lead to the development of a robust capital market with participation from both private and public enterprises (Antoniou et al, 2008). Risk will be accurately priced and firms will be able to decide on their funding preferences (equity, debt or a combination thereof) in an optimal manner.

The historical performance of bankruptcy and insolvency laws in India has been spotty. Liberalisation of the economy towards a free market is not possible without an effective framework dealing with insolvency and bankruptcy. The recent Bill is indeed a significant step in this direction. However, the Bill in its current form has some serious lacunae and is unlikely to meet the desired objective of balancing the interests of all stakeholders and maximization of debt recovery.

Government needs to address these shortcomings in the Bill on priority, by way of an amendment. The timeframe for resolution plan approval needs to be significantly extended from the current 180 days. The revised timeline should not be similar across defaulting firms and must incorporate a classification based on total assets, the severity of default and number of creditor claims. Creditors committee should have mandatory representation from employees. The bonafide of any disputes regarding claim of an operational creditor should be established by Adjudicating Authority. Union Government should take active part in the insolvency proceedings and protect the integrity of the bankruptcy resolution process by instituting a program similar to The United States Trustee Program. Detailed criteria, including minimum qualifications, need to be laid down for the appointment of key executants like IPRs and Liquidators. Government needs to specify a minimum threshold of default amount that will trigger initiation of insolvency proceedings. Members of creditors committee and other external executants should be mandated to provide a sworn declaration clearly specifying their interests, and perceived or real conflicts that may arise from their participation in the process. The rules and procedures regarding fraudulent conveyance of assets need to be strengthened. Finally, a mechanism for ascertaining cross-border assets needs to be incorporated.

The eventual effectiveness of the Bill will be judged based on the soundness of the proposed resolution process, harmonisation amongst its various provisions and future empirical results. In the absence of the above- suggested amendments, the Bill will fail to increase ease of doing business, will not accelerate GDP growth as contemplated, and will only result in higher cost of equity capital for businesses.

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Endnotes

i The Bill was passed by Rajya Sabha, Upper House of Indian Parliament on May 11, 2016.

ii Article 19(1) in The Constitution of India 1949 - All citizens shall have the right…..(g) to practise any profession, or to carry on any occupation, trade or business.

iii Nothing in sub clause (g) of the said clause shall affect the operation of any existing law in so far as it imposes, or prevent the State from making any law imposing, in the interests of the general public, reasonable restrictions on the exercise of the right conferred by the said sub clause.

iv Reserve Bank of India is India's Central Bank responsible for monetary policy and financial stability.

v Judgment of the Supreme Court in Harsh Govardhan Sondagar v. International Assets Reconstruction Company Ltd., (2014) 6 SCC 1.

vi The Bill mandates that all decisions of the committee of creditors shall be taken by a vote of not less than seventy-five per cent of voting share of the financial creditors.

vii The current United States bankruptcy code was enacted in 1978 which generally became effective on October 1, 1979. The current code completely replaced the former Bankruptcy Act of 1898, also referred as Nelson Act.

viii Refer 11 USC § 1121(b) of US Bankruptcy Code.

ix Bankruptcy Factsheet - US Department of Justice, https://www.justice.gov/ust/bankruptcy-fact-sheets/us- trustees-role-chapter-11-bankruptcy-cases.

x Refer Karnataka High Court Judgment in Kingfisher Airlines v/s CIT, ITA No. 165 of 2012.

xi Rule 2019(a) of the Federal Rules of Bankruptcy Procedure in United States provides that any entity or committee representing more than one creditor or equity security holder and, unless otherwise directed by the court, every indenture trustee, must file a verified statement with the court disclosing their interest.

xii A chapter of the US Bankruptcy Code that provides for reorganization, usually involving a corporation or partnership. A chapter 11 debtor usually proposes a plan of reorganization to keep its business alive and pay creditors over time.

xiii Adjudicating Authority in the Bill means National Company Law Tribunal constituted under Section 408 of the Companies Act, 2013.

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