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Estimating the potential number of personal insolvency cases at the DRT

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by Renuka Sane.

The Insolvency and Bankruptcy Board of India (IBBI) has recently proposed regulations that would bring into effect the personal insolvency sections in the Insolvency and Bankruptcy Code (IBC). These are to be initially applicable for guarantors and small businesses, and over the next few years, be applicable to all individuals. Under the IBC, Debt Recovery Tribunals (DRTs), that were established for adjudication and recovery of debts due to banks and financial institutions, are designated to be the adjudicating authority for personal insolvency.

This article examines the likely load on DRTs due to the notification of personal insolvency sections of the IBC by asking
three questions with respect to personal loans from the banking channel in India:

- What is the spread of personal loans across districts in India?
- How many cases are likely to emerge on account of defaults?
- How well prepared are the DRTs to handle these cases?

The article focuses only on personal loans for two reasons. First, data on bank loans is one of the only reliable sources of public data on individual borrowing. Data on borrowing from other sources is not easily available. Second, there is no ambiguity about personal loans being taken by individuals. Other categories of loans (such as retailers, industry, transport operators etc) may or may not be individuals. The estimates, therefore, are conservative. They exclude loans given by banks to individuals which are not classified as personal loans. They also exclude other formal and informal loans that individuals may have taken from sources such as NBFCs, micro-finance and others.

The question on DRT preparedness also narrowly focuses on the presence of the DRT in a particular district, and the expected case-load where DRTs are present. Questions on procedural efficiency at DRTs, as well as optimal judge strength will also be important, as will be the interaction between the resolution professionals and the DRTs.

Data

Data on credit outstanding is sourced from Table 5.9, Basic Statistical Returns of Scheduled Commercial Banks in India - Volume 45, March 2016, Reserve Bank of India. Personal loans are divided into three categories - loans used for housing, loans used for the purchase of consumer durables and loans for other reasons. Among these, it is likely that loans for housing and consumer durables are secured loans. Table 1 shows the summary statistics for the district-wise spread of outstanding personal loans and the number of accounts as of March, 2016.

Table 1: District wise outstanding accounts for personal loans (RBI, 2016)

	Min	Median	Mean	Max
Outstanding personal loans (in Rs. billions)	0.062	5.2	21.2	953.8
Outstanding personal loans accounts (in 000)	0.27	23.9	85.7	3949.6

The maximum credit outstanding in a district was INR 954 billion in 3.9 million accounts. The data also suggests that the spread of loans is not normally distributed, that is, there exist a few districts with very high outstanding personal loans (in terms of both, value and number of accounts).

Personal loans across India

An understanding of total credit outstanding in each district would be extremely important from the point of view of the impact of personal loans (and defaults on these loans) on the banking system. However, the question of interest is the number of potential insolvencies from the point of view of the DRTs. It is, therefore, more important to focus on the number of loan accounts, than the value of credit outstanding.

For example, if we have two districts with the same value of credit outstanding, but one district has twice as many loan accounts as the other district, the number of default cases are likely to be higher in the first district if one assumes similar rates of default. While it is true that if one DRT sees fewer cases of higher value, while the other sees larger number of cases of lower value, then the staffing, technology and expertise required in the two DRTs is likely to be different. However, from a pure case-load point of view, the number of potential defaults is the statistic of first-order importance.

Figure 1 shows the total number of personal loans outstanding by districts. The darker shaded districts have higher number of personal loan accounts. The yellow dots represent DRT locations.

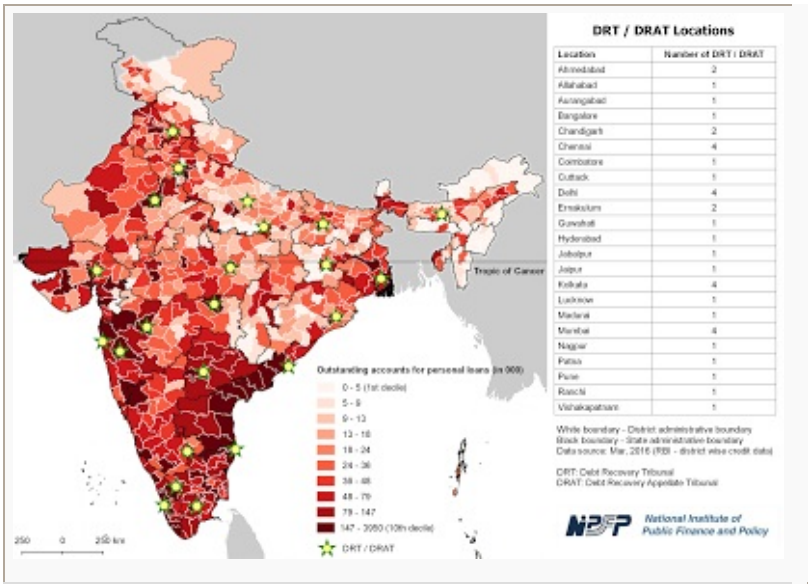

Figure 1: Number of accounts - outstanding personal loans

There is wide variation in the distribution of number of accounts across India. Though the map for credit outstanding is not presented, the variation is similar to that of number of accounts. The DRTs are located in regions with high number of personal loans. However, there are several districts in South and East India that have a large number of loan accounts, but do not have a DRT in their district. Similarly districts in Kutch, Rajasthan, Punjab also do not have a DRT.

If we focus only on the top 10% of districts by total number of personal loans, we end up with 63 districts. The median number of loan accounts in these 63 districts is 233,807 while the average number of accounts is 561,436. Of the 63 districts, almost 70% districts do not have a DRT. However, the top 10 districts in these 63 account for 62% of the total number of accounts, while the top 20 account for 74% of the total accounts. Of the top 10, two districts do not have a DRT. Of the top 20, seven do not have a DRT. From the narrow point of view of presence of DRTs, the situation is perhaps not that bad, as districts with a high concentration of loan accounts (barring the seven in the top 20) do have a DRT.

The absence of DRTs becomes prominent as we move to districts in the lower deciles. Even though the number of loan accounts in these districts may be low, borrowers will need some mechanism to be able to access the DRTs if they are to avail the provisions of the IBC.

Expected case load

Total number of accounts give us a stock of debt at a particular point in time. Not all loans will undergo default, and not all loans that undergo default will come to the IBC to get resolved. To arrive at a number of potential cases, we have to make assumptions about number of defaults, and the number of cases that may come through the IBC route.

Information on defaults on personal loans is sparse. Delinquency on education and housing loans is estimated to be around 8-9%, and 1% respectively. We, therefore, calculate the likely number of accounts that will default in

each district, under assumptions of a default rate of 1%, 5%, and 10%. This analysis assumes that the default rate is uniform across the country, though in reality, this will differ by district. The analysis further assumes that 10% of the cases that default will come to the IBC. This is a purely arbitrary number. Ex-ante we do not know how many cases will come to the IBC, and in fact, the efficiency of the IBC will drive this number over time.

Table 2 provides the potential number of accounts (in '000) that will default if the default rate were 1%, 5% and 10%.

Table 2: Number of potential defaults (in 000) in top 20 districts

State	District	1% of accounts	5% of accounts	10% of accounts	DRT present
NCT of Delhi	Delhi	39.50	197.48	394.97	Yes
Karnataka	Bangalore urban	34.13	170.63	341.27	Yes
Maharashtra	Mumbai Suburban	31.80	159.02	318.04	Yes
Maharashtra	Mumbai	27.47	137.33	274.66	Yes
Tamil Nadu	Chennai	24.78	123.88	247.76	Yes
Telangana	Hyderabad	17.37	86.85	173.71	Yes
Maharashtra	Pune	16.77	83.83	167.66	Yes
West Bengal	Kolkata	10.69	53.47	106.93	Yes
Maharashtra	Thane	8.14	40.71	81.41	No
Telangana	Rangareddy	7.84	39.19	78.37	No
Gujarat	Ahmedabad	7.25	36.23	72.47	Yes
Haryana	Gurgaon	5.06	25.28	50.57	No
Tamil Nadu	Coimbatore	4.77	23.86	47.73	Yes
Kerala	Ernakulam	4.63	23.13	46.25	Yes
Uttar Pradesh	Gautam Buddha Nagar	4.25	21.24	42.49	No
Gujarat	Vadodara	3.97	19.84	39.68	No
Rajasthan	Jaipur	3.87	19.36	38.71	Yes
Kerala	Thiruvananthapuram	3.87	19.35	38.70	No
Andhra Pradesh	Vishakhapatnam	3.51	17.56	35.13	Yes
Gujarat	Surat	3.39	16.95	33.91	No

As discussed earlier, several of the districts even in the top 20 districts by number of loan accounts, do not have a DRT presence. With a 1% default rate, and 10% of default cases going to the IBC, the following number of cases will not have an obvious choice of DRT in the district.

Table 3: Number of potential default cases in districts without a DRT

District	1% accounts	10% defaults

without DRT	default	go through IBC
Thane	8140	814
Rangareddy	7840	784
Gurgaon	5060	506
Gautam Buddha Nagar	4250	425
Vadodara	3970	397
Thiruvananthapuram	3870	387
Surat	3390	339

In the districts, where there is a DRT presence, the case-load may become too large. For example, if we assume a default rate of 1%, then Delhi should see 39,000 defaults. If the default rate is assumed to be 10%, then Delhi should see almost four lakh defaults. One could argue that several of these cases are housing or consumer loan cases which may not come to the IBC. While this is true, the number of loan accounts on housing and consumer durables are much smaller - for example after removing these two loans, Delhi would still see 37,000 defaults if 1% of accounts were to undergo default. Even if only 10% of these, i.e. 3,700 cases, were to make it to the IBC, it still adds up to a sizable number of cases.

Challenges

Currently, the DRTs deal with bank loans above INR 10 lakh. However, there are only 65 lakh loan accounts in this size threshold in the entire banking system. In contrast, there are 14 crore household loan accounts, and their average size is INR 2.3 lakhs. The logistics, procedures and skills required to deal with cases stemming from defaults on small personal loans will be very different from what the DRTs are typically used to dealing with. The analysis suggests two challenges for the DRTs in dealing with personal insolvency:

1. There are at least seven districts where the number of loan accounts is high, but there is no DRT presence. As one moves to districts with fewer loan accounts, the DRT presence becomes negligible. While it is true that defaults in these districts will not be as high as in the districts with a larger number of loan accounts, a mechanism for these borrowers to reach out to the DRTs needs to be designed and implemented.

2. The case load on existing DRTs will rise significantly even if 1% of personal loan accounts in a district were to default, and just under 10% of these were to be brought under the IBC. This is a concern as there were already a 109,518 cases pending at the DRTs as of 30 June 2017 . One way to deal with this issue is to have a larger role for the resolution professional combined with simplified forms and procedures to reduce the flow of cases to the DRTs.

Even conservative estimates of defaults only on personal loans from the banking channel, suggest that the DRTs have to increase their preparedness before they handle personal insolvency cases. The current functioning of the DRTs leave a lot to be desired. One issue that has been raised is that of low productivity of judges at the DRTs, where productivity is measured as the low disposal rate per judge. Low disposals also result in delays in cases. However, the delays are often a result of trial failures, on account of incompetence by the concerned parties to the case.

If these issues are not resolved, then the the DRTs will get overwhelmed with cases from individual insolvency. To effectively deal with resolution of such loans, there will need to be an increase in the presence of DRTs across India. The DRT rules of procedure, reach, infrastructure, as well as their use of technology for case management, will require a comprehensive re-think.

Renuka Sane is a researcher at the National Institute of Public Finance and Policy. I thank Mayank Mahawar for research assistance.

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Watching India's insolvency reforms: a new dataset of insolvency cases

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Abstract

In this paper, we introduce a new dataset of orders passed by the National Company Law Tribunal (NCLT) in the insolvency cases under the Insolvency and Bankruptcy Code or IBC. We build this dataset to attempt an empirical analysis of the economic effect of the IBC and the performance of the judiciary under the IBC. There are 23 fields of information recorded in the dataset for each case. We analyse orders passed during the first six months of operationalisation of the provisions of the IBC to answer questions such as who are the initial users of the insolvency process under the IBC, what kind of evidence are they using to support their claims before the NCLT, what is the average time taken by the NCLT to dispose off insolvency cases, what is the outcome of the proceedings and is there variation between the benches. Within this limited dataset and within such a short time from the passing of the law, we find behavioural shifts among credit market participants. As the insolvency cases increase, this data set will too increase in scope and size and will form the foundation to answer questions relating to the impact of the IBC and the overall functioning of the Indian bankruptcy regime.

Keywords: K10; K40; K41; K42; Y10

JEL Code: K10; K40; K41; K42; Y10

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Watching India's insolvency reforms: a new dataset of insolvency cases

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Contents

1 Introduction

The legal framework for insolvency resolution in India underwent a structural change when the Insolvency and Bankruptcy Code (IBC) was passed in May 2016. This single law is an overhaul of the insolvency and bankruptcy regime in India, replacing all laws relating to bankruptcy, some from as far back as 1924 (Bankruptcy Law Reforms Committee 2015). Once the provisions relating to corporate insolvency and bankruptcy were notified (November 2016), the first cases of insolvency started being admitted in the courts (December 2016). The final orders on these cases became the first public records of India's new insolvency and bankruptcy framework.

In this paper, we hand-collect information from these cases to understand the working of the new legal framework. There are two questions that we focus on: questions about the economic impact – how the law is being used, and questions about the judicial process – how the courts are functioning under the law.

The IBC is explicitly different from the existing legal framework and practices in many aspects (Sengupta, Sharma, and Thomas 2016). The law does not dictate the form of the resolution outcomes, but designs the form of the process leading to the resolution. For this, it adds new institutions to the ecosystem – the Insolvency Professionals (IPs), the Insolvency Professional Agencies (IPAs) and the Information Utilities (IUs)– to ensure efficient and speedy resolution of distress, with a statutory bankruptcy regulator to regulate the industries as well as the resolution processes. The law establishes a framework for collective action by creditors to resolve the financial stress of the debtor, another first in India. The process shifts away from a debtor-in-possession model to a model where creditors decide on the resolution while an impartial professional runs the operations of the debtor as a going concern.[1] Further, the law empowers the National Company Law Tribunal (NCLT) as the adjudicating authority, which does not intervene in the resolution process, but merely adjudges the fairness of the process and compliance with the law governing corporate insolvencies. The law designates the National Company Law Appellate Tribunal (NCLAT) as the appellate forum.

In this paper, we use information collected from the final orders published by the NCLT in the first six months of insolvency cases under the IBC to attempt an empirical analysis of the economic effect and the performance of

[1] In fact, Bankruptcy Law Reforms Committee 2015 noted that, "...Control of a company is not divine right. When a firm defaults on its debt, control of the company should shift to the creditors. In the absence of swift and decisive mechanisms for achieving this, management teams and shareholders retain control after default. Bankruptcy law must address this."

the judiciary. There are 23 fields of information for each case in the dataset. This includes parameters such as, who are the initial users of the insolvency process under the IBC, what kind of evidence are they using to support their claims before the NCLT, the average time taken by the NCLT to dispose off cases, the outcome of the proceedings and the variation between the benches. We use this data to try and answer the following questions:

About the economic impact of the law:

Q1: Does the law improve the balance between rights of the creditors and the firm debtor during insolvency?

Q2: Does the law empower various types of creditors when the firm defaults?

Q3: Does the law empower only large sized debt holders?

On the role of the judiciary:

Q4: Do the NCLT cases reflect a geographical spread of the insolvency cases?

Q5: Does the NCLT function within the timelines set in the law?

Q6: Is the role played by the NCLT as visualised within the IBC?

We answer these questions by analysing the insolvency cases for the period from December 2016 to May 2017. This has information for 110 cases, and includes orders of both the NCLT and the appellate tribunal, the NCLAT. Within this limited dataset and within such a short time from the passing of the law, we find behavioural shifts among credit market participants.

The data shows that 75 percent of the cases were filed by creditors and the remaining by debtors. This is contrary to the expectation that debtors would not trigger resolution under the IBC because the new law gives operating control to a third party (the insolvency professional). We also find that the new insolvency process is used by the operational unsecured creditors *more than* the financial creditors. About half the financial creditors who filed the insolvency petitions were secured creditors. But only one of the operational creditors who filed an insolvency petition was a secured creditor. This is a significant shift from the previous regime which empowered secured creditors. Lastly, there is wide variation in the size of the claims litigated by all creditors, with no perceptible skew towards only large creditors.

The role of the NCLT is similarly answered. We find that the data is more ambiguous about the change in the judiciary to fit within the role defined in the IBC. There is significant variation in the outcomes of insolvency petitions among the different benches of the NCLT, with no inherent bias towards the admission or dismissal of these cases across all benches. The data published by the NCLT does not readily allow us to assess the ability of the NCLT to

meet the timelines prescribed under the IBC. For those cases where the data is available, we find that the NCLT took an average of 24 days to dispose off a case, compared to 14 days that are visualised by the IBC. Finally, while the law sets out very specific grounds for dismissing an insolvency case and is largely biased towards allowing an insolvency to be triggered if the debtor has committed a default in repayment of an undisputed debt, the NCLT has also dismissed petitions on considerations not explicitly spelt out in the IBC. This indicates that the NCLT seems to be viewing the admission of an insolvency case as an excessively harsh outcome for a debtor. Thus, the data shows that the working of the NCLT is not always in line with the letter and spirit of the IBC.

Our data set allows us to simultaneously review the working of the law as a bankruptcy reform as well as to assess the functioning of the judiciary under a new law. There is one additional role that the dataset plays, which is to assess how well the institutions under the IBC deliver on the statistical functions visualised in the law. In reading the orders of the NCLT related to the IBC processes, we find that there exists no standardised format of recording case information. Several final orders are lacking in basic information such as the kind of creditor who filed the petition, the claim amount and the date on which the insolvency case was instituted.

We argue that there are three adverse consequences of such incomplete or inadequate information in the final orders of a tribunal. First, the absence of basic information about the case hinders the ability of the NCLT to monitor the efficiency of it's own benches. The lack of standardisation also constrains researchers from assessing the quality of the procedural requirements and outcomes of the law. Second, this early evidence on the quality of these orders of the NCLT is similar to analysis on the orders passed by Indian debt tribunals (Regy and Roy 2017) and suggests no improvement in the function of the NCLT under the IBC. This will hinder the ability to identify systemic lapses in the functioning of the tribunals and in designing appropriate interventions. Third, inadequate or incomplete data has implications for the overall accountability and transparency of these tribunals to the public, and in the long run, will erode the credibility of the NCLT as an institution.

Finally, the strength of the legal framework ultimately rests on the efficiency of the adjudicator of the law. This is especially so for a procedural law like the bankruptcy law. Structural lapses in the NCLT are likely to cripple the working of the legal framework, result in gaps in the efficiency of resolving insolvency cases as visualised by the IBC and leave the bankruptcy reforms process undone. Fortunately, these are early days yet, and it is important to correct these flaws in the processes as early as is possible.

The rest of the paper is organised as follows. Section 2 throws light on

the role of empirical research in policy. It contains the literature review for court related data collection endeavours in general and insolvency matters specifically. Section 3 provides an overview of what the dataset aims to achieve and introduces the dataset by describing the methodology of collection. Section 4 then describes the actual data fields captured. Sections 5 and 6 form the main body of the paper, answering the questions relating to a shift in the behaviour of credit market participants and the functioning of the NCLT through the findings from the data set. Section 7 sets out the policy recommendations based on the findings while Section 8 concludes the paper.

2 Role of empirical research in insolvency policy

As credit markets evolve, it is important that rules and regulations, as well as the primary law, remain relevant within the context of the current times. A study of the history of most economies show that they have gone through significant changes in their bankruptcy regimes, in response to changes in credit contracts and mechanisms. Those economies that did not undertake such reforms have often ended up with fractured and weak credit markets. Understanding the outcomes of current legal frameworks and designing appropriate interventions requies a continuous analysis of the performance of the current framework.

2.1 Analysing insolvency reforms

When the legal framework changes, research is needed to establish whether changes in the framework achieved the desired outcomes. If there is a gap between the expected and actual outcomes, analytical research is critical to identify what needs to be changed to close the gap. Sullivan, Warren, and Westbrook 1987 argue that bankruptcy policy cannot be firmly rooted in reality until empirical evidence about bankruptcy is gathered widely and routinely.

The importance of empirical analysis of the legal framework was less understood in emerging economies but increasingly, there is a recognition that monitoring and analysing outputs and outcomes of the legal framework is important. For example, the design and rationale document for the IBC by the Bankruptcy Law Reforms Committee (BLRC) emphasised the need for data collection and analysis (Section 4.1, Bankruptcy Law Reforms Committee 2015). The Committee recommended that a constant monitoring of the system by way of collecting data about the working of the processes and the various institutions under the new law was a critical input to ensure the

malleability of the law so as to achieve better credit market outcomes in the economy.[2]

In this paper, we focus on creating the data infrastructure to carry out the analysis that is visualised by the BLRC in evaluating the performance of the new law in achieving the target outcomes of the bankruptcy reforms. A dataset of legal cases that is amenable to research becomes an important input to the task of ensuring the malleability of the law. So much so that in some countries, building and publishing open access datasets is a regulatory function. Official research agencies maintain databases collating information on judicial proceedings, like the *Bankruptcy Petition NewSTATS Snapshots* (BPNS) database created by the Federal Judicial Center and the *Advanced level Bankruptcy Cases Database* maintained by the Securities Exchange Commission, in the United States.[3] Such databases are also built and maintained by academic institutions such as the *Advanced level Bankruptcy Database* built at the Duke Law School.[4]

2.2 The judiciary and outcomes of insolvency reforms

It is widely accepted that there is a positive link between the functioning of courts and economic activity (Chemin 2010). In the context of insolvency and bankruptcy, the regulatory framework and procedural regime tends to vary widely across jurisdictions (Djankov et al. 2008) and the bulk of empirical evidence on bankruptcy cases tends to be country-specific. In more developed economies with highly evolved bankruptcy regimes, the literature on bankruptcy has often shown linkages between judicial discretion, variation in judicial procedures and bankruptcy outcomes (Giammarino and Nosal 1994, Gennaioli and Rossi 2010). In developing countries, the literature has focused on the performance of courts and studying their impact on the effectiveness of bankruptcy reforms undertaken in these countries (Ponticelli 2014 and Ponticelli and Alencar 2016).

In India, the link between the performance of the judiciary and insolvency outcomes has not been empirically analysed. Ravi 2015 analyses a limited sample set of insolvency cases to measure the efficiency and problems of the present laws for firm bankruptcy in India. However, the scope of this analysis naturally did not extend to the newly enacted *IBC*.

[2] Section 4.1.1 in Bankruptcy Law Reforms Committee 2015 includes a statistical function in the role of the IBBI in order to ensure malleability of the legal framework and to track the performance of the law.

[3] *See* https://www.fjc.gov/research/idb/bankruptcy-cases-filed-terminated-and-pending-fy-2008-present; and https://www.sec.gov/open/datasets-bankruptcy.html

[4] https://law.duke.edu/lib/facultyservices/empirical/links/courts/

There is now a nascent literature developing on the working of the Indian judiciary. One strand of the literature has focussed on generic issues in the judicial process such as increasing the efficiency of courts (see, for instance, Shah and Datta 2015), increasing the efficiency of tribunals through a separate administrative body (see Datta 2016) and the reforms required to tackle the problem of reliable data collection by the judicial institutions (see Kumar and Datta 2016). Another strand of the literature analyses judicial delays and the pendency of cases in civil courts (DAKSH 2015, DAKSH 2016, Khaitan, Seetharam, and Chandrashekharan 2017). Similar work has been done on the performance of debt tribunals (Regy and Roy 2017) .Our paper adds to this literature by assessing the judicial efficiency of the NCLT from the insolvency case data under the IBC.

3 What does our dataset do?

The IBC, being a relatively new legislation, is in the nascent stages of its implementation. The provisions governing corporate insolvency were notified through December 2016. Since then, several applications to trigger the IBC have been filed across the country. Many of these applications have been disposed off and the process of resolution is ongoing.

The final orders disposing off these cases offer a natural opportunity to answer questions related to the first instances of use of a new bankruptcy law. The jurisprudence on the law is evolving and the cases disposed by the NCLT are frequently discussed in the popular media (Dasgupta 2017, Poddar 2017, Gada and Singh 2017, Bansal 2017). Till now, however, there is no comprehensive effort at understanding the outputs of the law, and what these outputs mean for the expected outcomes of the law.

Our paper is the first step towards achieving that goal. This will take two steps: (1) collect orders and parse them for information that is useful to answer questions related to the use of the law in the insolvency resolution process, and (2) record and archive this information in a format, which makes it readily accessible for empirical research to monitor the status of the reform and what is required for the next level of reforms. We take these two steps by building a dataset of insolvency cases disposed off under the *IBC*.

We follow this with examples of empirical analysis that our dataset can support. We illustratively apply the dataset to answer two kinds of questions. The first question focuses on the progress in bankruptcy reforms since the IBC. We ask how the creditors and the firm as debtor – two important economic stakeholders in the credit markets – – are using the new insolvency and bankruptcy processes. Our analysis includes questions on who is using

the process, and whether the usage patterns show a change compared to the use of the earlier insolvency and bankruptcy regime. The second question is on how the judicial systems are functioning under the IBC.

For understanding the dataset, an overview of the organisational structure of the NCLT and NCLAT and their role under the IBC, is imperative. The next two sub-sections provide this overview. The third sub-section describes the data collection methodology.

3.1 Organisation of the NCLT

The NCLT is established under the *Companies Act, 2013*, not the IBC, and has a broader purpose of discharging various functions under the former Act. This includes functions such as approving schemes of mergers and amalgamations and dealing with complaints of shareholder oppression and mismanagement. Under the IBC, additional powers are conferred upon the NCLT to deal with insolvency and bankruptcy proceedings of corporate entities.

The organisational structure of NCLT comprises of a President, judicial and technical members and staff. A judicial member is required to have been a judge of a District Court or a High Court or a lawyer with at least ten years of experience. A technical member is required to have been a member of the Indian legal services or the corporate affairs services. The employees and staff of the NCLT work under the superintendence of the President. Locations of the NCLT includes a principal bench located in New Delhi, and eight other benches located across India.[5] Each bench must have a technical member and a judicial member. The *Companies Act, 2013* empowers the Central Government to constitute as many benches of the NCLT as it may deem fit. Additionally, it empowers the presiding officer of the NCLT to constitute special benches for the rehabilitation, restructuring, reviving or winding up, of companies. Such special benches must consist of three or more members, with the majority necessarily being judicial members. For example, a special bench was set up in Guwahati to dispose off a limited question of law that arose in an insolvency petition before the Kolkata bench.

Appeals against the orders of the NCLT can be made to the NCLAT. The NCLAT comprises a Chairperson, a judicial and technical members, with specific qualifications.[6] The NCLAT has one bench located in New Delhi.

[5]These benches are located in Mumbai, Hyderabad, Allahabad, Ahmedabad, Kolkata, Chennai, Bengaluru and Chandigarh.

[6]The Chairperson must have been a judge of the Supreme Court or a chief justice of a High Court. A judicial member must have been a judge of a High Court or a judicial member of the NCLT for at least 5 years. A technical member must be a person of proven

Appeals against the orders of the NCLAT can be made to the Supreme Court.

Every proceeding before an NCLT or an NCLAT ends with the passing of an interim order or a final order. An order that does not finally dispose off an insolvency petition, is referred to an interim order. An order that finally disposes off an insolvency petition is referred to as a final order.

3.2 Role of the NCLT under the IBC

The Bankruptcy Law Reforms Committee 2015 discussed the role of the judiciary in the insolvency resolution process in detail, and the report of the committee underscores the need for the judiciary to focus on questions of procedure or due process, rather than the terms of the resolution itself, which must be left to the will of the creditors committee.[7]

In the scheme of the IBC, the adjudicating authority is necessarily involved in at least two stages of the resolution process,[8] as follows:

The process of invoking the IBC:

The IBC can only be triggered by petitioning the NCLT. This petition is referred to as an insolvency petition. When an insolvency petition is filed, the law defines that the role of the NCLT is to identify whether the debtor has committed a default in repayment of an undisputed debt to the petitioning creditor. If the NCLT finds that the debtor has defaulted to the creditor; and has not disputed the claim of default by the creditor beforehand, the NCLT must allow the petition to go through, else it must dismiss the petition.[9] Further, the law requires the NCLT to decide on the petition within 14 days from the date on which it is filed.

Thus, the IBC leaves little scope of discretion to the NCLT in deciding whether to admit or dismiss insolvency petitions.

Approval of a resolution plan:

When an IP presents a resolution plan that has been approved by the prescribed majority in the creditors committee, the NCLT must sanction the

ability, integrity and standing having special knowledge and experience, of not less than 25 years, in law, industrial finance, industrial management or administration, industrial reconstruction, investment, accountancy, labour matters, or such other disciplines related to management, conduct of affairs, revival, rehabilitation and winding up of companies

[7] The Bankruptcy Law Reforms Committee 2015 states, "The legislature and the courts must control the process of resolution, but not be burdened to make business decisions." Further, see Section 4.2.4.

[8] The NCLT may also be involved in other procedural details during the resolution process, such as in the replacement of the resolution professional during the resolution process.

[9] The petition may be filed by either a creditor or by the debtor itself. Where the debtor files for an insolvency petition, the NCLT must admit the insolvency petition if it is complete, and reject it if it is incomplete.

plan once it ensures that due process, as defined in the IBC is met in reaching the final vote.

At this stage too, the IBC leaves little scope for the NCLT to question or intervene in the commercial decisions of the creditors.

The two processes listed above are critical in the life-cycle of a resolution process under the IBC. The quality and efficiency of adjudication at these two stages can directly affect the outcomes of IBC. When the IBC is triggered, the law contemplates a moratorium on all pending and new legal proceedings against the debtor for a period of 180 days.[10]

An order of a tribunal permitting the IBC to be triggered has serious implications for all the parties involved. Further, the orders of these tribunals set precedents for those who wish to trigger the IBC in the future. The expeditious disposal by the NCLT of the insolvency petitions help to preserve the value of the firm (Section 3.4.1 of the Bankruptcy Law Reforms Committee 2015). Similarly, a robust adjudication process at the stage of approval of the resolution plan will ensure the integrity of the resolution process and build trust in the legal framework. The importance of a well-functioning adjudication process at the NCLT cannot be understated, for the sound functioning of the IBC (Shah and Thomas 2016, Datta and Regy 2016).

3.3 Data collection methodology

The dataset has been compiled by hand-collecting select information from the orders on insolvency petitions published on the website of both, the NCLT and the NCLAT. For this, we collect and evaluate all *final orders* passed by the NCLT for the first six months from the date of notification of the provisions on the insolvency of corporate bodies under the IBC. Thus, this study covers only the period from 1^{st} December, 2016 to 15^{th} May, 2017. We refer to this period as the sample period (sample period) for the rest of this paper. We create the dataset by capturing fields of information that we consider essential to assess the performance of the IBC.

Since the orders are non-standardised, we peruse each order in full to capture the selected data-fields. Where the order does not contain data on the relevant field, we record it as "not available".

[10] During this period, the insolvency professional takes charge of the business to ensure that it continues operation while the resolution is being decided upon, while the debtor can be temporarily dispossessed.

4 Fields captured in our dataset

The information collected includes the dates of various actions taken in the process of filing, the process of the insolvency resolution and the response of the NCLT. Much of the recorded information is in the form of a *categorical variable*. These can have binary values, such as whether the case is admitted or rejected, or whether the debt was secured or unsecured. They can also have one of a set of possible values, as in what was the reason that the NCLT dismissed the petition or which bench the petition was filed at. The collected data may also be a *numerical value* such as the amount of debt that is due.

At present, the data is a set with 23 information fields. We describe the fields[11] below, in the order that they are present in the dataset, along with reasoning behind their construction:

1. **Case number** This is the case number of the NCLT order which is the primary identifier. Since the orders of the NCLT and the NCLAT are indexed on the website by their case number, using the same referencing style in the data set, will allow ready tracking to the underlying case.

   Where an order passed by the NCLT has been appealed against, a separate case identifier is used by the NCLAT for the appeal proceeding. For appeals which have been disposed off, the case identifier of such appeal proceeding has been mentioned next to the order of the NCLT that was appealed against.

2. **Location of the bench where the case is filed** This field will contain one of a set of fixed names which are the benches of the NCLT at present. As more benches are set up, the list of possible names can increase.

   The orders on the NCLT website are classified based on the Bench where the insolvency petition was filed.

3. **Who filed?** This field captures one of three possible values: Not available, for where the information is not available in the order or record of whether the case was filed by a creditor or the corporate debtor.

   An innovation the IBC brings to the Indian insolvency framework is that it allows any creditor, or the debtor to trigger insolvency resolution of a stressed firm. In the earlier regime, this was restricted to a small set of secured creditors.

   A reading of the cases allows us to record whether the insolvency petition was filed by a debtor or a creditor. In case the insolvency petition is filed by the latter, the case records whether it was an operational or a financial creditor. If the former, we are able to identify what kinds of operational creditors are using the IBC to recover their claims.

   This helps us to record fields 4 to 7 that follow. By tracking the types of entities, it is possible to understand who considers the IBC as a suitable mechanism to resolve their claims.

4. **Type of creditor** This field captures what type of creditor has filed the petition.

   Under the IBC, a petition can be filed by financial or operational creditors.

[11] A technical description of each field of information is available in Appendix A, and a statistical description of the fields are available in Appendix B.

5. **Type of operational creditor** There are several possible operational creditors. From the dataset, they include decree holders, employee, franchiser, property buyer, service provider (such as electricity or telephone) or other suppliers.[12]

6. **Type of financial creditor** Among the different types of financial creditors who have filed at present, there are banks (who are the largest with 8 out of 20 cases), bond holders, corporate lenders, debenture holders, individuals, NBFCs, property buyers, service providers and trustees / debenture trustees.[13]

7. **Name of the debtor** This field captures the name of the debtor, as recorded in the order of the NCLT. It permits ease of search in identifying whether an insolvency petition has been admitted against a debtor, especially in cases when a user of the dataset is unaware of the case number of the proceedings before the NCLT.

8. **Amount of debt** The amount of debt (in Rs. value) against which the insolvency petitions is filed.

   The IBC allows insolvency proceedings to be initiated against a firm only when the value of the debt is equal to or exceeds Rs.100,000. This field allows us to analyse what are the typical values used to trigger insolvency.

9. **Secured or unsecured creditor** This field allows us to record whether unsecured creditors use the IBC mechanism.[14]

10. **Due date of payment** This field captures the due date of payment of debt as mentioned in the order of the NCLT.

    A measure of the time taken between the default date and the date of filing an insolvency petition indicates the time after default that creditors allow to elapse before pursuing insolvency proceedings.

11. **Date of demand notice** This field records the date of a demand notice issued by an operational creditor to a debtor to repay the debt, according to the process in Section 8 of the IBC.[15]

12. **Date of receipt / service of demand notice** This field records the date when the debtor receives the demand notice from a creditor.

    Under the IBC, the debtor is provided a period of ten days from the date of receipt of a demand notice, to either repay the unpaid operational debt or notify the creditor of the existence of a dispute concerning the debt.[16]

13. **Date of filing in NCLT** This field captures the date on which an insolvency petition is filed before the NCLT.

14. **First date of case listing** This field captures the date on which the case is first listed to be heard by the NCLT bench once it has been filed.

[12] Note that property buyers have been grouped separately from operational and financial creditor in a group termed as 'other creditors' as per the latest change to the insolvency regulations.

[13] Note that property buyers have been grouped separately from operational and financial creditor in a group termed as 'other creditors' as per the latest change to the insolvency regulations.

[14] In the pre-IBC regime, only secured creditors could take debt recovery action against debtors. They had a wide range of powers under the SARFAESI Act, 2002 as well as the Companies Act, 2013 for debt recovery against a debtor, while unsecured debtors were largely restricted in their ability to carry out similar debt recovery efforts.

[15] Section 8 of the IBC allows an operational creditor to deliver a demand notice or the copy of the relevant invoice to the corporate debtor, demanding payment of outstanding dues.

[16] Section 8 of the IBC

A delay in fixing this date at the first instance is likely to lead to subsequent delays in adhering to overall timelines. Thus, the first date of listing of an insolvency petition throws light on the urgency with which the NCLT treats the procedure after the insolvency petition has been filed. This could be attributed to the internal processes of the NCLT in scheduling hearings for a matter before it.

15. **Date of final disposal** This field captures the date of the NCLT order either admitting / dismissing an insolvency petition.

    This, along with the date of filing of the petition, provides an insight into the aggregate time that is taken for disposing off an insolvency petition.

    For example, an analysis of the duration between the date of first listing of an insolvency petition and this date tells us how much time is taken in the disposal of the insolvency petition once an insolvency petition is placed before a bench. The time taken between the date of first listing of an insolvency petition and this date may be attributed to the conduct of the parties themselves or the case load handled by an NCLT on a daily basis.

16. **Evidence of debt** This field records such evidence of debt as is relied upon by the petitioner, and may include information obtained from an IU or produced from other sources.

    This allows us to observe whether the IUs are playing the role that was envisaged for them and the extent to which NCLTs are relying on evidence that does not emerge from an IU.

17. **Admitted / dismissed** This field records the outcome of an insolvency petition. An insolvency petition may either be admitted or dismissed.[17]

18. **Category of reason for dismissal** This field captures various reasons for dismissal of an insolvency petition under various categories.

    We define categories of dismissal based on common reasons for dismissal recorded in the orders. At present, there are seven classifications we record for dismissal. This may change as the size of the data increases.

19. **Name of the IP** This field records the name of the IP appointed when an insolvency petition is admitted.

20. **URL for the case** This field stores the URL of the relevant page of the NCLT website to allow easy tracking of the order.

21. **Was the order appealed against?** This field records whether the final order of the NCLT captured in the dataset has been appealed against,[18] since the law allows for any person aggrieved by an order of the NCLT to appeal before the NCLAT.[19]

22. **Who appealed?** This field records whether the appeal in Field 21 was filed by the debtor or the creditor.

23. **Was the appeal admitted or rejected?** This field records the outcome of an appeal preferred to the NCLAT, which may either allow or reject the appeal.

In the present version of the data, these fields are recorded for all the cases in the sample period. However, this is an ongoing effort. As more case-law

[17] Note that for the purpose of this field, insolvency petitions which have been withdrawn by the petitioner have also been treated as dismissed on account of withdrawal.

[18] Note that this field has been populated on the basis of the list of final orders/judgments passed by the NCLAT, as found on the NCLAT website. It is possible that some orders from the dataset have been appealed against but such fact is not recorded in the dataset since the appeal has not been finally disposed off.

[19] Section 61 of the IBC.

emerges, the fields of information in this dataset will correspondingly change to ensure that the fields captured are capable of the most productive analyses of insolvency cases in India. For instance, if the orders of the NCLT reflect this information, the dataset may be expanded to capture the outcome of the resolution process and the recovery rates.

5 The insolvency cases data, analysis #1: shifts in use by credit market participants

In this section, we apply the dataset to understand the kind of cases which are being triggered under the IBC. To understand the same, we specifically ask the following questions:

Q1: Is there a change in the balance between rights of the creditors and the firm debtor during insolvency under the IBC?

Q2: Do the rights of creditors during insolvency under the IBC extend to various types of creditors of the firm debtor?

Q3: Is the IBC being used to trigger the insolvency resolution process only for large size debt, or are there defaults on smaller sized debts where insolvency resolution process is triggered?

5.1 Enhancing creditor rights in India

Prior to the enactment of the IBC, India was observed to be a country with greater debtor rights compared to creditor rights.[20] Even among creditors, unsecured and operational creditors had limited legal remedies to enforce their claims under firm debtor insolvency.

If a debtor defaulted to an unsecured creditor, the creditor had three remedies to recover its claim: civil suit, arbitration or petition the High Court for winding up if the debtor is a company. As the evidence from the literature shows, civil suits were not efficacious in a court system that is already riddled with a backlog of cases. Arbitration is expensive. Winding up a company in India takes anywhere between five to ten years (Ravi 2015).

The IBC is intended to provide unsecured creditors, particularly, an operational creditor, a forum to aggregate the creditors and have a legitimate

[20]For instance, the World Banks Ease of Doing Business Index 2015 ranked India 137 out of 189 countries on the ease of resolving insolvencies based on various indicators such as time, costs, recovery rate for creditors, the management of a debtors assets during the insolvency proceedings, creditor participation and the strength of the insolvency law framework.

chance to enforce its claim. The IBC defines *operational debt* as a claim in respect of the provision of goods or services, including employment or a debt in respect of statutory dues payable to the Central Government, any State Government or any local authority. *Financial debt* is debt, along with any interest, which is disbursed against the consideration for the time value of money.

Table 1 shows the break-up of applicants who petitioned the NCLT to trigger the IBC.[21] We find that out of the 110 orders studied, a little more than half the petitions were filed by operational creditors. This is in sharp contrast to the financial creditors who have filed less than twenty 20 percent of the insolvency petitions in the dataset.

Table 1 Who uses the IBC? Evidence from Dec 2016 to May 2017

No. of petitions filed by creditors	83
No. filed by operational creditors	62
No. filed by financial creditors	21
No. of petitions filed by debtors	26
No. of unknown applicants	1
Total	110

There may be multiple reasons for the contrast observed in the behaviour of the financial creditor. Anecdotal evidence suggests that firm debtors default to financial creditors the last. Financial creditors may largely be secured creditors who may choose to enforce their claim by realising their security. There is lack of regulatory certainty on provisioning norms for banks to the apprehension of scrutiny by the anti-corruption investigative agencies among bank management (Mehta 2017). However, in the absence of data on default or the enforcement of security by financial creditors in India, the reason for the divergence in creditor behaviour in triggering the IBC is unclear.

Another feature of interest is the behaviour of the debtor. There is a commonly voiced apprehension that the debtor will avoid resorting to insolvency because under the insolvency resolution process, the board of the debtor can be replaced by the resolution professional. Contrary to this apprehension, around 24 percent of the petitions in this early six month period have been filed by debtors.

[21] It is pertinent to point out that in one case, the final order was a one line order dismissing the insolvency petition, which did not articulate basic information on who was the applicant.

Table 2 Outcomes for insolvency petitions filed by different applicants

Applicant category	No. of cases		
	filed	admitted	dismissed
Creditors			
Operational	62	26	36
Financial	21	12	9
Debtors	26	23	3

Table 3 Cases filed by operational creditors

Employees	5
Vendors	43
Others	6
Not known	8
Total	62

Table 2 shows the admission and dismissal rates across different categories of petitioners. Table 3 shows that out of the cases filed by operational creditors, the largest fraction of them were filed by vendors. Nine of the insolvency petitions filed by financial creditors, and 36 of the insolvency petitions filed by operational creditors, were dismissed. This translates into 43 percent of the cases filed by the financial creditors and 58 percent of cases by the operational creditors that were dismissed. Further, we find where the operational creditors are employees of the firm debtor, three out of five cases filed are dismissed. In comparison, only 11.5 percent of the cases filed by debtors were dismissed.

This suggests that cases filed by financial creditors and debtors appear to have a greater probability of acceptance than operational creditors, especially employees. Of course, these are yet early days and more data is required before these features can be established in a robust manner.

Some other note-worthy observations are listed here:

- Among the other operational creditors who have petitioned the NCLT, one of the creditors is a holder of an arbitration award.
- While about half the financial creditors who filed the insolvency petitions were secured creditors, only one of the operational creditors who filed an insolvency petition is a secured creditor.
- Four creditors are buyers of under-construction flats who had paid an advance on which the builder debtor had offered guaranteed returns. The NCLT has dismissed these petitions.[22]

[22]Note that the status of property buyers under the IBC is currently in a state of flux. They have been notified as a third catergory of creditors under the relevant regulation but

Finally, we examine whether there is any pattern in the size of debt that is used to trigger insolvency under the *IBC* 2016. The law places a threshold of Rs.100,000 in order to trigger an insolvency case.

Table 4 shows the range of debt claims disposed off under the *IBC* 2016 during the sample period. The table also presents the distribution across the different quartiles, by showing threshold values at three different cut-off points: for the 25^{th} percentile point, the 50^{th} percentile and the 75^{th} percentile point. The 25^{th} percentile point is the value below which 25 percent of the cases will fall. Further, this has been done by the different types of stakeholders – financial creditors, operational creditors and the firm debtor.

Table 4 Size of debt in the insolvency cases at NCLT

	(All values in Rs. except for number of observations)		
Size of debt reported	Corporate debtors	Operational creditors	Financial creditors
Minimum	9,211,106	109,516	3,069,000
25^{th} percentile	98,160,525	1,276,884	15,085,632
50^{th} percentile	435,747,000	3,373,191	172,037,926
75^{th} percentile	128,97,93,692	28,027,382	772,448,220
Maximum	25,800,700,000	1,319,000,000	8,565,257,199
No. of observations	24	54	16

The table shows that the smallest claim to trigger the IBC was filed by an operational creditor with a claim of debt default of Rs.109,516 (or Rs.1.09 lakh). In comparison, the smallest debt against which a financial creditor triggered the IBC was Rs.3,069,000 (or Rs.30.69 lakhs) which was 30 times larger. The maximum debt default claimed by an operational creditor was Rs.1,319 million (or Rs.131.9 crores) while the largest default to a financial creditor was Rs.8,565 million (or Rs.856.5 crores) which was only 8 times larger. This shows that operational creditors, who had considerably weaker rights under the previous regime, had considerably large debt repayments due from firm debtors.

In this set of 110 cases, fifty percent of dues to operational claimants were at or below Rs.3.37 million or Rs.33.7 lakhs. In comparison, fifty percent of the dues to financial creditors were at or below Rs.172 million or Rs.17.2 crores.

From this, we infer that the threshold specified in the law does not appear to be a deterrent to trigger resolution under IBC against firm debtors so

it is expected that there are further changes to status.

far.

In each case of the firm debtor triggering the IBC, the size of the debt is relatively larger since the full debt that is owed is reported.

5.2 Summarising shifts in the behaviour of creditors and debtors

The above empirical analysis helps us to answer our questions about how the IBC is being used by two key stakeholders – creditors and debtors.

Q1: Is there a change in the balance between rights of the creditors and the firm debtor during insolvency under the *IBC*?

Answer: As explained above, the legal regime preceding the *IBC* conferred weak rights on creditors, especially unsecured creditors. It created tremendous scope for the judiciary to intervene in the commerical matters of debt re-structuring. The law itself and the courts and tribunals enforcing it, also exhibited a rehabilitation and pro-debtor bias (Ravi 2015). While the sample period represents the earliest days of operationalisation of the *IBC* and the dataset is small to conclusively answer this question, the data indicates that there has been a shift in enforcement of creditors' rights under the *IBC* 2016.

Of the 110 cases that we reviewed in this paper, 75 percent of the cases were triggered by creditors. Of these, 75 percent were filed by unsecured operational creditors. This indicates that operational creditors, who hitherto had weak enforcement rights, have resorted to the *IBC* 2016 to enforce their claims.

Of the 110 cases that were filed, 50% of them have been admitted by the NCLT and are now undergoing a mutually negotiated debt restructuring process. This indicates that the *IBC* 2016 largely dispenses with the pro-debtor bias exhibited by judicial bodies under the previous regime.

Within the caveat that these are early days and we still have to observe how these cases get resolved, the observed data suggests that creditors are able to use the new insolvency and bankruptcy regime with increasing confidence compared to the previous regime.

Q2: Do the rights of creditors during insolvency under the IBC extend to various types of creditors of the firm debtor?

Answer: Under the IBC, all creditors have shown the ability to trigger insolvency proceedings in the NCLT. This is in contrast to the previous regime where only a certain subset of creditors were able to trigger insolvency proceedings against firm debtors, and other creditors had to file cases in civil courts.

Q3: Is the IBC being used to trigger insolvency petition only for large size debt, or are there small defaults which trigger insolvency petition?

Answer: The IBC is being triggered by creditors on a wide range of size of defaults. While this is true, the empirical evidence suggests that most of the cases observed so far (more than 75 percent of the cases) tend to be triggered

using debt defaults that are approximately 10 to 100 times larger than the threshold of Rs.100,000 set in the law.

6 The insolvency cases data, analysis #2: the functioning of the NCLT

The second research focus is on the functioning of the judiciary under a new law. In this analysis, we aim to characterise how the NCLT has dealt with the case load of the insolvency petitions. We examine three aspects:

Q4: Do the NCLT cases reflect a geographical spread of the insolvency cases?

Q5: Does the NCLT function within the timelines set in the law?

Q6: Is the role played by the NCLT as visualised within the IBC?

At the start, we present a brief description of the NCLT to set the context for the empirical analysis of its functioning.

6.1 An empirical description of the NCLT orders on insolvency cases under the IBC

We start with simple descriptions of the case load and the geographic spread of the case loads observed in the insolvency cases at the NCLT in the sample period.

Table 5 IBC cases disposed, Dec 2016 to May 2017

	Final orders	
	passed	studied
NCLT	110	110
NCLAT	10	10
Total	120	120

Table 5 presents the number of cases that were disposed by the adjudicator under the IBC. As the data shows, this includes both the NCLT as well as the appellate tribunal under the IBC.

A question that arises when implementing a new law is how to ensure that there is sufficient judicial capacity to deal with it throughout the country. At present, there are nine benches of the NCLT, which are to deal with insolvency and bankruptcy matters as well as all other matters under *Companies Act, 2013*.

How have the first six months of cases been spread across the present locations? Table 6 contains a break-up of the number of orders passed by each

of the nine benches during the sample period, while Table 5 presents the final orders passed by the NCLAT disposing off appeals from the orders of the NCLT passed during the same period.

Table 6 Final orders passed by the NCLT across benches, Dec 2016 to May 2017

	Bench	Number of final orders
1.	New Delhi	32
2.	Ahmedabad	9
3.	Allahabad	5
4.	Bangalore	4
5.	Chandigarh	11
6.	Chennai	1
7.	Hyderabad	3
8.	Kolkata	4
9.	Mumbai	41
	Total	110

Out of the 110 orders studied, the Mumbai bench of the NCLT passed the maximum number of orders, followed by the Delhi bench (Table 6). The New Delhi bench of the NCLT had constituted a special bench for three of the orders.[23] The special bench that disposed off the three insolvency petitions comprised of two members, only one of whom is a judicial member. The reason for constituting a bench for some insolvency petitions and not others is unclear.[24]

This is a matter of some concern because the method of constituting benches for the disposal of insolvency petitions materially affects the outcome of the case. An irregularity in the constitution of a bench may well be a ground to challenge the final orders passed by such a bench. The final orders passed by special benches do not indicate the reason why these cases were selected to be disposed off by special benches.

[23]Section 419(4) of the *Companies Act, 2013* allows the President of the NCLT to constitute a special bench for rehabilitation, restructuring, reviving or winding up of companies. The law requires such special benches to consist of three or more members, with the majority necessarily being of judicial members.

[24]A special bench had also been constituted at Guwahati to dispose off a limited reference on a technical question of law arising in an insolvency petition filed before the Kolkata bench of the NCLT.

It is unclear why the limited technical reference, made to the special Guwahati bench, could not have been disposed off by the Kolkata bench adjudicating the insolvency petition in which such a question arose.

While the Guwahati bench disposed off this reference, we have not taken the final order that it passed into account, because the order was restricted to answering the limited reference and not the disposal of an insolvency petition.

Without attributing any impropriety to the constitution of such benches, it is important that the reasons for their constitution and the reasons why specific cases were allocated to such benches must be published. Moreover, the procedural irregularities in the constitution of the bench must be appropriately dealt with.

6.2 How long does it take to dispose an insolvency petitions

The orders have numerous information gaps owing to the absence of a standardised format for writing orders. While each order specifies the date on which it was passed, several orders do not capture information critical to assessing the timelines involved for disposal of insolvency petitions, such as:

1. the date on which the insolvency petition was filed and the date on which it first came up for hearing (T1);
2. the number of times hearings were scheduled before passing the final order;
3. the number of interim orders passed before the final order is passed.

Information in items 1 and 2 can potentially be hand collected from the list of cases scheduled for hearing that is published by each bench of the NCLT. These lists are commonly referred to as *cause lists* among practitioners. Since cause lists are prepared for a given day or a given month, continuous monitoring of the daily cause lists of each bench of the NCLT should give us data on the number of times an insolvency petition was scheduled for hearing. However, gathering data from daily cause lists suffers from the following two problems:

1. It is not possible to get historical data on the case-listing from the cause-lists. The daily cause-lists published by the NCLT are not archived and are available electronically to the public only for about 48 hours.
2. The fact that an insolvency petition is scheduled for hearing in the daily cause-list does not mean that the insolvency petition was, in fact, heard on the scheduled date.

The information display systems of the NCLT do not give an overview of the entire cycle of the case and bits and pieces of information are available in the final orders. This severely constrains the ability of both the court administration as well as external researchers to assess the performance of the NCLT.[25] With the limited data that is available from these orders, we

[25]This data may be available in the case files maintained by the NCLT itself. However, the absence of this data in public domain implies extensive costs and resources to facilitate any precise assessment of the performance and efficiency of the court.

have attempted to estimate the average time taken for disposal of these insolvency petitions. Table 7 contains a summary of our findings.

Table 7 Average time taken for disposal of insolvency petitions

Stages	Number of cases	Average time (calendar days)
T0 to T1	12	18
T1 to T2	52	16
T0 to T2	24	24

Table 7 shows that the average time taken from the date of filing the insolvency petition to the date on which it first came up for hearing is 18 days(T0 to T1) and the corresponding average from the date on which it first came up for hearing to the date on which it was finally disposed off is 16 days(T1 to T2). Finally, the average time taken for disposal from the date on which the insolvency petition was filed is 24 days(T0 to T2). This is significantly higher than the timeline of 14 days prescribed under the IBC.

6.3 Describing admission and dismissal of insolvency cases

Table 8 shows the number of insolvency petitions admitted and dismissed during the sample period. Close to 45% of the orders studied dismissed the insolvency petitions filed before the NCLT. This leads us to infer that there is no inherent bias to admit or dismiss insolvency petitions among the NCLT benches.

Table 8 Total number of cases admitted and dismissed

Cases admitted	61
Cases dismissed	49
Total	110

A breakup of admission and dismissal across locations in Table 9 shows that the Mumbai Bench has been observed to admit the highest percent of petitions at 76% of the total number of insolvency petitions disposed off during the sample period. The New Delhi bench, on the other hand, dismissed 72% of the insolvency petitions disposed off by it during the sample period.

Table 9 also shows that the admission to dismissal ratio for the Mumbai and New Delhi benches is almost reverse. In five final orders passed by the NCLT, the insolvency petitions was dismissed because the insolvency was resolved by the parties outside the NCLT.

Table 9 Admission and dismissal of insolvency petitions across benches, Dec 2016 to May 2017

		Final orders passed	
Bench	Total number	Admitted	Dismissed
Ahmedabad	9	4	5
Allahabad	5	3	2
Bangalore	4	3	1
Chandigarh	11	8	3
Chennai	1	1	0
Hyderabad	3	0	3
Kolkata	4	2	2
Mumbai	41	31	10
New Delhi	32	9	23

Reasons for dismissal

The IBC sets out specific and limited grounds on which the NCLT may dismiss an insolvency petition. For example, insolvency petitions filed by operational creditors may be dismissed on the following grounds:

1. the insolvency petition is incomplete;
2. the debtor has repaid the debt in respect of which the insolvency petition has been filed;
3. the operational creditor has not delivered the statutory demand notice or the invoice to the corporate debtor;
4. the operational creditor has received a notice of dispute or there is a record of dispute in an IU; or
5. any disciplinary proceeding is pending against the IP proposed by the operational creditor.[26]

The grounds for dismissing an insolvency petition filed by a financial creditor are even more limited to the following three reasons:

1. the debtor has not defaulted to the financial creditor on the payment of debt in respect of which the insolvency petition is filed;
2. the insolvency petition application is incomplete; or
3. any disciplinary proceeding is pending against the IP proposed by the operational creditor.[27]

Table 10 indicates the different grounds on which insolvency petitions were dismissed during the sample period. This shows that a little under 50 percent of the insolvency petitions were dismissed on grounds *not specifically listed* in the IBC (recorded as *Others* in the Table.

[26] See section 9(5) of the IBC.
[27] See section 7(5) of the IBC.

Table 10 Grounds of dismissal of insolvency petitions

Ground of dismissal	No. of insolvency petitions dismissed
Existing dispute	8
Applicant was not a creditor as defined in the IBC	7
Settled out of court	5
Debt recovery barred by limitation	3
Incomplete application	2
Operational creditor failed to issue statutory demand notice prior to filing the insolvency petition	2
Others	22
Total	49

A review of a sample of dismissals classified as "Others" in Table 10 shows that several cases have been dismissed on grounds not explicitly spelt out in the IBC. For instance, in an insolvency petition filed before the Mumbai bench, the Tribunal took cognizance of the fact that all the ingredients required under Section 9 of the IBC were present to admit the insolvency petition and declare a moratorium. However, the NCLT extended the scope of its inquiry to the balance sheet of the debtor and held that since the debtor had sufficient assets on its balance sheet, it would be unfair and inconvenient for the debtor if moratorium were to be declared. In delivering this order, the NCLT ignored the creditor's argument that the provisions of the IBC do not give any scope to the adjudicating authority to embark upon a balance sheet analysis.[28]

In some of these cases, the NCLT has endeavoured to ascertain the underlying intent of the petitioners filing the insolvency petition. For instance, two insolvency petitions were dismissed by the New Delhi bench because the applicants were shown to be pursuing simultaneous remedies for debt recovery. The NCLT viewed this to be a malafide use of the IBC framework.[29] Similarly, in an insolvency petition filed by a debtor, the NCLT suspected ulterior motives on the part of the debtor on the basis that the debtor had not, prior to filing the insolvency petition, attempted to collect their receivables.[30]

[28] See CP No. 40/1& BP/NCLT/MAH/2017.
[29] See IB-39(PB)/2017 and (IB) 22 PB/2017.
[30] See (IB)-78(ND)/2017.

The purport of these orders seems to be that an insolvency petition filed by a creditor must be backed with an underlying intent to restructure or liquidate the debtor. In other words, the intent of an insolvency petition must not be restricted to merely recovering a specific claim.

6.4 Summarising the functioning of the NCLT under the IBC

The first look at the functioning of the NCLT suggests that the NCLT is able to deliver on the role of adjudication under the IBC, in contrast to the concerns that were voiced during the design of the IBC and the subsequent discussions about the difficulty of implementing adjudicating capacity rapidly.

The present evidence is significantly different from the long delays and pendencies that have been recorded in insolvency cases at the Debt Recovery Tribunal (DRT) under the previous regime (Regy and Roy 2017) . However, while the current functioning of the NCLT has countered expectations from prior insolvency cases, there are gaps that are visible between the functioning of the NCLT under the IBC and what is expected under the law.

That there are gaps is seen both in the empirical analysis on whether the NCLT is able to deliver judgements within the timelines required under the law, and whether the judgements are in keeping with the role visualised under the law.

While the sections above present the gaps between what is required under the law and what is delivered by the NCLT, there is a common theme that runs through all the above which must ideally become the first and immediate stage of reforms for the insolvency and bankruptcy regime: standardisation and improvement in information that is recorded in every NCLT order issued.

In part, this must become part of the rules of procedure at the NCLT and the NCLAT. In part, this must be translated into implementing the proposal of an administrative support system for the adjudicating bodies under the IBC and indeed, the Indian judicial system as a whole, as described in Section 4.2.4 of the Bankruptcy Law Reforms Committee 2015. Such a system will help to reduce the present idiosyncrasies that arise across NCLT and NCLAT orders, improve the quality of data that feedback into improving the insolvency and bankruptcy process and sharpen the efficiency of the insolvency and bankruptcy reforms.

7 Policy recommendations for data management under the IBC

In addition to the insights on the impact of the IBC on the behaviour of stakeholders and the functioning of the adjudicating institutions, the work of this paper hold insights for the organisation and management of data on insolvency and bankruptcy cases under the IBC.

First, there is as much qualitative as there is quantitative information in these cases that can be used to understand the impact of the reforms as well as how to keep the framework malleable. In accessing such information, the manner in which information is organised can be increased or restricted in its accessibility. Restrictions are often subtle but have negative externalities for the entire system. Not only do they hinder research and productive assessments but also render institutions incapable of being monitored and re-designed on the basis of performance oriented data.

At present, the orders of the NCLTs are not text search-able or machine readable. This feature is regressive in a day and age when openness, transparency and easy access is being aggressively demanded of public institutions all around the world.

As a consequence, it becomes extremely expensive for a third party to identify the milestones in the life cycle of a given case. For example, data regarding important milestones such as

- when was the insolvency petition filed;
- when did it first come up for hearing;
- if it did not come up for hearing as scheduled, the reason for such lapse;
- number of interim orders passed;
- number of hearings before the final hearing or the number of final hearings

is simply absent or organised in a manner that does not yield itself to research or analysis. In the current scheme of the organisation of public data by the NCLT, we have been able to observe the life cycle of very few cases (as is presented in Table 7).

These problems can be readily resolved if there are standard formats that are adopted for basic case data. It would be extremely beneficial if every order, at the start, has certain compulsory fields which are applicable across every kind of case, and which are necessary to allow an assessment of the law and the performance of the institutions under the law. Some examples of such fields are illustrated in the dataset created in this paper.

A standard format will also reduce variation in the basic quality of the order. While some orders have all the basic necessary information, others commonly have typographical errors and suffer from excessive linguistic complexities that render them virtually incomprehensible by a common man. The standard format need not restrict the freedom of the adjudicator nor impose structure of the flow of the judgement. Rather, it addresses the notion of the basic information that adds to every judgement that is published. Such a basic format should become the norm for all the institutions under the IBC, with all information published having a common form and a standard format with minimum basic information published by each institution.

In order for research and data input to be effectively used in the continuous and effective monitoring of institutions, the design for data management and publication must be improvised. This has ramifications on the continuous assessment or monitoring of the IBC itself, as well as the credit markets of India.

8 Conclusion

While India has witnessed the enactment of a plethora of laws, continuous monitoring of the performance of these laws and the institutions themselves has been rare and difficult.

In this paper, we undertake the assessment of one such law, the IBC, which as enacted, implies structural changes for all stakeholders in the form of new incentives driving their interactions and new institutions that govern this interaction. Further, this is a law which provides immense scope for a factual analysis of its effectiveness. This paper identifies the insolvency case orders published by the NCLT as the first available source of factual observations that can be systematically collected in a standardised format about the working of the IBC.

At the first stage of this exercise, we run into barriers in the form of the lack of a standardised format for the orders which means that there is a high variation in the information available from each order, and the lack of a research ready form of access of information which makes the information opaque to comprehensive research efforts. As a consequence of these barriers, measuring the effectiveness and working of the law, is still vulnerable to speculation and subjective analysis. However, both these are barriers that can be readily solved so that the work of independent researchers, academic institutions and the civil society at large can be facilitated.

The need for such work finds support in the preliminary performance measurement exercise described in the analysis in Sections 5 and 6. These

empirical analyses, though preliminary, indicate that the IBC is likely to have a structural change in the behaviour of economic agents, as well as the areas where the NCLT functions well as the adjudicator under the IBC and where gaps are emerging which need to be fixed.

As the insolvency cases grow, this data will increase in scope and size, and will hopefully fuel many research questions on the behaviour of economic actors as well as institutions with which they interface, and will hopefully become the source of the next set of reforms based on systematic data-backed analysis.

A Key to the fields in the insolvency dataset

Table 11 Description of data fields in the database

The table below describes the different fields captured in the NCLT insolvency case dataset, up to 15^{th} May, 2017. For the fields which are categorical variables, an exhaustive list of sub-categories is mentioned in the last column.
For character, date and integer fields, an example or the format of reporting data is mentioned.

	Field	Data type	Formats or Sub-categories
1	Case Number	Character	Eg: CP(IB)/19/7/HDB/2017
2	Bench	Factor [9]	New Delhi bench, Mumbai bench, Hyderabad bench, Allahabad bench, Ahmedabad bench, Kolkata bench, Chennai bench, Bengaluru bench, Chandigarh bench.
3	Who filed?	Factor [3]	Corporate debtor, Creditor, Not available.
4	Type of creditor	Factor [3]	Operational creditor or Financial creditor, Not available.
5	Type of Operational Creditor	Factor [10]	Bank, Decree holder, Employee, Franchiser, NBFC, Property buyer, Service provider, Supplier, Not available.
6	Type of Financial Creditor	Factor [10]	Bank, Bond holders, Corporate lenders, Debenture holders, Individual, NBFC, Property buyer, Service provider, Trustee/debenture holder, Not available.
7	Name of the corporate debtor	Character	Eg:"Unigreen Global Private Limited"
8	Amount of debt	Numeric	In INR
9	Secured / Unsecured debt	Factor [5]	Partially secured, Secured, Unclear, Unsecured, Not available
10	Due Date for payment	Character	DD-MM-YYYY or NA
11	Date of Demand Notice	Character	DD-MM-YYYY or NA
12	Date of receipt / service of Demand Notice	Character	DD-MM-YYYY or NA
13	Date of filing in NCLT	Character	DD-MM-YYYY or NA
14	First date of case listing	Character	DD-MM-YYYY or NA
15	Date of final disposal	Character	DD-MM-YYYY or NA
16	Evidence of debt	Character	Eg*: Invoices, Flat purchase agreement, NA
17	Admitted / dismissed	Factor [2]	Admitted or Dismissed
18	Category of reason for dismissal	Factor [7]	Existing dispute, Incomplete application, No demand notice, Not a creditor, Other, Settlement, Time barred
19	Name of the IP	Character	Eg:"Anand Ramchandra Bhatt"
20	URL	Character	http://nclt.c2k.in/OtherNCLT/Publication/principal_bench/2017/Others/3.pdf
21	Appeal	Factor [2]	Yes or No
22	Who appealed?	Factor [5]	Corporate debtor,Financial creditor, Operational creditor, Third party, Not available.
23	Appeal allowed / rejected	Factor [3]	Allowed, Rejected, Withdrawn.

*The list of examples is not exhaustive.

B Count of fields in the insolvency case dataset

#2. Location of bench

	Count
Ahmedabad Bench	9
Allahabad Bench	5
Bengaluru Bench	4
Chandigarh Bench	11
Chennai Bench	1
Hyderabad Bench	3
Kolkata Bench	4
Mumbai Bench	41
New Delhi	32

#3: Who filed?

	Count
Corporate Debtor	26
Creditor	83
Not available	1

#4: Type of creditor

	Count
Financial	20
Operational	63
Not available	1

#5: Type of operational creditor

	Count
Bank	1
Decree holder	1
Employee	5
Franchiser	1
NBFC	1
Property buyer	4
Service provider	19
Supplier	23
Not available	8

#6: Type of financial creditor

	Count
Bank	8
Bond Holders	1
Corporate Lender	1
Debenture holder	1
Individual	3
NBFC	2
Property Buyer	1
Service provider	1
Trustee/Debenture holder	1
Not available	1

#8: Amount of debt

	Count
(0, 500 cr)	90
(500 cr, 1000 cr)	2
(1000 cr, 1500 cr)	1
(1500 cr, 2000 cr)	0
(2000 cr, 2500 cr)	0
(2500 cr, 3000 cr)	1
Not available	16

#9: Secured or unsecured debt

	Count
Partially secured	2
Secured	21
Unclear	2
Unsecured	69
Not available	12

#10: Due date for payment

Month	Count
01	2
02	5
03	2
04	3
06	3
07	1
08	2
09	1
10	1
11	3
12	3
Not available	84

#11: Date of demand notice

Month	Count
01	14
02	13
03	3
04	2
12	1
Not available	77

#12: Date of receipt/service of demand notice

Month	Count
01	6
02	1
Not available	103

#13: Date of filing in NCLT

Month	Count
01	3
02	6
03	9
04	6
Not available	86

#14: First date of case listing

Month	Count
01	9
02	7
03	19
04	15
05	2
Not available	58

#15: Date of final disposal

Month	Count
01	8
02	11
03	26
04	42
05	23

#17: Admitted/dismissed

	Count
Admitted	61
Dismissed	49

#18: Reason for dismissal

	Count
Existing dispute	8
Incomplete application	2
No demand notice	2
Not a creditor	7
Other	23
Settlement	5
Time barred	3

#21: Appeal (Yes/No)

	Count
No	100
Yes	10

#22: Who appealed?

	Count
Corporate Debtor	6
Financial Creditor	1
Operational Creditor	2
Third Party	1
Not available	100

#23: Appeal status

Appeal status	Count
Allowed	6
Rejected	2
Withdrawn	2

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The Indian bankruptcy reform: The state of the art, 2017

ajayshahblog.blogspot.in/2017/07/the-indian-bankruptcy-reform-state-of.html

by Ajay Shah and Susan Thomas.

There is an urgency about bankruptcy reforms in India. The credit boom of the mid 2000s gave rise to many failed firms. There are 14,900 non-financial firms in the CMIE database with recent accounting data, and of these, there are 1,039 firms where there is not enough cash (PBIT) to pay interest. Firms under extreme financial stress are a drag upon the economy: they are unlikely to add capital or labour or obtain productivity growth. The exit of such zombie firms will free up capital and labour, and will help improve the financial strength of healthy firms. The economic purpose of the bankruptcy process is to close the circle of life; to recycle this labour and capital into healthy firms.

The numbers above are likely to be an under-estimate. CMIE only tracks the biggest companies. There are a very large number of smaller firms which are likely to be in default. There are other organisational forms used by firms, where we do not have data, and where there will be failed firms. Demonetisation and GST have stressed firms' health. Taken together, tens of thousands of cases are likely to be headed for the bankruptcy process.

When the Insolvency and Bankruptcy Code came into effect on 28 May 2016, we raised questions about the Indian bankruptcy reforms in an overview article (Shah & Thomas, 2016). A year has passed and we revisit those question. What is the state of the play in bankruptcy reforms? What of the new process is working well, and what are the areas of concern?

When the government and RBI decided to put 12 big defaults into the IBC, some felt this demonstrated the capabilities of the new bankruptcy code. When we speak with practitioners, we get a rush of war stories and practical detail. In this article we try to distill the hopes and fears, and try to see the woods for the trees.

Inputs, Outputs, Outcomes

In public policy, it is useful to think in terms of inputs, outputs and outcomes. As an example from the field of education, the inputs are schools and teachers. The outputs are kids who enroll. The outcome is what kids know, as measured through tools like OECD PISA or Pratham's ASER.

For bankruptcy reform, once the Insolvency and Bankruptcy Code was pased, there are:

Inputs
: Laws (both Parliamentary law and subordinate legislation), the institutional infrastructure that is required for the IBC to work, and capabilities of various private persons.

Outputs
: Transactions that go through the system.

Outcomes
: Recovery rates, the growth of broader credit markets, and the deeper changes in behaviour by private persons who borrow and lend, who will re-optimise as the bankruptcy process starts working smoothly.

The inputs perspective

Nine inputs are required for the bankrutpcy process to work, as envisaged by the Bankruptcy Law Reforms Committee (BLRC):

1. An Amendment Act to fix the mistakes in the 2016 law.

2. The Insolvency and Bankruptcy Board of India (IBBI) has to achieve the scale required for a high performance regulator.
3. An array of well drafted regulations have to be issued by IBBI, with a feedback loop to feed from practical and statistical experience into a robust regulation-making process to refine the regulations.
4. A competitive industry of private Information Utilities (IUs) has to arise.
5. A competitive industry of private Insolvency Professional Agencies (IPAs) has to arise.
6. A competitive industry of private Insolvency Professionals (IPs) has to arise.
7. NCLT has to find its feet in dealing with corporate bankruptcy, and DRT has to do similarly for individual bankruptcy.
8. Financial firms have to develop capacity on how to best to initiate the insolvency resolution process and participate in the process to ensure an optimal restructuring plans collectively.
9. Strategic investors, distressed asset funds and private equity funds have to gain confidence about expected outcomes, either when making a bid for a going concern or when buying assets in liquidation.

Input 1: IBC Amendment Act

The IBC, 2016, suffers from conceptual errors. There are contradictions in definitions, ambiguous definitions, problems in the establishment of the IBBI, failure to establish sound processes at IBBI, the lack of legal foundations in the institutional infrastructure including insolvency professionals, insolvency professional agencies and information utilities, the lack of clear integration of secured credit (i.e. SARFAESI) into the main bankruptcy process, etc. As an example, the Working Group on Information Utilities, chaired by K. V. R. Murty (MCA, 2017) has a chapter on amendments required in the IBC in respect of information utilities.

The IBC has elementary drafting errors. Some examples of these are discussed in Malhotra & Sengupta, 2016, and Singh & Mishra, 2017. A fuller examination will reveal a larger list of such drafting errors.

The insolvency resolution and liquidation processes are procedural law where drafting errors can lead to litigation. As an example, Sibal & Shah, 2017, analyse an anomaly about antecedent transactions.

Many laws in India undergo a constitutional challenge in their initial days. Some founders/shareholders may go to the courts claiming that the IBC violates basic constitutional rights. Well funded attempts of this nature are likely with the 12 big cases. The Bombay HC dismissed an early challenge to the constitutionality of the IBC, but it did this without substantively deciding on its merits. We believe that, in the design of the IBC, sufficient thought was given towards ensuring due process and fairness to all creditors as well as the debtor. There may be certain drafting flaws in the IBC which the government may need to rapidly solve.

An Amendment Act is required which addresses these problems. In our knowledge, there is no drafting effort that is presently in motion to solve this.

Input 2: IBBI emerging as a high performance regulator

Indian regulators suffer from low State capacity. Capacity in a regulator comes about through five processes: (a) The composition and working of the board; (b) The legislative process; (c) The executive process; (d) The quasi-judicial process; (e) Reporting and accountability. Hygiene in these world-facing processes should have been codified in the IBC, but was not.

Considerable new knowledge has developed in the last decade on how to achieve State capacity by setting up such processes. A good deal of this is discussed in the report of the Working Group on the Establishment of IBBI, chaired by Ravi Narain (MCA, 2016). Many aspects of this report have yet to be brought into IBBI.

The IBBI has been set up. It has an office and a team. It has been shouldering the effort of drafting regulations

on a very tight timeline. IBBI has done a particularly good job in some respects, such as the recent unveiling of a mechanism to take feedback from the public in structured documents about the regulations that it has drafted. In this, IBBI is now ahead of SEBI and RBI on good governance practices.

The regulation-making process that has been used by IBBI so far has good features. The organisation structure used at IBBI respects the difficulties associated with setting up a regulator that violates the principle of separation of powers. However, these things are not in the IBC, or in rules under IBC, or in legal instruments issued by the board. There is the danger that good practices may be fall by the wayside at a future date.

IBBI is expected to perform a certain statistical system role, and a research capacity that can use this to strengthen regulatory capacity. The systematic process of using data to improve the working of the bankruptcy process is critical to the bankruptcy reform. Statistical system work at IBBI has, however, not yet commenced.

Thus, in critical aspects, IBBI is going down the route of conventional Indian regulators such as SEBI or RBI. This will reproduce the well known infirmities of conventional Indian regulators and runs counter to what the bankruptcy reform requires.

Input 3: Sound subordinate legislation

IBBI has issued 12 pieces of subordinate legislation. There are flaws in many of these regulations, some of which are described under the other sections in this article, which will hamper the working of the bankruptcy process and of the institutional infrastructure under the Act.

A critical part of the bankruptcy reform is individual insolvency. Advancing on this front will get India away from the recurrent loan waivers which spoil the repayment culture of borrowers, raise the cost of lending to individuals, and harm credit access to individuals as well as small entrepreneurs. This part of the law has not been notified, and IBBI has not released regulations that are required to operationalise the individual insolvency component of the IBC.

Input 4: The IU industry

Under normal circumstances in an insolvency resolution process (IRP), a considerable amount of human effort is required in order to construct the list of creditors and the size of their claims. The BLRC design envisaged that this information would be stored in `information utilities (IUs)', as electronic records of credit contracts in computer systems, authenticated by creditor and debtor, which would thus eliminate delays and costs. In the Indian legal system, disputes about facts are well acknowledged as the source of delays, wastage of judicial time, and payments to lawyers. Irrepudiable records from IUs would eliminate these problems.

So far, no IU has come into operation.

One part of the problem lies in the IU regulations issued by IBBI. Prashant et. al. 2017 point out its anti-competitive features. The licensing requirement for the IUs are overly stringent, particularly for an industry where the costs of implementation are likely to be low because of the constantly decreasing costs of information technology. The regulations ask for capital requirements that are excessive, given the low levels of value at risk in the business. This is a new business with no precedent anywhere in the world. Entrants into this are are taking on the risk of failure of the business model, which must be compensated by sufficient returns to investment. The IU regulations simultaneously prescribe shareholding arrangements that deter enterpreneurs from viewing this as a viable business opportunity.

These barriers are likely to keep the Indian bankruptcy system from achieving a competitive industry of technologically capable IUs to serve multiple types of borrowers and lenders, as was visualised by the BLRC when designing the IBC. There are also other technical flaws in the IU regulations as is pointed out in Prashant et. al, 2017.

Input 5: The IPA industry

Insolvency Professional Agencies were envisaged by the BLRC as a strategy to regulate professionals through the structure of a self-regulatory organisation. However, the IPA regulations issued by IBBI have many features that vitiate this objective. As a consequence, the key players who were envisaged in this industry by the BLRC have been barred from it.

The existing players are generally passive and are not performing the role that is required of IPAs in the bankruptcy reform. In most aspects, the IPAs are going down the route of conventional Indian regulators-of-professions such as ICAI or BCI. This is likely to reproduce the widely acknowledged infirmities of these organisations, and is counter to what the bankruptcy reform had attempted to achieve by way of well regulated insolvency professionals who act in the best interest of the stakeholders in the resolution process.

IPAs are expected to create certain supervisory databases. These would be extremely valuable in the process of diagnosing problems of the bankruptcy reform and addressing them. So far this has not come into being.

Input 6: The IP industry

A set of insolvency professionals (IPs) are in place. During the IRP, if required, the IP is expected to put together a temporary management team and temporary financing (under the guidance and approval of the creditors' committee) that will stabilise the firm. These are new roles for the IPs in India, who have yet to develop capabilities to carry out these functions, either within their organisations or through an extended network. It will take time and competition for IPs to develop the teams through which they are able to fully discharge such functions, particularly in complex cases.

One way to jump-start getting such capability would have been to open the industry to foreign insolvency professionals. Their participation, particularly at the early stages of the reforms implementation, would have helped augment capacity and diffuse knowledge. Most Indian IPs are likely to be in a repeated game with promoters; foreign IPs would be particularly valuable in their ability to be harsh with promoters, which would help set the tone for the working of the bankruptcy process. The entry of foreign IPs was, however, blocked by IBBI through the subordinate legislation (Burman & Sengupta, 2016).

A critical factor in dealing with a going concern is lining up interim financing. The IBC and the subordinate legislation fail to clarify the priority of interim financing, in case the firm goes into liquidation. This has hampered the ease of access to interim finance while in the IRP.

IPs are given considerable power in the working of the IRP. There is a need for regulation of the profession in order to deal with various kinds of misbehaviour that can arise. BLRC had developed sophisticated thinking on how the IP and IPA industries should work (Burman & Roy, 2015). A lot of this did not make it into the IBC or the subordinate legislation. The IPAs as constructed today are not performing the roles required of them in regulation of IPs. While IBBI has enforced against IPs on relatively trivial violations, IBBI itself is not equipped to enforce against the real challenge, of malpractice by IPs: it cannot overcome the lack of IPA capacity.

When IPs step into the shoes of the board, and make vital decisions, they are exposed to a new level of legal risk. There is a need for insurance against these risks. This is not yet available in the market.

Input 7: The working of NCLT and DRT

While the design of the IBC has many features that will yield speed under Indian conditions, the working of NCLT/DRT is still a key factor that will determine rapid resolution as part of the Indian bankruptcy reform (Datta and Regy, 2017).

At present, we see many problems, such as inconsistencies in the behaviour of NCLT across locations, a few

orders that are wrong, the lack of orders organised as structured documents, low transparency on the web, and delays. These may be a small precursor of the difficulties to come, as the case load has thus far been mild. Most defaults are, as yet, not going to the NCLT as creditors are waiting to see how the IBC works out. If the bankruptcy reform progresses, we will go from a case load of 20 per month to $10\times$ or $100\times$ as much (Damle & Regy, 2017). At this level of load, the unreconstructed NCLT will experience an organisational rout and will become the chokepoint of the bankruptcy reform.

NCLT has gone down the route of conventional courts and tribunals, which has reproduced the well acknowledged infirmities of the judicial process in India. This is not commensurate with what the bankruptcy reform requires. New knowledge needs to be brought to bear on the working of NCLT (Datta & Shah, 2015).

Input 8: The thinking of financial firms

New thinking by banks and insurance companies is required if they are to play their part in the new bankruptcy process. However, their thinking is greatly shaped by regulations. Errors in the present body of banking regulations, and the associated enforcement machinery, have created an incentive to hide bad news, to not initiate the IRP and to vote irrationally in the creditors' committee.

Sound micro-prudential regulation is one which would require that when a default takes place, the lender must rapidly mark down the value of the asset to zero. This loss should go into the Income and Expenditure statement immediately. Once this is done, there is no overhang of the past, and the lender will be rational about recoveries. Whether the asset is sold off, whether IRP is filed, how to vote on the creditors committee: All these decisions will be based on commercial considerations alone. Recoveries in the future would flow back into the Income and Expenditure statement.

These issues have yet to make their way into micro-prudential regulation of banks and insurance companies.

Assuming RBI and IRDA address these mistakes in micro-prudential regulation, we may see a new cycle being established within two years. New defaults should immediately show up as expenditure, and there would be a flow of cash from old defaults where the bankruptcy process has been completed. This is the opposite of the present arrangement, where it is claimed that all loans are profitable other than some old loans which induce losses.

In the case of NAV-based financial firms, such as mutual funds and pension funds, the event of default should influence the marked-to-market (MTM) prices even if the secondary market for the bond is not liquid. Here also, the bias in micro-prudential regulation should be to mark down the prices to near zero values quickly. This will create incentives for these funds to sell off these assets to distressed debt funds, when these transactions would yield a price that exceeds the MTM price that was used internally.

On 4 May 2017, an Ordinance was promulgated that gave RBI powers to push banks to initiate IRP. There is less to it than meets the eye (Datta & Sengupta, 2017). Backseat driving in a few cases, even if done wisely, cannot solve the regulation-induced bad behaviour of banks. There is no substitute for the slow hard work of reforms of bank regulation and supervision.

Input 9: A pool of buyers

The reforms requires the presence of two key groups of buyers. These are strategic players in the same sector, such as Jet Airways for the Kingfisher bankruptcy, and private equity funds (Shah, 2017).

Small firms lack the ability to set up dedicated teams that focus on opportunities coming up in the bankruptcy process. However, there should be teams at the top 2000 companies that watch the bankruptcy process and look to buy up useful things that come along, either in the form of going concerns or the liquidation process. Private equity funds have not yet started looking at this area on a significant scale. A few pioneers will get started. As they reap strong returns, other funds will follow, and new money will be raised to pursue these opportunities.

We could have developed these capabilities through `asset reconstruction companies' from 2002-2016, but through mistakes in the RBI regulations for these (Shah et. al. 2014), that opportunity was wasted.

As long as the IBC and its institutions are unproven, there will be a shortage of buyers, which in turn will lead to very low prices for the stressed assets. At the early stage, buyers will fear legal risk in the IBC, and will shy away from investing in building organisational capital. The critical story in the evolution of insolvency institutions in India is the emergence of thousands of skilled professionals at private equity funds and the 2000 big companies, each surrounded by an ecosystem of lawyers, accountants and consultants, armed with capital, process manuals and authorisations, who are ready to go. We are at the early stages of that journey.

Outputs

If completed transactions are the output of the bankruptcy process, we are still some way from observing outputs under the IBC. So far, roughly 100 transactions have begun on their journey in the IRP. None has completed it.

The intent of the law was that six months after the initiation, the IRP should end with either a successful vote for a restructuring plan or the start of the liquidation process. The threat of value destruction in the liquidation would create a focus in the minds of the creditors committee, and thus avoid the delaying tactics that are seen in India today.

The first case, Innoventive Industries, started on 17 January 2017. Six months from that date is 16 July 2017. The delay with which this first case is completed will be an important first milestone for the bankruptcy reform.

In the coming months, a series of important milestones is anticipated:

- First case where interim financing is obtained.
- First vote by a creditors' committee.
- First case to complete IRP with a super-majority in favour of a restructuring plan.
- First case where the IP ejects the promoters from the firm
- First case to commence liquidation.
- First case to complete liquidation.
- First individual insolvency to commence and complete.

An analysis of the orders passed by the NCLT (Chatterjee et. al, 2017 (forthcoming)) shows that some of these milestones will come soon. We will soon be talking in the language of cases per month and Rs.Bln. per month, in the aggregate and across categories of defaulters, which will be the output measures of the bankruptcy reform.

Outcomes

The proximate outcome of the bankruptcy process is the recovery rate. This expresses the NPV of recoveries on the date of default as a ratio to the face value of the debt on the date of default. What would give us a high recovery rate?

- The lack of delays in the IBC processes;
- The extent to which liquidation is avoided for recent defaults;
- Competition on the buy side, i.e. the number of prospective buyers; and
- The extent that buyers feel there is predictability and certainty in the IBC processes (i.e. the lack of a lemon model problem).

The value of a firm is greater than the liquidation value only when the firm is a going concern. Financial distress disrupts the smooth working of the firm and damages organisational capital. For this reason, it is optimal that the resolution process must commence a day after the first default. However, for the bulk of the cases which are now being brought to the IBC process, the first default is likely to have taken place a long time ago. The recovery rates obtained there are going to be low. This is not a comment on the bankruptcy reform.

We should focus on new defaults that are brought into the IBC. These are the real test of IBC, where there continues to be organisational capital, and there is an opportunity to obtain higher recovery rates. If the bankruptcy reform is successful, new defaults should result in restructuring plans that achieve the super-majority in the creditors committee, obtain a new management team, avoid liquidation, and achieve high recovery rates. An equally important issue for new defaults is the ability of the market to correctly distinguish between firms that are worth rescuing as going concerns versus those that should be put into liquidation.

In liquidation, good outcomes will be rapid sales through which the recovery rate is enhanced, and predictable flow of cash through the IBC waterfall.

Once a certain recovery rate is consistently obtained --- even if it is a low value --- this will bring a new level of confidence to lenders. The first milestone is to gain confidence that we will consistently get a (say) 20% recovery rate. The second milestone is to get the recovery rate up to better values. As these milestones are achieved, lenders will become more comfortable with a broader range of credit risk and maturity. Once many transactions are completed, we will be able to do statistical analysis of delays and recovery rates, differentiated between firms across size categories (small/medium/large) and date of default (recent/old). That will yield report cards of the Indian bankruptcy reform.

Looking forward

A story about organisational capability. Almost everything described here is a story about the capabilities of organisations: of MCA, IBBI, RBI, SEBI, NCLT, DRT, IPAs, IPs, IPAs, IUs, the biggest 2000 companies, distressed debt and private equity funds. A well functioning bankruptcy process involves all these persons skillfully playing their own part. At first, these organisational capabilities do not exist. Nine months after being setup, IBBI has just five senior officers. We need to assess gaps in organisational capabilities, and undertake steps which foster this capability, both in individual organisations as well as jointly across them all.

There is a coordination problem here: organisation x tends to underinvest in building organisational capacity as it sees that the remainder of the ecosystem lacks the requisite capabilities. This hampers the rate of return to its own investments in building organisational capability. If person i were sure that person j was going to invest in building organisational capital, then the marginal product of investment in organisational capital for person i would be higher.

Too often, new organisations in this field are emulating existing organisations. IBBI is slipping into the mores of SEBI and RBI, NCLT is built like a conventional Indian court, IPAs have become like their parents, the quality of drafting law and regulations is slipping closer to conventional Indian standards. This ends up in an environment of low expectations and low organisational capabilities. Instead, we must create a climate of excellence, and work to build high performance organisations.

The lack of data is shaping up as a big barrier. The BLRC design had envisioned a data-rich environment for bankruptcy reform. This included the NCLT issuing structured orders, IBBI building a statistical system, IPAs building supervisory databases and large-scale data capture at IUs. So far, a small part of this has begun. The fog of war is heightened, and all persons are faring poorly on strategy and tactics. The creation of data, and downstream research based on this, that has been done by projects such as Chatterjee et. al. (2017, forthcoming) is a critical element of the bankruptcy reform process.

From uncertainty to risk, and reduction of risk. As with the establishment of all markets, private persons avoid committing resources that are required for building human capital in the field. This leads to a chicken-and-egg

situation: lenders are loath to take distressed firms into IRP as the buyers are missing. The buyers are missing as there are not enough available transactions.

The ex-ante legal risk as seen by buyers is considerable. They know the inputs that are required to make the bankruptcy process work. They worry about the legal challenges that may materialise even after they have supposedly got a transaction. They compensate for these risks by low-balling their bids.

As cases move through the IBC processes, uncertainty about the working of the process is reducing for private persons. In time, uncertainty will be replaced by risk: they will understand the contours of the problem and they will build some priors about the process. In due course, more private persons will gain confidence and show up as buyers, thus yielding the ultimate desired outcome: high recovery rates.

Load and load bearing capacity. Big cases present a bigger load upon the fledgling institutions (Shah, 2017). With big cases, private persons have more to lose, and will use every means, fair or foul, to avoid losses. The high powered legal teams that have come together around the Essar Steel default are consistent with this prediction. Their actions, the precedents that they establish, and the way these events reshape the prior distributions of all the players, may end up harming the Indian bankruptcy reforms. The 12 big cases are hotspots for the bankruptcy reform where many things can go wrong. We are likely to obtain particularly weak recovery rates for these, as a big load is juxtaposed against a weak load-bearing capacity.

Success is not assured. There is universal optimism about the Indian bankruptcy reform. We worry that failure has not been ruled out. If the present effort at bankruptcy reform fails, it will be a tremendous loss of confidence in the eyes of creditors, and there will be sustained cynicism on the part of the private sector about future reform efforts. The Indian bond market is an example of persistent failure of reform, leading to endemic cynicism on the part of private persons. Such cynicism leads to reduced investments by private persons in organisational capital, and thus reduces the probability of success in the future.

Conclusion

The Indian bankruptcy reform is work in progress and there are many areas for concern.

A lot of the policy work in the bankruptcy reform has been approached as business as usual. In the Indian policy process, business as usual results in endemic failure. The success stories of the Indian policy process, like the telecom reforms, the equity market reforms, and the New Pension System, did not come from business as usual. The visible difficulties, after the first year of the bankruptcy reforms, call for higher resourcing and improved organisation for the nine areas of inputs, and a shift away from business as usual.

As Dr. Sahoo has emphasised, we will never have a perfect law and perfect regulations and a perfect IBBI at the early stages of a reform. What matters most is the intellectual capacity in discerning incipient problems, diagnosing them swiftly and correctly, and coming out with effective solutions. The private sector is ultimately watching the policy apparatus and waiting for this feedback loop to emerge.

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Indian bankruptcy reforms: Where we are and where we go next

ajayshahblog.blogspot.in /2016/05/indian-bankruptcy-reforms-where-we-are.html

by Ajay Shah and Susan Thomas.

Note: The 2017 state of the art is out.

Bankruptcy reforms have been moving forward at a blistering pace for the last few weeks, with the Insolvency and Bankruptcy Code ("IBC") being enacted by the Lok Sabha and then the Rajya Sabha. In this article, we take a look at where we are in Indian bankruptcy reform, and where we need to go next.

1 Bankruptcy reforms in the context of Indian economic reform

All business plans are speculative views of the future. Some will inevitably go wrong, either because of failures of conception or of execution. As India lacks the requisite institutional arrangements, at present, when a firm goes into default, the management, capital and labour get stuck in an interminable mess. With a sound bankruptcy process, we would be able to rapidly resolve the situation, and everyone would move on. This is the best outcome for society at large. In such a world, there would be more entrepreneurship, more risk taking, more debt, more unsecured debt, and more non-bank debt.

In India, the lack of a sound bankruptcy process implies a flawed legal foundation of limited liability companies. The classic definition of limited liability is a bargain: *Equity is in charge of the company as long as all dues to Debt are met. When the firm defaults on its debt obligations, control over the assets of the firm shifts from Equity to Debt*. This is not how India understands limited liability today. We tend to think that a company belongs to its founding family no matter what happens by way of firm default.

As a financial agency with a keen interest in good bankruptcy outcomes for banks, RBI has led many attempts at bankruptcy reform. These include CDR, SDR, wilful defaulters, and ARCs. However, these have not delivered results. Even if these policy initiatives had been better designed, the role of RBI in the credit market is inherently limited because there is much more to lending than lending by banks. The bankruptcy process requires a machinery that is grounded in Parliamentary law, which is beyond the powers of regulations or informal arrangements made by a financial agency.

One component needed for bankruptcy reforms was built by the Financial Sector Legislative Reforms Commission (FSLRC), led by Justice Srikrishna from 2011 to 2013. The `resolution corporation' in the draft `Indian Financial Code' (version 1.0 in 2013 and then version 1.1 in 2015) is a specialised bankruptcy process for two kinds of financial firms: those that make intense promises to consumers, and those that are systemically important. This component has been slowly moving towards implementation, after MOF first setup a `Task Force' on the subject, and then made an announcement in Para 90(i) of the budget speech of February 2016. But the bankruptcy process for all other firms was a project waiting to be done. Some work on these lines went into the Companies Act, 2013, but it only partly dealt with the mechanisms of restructuring and winding up.

2 The journey to the law

The Budget Speech in July 2014 had one sentence in Paragraph 106:

> *Entrepreneur friendly legal bankruptcy (sic) framework will also be developed for SMEs to enable easy exit.*

This sentence could have been done in an incremental way. Instead, it was taken on a more ambitious scale at the Ministry of Finance (MOF) with a policy project that would go beyond just an SME bankruptcy framework for India. In late 2014, MOF setup the Bankruptcy Legislative Reforms Committee or the BLRC, led by Dr. T. K. Viswanathan, with the objective of building a full fledged bankruptcy code.

The work of the BLRC was placed in the FSLRC division of the Department of Economic Affairs (DEA), so as to harness the institutional memory about the working of FSLRC. The BLRC submitted a two volume report on 4 November 2015. The report is similar to the output of the FSLRC: the economic rationale and design features of a new legislative framework to resolve insolvency and bankruptcy was in Volume 1 and the draft bill was in Volume 2. These materials were put on the MOF website. A modified version of this bill, with public comments incorporated, was tabled in Parliament in the winter session on 23 December 2015.

After the IBC was tabled, the Joint Parliamentary Committee on Insolvency and Bankruptcy Code, 2015 (JPC) was set up on the same day to analyse the draft bill in detail. The JPC submitted its report which included a new draft of the law. This is the draft Insolvency and Bankruptcy Code (IBC) that has since been passed by both houses of Parliament.

3 The key ideas of the BLRC report

The essence of the BLRC proposal is a formal procedure, termed the `insolvency resolution process' (IRP) which starts when a firm or an individual defaults on any credit contract. Any creditor is empowered to initiate an IRP: a financial firm or an operational creditor whether it is a non-financial firm or an employee. An insolvency professional (IP) called the `resolution professional' (RP) manages the working of the IRP, and is responsible for compliance with the law.

Once the IRP commences, power shifts from shareholders/managers to the Committee of Creditors. This includes the power to take over management of the firm, the ability to change management, to bring in fresh financing, to ask for all information required in order to invite bids for commercial contracts, including from the existing creditors and debtor, to keep the enterprise going. Decisions are made by voting in the Committee of Creditors.

For firms who have significant organisational capital, the value of the firm as a going concern in the eyes of a buyer would exceed the liquidation value of the assets of the firm. Such firms are likely to attract bids where the value of the firm is more than the value of its physical building blocks. However, organisational capital rapidly depreciates. Hence, it is critical for the IRP to begin quickly and move forward quickly, aiming to get closure while the firm is still a going concern, so as to avoid value destruction with the firm becoming defunct.

Speedy resolution is incentivised in the IBC by having a time limit of 180 days for the IRP. If, in 180 days, 75% votes in the Committee of Creditors do not favour one resolution plan, the debtor is declared bankrupt. The IBC then provides clarity about which assets are available for liquidation, and a clear prioritisation of who has rights to these assets for recovery, in liquidation.

In general, the recovery rate for creditors is lower when a firm goes into liquidation. This creates incentives for the creditors to be rational about their activities in the critical 180 days.

The process of resolving insolvency is similar for firms and for individuals. In the case of individuals, however, the final resolution plan must have the consent of the debtor. There are additional innovations in the process of individual insolvency in the IBC that will increase individual default resolution efficiency in India. One is the concept of the Fresh Start, which gives a debt write-off for individuals who are below certain thresholds of wealth and income at the time of default.

Another innovation concerns an individual who has offered personal guarantees to support firm loans. When the firm default triggers these guarantees, it is likely to stress the personal guarantor to default and trigger individual IRP. Under the IBC, ordinarily, this individual insolvency case is heard at a Debt Recovery Tribunal (DRT). S.60

establishes that the IRP of the personal guarantor will be heard in the same court as the firm IRP, which is the National Company Law Tribunal (NCLT). This can lead to a quicker resolution and recovery for creditors who lent to the firm based on the personal guarantee.

This is the essence of the IBC. In order to make this work in India, IBC envisages four critical pillars of institutional infrastructure:

1. Robust and efficient adjudication infrastructure will be required, on the lines of the Financial Sector Appellate Tribunal that is proposed in the Indian Financial Code.

2. A new regulated profession -- of Insolvency Professionals (IPs) who can be Resolution Professionals and Liquidators -- is required. India has a long history of failure in regulation of professions, as is seen with lawyers, chartered accountants, doctors, etc. The success story here is the regulatory system run by exchanges for brokers. These ideas need to be brought into making the insolvency profession work.

3. Delays destroy value, and disputes about *facts* in India can drag on for years. A new industry of `information utilities' (IUs) is required who will control trusted data, pertinent to the operation of the IRP as well as used during Liquidation. This would draw on the success that India has had with the working of the securities markets depositories.

4. A regulator is required, to perform (a) The legislative function of drafting regulations which embed details about the working of the IRP; (b) Legislative, executive and quasi-judicial functions for the regulated industries of information utilities and the insolvency profession; and (c) Statistical system functions.

4 Strengths of the BLRC process

The BLRC process had four sound features.

1. *Systemic reform*. BLRC embarked on a systemic reform. It did not incrementally modify existing laws such as the Companies Act, 2013, or SARFAESI.

2. *Using local domain knowledge*. The project was staffed with people who were grounded in knowledge of India. While international experience was fully utilised, it was not mechanically transplanted. As an example, the BLRC was aware of the US `debtor in possession' mechanism, and consciously chose to not use it based on wisdom about how this would work under Indian conditions. These decisions were made based on local knowledge about how alternative institutional arrangements would work in India.

3. *Innovation*. The BLRC was not merely imitative. The proposals were novel in many respects, with a focus on solving problems rather than reshuffling a fixed menu of possibilities. One example of this is the concept of a regulator that writes subordinate legislation in order to obtain malleability in the design of the bankruptcy process, which is not found in the bankruptcy process elsewhere in the world. Another example is the rearranging of incentives for rapid and rational thinking during the IRP, in recognition of the difficulties of banks in India.

The conventional Indian solution for information utilities would have been a government-run monopoly like MCA21. Instead, the BLRC envisaged a private competitive industry of IUs. The conventional Indian solution for regulated professionals would have been a monopolistic association, similar to ICAI, ICSI, MCI, BCI. Instead, the BLRC visualised a private competitive industry of self regulatory organisations, the IPAs, who would oversee IPs.

4. *Capacity building*. The journey to the BLRC report and draft law has created new knowledge (web site) and a community which has expertise on this subject. This opens the possibility of sustained progress on India's journey to bankruptcy reform, with a local community of expertise, who are committed to work on the reform over a sustained period.

5 Analysis of the law

Our reading of the law reveals seven areas of concern.

1. *Precision of language*. In all countries, insolvency and bankruptcy law is a detailed procedural law, where the efficiency of the outcome is driven by the clarity and precision of the provisions in the law. This is unlike other laws, e.g. the Indian Financial Code, which have more of concepts and less of gritty procedures. This clarity is critical to ensure that any party reading the law comes to the same interpretation of the law -- be it lawyers, practitioners or judges. Vijay Mallya and his ilk are not going to accept their loss of power and assets without a tough legal fight. IBC as passed by the Parliament has many flaws which give grounds for concern. As an example:

- The law is silent on what denotes evidence of default, which was proposed by the BLRC to be a record in an IU.
  The law requires a *financial creditor who has triggered an IRP to furnish a record of the default from an IU or such other record or evidence of default as may be specified by the Regulator.* Similarly, the law requires an interim RP to collect claims. However, it does not specify the kind of proof that a claimant needs to submit to the interim RP. Both these provisions negate the incentive to file financial information in an IU, especially where the law is generally silent on what kind of firms need to file financial information in IUs mandatorily.
- Section 30(2)(c) says the resolution plan must *provide for the management of the affairs of the Corporate debtor after approval of the resolution plan*. This imposes uncertainty on how the resolution plan can be assessed, which in turn, increases the possibility of higher judicial intervention.
- The numerical values included in the law for many time limits could give cause for the adjudicator to permit an extension on the time to decide on a resolution plan. This raises concerns about the extent to which the core objective of bankruptcy reform -- speed -- would be achieved.

2. *The working of the regulator*. India has ample experience with bad performance of regulators. One important source of these persistent failures is the faulty legal foundations that define the working of regulators. Other countries solve this problem by having a general legal framework for the working of regulators (as in the case of the U.S., but absent in India) or in the laws that establish regulators (which is present in IFC but missing in the IBC). While the report submitted by the JPC reiterates the criticality of role of the regulator, a sound chapter in the law that establishes the regulator is absent.
Particularly worrisome are elements such as S.226 which gives the power to the government to reconstitute and supercede the Board, which hampers regulatory independence.

3. *Information utilities*. The legal provisions for the IUs ought to have been as detailed as the Depositories Act. This has not been done. Examples of faulty provisions include:

- IUs are supposed to be a private competitive market. However, the law has failed to incorporate insights about the competitive market within which IUs were intended to operate. There was to be only one price, for data submission, and multiple IUs would compete in offering lower prices to those who submit mandatory information. The draft bill now has the concept of a one-time registration fee. It is not clear how IUs will have a revenue stream and effective mechanisms for competition.
- Provisions on authenticity and repudiability of IU records as evidence of claims and default have not been introduced into the draft bill.
- Provisions for data privacy are lacking.

4. *Insolvency profession* Provisions governing the legislative, executive and quasi-judicial functions of the IPAs ought to have been as detailed and complex as provisions governing the creation of exchanges and other such financial market infrastructure institutions as in the IFC. This is missing in the law.

5. *Forbearance*. At several places in the law, there are exemptions in the process that can be granted by the Central Government. This is a matter of grave concern. As an example, forbearance in banking regulation gave us the banking crisis today.

During the IRP, the Central Government can exempt transactions from the moratorium, in consultation with any financial sector regulator (Section 14(3)). Likewise during liquidation, while no suit can be instituted against the corporate debtor once a liquidation order is passed, the Central Government can exempt legal proceedings from this provision, again in consultation with any financial sector regulator (Section 33(6)). These provisions are dangerous.

6. *Judicial infrastructure*. The law does not set in motion a world class tribunal. By being silent on this issue, the draft bill ran the risk of delays and transactions costs associated with courts and tribunals in India today. A bankruptcy process that works in the unit of days is alien to today's courts that work in the unit of months.

7. *Transition issues*. Full care on repeals is required. Some of these are repeals of primary laws, and some are incompatibilities with subordinate legislation. However, these are absent in the law.

6 The way forward

That Parliament has passed the law is a major step forward. However, in and of itself, this does not yield success in the sense of getting to the desired economic outcomes. While some elements of the process that led up to this law were well done, in many respects, there were shortcomings compared with the 11 principles of sound process design for drafting of laws. The IBC, 2016, is an important milestone, an important way station in the long journey of Indian bankruptcy reform. But it does not, in and of itself, deliver an improved bankruptcy process for India. Now, seven areas of work are required.

7 Work area 1: Improvements of the law

The first area of concern is a thorough review of the law. This is a law that is going to be actively litigated. Defaulters of the future are not going to cede power to the Creditors Committee without a fight. Expert input should be sought now, on anticipating these problems, and strengthening the draft. This will require an understanding of not just the law, but all the points in the process which interacts with other laws of the land.

The alternative way to fixing the law will be to run through cases that are lost in the Supreme Court over the next five years. For example, in the case of the Companies Act, 2013, many years elapsed between enacting the law and starting to solve the problems of a poorly drafted law. If such delays can be avoided with the IBC, this would improve matters.

8 Work areas 2: Drafting of subordinated legislation

The law embeds large areas for subordinated legislation, both rules (by the government) and regulations (by the regulator). Even when the law is faulty, it is possible to rescue things by good quality drafting of this subordinated legislation. Whether this possibility materialises depends on the choice of team, and the regulation-making process that is employed.

9 Work areas 3,4,5,6: Building the four pillars of institutional infrastructure

The second key concern is the four pillars of institutional infrastructure. Enacting a law does not induce the requisite State capacity. The regulator has to be built. The DRTs have to be upgraded and the NCLT has yet to be set up. An engagement with the private sector is required in bringing forth the first wave of firms who will be information utilities (IUs) and insolvency profession agencies (IPAs). Without these four pillars of institutional infrastructure, the law is infructuous.

A well drafted IBC would have created better incentives for the sound working of the four pillars of institutional infrastructure. Given the flaws in the IBC, this task has become harder. An even higher quality effort is now

required, to achieve sound institutions. In parallel, the law requires many modifications as an integral part of this process of institution building.

For example, there are proposals today to improve adjudication infrastructure through the use of information technology. In and of itself, this will not deliver the desired results. Just as in education, it is necessary to have school buildings, but this is not a sufficient condition. The problem is much more complex, it is about establishing sound processes for the judiciary. The mere presence of a computer terminal in every court room will not deliver the outcomes desired here: to ensure that an IRP can be admitted within the day of the application, or that a creditors' committee can be finalised within a fortnight that the IRP starts.

A `Task Forces' process was used to implement institutional infrastructure for the FSLRC report. MOF initiated `Task Forces' with a group of subject experts to plan and oversee the implementation. A similar approach needs to be adopted by the implementing ministry for the IBC to create the four pillars of institutional infrastructure.

10 Work area 7: Project management for the transition

The last one year of the old regime and the first one year of the new regime are going to require particularly careful planning and handover.

For example, the RDDBFI Act needs to be amended in order to have the DRTs serve as the adjudication infrastructure for individual cases under IBC. At present, amendments have been proposed to both the RDDBFI Act as well as the SARFAESI Act, been tabled in the Lok Sabha and referred to the same JPC as IBC. The legislative process here should be taken as an opportunity to align these laws to suit the purpose of bankruptcy reform.

11 Conclusion

The BLRC process, and the law enacted by Parliament, are major milestones in India's economic reform. However, they are the beginning of the journey to bankruptcy reform and not the destination.

What would constitute tangible proof of success in Indian bankruptcy reform? Two events and four key data series define the report card for this.

Event 1. When a default of a Rs.10 billion firm takes place, it swiftly goes into the bankruptcy process, which leads to a transaction where the firm is sold as a going concern to a new strategic buyer or a private equity fund, and a good recovery rate is obtained by the lenders.

Event 2. When a default by a Rs.10 billion firm takes place, the firm gets smoothly put into liquidation within a short time, and a good recovery rate is obtained by the lenders.

Four key measures. Successful bankruptcy reform should mean an increase in four measures through time:

1. The leverage of firms (holding business risk constant),
2. The share of borrowing from the financial system in the total debt of firms.
3. The share of non-bank borrowing in borrowing from the financial system.
4. The share of unsecured borrowing in total debt.

Here is where we are on these metrics, based on non-financial firms in the CMIE database. In all cases, values shown are the average for 3 years, centred at the year of interest, and the firms that are observed in all 3 years are used for the computation. If bankruptcy reform makes progress in India, then we will see bigger values in coming years on all four metrics:

Indicator	Units	1990	2000	2013
1. Leverage	Times	3.41	2.87	2.77
2. Financial debt to total debt	Per cent	42.9	42.5	37.5
3. Non-bank debt to Financial debt	Per cent	56.2	56.0	31.3
4. Unsecured borrowing to total debt	Per cent	20.3	22.1	18.4
Number of firms		1163	5858	10594
Total assets	Rs.Trn.	1.37	12.44	94.35

On all four metrics, things in India have become *worse* over the 1990-2013 period. Everyone is keen on the outcome: the six dimensions of success articulated above. A strong team, with focus and competence, is needed to work on these issues, and this could yield success in a few years.

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