IBC in stress: Survival depends on commitment to its core principles

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The legislature decided to use default as the trigger for initiating proceedings to ease the burden on the NCLT and enable the swift admission of cases. (Illustration: Ajaya Mohanty)

The Indian Parliament in 2016 enacted the Insolvency and Bankruptcy Code (IBC) to address the country's persistent challenges of financial stress and managing bad debts, with the overarching objective of driving economic growth. In its initial years, the IBC benefited from rare institutional alignment. The legislature amended the code six times in the first five years to address implementation challenges and respond to the evolving economic environment. With alacrity, the executive issued the rules and regulations, established the Insolvency and Bankruptcy Board of India (IBBI) and National Company Law Tribunal (NCLT), accredited insolvency professionals, and built the supporting ecosystem. The judiciary reinforced the code's commercial and time-bound character through purposive and pragmatic interpretations.

This concerted effort, reinforced by stakeholder support, initially yielded remarkable outcomes: Faster resolutions, behavioural shifts among debtors, and improved credit discipline. India's global ranking for resolving insolvency improved from 136th to 52nd in the first three years of the IBC's implementation. However, this momentum appears to have waned. While shortcomings are visible across the insolvency ecosystem, this piece focuses on two sources of growing concern: The judiciary and the executive, whose recent actions seem to undermine the IBC's core objective of insolvency resolution.

Recent rulings of the Supreme Court have somewhat modified the foundational premise of the code, diluting the legislative vision and mandate. A recent unsettling instance is the verdict in the *Bhushan Steel and Power Ltd*, where the court set aside a resolution plan implemented years ago. The inordinate delay adds to the disquiet: It took five years to decide a matter under a law that explicitly mandates time-bound resolution. This judgment signals that any commercial transaction, no matter how long it has been implemented or how many layers of state approval it has received, can be unravelled years later.

There was a jolt from the *Rainbow Papers Ltd* case, where the Supreme Court accorded the government a first charge over the assets of a company. This was despite the IBC's long title explicitly providing "*alteration in the order of priority of payment of Government dues*", and the priority rule placing government dues below

unsecured debts. Unsurprisingly, a Coordinate Bench in the Pachimanchal observed that this statutory priority rule "*was either not brought to the notice of the court in Rainbow or was missed altogether*", acknowledging the legislative intent to subordinate government dues to claims of creditors.

The legislature decided to use *default* as the trigger for initiating proceedings to ease the burden on the NCLT and enable the swift admission of cases. The notes on clauses appended to the Bill reinforced this rationale, emphasising quick admission as essential to achieving faster and better outcomes. However, in *Vidarbha Industries Power Ltd*, the court departed from this intent by requiring the NCLT to assess the company's viability and overall financial health, a task it is neither mandated nor equipped to perform. It further held that the NCLT may "*keep the admission of the application of the Financial Creditor in abeyance, unless there is good reason not to do so*".

Now the executive. Timeliness is what makes the IBC valuable. A stressed company must be admitted to the process swiftly before it turns unviable.

A resolution plan must be approved and implemented expeditiously before it runs out of money. Resources locked in unviable companies must be released quickly before the value dissipates. Likewise, the value lost through avoidance transactions must be clawed back promptly before recovery becomes impractical.

Unfortunately, the NCLT often takes years to admit applications, approve resolution plans, or rule on avoidance matters. Meanwhile, resolution applicants remain bound to plans even when prolonged delays in approval render them unviable. Worse still, resolution plans may be unravelled years after implementation. These delays and uncertainties have eroded confidence in the IBC and dampened the market for distressed assets.

The root cause lies in the NCLT's limited capacity, whether in terms of Bench strength, expertise, infrastructure, technology, institutional culture, or case management, relative to its workload. Originally constituted with 63 members to administer company law, the NCLT now carries the burden of adjudicating complex IBC matters, without any addition to its capacity. Addressing the issue of expertise, a full Bench of the Supreme Court observed in a ruling in November last year: "The Members often lack the domain knowledge required to appreciate the nuanced complexities involved … Filling such vacancies with experts having adequate domain knowledge in the field must be prioritised." The NCLT urgently needs a structural and functional overhaul, primarily within the executive's domain.

Stress resolution is like an orchestra: Every stakeholder must play in harmony. Yet, revenue and enforcement authorities often act out of tune. While stakeholders are collaboratively shaping a resolution plan, the tax department may proceed to auction the company's assets for unpaid dues, or an investigative agency may freeze its bank accounts or properties, effectively stalling the process. The insolvency professional, the key *sutradhar* of the process, requires the cooperation of all concerned, including the police, to keep the company as a going concern. Yet, in at least one case, the professional was arrested.

The law explicitly states that a resolution plan approved by the NCLT is binding on all stakeholders, including the government. Any claim not dealt with in the resolution plan stands extinguished. This enables the resolution applicant to start afresh on a clean slate. Some tax authorities nonetheless fail to file their claims within the timeline. Subsequently, they attempt to submit their claims even after approval of the resolution plan, and pursue litigation up to the Supreme Court. They even raise fresh demands, contending that the approved plan did not fully satisfy their claims.

Public laws aim to keep the crime proceeds beyond the reach of criminals while punishing the criminals. Although these proceeds were never the state's property, the state benefits from their confiscation. At the same time, creditors may have extended loans secured against assets that are formally owned by the company but were created using the crime proceeds. The company's revival, utilisation of resources, and the recovery for secured creditors hinge on access to these assets. Acknowledging this, the legislature amended the IBC to allow resolution, without impairing the state's ability to prosecute offenders. However, enforcement agencies and courts do not seem to be on the same page. Unless the judiciary and the executive promptly reaffirm their commitment to the code's core principles, the IBC risks slipping beyond the point of redemption.

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