

IBC needs an institutional boost

PARADIGM SHIFT. Stress resolution shifted from paternalistic rehabilitation to market-driven resolution



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In May 2024, the Finance Minister observed that the Insolvency and Bankruptcy Code, 2016 (IBC) resolved in seven years as many cases as the Sick Industrial Companies (Special Provisions) Act, 1985 (SICA) did in three decades. The remark subtly reframed the discourse towards comparing like with like.

For years, critics often juxtaposed the IBC with the Recovery of Debts and Bankruptcy Act, 1993, or the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002. Such comparisons were always inapt. Those statutes are, by design, recovery mechanisms; under the IBC, however, recovery is incidental to resolution. Paradoxically, even on recovery metrics, the IBC has consistently outperformed these specialised recovery tools.

Therefore, a temporal and consequential comparison between the IBC and the SICA regime is both logical and necessary. Both seek to address corporate distress, but through diametrically opposed institutional designs and economic philosophies. As the IBC approaches a decade of operation, it is imperative to evaluate not merely the letter of the law but the distinct economic cultures they birthed.

THE SICA YEARS

India was ahead of its time when it enacted SICA in 1985 to address business failure, years before economic liberalisation in 1991 permitted freedom to establish and operate businesses. SICA emerged from the constitutional and economic ethos of the command-and-control era. It was enacted in the public interest and to advance the Directive Principles under Article 39 of the Constitution. The state assumed a paternalistic responsibility not merely to identify sick industrial companies, but also to rehabilitate them through financial infusions, concessions, and institutional support.

SICA effectively pathologised insolvency. Distressed companies became 'sick' companies, requiring 'rehabilitation'. This language tapped into a deep-seated cultural instinct of *karz*, which often generated undue sympathy for the promoter rather than concern for capital. The Board for Industrial and Financial Reconstruction (BIFR) functioned as a prolonged care ward where promoters checked in their distressed companies, often for years.



GAME CHANGER. The IBC has scored both on recovery rates and resolution time lines

Unfortunately, BIFR possessed neither the capacity nor the incentive to produce viable solutions to business distress.

Throughout this extended hospitalisation, promoters remained in control, while creditors waited outside, with little influence over diagnosis or treatment. As the late Finance Minister Arun Jaitley famously noted, SICA effectively placed debtors behind an iron curtain, shielding them indefinitely from creditor action. This was rooted not in economic logic, but in a regime where displacement of promoters appeared punitive.

RECONCEPTUALISING DEFAULT

The IBC reconceptualised stress, reflected through default, not as a moral failing, but as a neutral economic event. A company in default is simply a collection of assets trapped in an arrangement that no longer works. Consequently, the inquiry shifted from who deserves sympathy to who can deploy those assets most productively.

Modern markets are volatile, technology may become obsolete, expansion may turn reckless, or managerial ability may prove inadequate. The IBC is largely indifferent to the reason for failure. If a promoter fails, the law seeks to place the enterprise in the right hands, from anywhere in the world, to preserve its economic value. If no such value exists, the assets must be released through liquidation for alternative and more efficient uses. This operates on a fundamental contractual premise. A limited liability company is essentially a

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contract between equity and debt. As long as debt obligations are honoured, equity owners retain control and creditors have no say in the business. Upon default, however, the Code permits corporate insolvency resolution process (CIRP), which displaces the promoters and transfers control to creditors.

At that stage, the enterprise's residual value effectively belongs to creditors. They, rather than the state or the promoter, determine the company's fate. Their commercial wisdom enjoys primacy and remains largely immune from judicial second-guessing.

Section 29A provides teeth to the separation between the enterprise and promoter. It prevents defaulting promoters from regaining control of their companies through the CIRP at distressed valuations. The principle is simple: genuine business failure may be tolerated, but strategic default must never be rewarded.

A different statutory scheme inevitably produced vastly different outcomes. The SICA regime failed to resolve corporate distress efficiently, contributing to the twin balance sheet syndrome (TBS), which impaired both corporate and bank balance sheets. The IBC, by contrast, helped resolve this overhang and restore credit discipline. Gross non-performing assets (NPAs) of scheduled commercial banks, which peaked at 14.8 per cent in 2018, declined to around 2.2 per cent by 2025.

THE SUCCESS STORY

The improvement is visible in both recovery rates and resolution timelines. The World Bank's Ease of Doing Business indicators captured this shift, with India's ranking in resolving insolvency improving from 136 to 52 within three years of the IBC. Importantly, firms resolved under the IBC demonstrated renewed operational viability: within five years of resolution, average sales and capex doubled, asset turnover more than doubled, profitability ratios converged with

TABLE 1

Stress resolution scheme

Parameter	SICA	IBC
Foundation	Constitution	Contract
Objective	Public interest	Market efficiency
Stress	Moral concern	Economic event
Authority	State	Creditors
Asset Control	Debtor	Creditors
Resolution Agent	Promoters	Markets
Outcome	Rehabilitation	Resolution

TABLE 2

Stress resolution outcomes

Parameter	SICA	IBC
Recovery (%)*	26	72
Time (years)*	4.3	1.6
NPA (%)	14.8	2.2
TBS	Entrenched	Resolved
Post-resolution health	Untracked	Enhanced
Shadow resolutions	Negligible	Massive

TBS - Twin balance sheet

*Improvement in the first three years

industry benchmarks, and market capitalisation tripled.

Perhaps the IBC's greatest success lies in resolutions in its shadow. The credible threat of losing one's empire has fundamentally altered promoter behaviour. Tens of thousands of debtors have resolved after the filing of insolvency applications but before admission. Many more resolve even before an application is filed. This behavioural discipline was entirely absent under SICA.

The contrast between pre-IBC and post-IBC regimes is unmistakable. However, the IBC continues to face institutional and structural constraints. The Supreme Court recently noted that nearly 400 resolution plans are pending approval, with some delays extending to four years.

Unless such bottlenecks, which are preventing the IBC from realising its full potential, are addressed, we risk eroding the efficiency gains that distinguish the IBC from its predecessor. As IBC enters the next decade, the priority must be to strengthen the institutional foundations, ensuring that the iron curtain of the past never returns to shield inefficiency.

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