Evaluation of Debt Recovery Laws in India

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The reminisce of banking in India can be traced back to 4th century BC in the *'Kautilya Arthashastra'*, which contains references to creditors and lenders. However, the roots of commercial banking can be dated back to the second half of 18th century with establishment of Bank of Hindustan in 1770. Since then, the evolution of banking in India has undergone three broad phases –

Phase I – Early phase of embryonic Indian banks to nationalisation of banks *(1969)*
Phase II – From nationalisation to advent of liberalisation and banking reforms *(1991)*
Phase III – From liberalisation and banking reforms till date

Banking sector has to be dynamic enough to support the growth aspirations. However, it is seen after almost 250 years of commercial banking, this sector is facing the serious threat of deteriorating asset quality. Inefficient debt recovery framework further aggravates the wound.

Banks act as intermediaries between the depositories and borrowers. They accept deposits from depositors and grant loans to borrowers. The chain breaks when the borrower fails to repay the principal and interest. So, the challenge to extract value from the underlying loan accounts by adopting appropriate resolution strategies is huge because experience suggests that loan accounts are like *cube of ice,* they lose value overtime and rather fast. Consequently, a well-knit recovery mechanism supported by proper recovery laws is must for a healthy banking system.

Recovery of Debts due to Banks and Financial Institutions Act, 1993 (DRT Act) and Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (SARFAESI Act) are couple of explicit state-led interventions in this context. Both aimed at providing alternative recovery mechanism to the cumbersome court processes on the one side and safeguard public exchequer on the other. However, these state interventions did not seem to visualise the impacts on various stakeholders, in case the designated agencies/devices fail to execute their assigned tasks. This could result in huge cost/regulatory burden on stakeholders involved in addition to increased complexity and uncertainty associated with statutory obligation.

Debt Recovery Tribunals (DRTs) were originally set up under the DRT Act to expedite the recovery process, without being subject to lengthy procedures followed by civil courts. But the piling up of a huge number of cases with these tribunals and a significantly lower recovery rate defeats the very purpose. The amount recovered from cases decided in 2013-14 by DRTs was only about 13 per cent of the total amount at stake. Also, while the law indicates that cases before DRTs should be disposed off in six months, only about a fourth of the cases pending at the beginning of the year are disposed during the year. This has the potential to impose unreasonable costs in the form of interest gains foregone on creditors.

Similarly, with a view to make the debt recovery swifter, the SARFAESI Act was passed to enable banks and financial institutions enforce their security interest without having to resort courts and special purpose tribunals. But that too does not seem to have made sizable difference. The amount recovered in the fiscal 2013-14 is only 25.80 per cent of the total outstanding amount. As a result, even after assuming the total amount would be recovered in due course, still it will take around 4 years (akin to the DRTs) to recover that amount.

An impact assessment of existing regulatory interventions could address the above scenario. It is usually undertaken in the event of regulatory failures/ imminent regulatory failure, i.e. when existing regulations are not able to meet the desired objectives. This helps to ascertain the weakness in existing legislations and development of optimal regulatory alternatives, having the potential to achieve the desired objective, with maximum net benefits on the stakeholders involved.

One of the systemic approaches to critically assess such impact is Regulatory Impact Assessment (RIA). It is an important element of an evidence-based approach to policy making, as it essentially comprises stakeholder engagement in policy making and review. It aids in devising optimal regulatory interventions to alter natural state of market to achieve desired objectives. As regulatory interventions change behaviour of stakeholders, and thus impose additional costs on them, it helps in designing most justifiable regulatory intervention, benefits of which can outweigh their costs. Also, this tool will aid in making India an easy place to do business by improving the regulatory environment.

This paper will set out impact analysis of primary debt recovery laws in India to correctly understand the causes of regulatory failures in the area of debt recovery. In addition, legislative alternatives to the identified problems will also be suggested, to fix the problem of slow and low recovery. Such analysis would be done on the basis of comparison of costs and benefits of the baseline scenario and different alternatives using RIA tool.

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