DYSFUNCTION IN INDIAN INSOLVENCY AND DEBT RECOVERY: WHY LAWS CHANGE BUT PROBLEMS PERSIST

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ABSTRACT

India's journey in reforming its insolvency and debt recovery system has been marked by a recurring pattern: ambitious legislative reforms consistently fall short due to underlying structural weaknesses and institutional unpreparedness. Despite successive interventions, from the summary procedures of **Order 37 of the CPC** and the specialized **Debt Recovery Tribunals (DRTs)** under the **RDBA**, to the creditor-empowering **SARFAESI Act** and the resolution-focused **Insolvency and Bankruptcy Code (IBC)**, the core issues of rising Non-Performing Assets (NPAs), slow enforcement, and overburdened judicial bodies persist. This article argues that the disconnect between well-intentioned legal frameworks and their on-ground execution stems not from flaws in legislative design, but from a persistent failure to adequately equip and integrate the supporting institutional infrastructure, stakeholder discipline, and enforcement mechanisms. The analysis highlights that genuine reform requires a shift in focus from merely enacting new laws to strengthening systemic readiness, enhancing regulatory coordination, and ensuring accountability to bridge the persistent gap between legal promise and practical reality.

Introduction

India's insolvency and debt recovery system has long been caught in a cycle: new laws get passed, problems persist, and creditors & debtors stay stuck. The legal system has long struggled to offer timely remedies in cases of financial default and insolvency. Despite multiple legislative reforms, issues like rising NPAs, slow enforcement, and overburdened courts and tribunals persist. In 2023, the NPA ratio was at about 3.2%, amounting to over ₹5.71 lakh crores, a stark reminder that the disconnect between law and execution remains prevalent and grossly unaddressed.

Over the years, the State has introduced various legal mechanisms to fix this gap. From **Order 37 of the CPC**[1], which aimed to fast-track recovery suits but failed due to procedural delays, to the **Recovery of Debts and Bankruptcy Act**[2], which introduced Debt Recovery Tribunals (DRTs) but struggled with infrastructure and backlog; each of these reforms assured speed but largely failed on this promise.

The **SARFAESI Act, 2002**[3] marked a shift in the judicial approach, granting creditors direct enforcement powers. While it reduced delays, it raised concerns over borrower rights and institutional misuse. Eventually, in 2016, the **Insolvency and Bankruptcy Code (IBC)**[4] was enacted to prioritize resolution over recovery, a supposedly holistic approach in theory. Yet today, even the **IBC** faces criticism for slow proceedings and inconsistent outcomes. This article explores how every attempt at reform has ultimately been undercut by structural weaknesses and institutional lag.

Background: Order 37 CPC - A Summary Procedure that Wasn't

One of the earliest attempts to create a fast-track legal route for debts recovery in India was **Order 37** of the **CPC**. Introduced during the British colonial period, the goal was to ensure quick relief in matters involving money, especially for institutional creditors and merchants. The procedure allowed a plaintiff to file a "summary" suit without giving the defendant an automatic right to defend. Instead, the defendant had to apply for a "leave to defend," which

[1] Code of Civil Procedure, 1908, Act No. 5 of 1908
[2] Recovery of Debts and Bankruptcy Act, 1993, Act No. 51 of 1993
[3] Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002, Act No. 54 of 2002
[4] The Insolvency and Bankruptcy Code, 2016, Act No. 31 of 2016

could be granted only if the court was convinced that a substantial defence existed. This limited right to defend was meant to avoid frivolous delays in cases where the claim was crystal clear and backed by written contracts or promissory instruments.

While the intention behind **Order 37** was to reduce procedural burden, it largely failed to meet its purpose in practice. Indian courts adopted a broad interpretation of what qualifies as a "substantial" defence, which has affected the effectiveness of this summary process. Defendants often secure leave to defend based on vague grounds, and once the trial begins, it becomes almost indistinguishable from a regular civil suit. Even when creditors secure favourable decrees, enforcement remains slow and uncertain. It must be noted that the shortcomings of **Order 37** weren't due to a flawed drafting or concept, but because it assumed that procedural changes could overcome deep-rooted inefficiencies of the system in practical life.

This pattern of legislative intent falling short due to weak institutional delivery would repeat itself in later "reforms", including the **RDBA**, **SARFAESI**, and eventually the **IBC**. **Order 37**, therefore, stands not as an isolated shortcoming, but as the beginning of a series of reform attempts that underestimated the importance of institutional and systemic readiness.

RDBA – Legislative Hope, Operational Failure

The Recovery of Debts and Bankruptcy Act, 1993 (**RDBA**) was introduced during India's economic liberalisation era during the early 1990s, to address the increasing backlog of banking and financial disputes across courts. Prompted by the Narasimham Committee's recommendations, the Act led to the creation of the **Debt Recovery Tribunals (or DRTs)** which are specialised forums intended to offer quicker and creditor-friendly mechanisms for debt enforcement. Section 19 of the Act allows banks to file Original Applications (OAs) for recovery of debts above ₹20 lakh, while also empowering tribunals to issue interim orders, attach property, and bypass several procedural hurdles common in traditional civil courts. At its core, the **RDBA** was designed to seclude and fast-track financial litigation, marking a step away from general civil forums towards a more specialised approach.

While the Act appeared focused and well-intentioned, its implementation exposed the gap between legislative intent and institutional capacity. DRTs today remain chronically understaffed, underfunded, and burdened by case overload, defeating the very purpose they

were created for. Cases often take years to resolve, and even after favourable decisions, recovery remains delayed due to enforcement hurdles. In practice, the **RDBA** ended up mirroring the very problems it was introduced to fix: inefficient resolution, procedural delays, and limited practical relief for creditors. However, the Act's shortcomings did not stem from any flawed legislative intent or drafting, but from the system's inability to support such reforms practically. **RDBA** thus, just served to add another brick to the pattern of institutional unpreparedness of Indian insolvency and debt recoveries law.

SARFAESI – A solution in theory

The Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (**SARFAESI**) marked a fundamental shift in India's debt recovery regime. Frustrated by delays in civil courts and the inefficiencies of Debt Recovery Tribunals, the legislature granted secured creditors the power to enforce their rights independently. The aim was to cut down reliance on judicial systems and empower lenders to recover dues quickly. Under **Section 13(4)**, once an account is labelled a **Non-Performing Asset** (after 90 days of default as per **RBI**), creditors can issue a **demand notice under Section 13(2)**. If no payment is made within 60 days, they can take possession of the asset, manage it, or even sell it, all without prior court intervention. This pseudo-judicial authority represented a major shift toward creditor autonomy and was seen as a fast-track alternative to litigation heavy processes.

While **SARFAESI** promised efficiency, its impact in practice was far more checkered. The absence of early-stage judicial oversight led to concerns of overreach, infringement and procedural unfairness, with borrowers often left without adequate protection. Recovery remained inconsistent, as challenges in DRTs and appellate forums continued to delay final resolution. Thus, although **SARFAESI** addressed the procedural rigidity of earlier frameworks and aimed to solve them by giving enforcement rights to creditors, it too faltered due to weak institutional procedures and lack of oversight and served to add yet another brick in our continuing pattern of good legislative intent lacking short due to structural and procedural immaturity and unreadiness for such reforms.

Era of the IBC and "CIRP" – Resolution as opposed to Recovery

The Insolvency and Bankruptcy Code, 2016 (**IBC**) was enacted to streamline India's fragmented insolvency framework and shift the focus from recovery to resolution. Prior to the

IBC, insolvency was governed by overlapping laws like the Companies Act, **SARFAESI**, and **RDBA**, none of which offered a complete and cohesive solution. The **IBC** introduced a time-bound, creditor-driven process to revive distressed companies and avoid forced liquidation, aiming to maximise asset value and preserve enterprise continuity.

The Code's core mechanism is the **Corporate Insolvency Resolution Process (CIRP)**. Once admitted by the NCLT, control of the company shifts from its promoters to an **Interim Resolution Professional**, and a **Committee of Creditors (CoC)** is formed to evaluate resolution plans. The **IBC** also created an institutional framework of Information Utilities, Insolvency Professionals, and the IBBI to oversee implementation. Early on, the Code was hailed as a turning point, with high-profile resolutions like **Essar Steel**[5] and **Jet Airways**[6] giving credibility to its promise.

However, the **IBC**'s effectiveness too has been affected by increasing delays, frequent judicial interventions, and capacity issues at the NCLTs. Sections 7 and 9, while designed for quick creditor action, often suffer from prolonged admission timelines. Creditor recoveries are also inconsistent, with a large number of creditors often getting only a menial amount under the waterfall mechanism. Thus, much like its predecessors, the **IBC** also reflects the recurring pattern of a progressive statute held back by institutional lag and inadequate enforcement.

Conclusion & Recommendations

India's debt recovery laws have evolved significantly over the past three decades, from procedural shortcuts under **Order 37** to specialised tribunals through **RDBA**, creditor empowerment via **SARFAESI**, and a resolution focused model under the **IBC**. However, each reform has ultimately struggled with the same limitation of a lack of institutional readiness to support legislative goals. The problem isn't the intent or structure of these laws, but the repeated failure to match them with robust systems, stakeholder discipline, and functional capacity.

To make these laws effective, the focus must shift from drafting new legislation to improving execution on the ground. This might include real time tracking of insolvency cases, better staffing of NCLTs and DRTs, and stricter enforcement of procedural timelines. Moreover,

[5] Essar Steel India Limited v Satish Kumar Gupta, (2020) 8 SCC 531
[6] SBI v. Jet Airways (India) Ltd., 2021 SCC OnLine NCLT 11967

better regulatory coordination between institutions like RBI, IBBI, and enforcement bodies is critical to removing prevalent procedural overlaps. Creditors and professionals must also be held accountable for fairness and transparency. Ultimately, the reform isn't about adding another law, it's about making sure the ones we have actually work.