



BEYOND RECOVERY: RETHINKING LEGAL AND INSTITUTIONAL REFORMS FOR SUSTAINABLE RESOLUTION OF NON- PERFORMING ASSETS IN INDIAN PUBLIC SECTOR BANKS

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Abstract: The growing burden of Non-Performing Assets (NPAs) in Indian Public Sector Banks (PSBs) poses a significant threat to financial stability and economic growth. This article evaluates the effectiveness of current legal and institutional mechanisms for NPA resolution, such as SARFAESI, DRTs, and the Insolvency and Bankruptcy Code (IBC). Despite their roles, persistent issues like judicial delays, enforcement gaps, and inadequate institutional coordination hinder their success. Through critical evaluation and comparison with global practices, this article proposes a strategic shift from reactive recovery to proactive reforms aimed at sustainable resolution.

Index Terms - NPAs, Public Sector Banks, SARFAESI, IBC, DRT, Legal Reform, Sustainable Finance, Banking Law

I. INTRODUCTION

The growing burden of NPAs has emerged as a structural issue for Indian PSBs. These stressed assets reduce banks' capacity to lend and erode stakeholder confidence. Although the Indian government has introduced several legal mechanisms to tackle the issue, most have operated in silos or offered reactive solutions. This article calls for an integrated and proactive approach that not only strengthens enforcement but also addresses institutional and policy-level gaps¹.

¹ Reserve Bank of India. (2023). *Financial Stability Report*. RBI Publications.

II. UNDERSTANDING THE NPA PROBLEM IN INDIA

A loan becomes an NPA when its interest or principal remains overdue for more than 90 days, as per RBI norms. The post-2014 period witnessed a sharp escalation in NPAs, attributed to overleveraging in core sectors like power, telecom, and infrastructure. PSBs—due to their developmental mandate and exposure to large corporates—were the worst hit, accounting for nearly 85% of total NPAs by 2018².

III. LEGAL AND INSTITUTIONAL FRAMEWORK FOR NPA RESOLUTION

India's response has evolved through several legislative frameworks:

- **Debt Recovery Tribunals (DRTs):** Introduced via the RDDBFI Act, 1993, these aimed to speed up recovery proceedings. However, they face a massive backlog due to limited resources and manpower³.
- **SARFAESI Act, 2002:** This law empowers secured creditors to seize assets without court approval. While theoretically robust, its execution suffers from frequent judicial interventions and poor asset recovery rates.
- **Insolvency and Bankruptcy Code (IBC), 2016:** The IBC consolidated various insolvency processes and created a time-bound resolution framework. It is hailed as a landmark, but delays in NCLT admissions and execution hinder its full potential⁴.
- **Lok Adalats and Compromise Settlements:** These informal mechanisms offer a conciliatory approach, yet they are rarely effective in large-ticket NPAs.

IV. PERFORMANCE EVALUATION AND CRITICAL ANALYSIS

The initial success of the IBC, reflected in average recovery rates of around 45%, marked a significant improvement over earlier mechanisms. However, resolution times now exceed 400 days on average, far beyond the statutory limit of 330 days. DRTs, meanwhile, continue to be burdened by over 1.5 lakh pending cases. SARFAESI's recovery efficiency stands at a modest 26%, highlighting its limitations⁵.

Comparatively, countries like South Korea, China, and Spain have leveraged centralized asset reconstruction models and autonomous resolution agencies to fast-track clean-up.

² ICRA. (2021). *Banking Sector Report*.

³ Sastry, R. (2021). *DRT Effectiveness in India*. Journal of Banking Law, 12(4), 45–61.

⁴ Insolvency and Bankruptcy Board of India. (2022). *Annual Report*.

⁵ CRISIL. (2021). *SARFAESI and NPA Recovery*.

V. CHALLENGES IN EXISTING MECHANISMS

Several systemic bottlenecks persist:

- **Judicial Delays:** Procedural formalism and shortage of adjudicators have stalled resolutions⁶.
- **Weak Enforcement Infrastructure:** Issues in tracing, valuing, and liquidating collateral assets reduce recovery efficiency.
- **Fragmented Framework:** Overlapping jurisdictions between DRTs, NCLTs, and other bodies create confusion and delays.
- **Political Interference in PSBs:** Undermines the commercial judgment of banks and hinders accountability⁷.
- **Lack of Risk Anticipation Tools:** Existing credit monitoring systems fail to detect early warning signals.

VI. JUDICIAL RESPONSE AND LANDMARK JUDGMENTS

Indian courts have played a crucial role in affirming and clarifying NPA resolution laws:

- **Innoventive Industries v. ICICI Bank (2017):** Established the supremacy of IBC timelines and creditors' rights⁸.
- **Swiss Ribbons v. Union of India (2019):** Validated IBC's constitutional framework and policy rationale⁹.
- **Essar Steel v. ArcelorMittal (2019):** Cemented the CoC's autonomy in commercial decisions¹⁰.

Despite these clarifications, inconsistent interpretations by lower benches and frequent litigation dilute the efficiency of legal mechanisms.

VII. GLOBAL BEST PRACTICES

Global models offer useful policy lessons:

- **USA's TARP:** The Troubled Asset Relief Program allowed quick recapitalization of distressed banks.
- **Spain's SAREB:** Created a centralized 'bad bank' to absorb and liquidate non-performing assets¹¹.
- **China's AMCs:** State-run Asset Management Companies absorbed over USD 300 billion in bad loans from banks.
- **Korea's KAMCO:** Played a decisive role post-1997 crisis by acquiring and restructuring toxic assets¹².

India must draw from these models, focusing on technological integration, centralized resolution agencies, and regulatory independence.

⁶ World Bank. (2020). *Resolving Non-Performing Loans in Emerging Markets*.

⁷ Rajan, R. (2020). *A Reassessment of Banking Reforms*. Finance & Development, IMF

⁸ *Innoventive Industries Ltd. v. ICICI Bank*, (2017) 1 SCC 407

⁹ *Swiss Ribbons Pvt. Ltd. v. Union of India*, (2019) 4 SCC 17.

¹⁰ *Essar Steel India Ltd. v. Satish Kumar Gupta*, (2020) 8 SCC 531.

¹¹ European Central Bank. (2020). *Spain's SAREB and NPA Clean-up*.

¹² OECD. (2020). *Korea's Financial Crisis Response: KAMCO Model*.

VIII. RECOMMENDATIONS AND REFORM PROPOSALS

Based on the analysis, the following measures are proposed:

1. **National Asset Resolution Corporation (NARC):** With quasi-judicial powers and digital governance architecture.
2. **Strengthen Adjudicatory Bodies:** Create full-time benches at NCLTs and DRTs with financial law expertise.
3. **Real-time Risk Monitoring:** Integrate AI-based credit risk tools and blockchain-enabled data analytics.
4. **Autonomous PSB Governance:** Amend laws to insulate PSBs from political control.
5. **Unified Legal Portal:** Integrate proceedings across SARFAESI, IBC, and DRTs for coherence.
6. **Fast-track Mediation for MSMEs:** Introduce out-of-court mechanisms for quicker resolution.
7. **Legal Impact Audits:** Annual reviews of enforcement effectiveness with public performance scorecards.

IX. CONCLUSION

The NPA challenge in India is both a legal and institutional dilemma. While frameworks like IBC have provided a strong foundation, sustainable resolution demands coordinated, forward-looking reforms. By drawing on global experiences and embracing innovation, India can not only resolve NPAs but also restore the robustness of its public banking system.

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