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From Default to Resolution: Mediation and Arbitration as Strategic Tools for Managing NPAS in Indian Banking

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ABSTRACT

Non-Performing Assets (NPAs) remain a persistent challenge for Indian banking because prolonged stress can reduce recoverable value, increase enforcement costs and constrain the recycling of bank capital. India has developed specialised mechanisms through the Recovery of Debts and Bankruptcy Act 1993, the SARFAESI Act 2002 and the Insolvency and Bankruptcy Code 2016. This article argues that these mechanisms should be complemented, rather than displaced, by a graduated Alternative Dispute Resolution (ADR) framework. Mediation can operate as an early-intervention mechanism for commercially viable borrowers by facilitating structured disclosure, viability assessment, restructuring and negotiated settlement. Arbitration has a narrower role in determining contractual disputes that are legally arbitrable. The article examines the Mediation Act 2023, RBI stressed-asset and compromise-settlement frameworks, relevant Supreme Court jurisprudence and the 2026 EAEI Transformers decision. It proposes a time-bound architecture combining early warning, viability review, mediation, monitored settlement and statutory recovery where necessary.

Keywords: Non-Performing Assets; Banking Law; Alternative Dispute Resolution; Mediation; Arbitration; SARFAESI; Debt Recovery Tribunal; Insolvency and Bankruptcy Code; Stressed Assets; Debt Resolution.

I. INTRODUCTION

Bank lending is contractual in form but systemic in consequence. Deposits are converted into credit for households, businesses and productive activity. When a material portion of that credit stops performing, the resulting problem is not confined to the lender and borrower. Capital becomes locked in stressed accounts, recovery costs increase, provisioning pressure may rise and the lender's capacity to deploy funds into fresh credit can be affected. The regulatory treatment of non-performing assets is therefore inseparable from the broader objective of maintaining the soundness and efficiency of the banking system.1

1 Reserve Bank of India, Master Circular – Prudential Norms on Income Recognition, Asset Classification and Provisioning pertaining to Advances, RBI/2024-25/12, DOR.STR.REC.8/21.04.048/2024-25 (2 Apr. 2024), especially Part A, paras 2.1 and 4.1. See also RBI,

The legal response in India has developed through several specialised mechanisms. The Recovery of Debts and Bankruptcy Act, 1993 created a dedicated institutional route for adjudication and recovery of debts due to banks and financial institutions.2 The SARFAESI Act, 2002 strengthened secured creditors by enabling enforcement of security interests, subject to statutory conditions, without requiring the prior determination of the debt through an ordinary civil suit.3 The IBC, 2016 subsequently introduced a collective insolvency-resolution framework in which value maximisation and resolution, rather than mere individual debt enforcement, occupy central positions.4

These mechanisms remain essential. The question addressed in this article is not whether they should be replaced. The more difficult question is whether the recovery framework should intervene earlier, before financial stress becomes a prolonged and adversarial recovery dispute. A borrower may be unable to meet a scheduled instalment for reasons that do not necessarily destroy the long-term viability of the underlying enterprise. Conversely, some accounts may be fundamentally unviable or affected by conduct that makes restructuring inappropriate. A useful recovery system therefore needs an intermediate mechanism capable of distinguishing these situations.

ADR, particularly mediation, can provide such an intermediate layer. Mediation permits the parties to explore solutions with the assistance of a neutral third person without transferring the final commercial decision to the mediator. The Mediation Act, 2023 now provides a statutory framework for mediation, including principles governing the mediator’s independence, neutrality and impartiality and the legal treatment of mediated settlements.5 In the banking context, this framework can support a controlled process for examining cash flows, security, repayment capacity and restructuring possibilities while preserving the bank’s statutory rights.

The argument for mediation is principally preventive. If a viable business is pushed into prolonged enforcement before its operating value has been assessed, the process of recovery may itself reduce the value available for recovery. A functioning enterprise may be worth more as a going concern than through fragmented realisation of its assets. The relevant question is therefore not simply whether the bank possesses a legal power to enforce, but whether immediate enforcement is the economically optimal recovery strategy in the particular case.

Arbitration occupies a different position. It is adjudicatory rather than facilitative and depends upon a valid arbitration agreement and an arbitrable subject matter. The Supreme Court’s jurisprudence makes clear that the existence of an arbitration clause does not render every banking dispute arbitrable,

Master Circular – Prudential Norms on Income Recognition, Asset Classification and Provisioning pertaining to Advances (2024).

2 Recovery of Debts and Bankruptcy Act, 1993, long title; the Act provides for Tribunals for expeditious adjudication and recovery of debts due to banks and financial institutions.

3 Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002, ss. 13–17.

4 Insolvency and Bankruptcy Code, 2016, preamble and Part II.

5 Mediation Act, 2023, ss. 3(h), 15. Section 3(h) defines mediation as a process in which parties attempt to reach an amicable settlement with the assistance of a mediator who has no authority to impose a settlement.

particularly where Parliament has entrusted matters to a specialised statutory forum.6 Arbitration can therefore contribute to efficient resolution of appropriate contractual disputes, but it cannot be treated as a universal mechanism for NPA recovery.

This article develops a complementary model: early identification of financial stress; assessment of business viability; time-bound mediation where appropriate; implementation and monitoring of settlement; and recourse to SARFAESI, DRT or insolvency processes where consensual resolution is unsuitable or unsuccessful. The objective is to move from a binary choice between "settlement" and "enforcement" towards a graduated recovery strategy based on the expected economic outcome.

II. RESEARCH QUESTIONS, OBJECTIVES AND METHODOLOGY

The article is guided by three principal questions:

1. Can mediation be integrated into the Indian banking recovery framework as an early-intervention mechanism for viable stressed accounts?
2. What is the proper legal and functional relationship between mediation, arbitration, SARFAESI, DRT proceedings and the IBC?
3. What safeguards are required to ensure that ADR improves recovery without becoming a means of delaying legitimate enforcement?

The principal objective is to develop a legally coherent and commercially workable model for ADR-assisted NPA management. The article also seeks to distinguish the preventive role of mediation from the adjudicatory role of arbitration and to identify the circumstances in which consensual resolution should give way to statutory recovery.

The research adopts a doctrinal and analytical methodology. Primary legal materials, including statutes, judicial decisions and Reserve Bank of India regulatory instruments, form the principal basis of analysis. The article also uses a recent judicial decision as a case study to examine the practical importance of implementing a negotiated settlement correctly. The analysis is normative in its final stage: it proposes institutional safeguards rather than assuming that ADR is suitable for every stressed account.

III. UNDERSTANDING THE NPA PROBLEM

An NPA should not be understood merely as an accounting label. It is a regulatory indication that the underlying credit exposure has ceased to perform according to prescribed norms. RBI's prudential framework links income recognition, asset classification and provisioning to objective indicators of recovery and the period for which an asset remains non-performing.7 Behind the same classification, however, may lie very different commercial realities.

A borrower may face a temporary liquidity mismatch, delayed receivables, a sudden increase in input costs, loss of a major customer, regulatory disruption, project delay or a short-term working-capital

6 Vidya Drolia v. Durga Trading Corporation, (2021) 2 SCC 1; see also Supreme Court of India, Judgment dated 8 Mar. 2021.

7 Reserve Bank of India, Master Circular – Prudential Norms on Income Recognition, Asset Classification and Provisioning pertaining to Advances, RBI/2024-25/12, DOR.STR.REC.8/21.04.048/2024-25 (2 Apr. 2024), especially Part A, paras 2.1 and 4.1. See also RBI, Master Circular – Prudential Norms on Income Recognition, Asset Classification and Provisioning pertaining to Advances (2024).

shortage. Another borrower may have an inherently unsustainable business model, no realistic repayment capacity, diversion of funds or other conduct that makes restructuring commercially inappropriate. Treating these accounts identically may be legally convenient but economically inefficient.

The RBI's Prudential Framework for Resolution of Stressed Assets, 2019 places emphasis on recognition of financial stress and time-bound resolution.8 The regulatory emphasis is significant for the ADR debate because the value of mediation is generally greater when the enterprise still possesses operational capacity and credible future cash flows. Once financial deterioration becomes severe, the available choices narrow and the bargaining position of all stakeholders may become more difficult to manage.

The NPA problem should therefore be viewed on two levels. The first is the regulatory classification of the account. The second is the economic condition of the borrower and the likely recovery value under competing strategies. A sophisticated recovery framework must consider both.

IV. WHY FORMAL RECOVERY MAY NOT ALWAYS PRODUCE THE BEST COMMERCIAL OUTCOME

Formal recovery mechanisms provide certainty, enforceability and institutional discipline. Yet legal enforceability and economic recovery are not necessarily identical. A manufacturing unit may possess valuable machinery and land, but its overall value may depend on continued production, skilled employees, licences, customer relationships and working-capital access. If enforcement causes operations to collapse, the value of the enterprise may decline before the secured asset is ultimately realised.

This does not imply that enforcement is undesirable. In cases of persistent default, lack of cooperation or fundamental insolvency, enforcement may be the only realistic route. The point is narrower: the existence of an enforcement power should not prevent a bank from evaluating whether another legally permissible strategy will produce a better recovery.

The distinction becomes particularly important where the secured asset forms part of an operating enterprise. A commercial property, specialised industrial facility or project asset may have a higher value when integrated into an operating business than when sold in isolation. The preservation of going-concern value can therefore become a legitimate component of recovery strategy.

Prolonged litigation can also transform a manageable commercial disagreement into an adversarial dispute. Communication increasingly takes place through notices, pleadings and procedural applications. Each party may become focused on protecting its legal position rather than identifying a financially viable solution. Mediation changes the setting without removing the parties' substantive rights. The mediator facilitates communication, tests proposals and helps identify interests, while the parties retain control over whether to settle.

The distinction between adjudication and negotiated resolution is consequently central. Recovery law determines what a bank can legally do; ADR can help determine, through structured negotiation, what the bank should commercially do in a particular case.

8 Reserve Bank of India, Prudential Framework for Resolution of Stressed Assets, DBR.No.BP.BC.45/21.04.048/2018-19 (7 June 2019).

V. MEDIATION AS AN EARLY-INTERVENTION TOOL

Mediation has the strongest preventive potential among the ADR mechanisms considered here because it can be used before the dispute has fully hardened into litigation. Under the Mediation Act, mediation is a process in which parties attempt to reach an amicable settlement with the assistance of a mediator who has no authority to impose a settlement.9 This feature makes mediation particularly suitable for banking disputes where a negotiated restructuring may be preferable to immediate enforcement.

A banking mediation process should begin with eligibility screening. Before referral, the lender should assess:

1. the immediate and underlying reasons for the stress;
2. present and projected cash flows;
3. the commercial viability of the enterprise;
4. the nature and value of available security;
5. the borrower's willingness and capacity to cooperate;
6. the feasibility of restructuring or rescheduling;
7. the existence of other lenders or material creditors; and
8. the probable recovery under enforcement as compared with a negotiated resolution.

The assessment should not be reduced to a mechanical formula. Its purpose is to determine whether the account presents a credible prospect of value-preserving resolution.

Where mediation is considered appropriate, the parties may explore measures such as rescheduling, restructuring of repayment obligations, a limited repayment moratorium, additional working capital subject to safeguards, disposal of non-core assets, partial settlement, an authorised One-Time Settlement, changes in security arrangements, fresh equity or management measures, or repayment linked to identifiable future cash flows.

The principal benefit is flexibility. Different causes of financial stress require different responses. A temporary liquidity problem may justify a revised repayment schedule; a structural business problem may require deeper restructuring; and an irretrievably unviable business may not justify further accommodation at all.

Flexibility, however, must remain within the bank's delegated authority, regulatory requirements and approved settlement policy. Mediation should not create an informal parallel banking system in which individual officers make concessions without adequate institutional scrutiny.

VI. THE MEDIATION ACT, 2023 AND BANKING DISPUTES

The Mediation Act, 2023 gives mediation a clearer statutory basis in India. Section 15 requires the mediator to act independently, neutrally and impartially and to be guided by objectivity, fairness, voluntariness, confidentiality and party self-determination. 10 These principles have particular

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9 Mediation Act, 2023, ss. 3(h), 15. Section 3(h) defines mediation as a process in which parties attempt to reach an amicable settlement with the assistance of a mediator who has no authority to impose a settlement.

10 Mediation Act, 2023, ss. 3(h), 15. Section 3(h) defines mediation as a process in which parties attempt to reach an amicable settlement with the assistance of a mediator who has no authority to impose a settlement.

significance in financial disputes because restructuring proposals, financial statements, projected cash flows, security details and business plans may contain commercially sensitive information.

The Act also gives legal structure to the outcome of mediation. Section 19 recognises a mediated settlement agreement as a written settlement resulting from mediation and authenticated by the mediator, subject to the statutory requirements.11 The statutory recognition of settlement is important because banking mediation should not end with an informal understanding. A settlement must be documented with sufficient precision to identify the amount payable, dates, conditions, security arrangements, reporting obligations and consequences of default.

Time discipline is equally important. A bank cannot reasonably be expected to allow an indefinite negotiation while security deteriorates and statutory recovery considerations continue to develop. A banking mediation protocol should therefore prescribe eligibility criteria, a defined period for negotiations, disclosure requirements and a clear consequence if settlement is not reached.

Mediation must also remain subject to the statutory boundaries of the process. Not every dispute is capable of being resolved by private negotiation. Where law assigns a matter to a particular statutory process, or where the nature of the dispute makes consensual resolution inappropriate, the relevant statutory forum must remain available.

VII. MEDIATION AND NEGOTIATED SETTLEMENTS

Mediation may be especially useful where the bank already possesses the legal authority to consider a compromise or restructuring but requires a structured process through which the proposal can be examined. A compromise should not automatically be regarded as a concession. If a negotiated settlement results in earlier, more certain and less expensive recovery, it may be commercially superior to prolonged enforcement.

The RBI's Framework for Compromise Settlements and Technical Write-offs, 2023 expressly recognises compromise settlements as part of the resolution framework for stressed accounts and requires regulated entities to maintain appropriate board-approved policies.12 The framework therefore provides an institutional basis for considering settlements through controlled processes rather than treating compromise as an exceptional or informal act.

The mediator should not decide what the bank must accept. The mediator's role is to facilitate communication, identify areas of agreement and help structure alternatives. The actual decision remains with the competent authority of the bank. This distinction is vital for institutional accountability.

For example, where a borrower proposes to repay a substantial part of the outstanding amount over a defined period, mediation can assist the parties in determining payment milestones, additional security, reporting obligations and the consequences of another default. The mediation process thus facilitates the settlement; it does not replace the bank's internal decision-making process.

VIII. CASE STUDY: EAEI TRANSFORMERS AND THE IMPORTANCE OF SETTLEMENT IMPLEMENTATION

A recent illustration of the practical significance of consensual banking resolution is *M/s EAEI Transfor-*

11 Mediation Act, 2023, s. 19 (mediated settlement agreement).

12 Reserve Bank of India, Framework for Compromise Settlements and Technical Write-offs, RBI/2023-24/40, DOR.STR.REC.20/21.04.048/2023-24 (8 June 2023).

mers Private Limited v. The Reserve Bank of India & Ors., decided by the Patna High Court on 2 February 2026.13 The case concerned accounts maintained by EAEI Transformers with the State Bank of India that had become irregular and were classified as NPAs. The parties subsequently reached a settlement before the Lok Adalat attached to the Debt Recovery Tribunal, Patna.

The Court recorded that an outstanding amount of approximately ₹17.11 lakh was settled for ₹11.80 lakh as full and final payment. The borrower complied with the settlement, after which the bank issued a No Due Certificate and released the securities.14 The later dispute arose because the bank's reporting and internal records did not consistently reflect the completed settlement.

The Patna High Court treated the Lok Adalat award as binding and held that the borrower could not be penalised for the bank's subsequent lapses. The Court directed correction of the credit reporting position and rejected the bank's later demand in respect of the loan account that had already been settled.15 The decision demonstrates that successful ADR requires more than obtaining a settlement document. The settlement must be implemented accurately: payments must be accounted for, securities must be released where appropriate, closure documentation must be issued and credit information must reflect the legal position.

The case is important to the present argument for another reason. It illustrates that consensual resolution and statutory recovery are not opposites. The settlement took place within an institutional dispute-resolution setting, while the High Court's later intervention concerned the legal consequences of the completed settlement. ADR can therefore reduce the need for contested recovery while leaving ordinary legal remedies available to address implementation failures.

The case also supports a broader institutional lesson: banks should establish a post-settlement compliance checklist. Closure of the account, release of securities, issuance of No Due Certificate, correction of credit information and closure of ancillary facilities should be treated as part of the resolution process rather than as administrative matters left to chance.

13 M/s EAEI Transformers Private Limited v. The Reserve Bank of India & Ors., Civil Writ Jurisdiction Case No. 6144 of 2025, Patna High Court, judgment dated 2 Feb. 2026 (A. Abhishek Reddy J.). The Court recorded settlement of approximately ₹17.11 lakh for ₹11.80 lakh, payment of the settlement amount, issuance of a No Due Certificate and release of securities, and directed correction of the credit-reporting position.

14 M/s EAEI Transformers Private Limited v. The Reserve Bank of India & Ors., Civil Writ Jurisdiction Case No. 6144 of 2025, Patna High Court, judgment dated 2 Feb. 2026 (A. Abhishek Reddy J.). The Court recorded settlement of approximately ₹17.11 lakh for ₹11.80 lakh, payment of the settlement amount, issuance of a No Due Certificate and release of securities, and directed correction of the credit-reporting position.

15 M/s EAEI Transformers Private Limited v. The Reserve Bank of India & Ors., Civil Writ Jurisdiction Case No. 6144 of 2025, Patna High Court, judgment dated 2 Feb. 2026 (A. Abhishek Reddy J.). The Court recorded settlement of approximately ₹17.11 lakh for ₹11.80 lakh, payment of the settlement amount, issuance of a No Due Certificate and release of securities, and directed correction of the credit-reporting position.

Table 1. Proposed ADR-Assisted Banking Resolution Pathway

Stage	Principal Action
1. Stress Identification	Detect material early-warning indicators.
2. Viability Review	Assess business viability, cash flow and recovery prospects.
3. ADR Referral	Refer eligible cases to a trained banking mediator.
4. Financial Disclosure	Obtain relevant financial and security information.
5. Structured Negotiation	Examine restructuring, settlement and repayment options.
6. Resolution Proposal	Prepare a commercially supportable proposal.
7. Bank Approval	Obtain approval under the bank's delegated authority and policy.
8. Documentation	Execute an enforceable settlement with defined milestones.
9. Monitoring	Track compliance and financial performance.
10. Recovery on Failure	Invoke appropriate contractual or statutory remedies.

Source: Author's proposed framework.

IX. ARBITRATION IN BANKING DISPUTES

Arbitration must be conceptually separated from mediation. Mediation is facilitative; arbitration is adjudicatory. The Arbitration and Conciliation Act, 1996 provides the statutory framework for domestic arbitration, international commercial arbitration and enforcement of foreign awards.16

Banking and finance agreements may contain arbitration clauses covering contractual questions concerning repayment obligations, interest calculations, guarantees, representations, restructuring arrangements or other matters capable of determination through arbitration. Where a valid arbitration agreement exists and the dispute is legally arbitrable, arbitration can provide a specialised and procedurally focused forum.

The existence of an arbitration clause, however, does not make every banking dispute arbitrable. In *Vidya Drolia v. Durga Trading Corporation*, the Supreme Court articulated the modern Indian approach to non-arbitrability and emphasised that certain disputes are reserved for statutory or public fora.17 In the banking context, the significance of the principle is that a contractual arbitration clause cannot automatically displace the jurisdiction assigned by legislation to a specialised tribunal.

The proposition that arbitration can "reduce NPAs" must therefore be stated carefully. Arbitration can reduce uncertainty and delay in appropriate contractual disputes. It can determine rights where the dispute falls within the scope of the arbitration agreement and is legally capable of arbitration. It is not, however, a substitute for the DRT's statutory jurisdiction or a universal mechanism for enforcing security.

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16 Arbitration and Conciliation Act, 1996, long title and Part I.

17 Vidya Drolia v. Durga Trading Corporation, (2021) 2 SCC 1; see also Supreme Court of India, Judgment dated 8 Mar. 2021.

X. ARBITRATION AND SARFAESI: DIFFERENT FUNCTIONS, POSSIBLE COEXISTENCE

The relationship between arbitration and SARFAESI is best understood by examining the function of each remedy. In *M.D. Frozen Foods Exports Pvt. Ltd. v. Hero Fincorp Ltd.*, the Supreme Court recognised that arbitration and SARFAESI proceedings can coexist because they operate in different fields and serve different purposes.18

Arbitration may determine an arbitrable contractual controversy, whereas SARFAESI provides a statutory mechanism for enforcement of security interests when its conditions are satisfied. The existence of an arbitration clause therefore does not automatically eliminate the secured creditor's statutory enforcement rights.

The Supreme Court's decision in *Transcore v. Union of India* also remains important in understanding the relationship between DRT proceedings and SARFAESI. The Court recognised the statutory scheme permitting recourse to the SARFAESI mechanism notwithstanding the pendency of recovery proceedings, subject to the structure of the legislation.19

The appropriate legal inquiry is consequently functional rather than competitive: what is the nature of the dispute, what remedy does the statute provide, what relief can arbitration lawfully grant, and whether the two processes can operate without undermining statutory jurisdiction? This approach prevents ADR from being treated either as an obstacle to recovery or as a substitute for every statutory remedy.

XI. WHY EARLY INTERVENTION MATTERS MORE THAN POST-NPA MEDIATION

The timing of ADR can determine its effectiveness. Once an account has substantially deteriorated, working capital may have been exhausted, receivables may have declined, employees and customers may have moved away and multiple creditors may have initiated separate proceedings. The bargaining space available to the parties can consequently shrink.

Earlier intervention offers a different possibility. The enterprise may still possess functioning operations, productive assets, employees, customer relationships and future cash flows. Those features create the economic foundation for restructuring or negotiated repayment.

The RBI's emphasis on early recognition and time-bound resolution of stressed assets supports this preventive approach.20 The regulatory framework should therefore be connected to internal early-warning systems rather than waiting until every account has reached a fully adversarial recovery stage.

The practical implication is that banks should develop objective referral criteria. An account should not be sent to mediation merely because a borrower requests additional time. Equally, a potentially viable account should not be excluded simply because the account has crossed a regulatory threshold. The relevant question should be whether structured negotiation has a reasonable prospect of producing a superior recovery outcome.

XII. A PROPOSED MODEL FOR BANKING MEDIATION

A workable banking mediation system should contain the following stages.

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18 M.D. Frozen Foods Exports Pvt. Ltd. v. Hero Fincorp Ltd., (2017) 16 SCC 741.

19 M/s Transcore v. Union of India & Anr., (2008) 1 SCC 125.

20 Reserve Bank of India, Prudential Framework for Resolution of Stressed Assets, DBR.No.BP.BC.45/21.04.048/2018-19 (7 June 2019).

Stage I – Stress Identification. Internal monitoring should identify credible signs of financial stress, including repeated payment irregularities, declining cash flows or other relevant indicators.
Stage II – Viability Review. The bank should distinguish temporary stress from structural unviability and assess whether the business can generate sufficient future cash flows.
Stage III – Referral. Eligible cases should be referred to a trained mediator under a defined institutional protocol.
Stage IV – Financial Disclosure. The borrower should provide relevant information concerning cash flows, liabilities, assets, receivables, security and realistic repayment capacity.
Stage V – Structured Negotiation. The lender and borrower should explore repayment, restructuring, compromise or other commercially supportable options.
Stage VI – Resolution Proposal. The agreed proposal should identify the amount payable, source of repayment, timeline and safeguards.
Stage VII – Bank Approval. The proposal should be considered by the competent authority under the bank's board-approved policy and delegated powers.
Stage VIII – Documentation. The settlement should be reduced to a clear and enforceable written instrument.
Stage IX – Monitoring. The bank should monitor compliance against agreed milestones.
Stage X – Recovery on Failure. If mediation fails or the settlement is breached, the bank should be free, subject to law, to pursue appropriate contractual and statutory remedies.
This sequence prevents mediation from becoming an indefinite moratorium against recovery. It also creates an institutional bridge between credit monitoring and formal enforcement.

XIII. SPECIALISED BANKING MEDIATORS

Banking disputes frequently involve technical questions concerning financial statements, collateral structures, project finance, consortium lending, guarantees, valuation, restructuring and insolvency. A specialised panel of banking mediators can therefore improve the quality of discussions.
Specialisation should not compromise neutrality. The mediator should not become an adviser to the lender or borrower and should not determine the merits of the dispute. Subject-matter competence is valuable because it enables the mediator to understand whether a proposal is commercially coherent and to communicate effectively with financial and legal professionals.
A credible panel should ideally include professionals with demonstrated experience in banking and finance, insolvency, restructuring, valuation, commercial contracts and dispute resolution. Training should include the regulatory environment in which banks make compromise decisions so that the mediation process does not generate proposals that are institutionally incapable of approval.

XIV. LIMITATIONS OF ADR IN NPA RECOVERY

ADR is not a universal solution. First, mediation depends upon meaningful participation. A borrower who deliberately withholds financial information or uses the process merely to delay enforcement can undermine the mechanism.
Second, mediation cannot create economic viability where none exists. If the enterprise has no credible repayment capacity, continued negotiation may merely postpone necessary enforcement or insolvency action.

Third, allegations of fraud, diversion of funds or serious misconduct may require investigation and statutory intervention rather than consensual settlement alone.

Fourth, multi-creditor situations can complicate bilateral mediation. A settlement with one bank may not stabilise a business that is simultaneously indebted to several financial institutions or operational creditors.

Fifth, post-default mediation without firm timelines may allow security value to deteriorate. The process must therefore preserve the lender's ability to protect limitation positions and take lawful protective steps.

Finally, bank officers may hesitate to approve reasonable settlements where internal accountability mechanisms are unclear. The solution is not to eliminate discretion, but to create transparent board-approved policies, documented decision-making and appropriate delegated authority. The RBI's 2023 compromise-settlement framework is relevant in this regard.21

ADR should therefore remain a selective instrument. The objective is not to mediate every NPA, but to identify the accounts where structured negotiation can plausibly improve the recovery outcome.

XV. ADR AND THE INSOLVENCY AND BANKRUPTCY CODE

The IBC operates differently from ordinary bilateral debt recovery. It establishes a collective framework in which the interests of creditors and other stakeholders are addressed through a statutory process and value maximisation is a central objective.22

Negotiated resolution nevertheless has a place within the statutory framework. Section 12A permits withdrawal of an admitted application under sections 7, 9 or 10 with the requisite approval of the Committee of Creditors. 23 This demonstrates that settlement and insolvency proceedings are not conceptually incompatible.

The limitation is equally important. Once a collective insolvency process is underway, bilateral negotiations cannot be allowed to defeat the rights of the broader creditor body or the statutory structure of the IBC. The strongest preventive role for ADR may therefore arise before insolvency proceedings are commenced, when the relevant parties can explore restructuring without undermining collective rights.

The correct relationship is thus sequential and complementary: ADR may prevent or resolve distress where appropriate; the IBC remains available where consensual resolution is inadequate or where the circumstances require a collective statutory process.

XVI. PRESERVING GOING-CONCERN VALUE

The preservation of going-concern value provides one of the strongest commercial arguments for mediation. The value of an enterprise is not always equal to the aggregate liquidation value of its individual assets. Machinery, land, licences, employees, customer relationships, supplier arrangements and goodwill may together produce a value that disappears when the enterprise is dismantled.

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21 Reserve Bank of India, Framework for Compromise Settlements and Technical Write-offs, RBI/2023-24/40, DOR.STR.REC.20/21.04.048/2023-24 (8 June 2023).

22 Insolvency and Bankruptcy Code, 2016, preamble and Part II.

23 Insolvency and Bankruptcy Code, 2016, s. 12A.

A negotiated repayment plan can, in appropriate cases, allow the business to continue operating while generating cash for repayment. This is not an argument for indefinite tolerance of default. It is an argument for selecting the recovery strategy after comparing the expected economic consequences of different options.
Mediation is particularly suited to this analysis because it allows the parties to discuss future cash flows, business operations, restructuring measures and commercial interests in a setting that is not limited to determining past contractual rights.
The concept of going-concern preservation should therefore become part of the bank's recovery assessment. Before taking an irreversible enforcement step in an apparently viable business, the bank should consider whether a time-bound negotiated arrangement can reasonably yield a higher net recovery after accounting for enforcement costs, delay and loss of enterprise value.

XVII. FROM LEGAL ENTITLEMENT TO RECOVERY VALUE: A NORMATIVE FRAMEWORK

The central weakness in a purely enforcement-oriented approach to stressed banking assets is that it tends to measure success by the availability and exercise of legal remedies rather than by the value ultimately recovered. A bank may possess a clear right to enforce security, yet enforcement may still produce an inferior economic outcome if the secured asset is highly specialised, if the borrower's business remains viable, or if the enforcement process materially reduces the value of the enterprise. The relevant legal-policy question is therefore not whether enforcement powers should be weakened, but when and how they should be exercised.24
This distinction permits a more precise understanding of ADR. Mediation is not valuable merely because it is less adversarial. Its real value lies in its capacity to generate information and options before the parties become locked into a single recovery strategy. The lender can test whether the borrower's difficulty is one of liquidity, profitability, project execution, management, market conditions or fundamental insolvency. The borrower, in turn, must demonstrate whether its proposed solution is supported by credible cash flows and realistic assumptions. The mediator can structure that exchange without assuming the role of either the bank's credit committee or an adjudicatory forum.
Such a model also responds to a legitimate concern about moral hazard. If borrowers believe that mediation automatically postpones enforcement, the process may encourage strategic delay. The answer is not to reject mediation, but to make eligibility and continuation conditional upon measurable criteria. These may include timely financial disclosure, cooperation with valuation, absence of material misrepresentation, a credible repayment proposal and compliance with agreed interim obligations. Where these conditions are absent, the bank should be free to discontinue negotiations and proceed with the appropriate remedy.
The same principle should guide settlement approval. A mediated proposal should be evaluated against a counterfactual recovery analysis: what is the likely net recovery from enforcement after taking account of time, legal expense, valuation uncertainty, deterioration of security and the possibility of business failure? The alternative should then be compared with the expected recovery under settlement, including the probability of default under the proposed arrangement. This approach does not require a bank to

Reserve Bank of India, 'Prudential Framework for Resolution of Stressed Assets', DBR.No.BP.BC.45/21.04.048/2018-19 (7 June 2019).

predict the future with mathematical precision. It requires the decision-maker to record why the negotiated outcome is commercially rational.

The proposed approach therefore treats mediation as an information-generating and value-preserving stage in the recovery process. It is strongest where the borrower has a plausible path to repayment but requires temporary flexibility, restructuring or a negotiated settlement. It is weakest where the enterprise is irretrievably insolvent, where there is serious misconduct, or where the legal dispute concerns rights that cannot lawfully be compromised through private negotiation.

XVIII. SAFEGUARDS AGAINST DELAY, EVERGREENING AND INCONSISTENT SETTLEMENTS

The principal criticism that may be directed against expanded use of mediation in NPA management is that it could become another layer of delay. This concern deserves serious treatment. Banking regulation has repeatedly emphasised that restructuring cannot be used to disguise a weak or unviable credit exposure. A mediation framework that ignores this principle would risk reproducing the very problem it seeks to solve.25

First, referral should be based upon a documented viability assessment. A bank should identify the source of distress and determine whether the proposed remedy is capable of restoring repayment capacity. A mere promise to pay, unsupported by financial information, should not be sufficient. Secondly, mediation should be time-bound. A defined referral period, a limited number of sessions and a clear decision point would prevent the process from becoming an indefinite standstill. Thirdly, the bank should retain the ability to take protective steps necessary to preserve security and comply with limitation requirements, subject always to the governing law and the circumstances of the case.

Fourthly, settlement decisions should be institutionally separated from informal bargaining. The mediator may facilitate discussions, but approval should remain with the authority competent under the bank’s internal policy. The RBI’s 2023 framework for compromise settlements requires regulated entities to maintain Board-approved policies and provides a regulatory basis for transparent settlement decision-making. A mediated proposal should therefore be treated as a recommendation for consideration under the bank’s established governance structure rather than as an agreement that becomes binding merely because it was discussed in mediation.

Fifthly, settlement implementation requires as much attention as settlement formation. Payment schedules, reporting obligations, release of securities, issuance of discharge documentation and correction of credit records should be expressly addressed. The EAEI Transformers decision demonstrates why this is important: the borrower had complied with the settlement, yet subsequent difficulties concerning the bank’s records and credit reporting generated further litigation. An efficient recovery framework must therefore measure success not only by the signing of a settlement but by complete and accurate implementation.

Finally, consistency is essential. If similarly situated borrowers receive radically different outcomes without recorded reasons, mediation may create perceptions of arbitrariness and expose bank officials to internal scrutiny. Board-approved parameters, delegated authority, valuation standards and documented

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Reserve Bank of India, ‘Framework for Compromise Settlements and Technical Write-offs’, RBI/2023-24/40, DOR.STR.REC.20/21.04.048/2023-24 (8 June 2023).

reasons for material concessions can reduce this risk. The objective is not to eliminate commercial discretion, but to make the exercise of that discretion reviewable and defensible.

XIX. ADR, CREDIT INFORMATION AND THE POST-SETTLEMENT STAGE

Debt resolution does not conclude when the borrower makes the final payment. The legal and commercial consequences of settlement continue until the lender's records, security documentation and credit information accurately reflect the position. This is especially important because credit reporting can affect the borrower's access to future finance, the functioning of its business and its ability to re-enter the formal credit system.26

A settlement framework should therefore identify the obligations of the lender after payment. Where the borrower has discharged the agreed amount and the settlement terms require release of securities or issuance of a No Due Certificate, those steps should be completed promptly and consistently with the settlement. If the account is reported to a credit information company, the classification should correspond to the legal and contractual position and to applicable regulatory requirements. A failure at this stage can convert a successful settlement into a new dispute.

The post-settlement stage also has significance for the credibility of mediation. Borrowers and lenders will have limited confidence in a process if the agreement reached through it does not produce reliable closure. For the lender, closure protects the integrity of its books and recovery statistics. For the borrower, it provides certainty about the consequences of compliance. For the financial system, accurate reporting reduces information asymmetry and assists future credit decisions.

XX. THE PROPOSED GRADUATED RECOVERY ARCHITECTURE

The analysis supports a five-stage architecture for managing stressed credit. Stage One is early detection through internal monitoring and regulatory asset-classification mechanisms. Stage Two is viability assessment, in which the lender determines whether the account is suitable for restructuring, settlement or mediation. Stage Three is structured ADR, principally mediation for consensual resolution and arbitration where an arbitrable contractual dispute requires adjudication. Stage Four is monitored implementation of the agreed solution. Stage Five is formal enforcement or insolvency resolution where consensual mechanisms fail or are legally inappropriate.27

The significance of this architecture lies in sequencing. The stages should not be treated as mutually exclusive silos. A bank may preserve statutory remedies while exploring a negotiated solution, provided that the legal requirements of the relevant recovery mechanism are respected. Similarly, a settlement may include provisions that operate alongside security enforcement rights in the event of breach.

The model also permits differentiation between types of borrowers. A temporarily stressed but commercially viable enterprise may benefit from early mediation. A borrower with weak but recoverable cash flows may require restructuring or a compromise settlement. An enterprise facing fundamental insolvency may be better dealt with through the IBC or another statutory mechanism. A borrower associated with fraud or serious misconduct may require immediate protective and investigative measures rather than a prolonged consensual process.

M/s EAEI Transformers Private Limited v The Reserve Bank of India & Ors, Civil Writ Jurisdiction Case No 6144 of 2025 (Patna HC, 2 February 2026).

Mediation Act 2023, s 15.

The proposed architecture thus moves the legal debate away from the question whether ADR is an alternative to recovery law. The more useful question is where ADR should be positioned within recovery law. Properly designed, it occupies the space between early financial stress and formal coercive enforcement. It does not diminish the bank's statutory powers; instead, it may help the bank determine when exercising those powers is likely to maximise recovery.

XXI. CONTRIBUTION OF THE ARTICLE AND FUTURE RESEARCH

The contribution of this article is to connect three ideas that are often examined separately: the preventive logic of mediation, the adjudicatory function of arbitration, and the statutory architecture for recovery of stressed banking assets. The article does not claim that ADR is a universal solution to NPAs. Rather, it proposes a functional allocation of roles. Mediation should be considered primarily as an early and consensual intervention; arbitration should be used for disputes that are legally arbitrable and contractually referable; SARFAESI and DRT mechanisms should remain available for statutory recovery; and the IBC should govern collective insolvency where its conditions are satisfied.28

This framework also suggests a future empirical research agenda. The effectiveness of banking mediation should be measured through indicators such as time to recovery, percentage recovery against outstanding dues, enforcement costs avoided, preservation of going-concern value, recurrence of default after settlement and the treatment of settlement accounts in credit information systems. Comparative data from banks using structured mediation protocols could help determine whether early ADR actually produces better recovery outcomes than immediate enforcement in different classes of stressed accounts.

Further research may also examine the relationship between mediation and consortium or multiple-creditor lending, where bilateral settlement may be insufficient. Another area is the design of digital mediation platforms capable of secure exchange of financial information while maintaining confidentiality and procedural fairness. The legal framework for such mechanisms should balance speed with the need for informed consent, record integrity and protection against coercion.

A final area for research concerns accountability. Banks operate within public, regulatory and fiduciary constraints, and settlement decisions may later be scrutinised by auditors, regulators or investigative agencies. Any expansion of mediation must therefore be accompanied by clear institutional standards explaining when a settlement is commercially reasonable. If officers have no confidence that a properly documented commercial decision will be respected, the existence of a mediation mechanism will not necessarily produce greater use of settlement.

XXII. RECOMMENDATIONS

1. **Integrate early-warning systems with ADR referral.** Banks should create an internal pathway through which eligible stressed accounts can be considered for mediation before enforcement becomes unavoidable.
2. **Develop specialised banking mediation panels.** Mediators should possess relevant competence in banking, restructuring, insolvency, finance and commercial disputes.
3. **Adopt strict timelines.** Mediation should have a defined commencement, review and closure process so that it cannot become an indefinite stay against recovery.

Mediation Act 2023, s 15; Insolvency and Bankruptcy Code 2016, s 12A.

4. **Protect legal positions.** Participation in mediation should not, subject to law and appropriate institutional safeguards, prevent the bank from protecting limitation positions or taking necessary interim and statutory measures.
5. **Require meaningful disclosure.** Continued participation should depend upon adequate disclosure of relevant financial and security information.
6. **Maintain transparent settlement policies.** Banks should have board-approved policies and clear delegated authority for restructuring and compromise decisions, consistent with applicable RBI directions.29
7. **Make settlements operationally complete.** Every settlement should specify payment milestones, security arrangements, reporting requirements, consequences of breach and post-settlement closure obligations.
8. **Preserve the statutory hierarchy.** ADR should operate alongside SARFAESI, DRT proceedings and the IBC rather than being presented as a mechanism that displaces them.
9. **Use technology where appropriate.** Online mediation can be considered for suitable disputes involving geographically dispersed parties, subject to the statutory framework.30
10. **Measure outcomes rather than settlement counts.** Banking mediation should be evaluated by actual recovery, time saved, reduction in enforcement costs, preservation of viable enterprises and compliance with settlements—not merely by the number of matters referred or settled.

XXIII. CONCLUSION

ADR cannot eliminate NPAs. Financial stress may arise from economic contraction, business failure, poor project execution, liquidity problems, managerial difficulties, market disruption or misconduct. No single dispute-resolution mechanism can address all of these causes.

The more defensible proposition is that ADR can reduce the likelihood that manageable financial stress will become a prolonged and value-destructive recovery dispute. Mediation has the greater preventive potential because it can create a structured dialogue while the borrower and the underlying enterprise may still possess sufficient economic value to support recovery.

Arbitration has a more defined but narrower role. Where a valid arbitration agreement exists and the dispute is legally arbitrable, arbitration can efficiently determine contractual controversies. It cannot, however, override statutory jurisdiction simply because a financing agreement contains an arbitration clause. The jurisprudence concerning DRT jurisdiction and the coexistence of arbitration with SARFAESI demonstrates the need for a functional analysis of remedies.3132

SARFAESI, DRT proceedings and the IBC remain indispensable parts of India's recovery architecture. ADR should therefore be viewed as an additional layer rather than an alternative that displaces statutory

29 Reserve Bank of India, Framework for Compromise Settlements and Technical Write-offs, RBI/2023-24/40, DOR.STR.REC.20/21.04.048/2023-24 (8 June 2023).

30 Mediation Act, 2023, ss. 3(h), 15. Section 3(h) defines mediation as a process in which parties attempt to reach an amicable settlement with the assistance of a mediator who has no authority to impose a settlement.

31 Vidya Drolia v. Durga Trading Corporation, (2021) 2 SCC 1; see also Supreme Court of India, Judgment dated 8 Mar. 2021.

32 M.D. Frozen Foods Exports Pvt. Ltd. v. Hero Fincorp Ltd., (2017) 16 SCC 741.

mechanisms. The appropriate model is graduated: early warning, viability assessment, mediation, restructuring or settlement, monitoring, and statutory recovery where necessary.

The ultimate objective of banking recovery should not be limited to obtaining an order or selling a secured asset. It should be the maximisation of legitimate recovery while avoiding unnecessary destruction of economic value. Properly designed, ADR can help banks distinguish between borrowers for whom enforcement is necessary and enterprises that can still generate sufficient value to repay their obligations.

The central policy proposition is therefore simple: **the earlier a bank identifies genuine financial stress, the greater the possibility of resolving it before the account becomes a costly and entrenched NPA dispute.** Mediation can supply the structured negotiation necessary for that early intervention, while arbitration, SARFAESI, DRT proceedings and the IBC provide distinct mechanisms for disputes and defaults that cannot or should not be resolved consensually. A modern banking recovery framework should use all of these mechanisms according to their legal function, commercial utility and appropriate timing