How Consumer Bankruptcy Reforms Can Help Save Microfinance in India

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The microfinance industry, once touted as one of the best hopes for alleviating poverty in rural India, faced a near collapse in the winter of 2011 as nearly all borrowers in Andhra Pradesh, one of the largest states in India, stopped repaying their loans. This borrower backlash was fueled by widely reported stories of farmer suicides and unscrupulous lending practices. Politicians have responded with populist legislation aimed at curtailing microfinance in India—for example, by capping interest rates. The Article argues that these proposals are misguided in that they would constrict lending to poor villagers.

The Article questions why Indian policymakers have overlooked the role of legal debt relief in addressing these grievances and stabilizing lending in rural India. Strengthening the consumer bankruptcy laws in India, I argue, can help stabilize the development of consumer finance while addressing the legitimate grievances raised by the microfinance rebellion—namely, the imbalance of power that exists between lender and borrower. Doing so may reduce the political pressure to adopt misguided proposals restricting microfinance, which would hurt the very people that such laws are meant to protect.

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I. Introduction

Lalitha Nursilmula was a cheerful 16 year old girl, who could often be found singing along to popular Bollywood tunes on her way to class. She was also bright and determined, focusing on studying commerce and economics at a local college, in Godhumagudu. One day, while she was home alone, an employee of a microfinance company came to her village and asked her to travel to the community office where he could ask her a few questions. Once they arrived, the agent, the village head, and four members of the family’s “joint liability group”—villagers that had assumed collective responsibility for the debt—cornered her and demanded payment on an outstanding loan of 66,000 rupees that the family had ran up to pay for the wedding of their elder daughter. They threatened that they would humiliate her and her entire family if she didn’t bring the money by the end of the day. “Sell your body if you have to,” the agent reportedly said.

Lalitha ran home, crying the whole way. She called her mother, and tried to explain what happened, but her mother could barely make out the words in the midst of Lalitha’s sobbing. She then swallowed a lethal dose of pesticide. Although her relatives scrambled home to save
her, they were too late. Before taking her own life, Lalitha left a note imploring her parents to not take out any more loans, except to invest in the education of their younger son.

Lalitha’s suicide was one of many tragedies that swept over rural villages in Southern India this past year. At least 75 people have committed suicide in the fall of 2010 in the state of Andhra Pradesh, facing pressure to repay loans to microfinance firms. These suicides are generally linked with the deep shame that Indians feel towards failing to repay debt.

Many more have found themselves in desperate straits, taking out further loans to pay old ones, and creating a spiral of crushing debt. Widely reported stories of Lalitha’s fate, and many other tragic suicides, have stirred anger against unscrupulous microfinance lenders. In the winter of 2011, the microfinance industry faced a near collapse as nearly all borrowers in Andhra Pradesh, one of the largest states in India, had stopped repaying their loans. These revelations have pushed the microfinance industry to the brink of collapse. Moreover, it appears that the

10 Id.
11 Id.
14 See Buncombe, supra note 12.
15 See Polgreen et al., supra note 13 (tracing the building crisis over alleged coercive practices of some microlenders).
16 Id.
17 Id. ("Indian banks, which put up about 80 percent of the money that the companies lent to poor consumers, are increasingly worried that . . . they could now face serious losses."). Moreover, at least one Indian state has enacted laws that would harm the profitability of microfinance firms. See All Things Considered, India's Poor Reel under Microfinance Debt Burden, NPR, Dec. 31, 2011, 2010 WLNR 25689175 ("[This] legislation . . . will, in effect, put the microlenders out of business.").
perception of microlending has shifted among the elites, marking a dramatic change of fortunes for the microfinance industry.\textsuperscript{18}

A second line of assault has come from the politicians. Legislators in the state of Andhra Pradesh have responded to abusive practices in the microfinance industry by passing a strict new law regulating how the microfinance industry can make loans and collect payments.\textsuperscript{19}

Proponents of this crack-down effort point to growing reports of suicides among poor people unable to pay their debts, and argue that an unregulated microfinance industry has led to the proliferation of abusive practices.\textsuperscript{20} They argue that as the microfinance industry has shifted from a focus on charity to a focus on profits, the banks have extended loans without making sure

\textsuperscript{18} Microfinance Focus conducted an opinion poll of 165 delegates to the Microfinance India Summit 2009, including key stakeholders in the microfinance world. Notably, when asked whether the government should impose a cap on interest rates charged by microfinance institutions, 51\% said “no.” Opinion Poll Brings Forth Key Trends in Indian Microfinance, Microfinance Focus, Nov. 2, 2009, http://www.microfinancefocus.com/news/2009/11/02/opinion-poll-brings-forth-key-trends-of-indian-microfinance. This polling data, though from an unfamiliar source, gives some evidence that, before the microfinance scandals erupted, the elites had opposed capping interest rates, a proposal that has subsequently gained support in some Indian states. See e.g., Andhra Law To Curb Microfinance Firms Comes into Force, Business Standard, Jan. 2, 2011, 2011 WLNR 38569; AP Law To Curb Microfinance Firms Implemented, Daily Pak Banker (Pakistan), Jan. 2, 2011, 2011 WLNR 60086. Hostile newspaper articles directed at microfinance also provide some evidence of a shift of opinion among the elites, as do articles from pro-business sources defending microfinance against aggressive reforms and offering incremental solutions. See e.g., Help Microfinance, Don't Kill It, The Indian Express, Nov. 26, 2010, 2010 WLNR 23517175 (“But politicians also need to be wary - in taking aim at the occasional overstep, they may find themselves inadvertently destroying the whole business, at great cost both to the poor, and the financial institutions that have stepped in to work with them.”); R. Jagannathan, Why Microfinance is Not Half the Villain it Seems To Be, Daily News & Analysis, Dec. 9, 2010, 2010 WLNR 24363054 (“The Andhra ban on coercive collections is a palliative, but the real solution lies in regulating the sector better.”); Leave Well Alone: Capping Microfinance Interest Rates Will Hurt the Poor. There Are Better Ways to Regulate the Industry, The Economist, Nov. 18 2010, http://www.economist.com/node/17522606?story_id=17522606. Finally, a periodical search did not reveal any polling regarding how the Indian public views microfinance, or whether these views have shifted.

\textsuperscript{19} See Andhra Pradesh Micro Finance Institutions (Regulation of Money Lending) Act, 2011, http://indiamicrofinance.com/wp-content/uploads/2010/10/Andhra-MFI-Ordinance.pdf (imposing registration requirements, conferring authority to an agency to cancel such registration upon complaints from the public and after a hearing, prohibiting individuals from joining more than one self-help group (e.g., a joint liability group), imposing interest rate caps, prohibiting generally the issuance of multiple loans, banning any coercive measures, etc.); see also Polgreen et al., supra note 13 (making note of this law); Daily Pak Banker, AP Law, supra note 1 (noting that the governor signed it into law on January 1\textsuperscript{st}, 2011).

these loans were applied to start-up businesses.\textsuperscript{21} Indeed, it seems that many poor Indian borrowers, like Lalitha’s family, have started using microfinance loans to pay for education, increase quality of life, and boost their consumer activity in addition to promoting business production.

Opponents of a crack-down argue that many of these proposals are misguided and would constrict lending to poor villagers.\textsuperscript{22} They contend that the microfinance industry, though imperfect, is too important to abandon, as India’s poor citizens start to gain power and increase their activity as consumers and producers within the capitalist system.\textsuperscript{23} Clearly, however, some reforms must be implemented to respond to the legitimate grievances of the public. What has been overlooked in this debate is the role of legal debt relief in addressing these grievances and stabilizing lending in rural India.

Although India has a consumer bankruptcy law on the books, it has not been significantly updated for 100 years.\textsuperscript{24} Nor does it appear that Indians tend to take advantage of its protections.\textsuperscript{25} Does the statutory text of India’s consumer bankruptcy law contain provisions that severely restrict who can file for bankruptcy? Do cultural reasons explain why Indians do not take advantage of bankruptcy relief? Is the deep shame associated with failing to pay debts in Indian culture equivalent to the shame associated with becoming a bankrupt? If a rural Indian farmer, overburdened with debt, feels that his situation is hopeless and that there is no way out, could bankruptcy relief provide a way out?

\textsuperscript{21} See India PM Panel: Microfinance Institutions' Business Model is Full of Fault, Daily Pak Banker (Pakistan), Jan. 6, 2011, 2011 WLNR 371051 (“[Microfinance institutions] have been indulging in multiple lending and large parts of the loans are given for consumption purposes.”) [hereinafter "Daily Pak Banker, India PM Panel"].
\textsuperscript{22} See The Economist, Leave Well Alone, supra note 18.
\textsuperscript{23} Id.
\textsuperscript{24} See Adam Feibelman, Consumer Finance and Insolvency Law in India, A Case Study, 36 BROOK. J. INT'L L. 75, 107 (2010) [hereinafter "Feibelman, India"].
\textsuperscript{25} Id., at 114.
The microfinance crisis provides an opportunity to consider these questions and examine the role of consumer bankruptcy in facilitating development. Much ink has been spilled in legal circles writing about microfinance, with many articles addressing the problems and potential of consumer finance as a development tool. However, consumer finance is only one piece of the puzzle when it comes to sustainable and inclusive development. Another big piece, consumer debt relief, has received scant attention.

This Article advocates for the role of consumer bankruptcy in facilitating development in India, and argues that strengthening the consumer bankruptcy system would address the root of the grievances raised by the rebellion against microfinance—that is, it would serve to correct the imbalance of power that exists between lender and borrower. Doing so may reduce the political pressure to adopt misguided proposals restricting microfinance, which would hurt the very people that such laws are meant to protect.


27 But see Claire Moore Dickerson, Informal-Sector Entrepreneurs, Development And Formal Law: A Functional Understanding Of Business Law, 59 AM. J. COMP. L. 179, 197 (2011) (“Historically, little practical attention has been paid to bankruptcy and insolvency laws in Sub-Saharan Africa. . . This is unfortunate since these laws can be an effective means of putting unproductive assets back to productive use. . . OHADA does provide an interesting and flexible three-level approach, allowing a business in sudden crisis to request the court's protection, and then also permitting reorganization, unless liquidation is the only realistic option.”) [hereinafter "Dickerson, Informal-Sector Entrepreneur”]; Adam Feibelman, Consumer Bankruptcy as Development Policy, 39 SETON HALL L. REV. 63 (2009) (advocating for consumer bankruptcy as development policy) [hereinafter "Feibelman, Consumer Bankruptcy”]; Feibelman, India, supra note 24.

28 See note 201, infra and related text.

29 The preamble to the Andhra Pradesh law restricting microfinance states: “Whereas these SHGs are being exploited by private microfinance institutions through usurious interest rates and coercive means of recovery resulting in their impoverishment & in some cases leading to suicides, it is expedient to make provisions for protecting the interests of the SHGs, by regulating the money leading transactions by the money lending [microfinance institutions].” Andhra Pradesh Micro Finance Institutions (Regulation of Money Lending) Act, 2011, http://indiamicrofinance.com/wp-content/uploads/2010/10/Andhra-MFI-Ordinance.pdf. Despite the stated purpose of this populist legislation, the legislators in Andhra Pradesh may have a variety of motives beyond protecting poor debtors.
Part II provides a brief summary of the history of microfinance and explains how it works. Part III recounts the recent rebellion against microfinance in India. Part IV explores some of the populist legislation aimed at curbing its excesses. Finally, Part V argues that strengthening the consumer bankruptcy laws in India can help stabilize consumer finance while addressing the legitimate grievances that the people have against the microfinance industry.

II. Microfinance: A Brief History

This Part will briefly summarize the history of international microfinance and explain how it works. In contrast to the shiny public perception of microfinance, it has evolved into a much darker reality.

The Grameen Bank is credited with starting the microfinance revolution in the 1970s. Microfinance institutions were originally intended to extend small loans to poor borrowers, who use this capital to fund small businesses. These are often short-term loans, having a duration of less than two years, and typically range from $10-$1,000.

At its best, microfinance institutions offer economic opportunity to poor people, who otherwise would be shut out of the formal lending sector. Traditional financial institutions do not typically make loans to small businesses because such loans carry a high risk of default and

30 See Molly Richardson, Increasing Microlending Potential in the United States Through a Strategic Approach to Regulatory Reform, 34 J. CORP. L. 923, 925 (2009); Rashmi Dyal-Chand, Reflection in a Distant Mirror: Why the West has Misperceived the Grameen Bank's Vision of Microcredit, 41 STAN. J. INT'L L. 217, 219 (2005) (“Formed in 1976, the Grameen Bank's mission is to lend to those whose needs are not met by commercial lenders.”). A few economists, working for the major neo-liberal funding organizations, helped to lay the intellectual framework for microfinance by championing the development potential of the informal sector. See Dickerson, Informal-Sector Entrepreneur, supra note 27, at 200. For example, the Peruvian economist Hernando de Soto was highly influential in advocating that property rights in the informal sector should be formalized. Id. at 200-01.
31 See Richardson, supra note 30, at 925.
32 Id. at 925. These loan amounts are typically at the lower end of this range. See Hardikar, supra note 20 (reporting that among the loan portfolios of the 146 self-reporting microfinance institutions in 2009, there was an average per borrower loan of $144.5).
33 For present purposes, the term small business refers to businesses with fewer than five employees.
have high transaction costs.\textsuperscript{34} Even now, when microfinance loans have become widely accessible, many members of the farming classes rely instead on village loan sharks to provide the bulk of rural credit in poor countries.\textsuperscript{35} The problem is that loan sharks are notorious for high interest rates and abusive collection methods.

Microfinance has been credited with lifting many people out of poverty, by increasing these borrowers’ income and quality of life.\textsuperscript{36} Indeed, some scholars say that the rapid growth of global microfinance provides some evidence that “expanding access to consumer finance can promote development.”\textsuperscript{37} Microlenders often require these loans to be used for productive purposes associated with expanding a businesses, as opposed to personal consumption.\textsuperscript{38} For example, such productive uses may include purchasing raw materials and supplies, such as food ingredients or even cell phones.\textsuperscript{39}

Unlike traditional financial institutions, which often require the borrower to pass a credit check and put up collateral in exchange for a loan, microfinance institutions employ innovative

\textsuperscript{34} See Richardson, supra note 30, at 925. However, there is reason to believe that the risk of default for microloans was often low because, until the recent crisis erupted, the banks enjoyed repayment rates of approximately 95%. See Buncombe, supra note 12. Nevertheless, it is true that microlending is time and labor intensive. See All Things Considered, supra note 17 (“Microfinance lenders do their business on the client’s doorstep, meaning that representatives have to travel to slums or rural villages to make the loans and then come back weekly to collect the payments.”).

\textsuperscript{35} See The Economist, Leave Well Alone, supra note 18 (82% of households in [Andhra Pradesh] hold informal loans).

\textsuperscript{36} See Richardson, supra note 30, at 925-26; Hardikar, supra note 20. However, there is considerable dissent from this view. See Vikas Bajaj, Microlenders, Honored With Nobel, Are Struggling, N.Y. Times, Jan. 5, 2011, http://www.nytimes.com/2011/01/06/business/global/06micro.html (“Most borrowers do not appear to be climbing out of poverty, and a sizable minority is getting trapped in a spiral of debt, according to studies and analysts.”), (“’Credit is both the source of possibilities and it’s a bond’ . . . [and it] is often operating at this knife’s edge, and that gets forgotten,’ [said David Roodman, a senior fellow at the Center for Global Development].”) The Economist takes guardedly optimistic position on microfinance, stating “research suggests that it does work—for some people some of the time, as you would expect. It is not a magic bullet, but nor is it intrinsically harmful.” See The Economist, Under Water, supra note 1.

\textsuperscript{37} See Feibelman, Consumer Bankruptcy, supra note 27, at 77.

\textsuperscript{38} See Richardson, supra note 30, at 926.

\textsuperscript{39} Id.
methods to reduce the risks associated with lending to poor borrowers.\textsuperscript{40} In other words, microfinance institutions rely on informal constraints on behavior to encourage borrowers to repay their loans.\textsuperscript{41} For example, the Grameen Bank employs peer lending circles, usually consisting of women, which rely on social pressure to assure loan repayment.\textsuperscript{42} The group may have joint responsibility for paying the loan, or the entire group may be cut off from future loans if one member of the group fails to repay her loan.\textsuperscript{43}

The microfinance industry has been widely applauded for extending loans to millions of poor people in over 100 developing countries around the world, including Asia, Africa, and the Americas.\textsuperscript{44} For example, ACCION International, a leading microfinance institution, has lent $12.3 billion dollars to nearly 5 million people between 1997 and 2006, all while achieving a repayment rate of 97\%.\textsuperscript{45} Many NGOs and philanthropic groups joined this bandwagon in the 1970s, and started offering microloans in developing countries,\textsuperscript{46} with the goal of alleviating poverty in developing countries by vastly increasing accessibility, aiming to reach many of the three quarters of Indians who survive on less than $2 a day.\textsuperscript{47}

As microfinance has come to be viewed as a high-growth area, the number of commercial microcredit lenders has increased dramatically.\textsuperscript{48} The microfinance industry gradually shifted

\textsuperscript{40} Id. However, there is reason to believe that variations of these “innovative” methods have existed for quite a long time at the local level.

\textsuperscript{41} Id.; Hardikar, supra note 20 (“[T]he Grameen methodology [includes] identify the poor, organise them (so there's homogeneity and moral liability of repayment in the absence of any collateral), and standardise products and systems, enforce discipline, and ensure that any breach is dealt with severely and sternly.”).

\textsuperscript{42} See Richardson, supra note 30, at 926.

\textsuperscript{43} “Other methods include information gathering about a potential borrower, joint liability contracts, short term contracts, or ‘loan ladders,’ which increase subsequent loan amounts after each repayment.” Id.

\textsuperscript{44} Id. A number of articles have exploring the potential for importing the microfinance model to developed countries, including the Unites States. See note 26, supra.

\textsuperscript{45} See Richardson, supra note 30, at 926.

\textsuperscript{46} Id.

\textsuperscript{47} See The Economist, Under Water, supra note 1.

\textsuperscript{48} See Richardson, supra note 30, at 926.
from a non-profit model reliant on donors to a for-profit model driven by shareholders.\textsuperscript{49} Amidst this shift, some microfinance institutions have growth at a rapid clip, achieving growth rates as high as 100% a year.\textsuperscript{50} The markets came to view the growth prospects of microfinance so bullishly that SKS Microfinance raised $357 million in its IPO on the Mumbai stock exchange.\textsuperscript{51}

Did microlending start out with a charitable heart but came to be exploited by big banking interests? Has the microfinance system transformed from a non-profit philanthropy to a for-profit industry? In the midst of this shift, has the balance of power shifted between lender and borrower in a way that is disadvantageous or crippling to the borrower?

\textbf{III. Microfinance on the Brink of Collapse in India}

The world of profit-based microfinance in India has been badly shaken by recent scandals, pushing the microfinance industry to the brink of collapse.\textsuperscript{52} Microlending is failing in India for several reasons. First, there has been a cultural backlash generated by widely publicized stories of farmer suicides, abusive lender practices in a changing industry, and the political targeting of microfinance. Second, there have been economic setbacks associated with its fast growth in India followed by a wave of recent defaults.

Interestingly, the exploitation of the shame of failing to pay your debts, coupled with intense peer pressure from the surrounding group,\textsuperscript{53} is exactly what has made microfinance so successful. In countries where this shame/peer pressure combination is effective, microfinance

\textsuperscript{49} See Hardikar, supra note 20.
\textsuperscript{50} See Bajaj, supra note 36. However, the profitability of these lenders has decreased dramatically in light of recent events. See note 74, infra and related text. In addition, some argue that these high profit margins have made the loans less effective. Id.
\textsuperscript{51} See All Things Considered, supra note 17.
\textsuperscript{52} See Polgreen et al., supra note 13.
\textsuperscript{53} This refers to practices such as requiring collective responsibility for loan repayment. See note 41, supra and related text.
institutions have enjoyed extremely high national payback rates. However, the exploitation of the deep shame rural Indians associate with debt has led to the proliferation of farmer suicides. This shame has been compounded by abusive practices by microfinance companies that detractors say have contributed to widespread tragic outcomes.

First, it seems that microfinance institutions placed too much reliance on community pressure, instead of considering the individual borrower’s ability to repay. Second, they assert that microfinance institutions started using coercive methods to collect on debts, including intimidation. For example, bankers have hired underlings to coerce debtors into repaying by threatening to humiliate them before their community. Third, they argue that microfinance institutions, such as SKS Microfinance, have made huge profits on the backs of the poor, impoverishing rural Indians by cajoling them into accepting loans at exorbitant interest rates.

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54 Although this topic is beyond the scope of this article, it would be interesting to explore how microfinance institutions rely on exploiting informal constraints on behavior to achieve high repayment rates. One could contrast the act of taking out a loan in the United States, which (at least in urban areas) is typically a very individual experience (rather than a communal one). Is the peer pressure model not applicable in the United States, which lacks the kind of communal pressures that make it successful in India? Do the recent debt rebellions suggest that relying on informal constraints is fatally flawed as a model, or can it survive with reforms?

55 See note 13, supra and related text (citing anthropological articles).

56 See e.g., Polgreen et al., supra note 13; Burke, supra note 20; Hardikar, supra note 20. For a discussion of corporations have engaged in human rights abuses in India in different contexts, see Claire Moore Dickerson, Ozymandias As Community Project: Managerial/Corporate Social Responsibility and the Failure of Transparency, 35 CONN. L. REV. 1035, 1048-51 (2003) (detailing human rights abuses in India by Enron) [hereinafter “Dickerson, Ozymandias”].

57 See Polgreen et al., supra note 13. In other words, they were just in it for the money, rather than channeling money to activities that generate income for poor Indians. See Bajaj, supra note 36 (“Many had used the money to pay for televisions or health care or to soften the blow of failed crops, rather than as seed money for businesses.”). On the other hand, Indians can benefit from the smoothing effect that receiving microloans may have on their income.

58 See Polgreen et al., supra note 13; The Economist, Under Water, supra note 1 (“Some ‘recovery’ methods have involved intimidation.”).

59 For example, in the account of one borrower, “collectors from the finance companies hounded her day and night, shaming her in front of her neighbors. They told her to get the money any way she could, by stealing if necessary, and they told her she’d be better off dead.” See All Things Considered, supra note 17.

60 See Polgreen et al., supra note 13. These microfinance institutions typically charged interest rates of up to 36 percent. See Daily Pak Banker, India PM Panel, supra note 21. However, it appears that some microfinance institutions admitted to charging 50 to 60 per cent interest. See Business Standard, Andhra Law, supra note 18. Presumably, the competition with non-profit firms, as well as with loan sharks, would serve to keep interest rates down. Moreover, these interest rates might be more justified in light of the inflation picture. It seems, however, that part of the anger stems from the very idea of earning profits from making loans to poor people. See Hardikar, supra note 20. Muhammed Yunus, the Grameen Bank founder, reflected this mood by criticizing microfinance institutions
To many local politicians, the microfinance industry has become just as bad as the widely hated village loan sharks that microfinance promised to replace.\(^6^1\)

Arguably, as the microfinance industry shifted from charity to profits, it lost sight of its traditional focus of helping the poor.\(^6^2\) One might ask whether making profits and helping the poor are ever compatible, or if this just a pipe dream of “social entrepreneurs”?\(^6^3\)

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61 See Hardikar, supra note 20 (“‘We created microcredit to fight the loan sharks,’ reasoned Professor Muhammed Yunus . . . ‘We didn’t create microcredit to encourage new loan sharks.’”); Polgreen et al., supra note 13. Ironically, one senior official in Andhra Pradesh, Reddy Subrahmanyam, expressed nostalgia for the village loan sharks, stating “[t]he money lender lives in the community. . . At least you can burn down his house. With these companies, it is loot and scoot.” See Polgreen et al., supra note 13. In other words, is it better to have the devil you know (and whose house you can set on fire) than the devil you don’t (who lives in a high-rise condo downtown)? However, it appears that the microfinance industry has received a disproportionate share of the blame for farmer suicides in India, for many of these borrowers owed even larger sums of money to the local loan shark. See e.g., The Economist, Under Water, supra note 1 (“Anthaiah took his own life as a payment loomed on a 15,000 rupee ($333) [microfinance] loan. Heavy rain had waterlogged his cotton crop and left the family struggling to pay the interest rate of 36% a year. But the couple, who had borrowed to build this house, also owed 34,000 rupees to a local moneylender, who charged over 50%.”).

62 See Hardikar, supra note 20 (“But what was pitted as an innovating financial practice to address poverty, is now being viewed as the next big investment opportunity, a concept that critics say is antithetical to its charitable roots.”). In addition, it is not clear whether the interest rates charged by for-profit microfinance firms materially differed from non-profit firms. Non-profit firms, like for-profit firms, operate under pressure based on the bottom line. Perhaps, however, the managers of for-profit firms are under a more intense form of pressure.

63 Generally speaking, “social entrepreneurs” are liberals that want to solve social problems with capitalist and/or market-based solutions. See e.g., Nicholas Kristof, The Role of Microfinance, N.Y. Times, Dec. 28, 2009 http://kristof.blogs.nytimes.com/2009/12/28/the-role-of-microfinance/ (praising the “remarkable achievement” of microfinance); Nicholas Kristof, Do-Gooders with Spreadsheets, N.Y. Times, Jan. 30, 2007, http://select.nytimes.com/2007/01/30/opinion/30kristof.html (quoting approvingly a description of social entrepreneurs as “the most important historical force at work today”); Nicholas Kristof, You, Too, Can Be a Banker to the Poor, N.Y. Times, March 27, 2007, http://select.nytimes.com/2007/03/27/opinion/27kristof.html (“For those readers who ask me what they can do to help fight poverty, one option is to sit down at your computer and become a microfinancier.”); Stephanie Strom, Thanksgiving Reading: Charity with a Bottom Line, N.Y. Times, Nov. 23, 2006, http://dealbook.nytimes.com/2006/11/23/thanksgiving-reading-charity-with-a-bottom-line/ (“[This] year, as never before, the line between philanthropy and business is blurring. A new generation of philanthropists . . . believe that [capitalism] can be applied in the service of charity. They are “philanthropreneurs,” driven to do good and have their profit, too.”); Thomas L. Friedman, ‘Patient’ Capital for an Africa That Can’t Wait, N.Y. Times, Apr. 20, 2007, http://select.nytimes.com/2007/04/20/opinion/20friedman.html (“Africa needs many things, but most of all it needs capitalists who can start and run legal companies . . . People grow out of poverty when they create small businesses that employ their neighbors. Nothing else lasts.”). Perhaps the microfinance movement taps into a famous idiom, “you can give a man a fish, and he’ll eat for a day. But if you teach him how to fish, he’ll eat for a lifetime.” In this case, the microfinanceer is not teaching how to fish, but is fronting some money to buy the bait.
The public outcry stemming from these perceived abuses has been thunderous, directed largely at unscrupulous microfinance lenders.\(^6^4\) In the winter of 2011, the microfinance system faced collapse as nearly all borrowers in Andhra Pradesh, one of the largest states in India, stopped repaying their loans.\(^6^5\) In fact, loan-recovery rates plummeted from higher than 95% to below 15%.\(^6^6\) Local politicians, seeing this crisis as an opportunity to burnish their populist credentials with the rural poor, encouraged borrowers to default en masse.\(^6^7\) Ironically, the microfinance industry’s success in India has sometimes made it a political target because so many voters owe them money.\(^6^8\) Championing the cause of poor microfinance borrowers, politicians have characterized microlenders as profiteering on the backs of the poor.\(^6^9\)

This crisis portends ill for the future of microfinance in India. For starters, the microfinance industry in India is highly concentrated in Andhra Pradesh, where half of all microcredit borrowers reside.\(^7^0\) Therefore, if the microfinance crisis were contained in Andhra Pradesh, that would be damaging enough. However, the loan rebellion in Andhra Pradesh has had ripples across the nation.\(^7^1\) Lending has slowed down considerably in other states due to

\(^{6^4}\) See Buncombe, supra note 12.
\(^{6^5}\) See Polgreen et al., supra note 13.
\(^{6^6}\) See Buncombe, supra note 12; The Economist, Under Water, supra note 1.
\(^{6^7}\) See The Economist, Under Water, supra note 1. In the past, political parties have used their opponents’ ties to foreign banks as a political wedge issue. Id. (“The main opposition Telugu Desam Party lost power in 2004 partly because it was seen as in thrall to the IT industry and foreign investors.”). However, the extent to which this debt revolt was centrally organized by politicians and/or activists is not clear. In some cases, local activists overstepped the bounds of persuasion by “physically prevent[ing] loan collectors from entering . . . villages.” See Buncombe, supra note 12. Either way, the effect was to create a massive boycott against microfinance.
\(^{6^8}\) See The Economist, Under Water, supra note 1.
\(^{6^9}\) See Bajaj, supra note 36.
\(^{7^0}\) See Jagannathan, supra note 18 (“Andhra Pradesh is now second only to Bangladesh as the most microfinance saturated place on earth, with a full 17% of the population in possession of a microloan account.”); The Economist, Under Water, supra note 1 (“[Andhra Pradesh] accounts for at least half India’s total, with more than 25m borrowers, up from 8m in 2007.”); but cf Polgreen et al., supra note 13 (one-third reside in Andhra Pradesh). As The Economist has put it, “Andhra Pradesh is not so much the jewel in its crown as the crown itself.” See The Economist, Under Water, supra note 1.
\(^{7^1}\) See Polgreen et al., supra note 13.
growing fears of defaults. Until recently, the microfinance industry was growing at a rapid pace, but this political backlash has halted its expansion. Worse, these trends, if they continue, could potentially destroy microfinance in Andhra Pradesh and possibly beyond.

This widespread hostility toward microfinance marks a dramatic reversal of fortunes for the industry, which previously was touted as the one of the best hopes for alleviating poverty in rural India. Not long ago, the microfinance industry was showered with praise (and cash) by politicians, philanthropists, and bankers. In 2000, world leaders enshrined microfinance as one of the pillars of the United Nations’ ambitious Millennium Development Goals for 2015, which sought to reduce the number of people living in extreme poverty by half. This trickle up form of capitalism was so appealing to leaders in the developed world that Muhammad Yunus, one of the founders of microfinance, was given the Nobel Peace Prize in 2006.

The current reaction to the scandals associated with microfinance could destroy the industry, an outcome having severe consequences for poor borrowers. First, because traditional banks are unwilling to extend loans in small amounts, or to risky borrowers, destroying

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72 Id. “Banks, the primary source of money for microlenders, have turned off the tap because they are worried about the industry’s future. As a result, microlenders have slowed or stopped lending nationwide.” See Bajaj, supra note 36.
73 There are at least two components to the political backlash against microfinance: first, the mass boycott in Andhra Pradesh; and second, the legislation promulgated to address abusive practices. For present purposes, they are conflated together into one large political backlash that threatens the future of the microfinance industry.
74 The Indian credit rating firm Crisil Ltd. has downgraded the credit ratings of 12 microfinance institutions to “rating watch with negative implications.” See Crisil Puts 12 Microfinance Lenders on Ratings Watch, Mint, Nov. 23, 2010, 2010 WLNR 23289133. Mover, the stock price of the leading commercial lender, SKS Microfinance, had dropped by 36.79% from October 15th 2010 to November 23rd 2010. Id.
75 See The Economist, Under Water, supra note 1. This crisis has spread to microlenders in other developing countries. Id. (“In Pakistan’s Punjab province, for example, it became fashionable in 2008-09 for politicians to encourage borrowers to default on microloans.”); The Economist, Leave Well Alone, supra note 18 (“In Bangladesh the government has capped the annual interest rate that microfinance institutions . . . can charge at 27%.”).
76 See note 63, supra and related text.
77 See Bajaj, supra note 36. “Philanthropists and investors poured billions of dollars into nonprofit and profit-making microlenders.” Id. The success of microfinance was also illustrated by SKS’s IPO.
78 Id.
79 See All Things Considered, supra note 17.
80 See Polgreen et al., supra note 13.
microfinance would cut off an important source of capital to poor borrowers. 81 Second, borrowers may be forced to rely on village loan sharks once again. 82

IV. Populist Legislation Aimed at Protecting the Poor Harms Debtors

Responding to a series of scandals in the microfinance industry, Indian policymakers have recently undertaken to address the costs and negative externalities associated with expanding consumer finance, such as consumer financial distress and over-indebtedness. 83 In general, a variety of options are available to policymakers to address these problems, including “usury laws, disclosure requirements, financial education, laws prohibiting particular transactions or terms, limits on debt collection, and debt relief.” 84 This Part will explain how some of these legislative proposals end up hurting poor borrowers by reducing consumer lending, therefore illustrating the need to empower consumers in another way, by strengthening the consumer bankruptcy laws.

A number of states in India have advanced policies aimed at stabilizing lending and addressing the costs associated with consumer indebtedness. 85 Legislators in Andhra Pradesh passed a stringent new law regulating consumer finance, which changes the business practices of microfinance institutions in a number of ways, such as capping interest rates. 86 Moreover, the

81 See The Economist, Leave Well Alone, supra note 18. Some have portrayed this result—cutting off capital to poor borrowers—as “financial apartheid.” See Polgreen et al., supra note 13. However, this ignores the important role that the informal lending sector has and continues to play in allocating capital in rural areas. Moreover, modest government lending programs exist that could help fill the void.
82 Id.
83 See Feibelman, Consumer Bankruptcy, supra note 27, at 67. These costs have existed for some time, but it seems that the recent scandals have heightened the urgency to deal with them. See infra note 179 and related text (discussing how the costs of expanding consumer finance have been ignored in India).
84 See Feibelman, Consumer Bankruptcy, supra note 27, at 67.
85 See Polgreen et al., supra note 13.
86 See id.; note 19, supra and related text.
The federal government is coordinating with the reserve bank of India, the country’s central bank, on a new set of comprehensive federal regulations to govern the microfinance industry.\textsuperscript{87}

The policy of capping interest rates, despite its good intentions of trying to prevent the poor from getting deep into debt, is misguided for several reasons.\textsuperscript{88} Although microfinance institutions appear to charge high interest rates, they typically have thin profit margins due to high administrative costs associated with making millions of small loans and collecting them.\textsuperscript{89} Until recently, microfinance institutions were able to attract large amounts of private capital,\textsuperscript{90} and this success could be squandered if the government forces down interest rates, thus diminishing the growth prospects of for-profit microfinance firms.\textsuperscript{91} Moreover, slow growth would hinder the ability of microfinance institutions to “harness economies of scale in order to lower transaction costs and cut rates of their own accord.”\textsuperscript{92} Second, capping interest rates may decrease the incentive for new companies to enter the market, therefore reducing competition.\textsuperscript{93}

Should capping interest rates lead to lower loan availability, it is worth considering whether this could have unintended negative consequences. For example, insofar as capping interest rates decreases the amount of capital that microfinance firms are willing to lend, the poor could be forced to rely more on village loan sharks.\textsuperscript{94} Notwithstanding that microfinance has made significant inroads into rural areas of developing countries, village money lenders still

\begin{footnotesize}
\textsuperscript{87} See Bajaj, supra note 36. The Economist, while rejecting “wrongheaded” interest rate caps, has endorsed a host of “[s]ensible regulation[s],” including setting up a credit bureau and permitting microfinance institutions to take deposits. See The Economist, Leave Well Alone, supra note 18.
\textsuperscript{88} See The Economist, Leave Well Alone, supra note 18.
\textsuperscript{89} Id. As discussed earlier, although the 97\% repayment rate would suggest these investments are not very risky, the extension of microloans is labor and time intensive. See note 34, supra and related text.
\textsuperscript{90} See All Things Considered, supra note 17 (discussing SKS Microfinance’s $357 million IPO).
\textsuperscript{91} See The Economist, Leave Well Alone, supra note 18.
\textsuperscript{92} Id.
\textsuperscript{93} Id.
\textsuperscript{94} On the other hand, one could argue that lowering the interest rates for microfinance firms would widen the gap with the larger interest rates charged by village loan sharks, therefore reducing the latter’s attractiveness. However, this assumes that loan sharks have such high structural costs that they cannot lower their own interest rates in response to these competitive pressures.
\end{footnotesize}
“provide the bulk of rural credit.”95 In fact, in the rural areas of Andhra Pradesh itself, only 11% of households held loans from microfinance institutions, but an astonishing 82% held informal loans.96 Is this the result that policymakers wish to achieve, the empowerment of loan sharks?

In conclusion, these policymakers should be wary of hurting the very consumers they are ostensibly trying to protect, for many of these policies have ambiguous welfare benefits.97 For example, “most substantive regulations of consumer lending, such as usury laws or property exemptions, are likely to increase the cost and/or reduce the availability of credit.”98 Such regulations can slow the expansion of consumer finance, as illustrated by the Indian banks that have turned off the lending spigot due to fear of rising defaults.99 Should the solution be to put loans out of reach of nano-entrepreneurs? Is there another way to empower nano-entrepreneurs, while preserving the microfinance industry?

V. Solution: Bolster the Consumer Bankruptcy System

As Indian policymakers consider how to address the costs and negative externalities associated with expanding consumer finance, particularly the plague of over-indebtedness, they would do well to consider strengthening the consumer bankruptcy regime.100 Doing so would likely help provide more stable growth in consumer finance by increasing the predictability of debt collection. However, if this were true, why has consumer bankruptcy reform been largely absent from the debate over how to respond to the microfinance scandals? Would the legal machinery of bankruptcy be accessible to farmers and small businessmen? Is bankruptcy so
absent from the cultural discourse in India that small farmers and businessmen would not take advantage of it even if it were accessible? Would bankruptcy carry the same shame load that caused farmers to commit suicide?

This Part explores the current consumer bankruptcy laws on the books in India, draws comparisons to U.S. consumer bankruptcy laws, and considers what aspects of India’s consumer bankruptcy laws hinder its accessibility. This Part goes on to explore whether this regime works in practice, finding that there are a number of cultural, administrative, and economic obstacles to making consumer bankruptcy in India accessible on a larger scale. This Part concludes by advocating for the strengthening of India’s consumer bankruptcy system 1) to address the costs associated with expanding consumer finance in India, and 2) to help save the microfinance industry by correcting the imbalance of power between debtor and creditor which, in turn, would remove the impetus for misguided populist laws aimed at protecting the poor.

**A. How Effective Is India’s Current Consumer Bankruptcy System?**

This section starts by comparing the consumer bankruptcy laws in the United States and in India as it relates to property exemptions and relief of debt. Then this section focuses on a few provisions of India’s insolvency system that discourage consumers and small businessmen from seeking bankruptcy protection. Finally, this section discusses other psychological and cultural factors that may limit its accessibility. Indian policymakers ought to remove these barriers where possible.
1. Current Laws on the Books

India has a consumer bankruptcy regime that is approximately 100 years old, dating back to British colonial rule,\(^{101}\) and India has not significantly altered this regime since its adoption.\(^{102}\) Two separate statutes provide the formal sources for India’s consumer insolvency regime: the Presidency Towns Insolvency Act and the Provincial Insolvency Act.\(^{103}\)

i. Property Exemptions

As a general matter, under the U.S. bankruptcy code, the general rule is that property exempted by the debtor is not liable during or after the case for any pre-petition debt or any debt deemed to have arisen before bankruptcy.\(^{104}\) There are two main policy considerations at play.\(^{105}\) First, because everyone needs certain basic things to live day-to-day, society should not deprive debtors of such items, considering basic notions of fairness.\(^{106}\) Second, there is a third-party interest and a public interest in letting debtors obtain a fresh start, and in not letting debtors become completely destitute.\(^{107}\)

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\(^{101}\) See Feibelman, India, supra note 24, at 106. Many developing countries do not have any provisions for consumer bankruptcy. See Rafael Efrat, Global Trends in Personal Bankruptcy, 76 AM. BANKR. L.J. 81 (2002) (discussing how many nations, including China, Vietnam, Mongolia, Hungary, Bulgaria, the Ukraine, Brazil, Mexico, Argentina, and Venezuela, do not allow debt forgiveness for consumers).

\(^{102}\) See Feibelman, India, supra note 24, at 107.

\(^{103}\) Id. (noting that these two Acts are largely equivalent in substance).

\(^{104}\) See 11 U.S.C.A. § 522(c) (West 2004).


\(^{107}\) See Rafael Efrat, The Moral Appeal of Personal Bankruptcy, 20 WHITTIER L. REV. 141, 141 (1998) (“The fresh start principle generally takes the form of forgiving the debtor part or all of the debts she incurred prior to her bankruptcy filing.”); Katherine Porter & Deborah Thorne, The Failure of Bankruptcy's Fresh Start, 92 CORNELL L. REV. 67, 68 (2006). The fresh start principle has deep roots in American jurisprudence. In 1934, the United States Supreme Court stated that bankruptcy “gives to the honest but unfortunate debtor who surrenders for distribution the property which he owns at the time of bankruptcy, a new opportunity in life and a clear field for future effort, unhampered by the pressure and discouragement of preexisting debt.” Local Loan Co. v. Hunt, 292 U.S. 244 (1934).
Under the Indian insolvency acts, some property is exempt from recovery by creditors.¹⁰⁸ These exemptions generally incorporate those available under the Code of Civil Procedure.¹⁰⁹ Specifically, section 60 of the latter provides that the following property is liable to attachment and sale in execution of decree: lands, houses or other buildings.¹¹⁰ However, this section goes on to list the property exemptions, providing that the following particulars shall not be liable to such attachment or sale:¹¹¹

(a) the necessary wearing-apparel, cooking vessels, beds and bedding of the judgment debtor, his wife and children, and such personal ornaments as, in accordance with religious usage, cannot be parted with by any woman;
(b) tools of artisans, and, where the judgment-debtor is an agriculturist, his implements of husbandry and such cattle and seed-grain as may, in the opinion of the court, be necessary to enable him to earn his livelihood as such, and such portion of agricultural produce or of any class of agricultural produce as may have been declared to be free from liability under the provisions of the next following section;
(c) houses and other buildings (with the materials and the sites thereof and the land immediately appurtenant thereto and necessary for their enjoyment) belonging to [an agriculturist or a labourer or a domestic servant] and occupied by him;

The U.S. bankruptcy code mirrors the Indian insolvency act in certain respects. Specifically, it provides that the following property of the debtor are exempt from recovery: (1) homestead used as a residence; (2) one motor vehicle; (3) household goods, crops, animals; (4) jewelry; (5) tools of the trade; etc.¹¹² Notably, there is often a dollar limitation attached to these exemptions.¹¹³ For example, in the United States, the federal homestead exemption covers the debtor's aggregate interest up to approximately $20,200.¹¹⁴ However, it is important to note that federal bankruptcy law permits states to opt-out of the federal exemptions and provide their

¹⁰⁸ See Feibelman, India, supra note 24, at 109.
¹¹⁰ Id. at ¶ 60.
¹¹¹ Id.
¹¹³ Id.
¹¹⁴ Id.
own. At least 35 states have done so, and a number of these states provide much more generous homestead exemptions.

Why do individual Americans tend to file for bankruptcy? Available data suggests that most consumers in this country are likely to become insolvent or experience financial distress because they experience unexpected exogenous shocks, such as involuntary unemployment or sickness. Moreover, the data indicates that many middle-class debtors are homeowners that use bankruptcy to attempt to hang on to their homes. This indicates that in America, the homestead property exemption is a major incentive to file for bankruptcy; indeed, a more generous property exemption may even encourage entrepreneurial activity.

Why doesn’t the Indian homestead exemption provide the same kind of incentive to file for bankruptcy that the American homestead exemption does? It seems that the Indian insolvency scheme also provides a kind of homestead exemption, as it exempts the houses and related land of agriculturists, laborers and domestic servants. However, for the large proportion of Indian debtors that are not homeowners, this homestead exemption would not incentivize filing for bankruptcy. Perhaps this insight helps to explain why Indians do not tend to take advantage of their bankruptcy system.

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115 Id.
116 See Hynes, supra note 105 (“Twenty-two states have exemptions that would allow them to exempt at least [fifty thousand dollars].”).
117 See Feibelman, India, supra note 24, at 79.
119 See Wei Fan & Michelle J. White, Personal Bankruptcy and the Level of Entrepreneurial Activity, 46 J.L. & Econ. 543, 543-44 (2003) (arguing that higher levels of homestead exemption encourages entrepreneurial activity by providing “wealth insurance” that reduces risk for small business owners).
ii. Discharge of Debts

India’s consumer bankruptcy law provides for the discharge of debts in some circumstances. However, in a variety of circumstances discharge is not available. Although some of these conditions for discharge are relatively objective, others are more subjective. The latter permits a judge to exercise considerable discretion, and courts have the power to grant a conditional discharge. Moreover, a number of debts are non-dischargeable, including debts to the government and debts involving fraud.

Under the U.S. bankruptcy code, creditors may make two types of challenges to discharge. First, they may object to discharge of particular debts under §523. These include, among others, taxes, debts obtained by fraud, family support, student loans, and condominium fees. Second, creditors may object to the discharge of all debts under §727. These include the transfer of property with intent to hinder, delay, or defraud creditors; destruction or concealment of books or records; perjury, bribery, extortion, and other fraudulent acts; etc.

It appears that the provisions in the Indian insolvency act for the discharge of debts are relatively similar to those in the U.S. bankruptcy code. Both have a mix of objective and subjective conditions for discharge that require an inquiry into the debtor’s frame of mind. Although this taxes judicial resources, the U.S. consumer bankruptcy system is widely used by

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120 See Feibelman, India, supra note 24, at 110 (“Where the debtor’s assets cannot satisfy his or her obligations, the debtor can apply for a discharge of the remaining obligations.”).
121 Id. at 111.
122 Id. (“For example, a debtor will not receive a discharge if the presiding court determines that the debtor ‘has brought on or contributed to his insolvency by rash or hazardous speculations or by unjustifiable extravagance in living or by gambling, or by culpable neglect of his business affairs.’”).
123 Id.
124 Id.
126 Id.
128 Id.
debtors, while it seems that the Indian system is not. Therefore, there must be other factors that account for the inaccessibility of the Indian consumer bankruptcy system.

2. In Practice

Although there appears to be practically no data on how the Indian insolvency system functions,129 some evidence suggests that few Indians take advantage of it.130 If true, this would be somewhat surprising because—on paper, at least—India’s insolvency system provides a significant measure of protection and debt relief to consumer debtors.131

This scant available evidence is derived from published appellate court decisions, which offer an interesting window into the operation of India’s insolvency system.132 For example, in a case arising from the state of Andhra Pradesh, Mohammed Abbas AH v. Masood Bin Mohammed Al-Khaili, the high court requested his clerks to report on the number of pending insolvency petitions.133 These clerks reported a total of 6,113 petitions pending in Andhra Pradesh, out of a population of 75.7 million in 2001.134 Six thousand insolvency petitions is a small number per capita, especially considering that about a million households file for bankruptcy each year in the United States135 out of a population of approximately 310 million. In other words, there are approximately 323 bankruptcy filings a year per 100,000 citizens in the United States, but only approximately 8 bankruptcy filings a year per 100,000 citizens in the state of Andhra Pradesh, a fortyfold difference.

129 See Feibelman, India, supra note 24, at 111 (“[It is] extremely difficult to discern even the most general aspects of the operation of this scheme. There are no available data about insolvency cases in India— for example, no state-wide or country-wide data exists concerning how many cases are filed.”).
130 Id. at 114. However, Professor Feibelman stated in an interview that based on his travels to rural India, he came away with an impression that there is a functional system, but it functions very slowly. These are things that we tend to think of as defects, but that does not mean the system is dysfunctional. There are a lot of cases that get decided, and many disputes are resolved.
131 Id.
132 Id.
133 Id. (citing Mohammed Abbas Ali v. Masood Bin Mohammed Al-Khaili and Anr., 2007 A.L.D. 1 (A.P.) 60).
134 Id.
135 See Warren, Debtors, supra note 118, at 113.
3. Why Do So Few Indians Take Advantage of Bankruptcy Protection?

Why do so few Indians take advantage of the bankruptcy provisions on the books? It seems that there are at least three categories of explanation: financial barriers to the poor, a perception that the system is ineffective, and cultural stigmas associated with bankruptcy. Analyzing what hurdles currently exist to making the Indian consumer bankruptcy system more accessible will help shape the discussion of what set of reforms are appropriate.

As an initial matter, the effectiveness of the current bankruptcy system is not simply a product of the number of Indians that file for bankruptcy. For a consumer bankruptcy regime to be effective, “it should be viable enough to influence consumer financial transactions ex ante and to affect the relationships between creditors and debtors ex post, especially their motivations to renegotiate.” Likewise, it is often said that negotiations between creditor and debtor take place “in the shadow of bankruptcy.” Is the consumer bankruptcy regime sufficiently accessible and effective to shape the negotiating leverage between debtors and creditors? Even if Indians do not tend to take advantage of the consumer bankruptcy system in large numbers, it may still be useful to have it there in the background. Failing to take the ex ante effect of bankruptcy into account could understate the benefits it affords to consumers through enhanced leverage in negotiations with creditors, even if they do not end up filing for bankruptcy. That being said, it is

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136 In general, because there is so little data available, the author must resort to some degree of speculation. But cf Feibelman, India, supra note 24, at 113 (“In fact, there are reasons to believe that the role of consumer insolvency in India's society and economy is underestimated. Based on an informal review of the few dozen reported consumer insolvency-related opinions from the last decade available in Manupatra, a commercial legal database, it appears that a surprising number of consumer insolvency petitions are filed each year in India.”), 114 (“[Certain data] suggests that a non-trivial number of individuals-- debtors as well as creditors--view it to be in their interest to employ the regime. It may also reveal that the existing legal regime plays a more significant role in Indian society than is currently understood.”).

137 Id. at 116.
not at all clear whether the current regime is effective enough to impact the motivations of creditors to renegotiate ex ante.\textsuperscript{138}

\textit{i. Financial Barriers to the Poor}

There is reason to believe that consumer bankruptcy will hardly ever be a viable option for the poor.\textsuperscript{139} For example, the process of filing for bankruptcy may be prohibitively expensive in India, when you factor in the prospect of hiring an attorney, the cost of traveling, etc.\textsuperscript{140} Moreover, the same set of reasons that makes the rural poor—in India or elsewhere—less likely to take advantage of formal commercial systems, instead relying on customary ways of conducting business, would presumably apply to the reluctance of rural Indians to take advantage of the formal bankruptcy system.\textsuperscript{141}

\textsuperscript{138} Id.
\textsuperscript{139} For arguments about how bankruptcy fees discourage bankruptcy filing in the United States, see generally Rafael Efrat, \textit{The Disadvantaged in Bankruptcy}, 19 \textit{Bank. Dev. J.} 71, 74 (2002) (suggesting that filing costs, coupled with the expense of hiring an attorney, may disproportionately discourage disadvantaged groups from filing bankruptcy); Richard E. Flints, \textit{Bankruptcy Policy: Toward a Moral Justification for Financial Rehabilitation of the Consumer Debtor}, 48 \textit{Wash. & Lee L. Rev.} 15 (1991); Nathaniel C. Nichols, \textit{The Poor Need Not Apply: Moralistic Barriers to Bankruptcy's Fresh Start}, 25 \textit{Rutgers L.J.} 329 (1994); Otis B. Grant, \textit{Are the Indigent Too Poor for Bankruptcy? A Critical Legal Interpretation of the Theory of Fresh Start Within a Law and Economics Paradigm}, 33 \textit{U. Tol. L. Rev.} 773, 782-84 (2002). However, there are a lot of rules that are essentially debt relief, but do not require someone to file for bankruptcy—for example, generous property exemptions.
\textsuperscript{140} In the United States, although hiring an attorney is generally a good idea, the bankruptcy code permits \textit{pro se} filings in certain circumstances. See \textit{Bankruptcy Abuse Prevention and Consumer Protection Act of 2005}, S. 256, 109th Cong. § 418 (2005)
\textsuperscript{141} See Dickerson, \textit{Informal-Sector Entrepreneur}, supra note 27, at 208 (“At a 35,000 foot level, Sub-Saharan countries' basic legal regimes applicable to commercial transactions are of a dual nature. For the foreigners and the elites, there is a version of a transplanted European system; and for the poor--but also for the elites when they wish to avail themselves of it--there is a quasi-traditional system. Inevitably, considerable hybridization occurs, and the boundary between the two principal regimes is blurry.”), 220 (arguing that formal bankruptcy laws are not likely to help nano-entrepreneurs in the short term); Claire Moore Dickerson, \textit{The Cameroonian Experience Under OHADA: Business Organizations in a Developing Economy}, 112 \textit{Bus. & Soc'y Rev.} 191, 201 (2007) (noting that small businesses in OHADA countries tend to make decisions based on local norms rather than OHADA legal rules); Claire Moore Dickerson, \textit{Harmonizing Business Laws in Africa: OHADA Calls the Tune}, 44 \textit{Colum. J. Transnat'l L.} 17 (2005) (arguing for increased use of general economic cooperative initiatives in Africa). Additional research would be useful in determining whether rural Indians tend to take advantage of formal system regarding enforcing contracts.
**ii. Perception that the System is Ineffective**

Another reason why so few Indians take advantage of consumer bankruptcy could be that the system does not work very efficiently, indicating to consumers that the costs outweigh the benefits.\(^{142}\) A good place to start is looking at the practical effects of discharge in India.\(^{143}\) In the United States, one of the biggest negative consequences of filing for bankruptcy is the hit that is made to a debtor’s credit rating, which lasts for a number of years.\(^{144}\) With regard to India, “[i]t is not clear if individuals who receive a discharge can effectively obtain credit thereafter” because there is no available data.\(^{145}\)

Moreover, the glacial pace of the judicial system may discourage consumers from filing from bankruptcy.\(^{146}\) Since insolvency cases move very slowly through the judicial system, debtors may believe that it is not worth their time, money, and effort to file for bankruptcy to protect their assets.\(^{147}\) If these cases are filed, and the debtor dutifully waits as the case slowly unfolds, the debtor is still not home free because the substantive provisions of India’s consumer bankruptcy law often afford great discretion to judges, making “judicial outcomes . . . unpredictable.”\(^{148}\)

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\(^{142}\) See Feibelman, India, supra note 24, at 112 (“In fact, there are reasons to doubt that many debtors are inclined to utilize the regime or that they have reason to believe that it would be useful to do so. The consequences of being deemed an insolvent can be severe while the regime's potential benefits to debtors and creditors appear uncertain and may be slight in many instances.”).

\(^{143}\) For starters, under both systems, there are restrictions and/or prohibitions on multiple filings.

\(^{144}\) See generally, Katherine Porter, Life After Debt: Understanding the Credit Restraint of Bankruptcy Debtors, 18 AM. BANKR. INST. L. REV. 1 (2010).

\(^{145}\) See Feibelman, India, supra note 24, at 111. Although there may not be a formal credit rating system in rural India, there may be an informal one—for example, village money lenders certainly remember who failed to repay a debt.

\(^{146}\) Id. at 113. For example, if it is generally known that court cases take years to work their way through the system, individuals may come to the conclusion that it is not worth their time to file for bankruptcy. However, as Professor Feibelman notes, “there are some indications that cases filed recently may be more likely to be resolved quicker than older cases, sometimes within a year or two.” Id. at 113-14.

\(^{147}\) Id. at 112.

\(^{148}\) Id.
In what circumstances do Indians tend to brave these obstacles and file for bankruptcy? There is some indication that voluntary petitions are often filed in India “to protect the debtor from incarceration or otherwise aggressive debt collection.” This indicates that many Indians only file for bankruptcy when their physical security is put at risk.

### iii. Cultural Norms

Another factor might be cultural norms; there might be a stigma associated with filing for bankruptcy. In Indian culture there is a deep shame associated with failing to pay one’s debts, which is compounded by the intense peer pressure associated with the lending practices of microfinance firms. This phenomenon is illustrated by the wave of farmer suicides that have swept across rural India. It is possible that the deep shame associated with failing to pay debts in Indian culture is equivalent to the shame associated with becoming a bankrupt. Assuming that some degree of stigma exists in Indian culture regarding filing for bankruptcy, this stigma might prevent debtors from taking advantage of bankruptcy protections, even if it were in their

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149 Id. at 113.
150 Indeed, Professor Claire Moore Dickerson has noted that one major function of insolvency law is to provide physical security for the businessman’s person and property. See Dickerson, Informal-Sector Entrepreneur, supra note 27, at 189.
151 As Professor Rafael Efrat notes, “[s]tigma is the social devaluation of a person who is deviant from or contrary to a social unit's norm.” Rafael Efrat, Bankruptcy Stigma: Plausible Causes for Shifting Norms, 22 EMORY BANKR. DEV. J. 481, 483 (2006) [hereinafter, “Efrat, Bankruptcy Stigma”].
152 See note 56, supra and related text.
153 In the United States, there has been considerable debate about the extent that such a stigma has evolved over the years. See e.g., Rafael Efrat, The Evolution of Bankruptcy Stigma, 7 THEOR. INQ. L. 365 (2006) (attempting to measure stigma by studying references to bankrupts in media portrayals, and finding insufficient evidence to conclude that changes in the perception of stigma is directed related to increased bankruptcy filings); Efrat, Bankruptcy Stigma, supra note 151, at 485 (discussing the decreasing social stigma of consumer bankruptcy and the shift away from the “traditional” view that disparages debtors as financially irresponsible); Elizabeth Warren, & Jay Lawrence Westbrook, Less Stigma or More Financial Distress: An Empirical Analysis of the Extraordinary Increase in Bankruptcy Filings, 59 STAN. L. REV. 213, 218 (2006) (observing that rising levels of debt is associated with financial distress); Gordon Bermal, What's Stigma Got to Do with It?, 22 AM. BANKR. INST. J. 22 (2003) (reviewing studies trying to connect increased individual bankruptcy filings with the decline in shame and stigma, and questioning the soundness of using certain proxies making this connection); 151 Cong. Rec. S2421 (daily ed. Mar. 10, 2005) (statement of Sen. Durbin) (“People I have known who have gone through bankruptcy are not proudly announcing to their friends: Well, I had a great day in bankruptcy court. These are people who are a little embarrassed, a little ashamed of what they had to go through.”).
economic interests to do so. In other words, is the shame associated with bankruptcy so great that it would negate the effectiveness of any reforms designed to make the consumer bankruptcy system more accessible?

Nevertheless, it is likely that cultural attitudes about debt and bankruptcy are not uniform throughout India, for it is a nation of 1.18 billion people, five major religions, and over a dozen languages.\textsuperscript{154} Even assuming that many subsets of Indian society have cultural beliefs that stigmatize debt and/or bankruptcy, these beliefs may not be uniform, so meaningful bankruptcy reforms could potentially be effective for a large minority of the country—for example, those located in urban areas.

\textbf{B. Specific Proposals for Strengthening Consumer Bankruptcy}

The form that proposals for strengthening consumer bankruptcy take is dependent on an assessment of the effectiveness of the current regime. Generally speaking, there may be economic, psychological, and cultural explanations for why Indians tend not to take advantage of the bankruptcy system. These barriers to greater accessibility of the consumer bankruptcy system could be addressed with properly targeted reforms.

Professor Feibelman has offered a set of general proposals for strengthening the consumer bankruptcy regime in India.\textsuperscript{155} First, Indian policymakers could adopt procedural reforms that would make it easier for consumers to file for bankruptcy, and therefore make an impact on the negotiating leverage of creditors and debtors.\textsuperscript{156} In particular, they could improve

\begin{footnotesize}
\begin{enumerate}
\item See Feibelman, India, supra note 24, at 115-21. “Assuming that India’s consumer insolvency regime is operational yet dysfunctional in many crucial respects, it is entirely possible that the regime could be markedly improved with carefully designed reforms. This Part does not argue that Indian policymakers should adopt any particular reform. Rather, it assumes that the role of consumer insolvency law in India can be enhanced, and it discusses some general approaches to reforming the regime that might help achieve this result.” Id. at 116.
\item Id. at 118.
\end{enumerate}
\end{footnotesize}
the administration of consumer bankruptcy cases by addressing the components of the current regime that tend to make the process slow and relatively unpredictable; for example, a number of rules could be reformed to reign in judicial discretion.\textsuperscript{157} Indeed, professor Claire Moore Dickerson has observed that it is especially dangerous to grant judges wide discretion to apply legal standards in certain circumstances in developing countries—for example, when “judges are venal or incompetent, or that they have been merely co-opted by the government through blackmail by starvation.”\textsuperscript{158} Therefore, improving the speed and predictability of India’s consumer bankruptcy regime might make it more appealing to creditors and debtors.\textsuperscript{159} Second, Indian policymakers could adopt substantive reforms that expand the availability of debt relief.\textsuperscript{160}

\textbf{C. Benefits of Strengthening Consumer Bankruptcy}

Strengthening the consumer bankruptcy system in India is promising for a variety of reasons. First, it may facilitate a more stable consumer finance market. Second, it is a good way to address the costs associated with expanding consumer finance. Third, it may help to save the microfinance industry in India by addressing the core grievances of the revolt against it—namely, an imbalance of power that exists between debtor and creditor—while removing the impetus for misguided populist laws aimed at protecting the poor.

\textsuperscript{157} \textit{Id.} at 116-17. Rules that enable judicial discretion could be replaced with rules that apply automatically, thus demanding less judicial energy. \textit{Id.} at 16. For example, the rule that requires courts to determine whether a debtor is insolvent could be replaced with a presumption of insolvency. \textit{Id.} at 116-17. Such reforms “would be consistent with some broad trends in consumer insolvency and bankruptcy regimes across the globe in recent decades.” \textit{Id.} at 117. \textsuperscript{158} Claire Moore Dickerson, Sex and Capital: What They Tell Us About Ourselves, 79 St. JOHN’S L. REV. 1161, 1175 (2005) (corporate governance context). \textsuperscript{159} See Feibelman, India, \textit{supra} note 24, at 116. A more ambitious approach may include adopting a separate tribunal for consumer bankruptcy cases. \textit{Id.} For a comparison to the approach taken in other countries to streamline their consumer bankruptcy system, see Jason J. Kilborn, Out with the New, In with the Old: As Sweden Aggressively Streamlines Its Consumer Bankruptcy System, Have U.S. Reformers Fallen Off the Learning Curve?, 80 AM. BANKR. L.J. 435 (2006). \textsuperscript{160} See Feibelman, India, \textit{supra} note 24, at 116, 119-21. “Expanding the availability of substantive protections and the scope of potential discharge of debts might also increase the beneficial impact of insolvency law on economic growth and development in India.” \textit{Id.} at 119.
1. Facilitates a More Stable Consumer Finance System

Consumer bankruptcy law can benefit both debtors and creditors in a way that facilitates financial transactions. As to the former, bankruptcy regimes provide a way for insolvent debtors to seek an orderly restructuring of his obligations, permitting the debtor a “fresh start” after his non-exempt assets are distributed. As to the latter, bankruptcy regimes solve the collective action problem that would exist in the absence of a bankruptcy mechanism, which harms creditors for at least two reasons. First, it can make the collection from insolvent debtors unpredictable. Second, in certain circumstances, it can reduce the creditor’s overall recovery—for example, when another creditor seizes the debtor’s valuable assets first.

Moreover, having a robust system in place for discharging debts is superior to the kind of ad hoc rebellions against paying debts that are more likely to occur when there is little meaningful avenue for formal debt relief. In Andhra Pradesh, a series of scandals with the microfinance industry triggered a rebellion against paying debts, causing the repayment rate to plummet from over 95% to 15%. As a result, the microfinance industry was pushed to the brink of collapse, and its future prospects are uncertain.

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161 Id. at 105.
162 Id.
163 Id.
164 Id.
165 Id.
166 Although the boycotts that erupted in Andhra Pradesh against microfinance were not entirely spontaneous—at some point as the protests gained momentum politicians and activists seemed to have taken the reins—for the purposes of this discussion they should nonetheless be considered “ad hoc,” in the sense that the people’s anger coalesced rapidly into action, which the elites did not see coming. One could compare the uprisings in Egypt to oust former President Mubarak and how the Muslim brotherhood joined the movement as its momentum gained popular strength.
167 See Buncombe, supra note 12; The Economist, Under Water, supra note 1.
168 See Polgreen et al., supra note 13.
It seems reasonable to speculate that the absence of any meaningful avenue of legal debt relief played some role in exacerbating the scope of this crisis.\footnote{Although this is a reasonable assumption, it is impossible to conclude with any certainty that, had the consumer bankruptcy regime been more widely accessible, these ad hoc rebellions would not have occurred.} The existing regime, where formal debt relief was out of reach for the ordinary Indian in Andhra Pradesh, became viewed as intolerable when various industry abuses came to light.\footnote{Id.} In other words, the status quo lost its legitimacy.\footnote{To be sure, one may question whether this is nothing more than throwing a bone to the public. But any law that lacks legitimacy with the people rests on shaky foundations. In this light, it is entirely appropriate to take steps to address popular grievances in a way that promotes long-term growth.}

Arguably, the long-term interests of the microfinance industry would be served by allowing a more predictable method of discharging debts. To some extent, this ad hoc rebellion is akin to a massive discharge all at once. A formal structure for discharging debts would benefit the banks over the long-term because it would be more predictable, and small losses in small amounts could be more easily absorbed than one big shock.\footnote{This assumes that the microfinance firms will permanently give up trying to collect the micro-loan debts. In fact, this assumption is bolstered by the text of Andhra Pradesh’s law that places new restrictions on microfinance, and applies retroactively. For example, it provides “No [microfinance institution] shall recover from the borrower towards interest in respect of any loans advanced by it, whether before or after commencement of this Ordinance, an amount in excess of the principal amount.” Andhra Pradesh Micro Finance Institutions (Regulation of Money Lending) Act, 2011, http://indiamicrofinance.com/wp-content/uploads/2010/10/Andhra-MFI-Ordinance.pdf. Therefore, microfinance companies are permanently enjoined from collecting their loans at least in excess of this specified amount.}

2. \textit{Addresses the Costs Associated with Expanding Consumer Finance}

Until recently, the elites’ perception of the costs associated with expanding consumer finance to poor people in developing countries have been largely drowned out by a pro-microfinance ideology in media, political, and philanthropic circles.\footnote{See note 63, supra and related text. For a discussion of the lack of media coverage and public interest in the disclosure of corporate human rights abuses, see Dickerson, Ozymandias, supra note 56, at 1065.} Research indicates that microfinance does a lot of good, but its overall benefits are more modest than is widely
believed—it is far from a magic bullet, but it does work “for some people some of the time.”174 The costs associated with expanding consumer finance, long ignored, are now in the spotlight, and the close scrutiny it is receiving could instigate an overreaction.

Importantly, the expansion of consumer credit could generate costs and negative externalities for society.175 First, consumers may borrow more than they can afford in view of their projected incomes due to a variety of reasons:176 they may be overly optimistic about their expected incomes, they may be uninformed about business risks, or they may lack the discipline necessary to turn their start-up business into a thriving enterprise.177 Second, the recent wave of suicides in India illustrates the psychological dimension to financial distress.178 Although some of those struggling with indebtedness have taken the final plunge, many more endure under crushing debt, which carries its own set of societal costs.

As the costs of expanding consumer finance have been ignored, so have the inadequacies of the consumer bankruptcy system. Professor Feibelman has speculated that the dearth of secondary literature on consumer insolvency in India, either by academics or by the various national reports, “creates a strong impression that commentators, scholars, and policymakers in India do not believe that the regime is a significant aspect of Indian society or of its economy.”179

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174 See The Economist, Under Water, supra note 1; Subir Roy, Lessons for Micro-Finance from 2010, Business Standard, Jan. 5, 2011, 2011 WLNR 161959 (“[I]t should be clear to all that micro-finance on its own cannot remove poverty. It can at best make a dent in income poverty. A setback, be it a flood or drought or illness, can and does take a family back to destitution.”).
175 See Feibelman, Consumer Bankruptcy, supra note 27, at 79. Other types of costs associated with expanding consumption are an increased likelihood of harmful inflation and an erosion of the domestic savings rate. Id.
176 Other factors may include imperfect knowledge and pure luck.
177 Id. Or the community in which they start a business may not be able to support it, if there isn’t enough cash flow/liquidity.
178 Id. at 80.
179 See Feibelman, India, supra note 24, at 112.
Bankruptcy’s role in facilitating development has not only been ignored in India; in fact, it has received scarce attention in the global debates over development policy.\textsuperscript{180} This is curious, considering that a general consensus exists that corporate bankruptcy law serves to facilitate sustainable economic growth.\textsuperscript{181} Downplaying the importance of consumer bankruptcy in this way is misplaced because a consumer bankruptcy system that allows for meaningful debt relief “can be an effective tool for reducing the social costs of consumer finance.”\textsuperscript{182}

In other words, it is at least arguable that consumer bankruptcy can provide a safety valve to financial distress.\textsuperscript{183} First, bankruptcy protection encourages its citizens to become entrepreneurs and to engage in risk taking by cushioning the impact when they fail.\textsuperscript{184} Second, bankruptcy provides a way to handle financial problems in an organized way, adding an element of stability to the country’s economic structure.\textsuperscript{185}

Insofar as Indian legislators are concerned with the psychological distress associated with over-indebtedness, “[a]llowing debtors to discharge at least some obligations effectively insures them from some of the effects of financial distress.”\textsuperscript{186} What’s more, the availability of bankruptcy protection may ease some of the worries of those that do not actually file for bankruptcy. Such individuals know that bankruptcy protection is an option, and as a result, they may suffer less of an emotional toll from their financial troubles.

\textsuperscript{180} See Feibelman, Consumer Bankruptcy, supra note 27, at 89.
\textsuperscript{181} Id.
\textsuperscript{182} Id. at 91.
\textsuperscript{184} Id. at 5.
\textsuperscript{185} Id.
\textsuperscript{186} See Feibelman, Consumer Bankruptcy, supra note 27, at 92.
If expanding access to the consumer bankruptcy system were proven to promote economic growth, one might expect that a global consensus would emerge around this policy.\footnote{If expanding access to the consumer bankruptcy system were proven to promote economic growth, one might expect that a global consensus would emerge around this policy.} Specifically, it would be reasonable to expect developing economies to incorporate a robust consumer bankruptcy regime into their overall development strategy.\footnote{Specifically, it would be reasonable to expect developing economies to incorporate a robust consumer bankruptcy regime into their overall development strategy.} However, the recent trends tell a different story.\footnote{However, the recent trends tell a different story.}

It seems that Indian policymakers have been hesitant to modernize their consumer bankruptcy regime, even though providing meaningful debt relief could carry many potential benefits.\footnote{It seems that Indian policymakers have been hesitant to modernize their consumer bankruptcy regime, even though providing meaningful debt relief could carry many potential benefits.} India is not alone in its reluctance to increase the accessibility of consumer bankruptcy, for some of the largest and most rapidly developing countries have outdated consumer bankruptcy regimes.\footnote{India is not alone in its reluctance to increase the accessibility of consumer bankruptcy, for some of the largest and most rapidly developing countries have outdated consumer bankruptcy regimes.} What does this suggest about how policymakers in these countries view consumer bankruptcy?

A probable explanation is policymakers’ concern that a “bankruptcy regime with debt relief would harm nascent credit markets more than help them.”\footnote{A probable explanation is policymakers’ concern that a “bankruptcy regime with debt relief would harm nascent credit markets more than help them.”} Indeed, expanding access to consumer bankruptcy may have some negative consequences. First, it could encourage poor consumers to borrow even more than they are currently, due to the insurance function of debt relief, which diminishes some of the risks of borrowing.\footnote{First, it could encourage poor consumers to borrow even more than they are currently, due to the insurance function of debt relief, which diminishes some of the risks of borrowing.} If creditors believe that borrowers will become more unwilling to repay debts subject to discharge, they may refuse to lend to such
borrowers.\textsuperscript{194} As a result, credit could be reduced overall or at least to some borrowers. Second, it will presumably lead to somewhat higher interest rates.\textsuperscript{195} Third, leading policymakers may be subject to the influence of the elites, including the credit interests. It is unlikely that consumer advocates have enough power to counterbalance these powerful interest groups.\textsuperscript{196} Even if an organized constituency existed to promote consumer interests, there may simply be a lack of social demand for these reforms.\textsuperscript{197}

Finally, there may be a lack of resources to expand access to consumer bankruptcy. In particular, the judicial or administrative infrastructure necessary to carry out these reforms may not currently exist, and their creation may cost a significant amount of money.\textsuperscript{198} For example, it may take significant resources to expand the judiciary’s capacity to take more consumer bankruptcy cases. To the extent these costs are borne at the state level, it may be even more difficult to find these scarce resources.

\textbf{3. Helps To Save the Microfinance Industry in India}

Strengthening the consumer bankruptcy laws may help to save the microfinance industry in India by addressing the very problems that led to the debt rebellion. First, it may serve to correct the imbalance of power that exists between debtor and creditor. Second, it would presumably remove the impetus for misguided populist laws aimed at protecting the poor.

\textsuperscript{194} Id. at 69.  
\textsuperscript{195} Id. at 92. But cf id. at 93-94. (“Even if such relief reduces creditors' insolvency-state returns from debtors who experience financial distress, however, it might improve their credit-granting decisions ex ante, reducing defaults and over-indebtedness in the first place. Exposing creditors to the possibility of discharge of obligations owed to them may give creditors additional incentives to gather reliable aggregate and borrower-specific information bearing on the probability of default. Lower-risk borrowers would in turn have incentives to provide information indicating that their actual risk profile justifies credit.”).  
\textsuperscript{196} Id. at 70.  
\textsuperscript{197} Id. (“Consumers and households are unlikely to clamor successfully for effective bankruptcy laws in the absence of widespread over-indebtedness.”).  
\textsuperscript{198} Id.
i. Corrects an Imbalance of Power Between Debtors and Creditors

The outrage directed towards the microfinance industry took many forms, including charges that it was profiting on the backs of the poor, engaging in abusive practices, etc.\textsuperscript{199} The core of these grievances against the microfinance industry dealt with the imbalance of power that exists between debtor and creditor. Interestingly, one commentator, while criticizing the Andhra Pradesh law, suggested that a better solution would be to enhance the “collective safety net for the poor.”\textsuperscript{200} Indeed, one way to bolster the social safety net in India would be to strengthen the consumer bankruptcy laws.

Reforming the consumer bankruptcy regime could serve to address the core grievances against the microfinance industry by correcting the imbalance of power that exists between lender and borrower. In comparison to countries with robust consumer bankruptcy systems, Indian debtors appear to have less leverage in his dealings with creditors. For example, insofar as there is a widespread view that the bankruptcy system is not a serious option, the threat of filing for bankruptcy probably cannot compel the creditor to renegotiate the debt burden. Therefore, such reforms would have to be strong enough to lend credibility to a debtor’s threat of filing for bankruptcy—for example, by streamlining the consumer bankruptcy process.\textsuperscript{201} Otherwise, debtors in India may always lack the leverage to force renegotiations with his creditor, and future tragedy will be assured.

Reform of India’s consumer bankruptcy system could help shift public attitudes towards viewing the consumer bankruptcy system as part of the social safety net, while reducing the stigma associated with the bankruptcy system. For example, there is some indication that debtors

\textsuperscript{199} See Polgreen et al., supra note 13.
\textsuperscript{200} See Jagannathan, supra note 18.
\textsuperscript{201} See, e.g., Kilborn, supra note 105.
view consumer bankruptcy as “a form of punishment or purely a debt-collection tool.”

However, there is an alternative way to view consumer bankruptcy protection—it can also be viewed as a populist tool, and instituting these reforms could help debtors see that consumer bankruptcy is in their interests. In the United States, it seems that consumer bankruptcy is viewed as an integral part of the social safety net. While consumer finance has expanded rapidly, its costs have been often ignored, and many unfortunate people have fallen through the gap in India’s social safety net—that is, its lack of a robust consumer bankruptcy system.

It seems that societal upset over these costs have come to a boil after so many years, until finally the top has blown off the microfinance industry, threatening its future. Ideally, consumer finance and consumer bankruptcy should work in harmony to ensure sustainable growth, but achieving this equilibrium requires tempering the costs associated with expanding consumer finance. Moreover, strengthening the consumer bankruptcy system could also address another apparent inequity in the system—the asymmetry between consumers and businesses. Specifically, it appears unjust to have a system where bankruptcy is available to businesses, and even to banks no less, but not to poor consumer borrowers.

**ii. Remove Impetus for Bad Populist Laws Aimed at Protecting the Poor**

Strengthening the consumer bankruptcy system may also remove the impetus for misguided laws, such as capping interest rates, which would only serve to harm the very debtors they are meant to protect. For example, consumers may be forced to rely more on village loan

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202 See Feibelman, India, [supra](#) note 24, at 118 (suggesting that eliminating involuntary petitions could shift this viewpoint).
203 [Id.](#)
204 See note 107, [supra](#) and related text (discussion the policy rationales of consumer bankruptcy).
205 See notes 179-80, [supra](#) and related text.
206 See notes 88-96, [supra](#) and related text.
sharks who abuse their position of power.\textsuperscript{207} These laws would also harm the future of the microfinance industry in India by, among other things, slicing the latter’s profit margins and reducing competition.\textsuperscript{208} Insofar as the core grievances of the debt rebellions have stemmed from an imbalance of power between debtor and creditor, this concern could be addressed through reforming the consumer bankruptcy regime.\textsuperscript{209} In other words, if policymakers address some of the underlying inequities in the system—specifically the imbalance of power between creditor and debtor—the need to promulgate laws restricting the business practices of microfinance firms will be greatly reduced.\textsuperscript{210}

Finally, it is possible that increasing the accessibility of consumer bankruptcy could, over time, influence cultural attitudes towards debt in a way that would make these tragic farmer suicides less likely.\textsuperscript{211} Microfinance companies have become successful by exploiting the shame that rural Indians feel towards debt. Although this makes for a very efficient business model, it also comes with significant social costs.\textsuperscript{212} It is possible that if the consumer bankruptcy system were reformed in a way to make it more accessible, the stigma associated with filing for bankruptcy could be reduced over time. For example, policymakers could invest in financial education that paints debt relief in a positive light.\textsuperscript{213}

To be sure, it is unlikely that policymakers could significantly alter deeply rooted cultural norms disfavoring debt relief, but perhaps they could reduce enough resistance to make enhanced

\textsuperscript{207} See note 94, supra and related text.
\textsuperscript{208} See note 93, supra and related text.
\textsuperscript{209} See notes 199-205, supra and related text.
\textsuperscript{210} To be sure, it appears that strengthening the consumer bankruptcy system would not directly address the goals of microfinance: funneling money to the poor, alleviating poverty, etc. However, the social safety net function of consumer bankruptcy would help address the costs associated with expanding consumer finance markets.
\textsuperscript{211} See Feibelman, Consumer Bankruptcy, supra note 27, at 103. Changing policies could serve to “increase the social demand for or reduce the social resistance to consumer bankruptcy law.” Id.
\textsuperscript{212} See note 84, supra and related text.
\textsuperscript{213} See Feibelman, Consumer Bankruptcy, supra note 27, at 103. India is more fortunate than some developing countries in that it has a longstanding bankruptcy system. This makes it easier to “identify[] familiar forms of debt relief and build[] a bankruptcy regime upon those indigenous institutions.” Id.
consumer bankruptcy protections worthwhile.\textsuperscript{214} Moreover, the recent debt rebellions provide some evidence that the social demand for debt relief in India is fluid—that is, the rise of overindebtedness makes citizens and policymakers more open to expanding consumer bankruptcy protections.\textsuperscript{215} Before the populist revolts, there was a seemingly entrenched cultural belief regarding the shamefulness of failing to repay debts.\textsuperscript{216} It seems that these revolts changed attitudes overnight, for repayments levels plummeted from over 95\% to 15\%.\textsuperscript{217} At a minimum, the people no longer felt ashamed to repay these particular debts. Perhaps the reason is that the community pressure was reversed—whereas before the revolts the pressure was strongly in favor of paying one’s debts to the microfinance companies, after the revolts the pressure was strongly against paying these debts. It seems that community anger rooted in a sense of injustice was sufficient to change the context around cultural attitudes.

In addition, perhaps consumer bankruptcy reforms could have a feedback effect to cultural attitudes towards failing to pay debts in general, reducing the deep shame level that such a failure generates. In other words, codifying into law the notion that it is normatively acceptable to discharge your debts could have the effect of reducing the shame regarding debts that is widespread in Indian culture.

\textbf{VI. Conclusion}

Expanding consumer bankruptcy protections in India is an idea whose time has come. The recent rebellion against microfinance in Andhra Pradesh is troubling because microfinance, though imperfect, is an essential means of lifting the rural poor out of poverty. The root of the

\textsuperscript{214} Id.
\textsuperscript{215} Id. “This may help explain why recent reforms and adoptions have tended to occur in countries that have experienced such problems.” Id.
\textsuperscript{216} See note 13, supra and related text.
\textsuperscript{217} See note 66, supra and related text.
people’s grievances against the microfinance industry is broader than particular examples of abusive lending practices; its core is a sense of injustice over an imbalance of power that exists between lender and borrower. Strengthening the consumer bankruptcy system in India is an excellent way to address these grievances, while at the same time fostering stable development of the consumer finance system.

The success of consumer bankruptcy reform could depend on whether it rides the sort of populist wave illustrated by the debt rebellions. If the consumer bankruptcy reforms could be framed in a way that captures populist, anti-bank sentiment, then it could perhaps move the commonly held beliefs that stigmatize debt relief in bankruptcy. For example, to the extent a farmer unable to pay his debts believes “there’s no way out for me,” then could this belief be mollified through a more liberalized consumer bankruptcy regime, which could show this farmer “a way out.” More importantly, perhaps, the elites must be persuaded that it is in the country’s best interests to strengthen the consumer bankruptcy system. This article has aimed to do just that—convince academics and policymakers to take up the cause of consumer bankruptcy reform.