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Insolvency Professionals and the Code of Conduct

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“Where your talent and the needs of the world cross, there lies your purpose.”

Aristotle

In today's world, the success or failure of any activity depends upon the kind of professionals involved. The professionals are persons having domain knowledge and experience. In the era of super speciality, their role has become more significant. There are as many professions as the numbers of activities or services. No individual, institution or industry works without professionals. Professionals, by and large, are associated with trade and business of every sector. They are responsible for a higher rating of any institution or industry or establishment. In other words, professionals lay down the benchmark for their quality, efficiency and good governance. In business, failures are due to managing the business in an unprofessional manner or not engaging the right professionals or intentionally not following the advice of the professional. Obviously, this results into the state of insolvency.

Since ancient times, though professionals are revered, the credibility of any individual has been measured across all civilisations in terms of the state of solvency. It has been seen that an undischarged insolvent is disqualified to occupy public offices under various laws. Thus, society and the system of governance do not take the state of insolvency in a good taste. Further, the state of insolvency is not limited to individuals but extends to the universe of corporate persons having limited liability. The business plans of corporates, as per the usual market practice, are incomplete without debt component. Large number of corporate debtors are defaulters and account for huge non-performing assets thereby adversely affecting the economic growth of the country. The findings of the World Bank in its Report (2014), especially with regard to time taken in recovery of debts and rate of recovery, have been matters of grave concern for the ease of doing business. To address these issues and other related issues, the Insolvency and Bankruptcy Code, 2016 (the Code) has been enacted which contemplates special class of Insolvency Professionals (IPs) from various streams of professions.

LEGAL FRAMEWORK

The legal framework for insolvency and bankruptcy prior to the enactment of the Code was inadequate and ineffective. There have been undue delays in resolution of issues despite special laws being in place for the recovery actions by creditors, for example, in case of corporates, the Recovery of Debts Due to Banks and Financial Institution Act, 1993, the Securitisation and Reconstruction of Financial Assets and Enforcement of Securities Interests Act, 2002, the Sick Industrial Companies (Special Provisions) Act, 1985 and the winding up

provisions under the Companies Act, 2013, and also the non-statutory corporate debt restructuring mechanism, such as Strategic Debt Restructuring (SDR), Corporate Debt Restructuring (CDR) and Joint Lenders Forum, while in case of individuals, the Presidential Towns Insolvency Act, 1909 and the Provincial Insolvency Act, 1920 had been enacted.

A new legislation was required to deal effectively with insolvency and bankruptcy and as also for development of credit markets in the country and improving ease of doing business to facilitate investments. The Bankruptcy Law Reforms Committee (BLRC) was constituted under Chairmanship of Dr. T. K. Vishwanathan with a mandate to suggest comprehensive reforms covering all aspects of insolvency and bankruptcy of both corporates and individuals. Based on its recommendations, the Code was enacted on May 28, 2016, to consolidate and amend the laws relating to reorganisation and insolvency resolution of corporate persons, partnership firms and individuals in a time-bound manner for maximisation of value of assets of such persons, to promote entrepreneurship, availability of credit and balance the interests of all the stakeholders. It came into force on December 1, 2016. It has paved the way for much needed effective reforms while focussing on creditor driven insolvency resolution.

The Code envisages a sound insolvency regime with a paradigm shift in jurisprudence of procedure for insolvency resolution under the Code, *i.e.*, from a debtor-in-control regime to creditor-in-control regime, for timely revival of the business of the debtor companies and limited liability partnerships as well as for individuals and unlimited liability partnership. The Code also envisages a shift from profit maximisation to value maximisation of the firms. In this context, it is relevant to refer the observations of former Governor of the Reserve Bank of India, Mr. Raghuram G. Rajan :

‘The shift to firm value maximisation is not just good for the society (in that a value enhancing investment takes place regardless of how the fruits are shared), it is good for employees (since their wages go up) and even it is good for shareholders.’¹

He further observed:

‘The firm value maximising management will continue to take hard decisions, a necessity, if the firm is to stay competitive and survive.....Tough decisions will continue to enhance productive efficiency, a key contribution of private corporations.’²

The Code lays down effective ecosystem for implementation of the provisions of the Code which consists of four pillars, *viz.*, the Adjudicating Authorities (the National Company Law Tribunals and Debts Recovery Tribunals), IPs and Information Utilities (IUs), Insolvency Professional Agencies (IPAs) and the Insolvency and Bankruptcy Board of India (IBBI) to exercise regulatory oversight over IP agencies, IPs and IU.

The Code provides for a time bound institutionalised process for resolution of insolvency to be completed within 180 days after admission of the application.³ In case of corporate insolvency resolution process (CIRP), the period is extendable by another 90 days and maximum period to be 330 days⁴ (inclusive of the litigation time) as also provisions for fast-track resolution of corporate insolvency within 90 days extendable by 45 days.⁵ The financial

¹ Raghuram G. Rajan, (2017). The Third Pillar. p.376.

² *Id.* at p. 377.

³ Sections 12 and 101 of the Code

⁴ Proviso to section 12.

⁵ Section 56.

creditor or operational creditor or corporate debtor (CD) can trigger the process for resolution of corporate insolvency even after first default by the corporate debtor. The Insolvency resolution professional is appointed by the Adjudicating Authority (AA) to conduct the entire process, manage the operations of the CD⁶ as also to facilitate the committee of creditors (CoC) in taking prudent decisions for resolution of insolvency. At every stage, flexibility in the process, such as withdrawal of the CIRP application⁷ by the applicant or resolution to liquidate by CoC⁸ at any time after the initiation of the CIRP gives an added opportunity to revisit their decisions. In case of individuals, the Code envisages two distinct processes, namely, Fresh Start and insolvency resolution process. The failure of the resolution process of the CD resulting in liquidation facilitates ease of exit and failure of the resolution process of individual debtor leads to bankruptcy. Further, declaration of moratorium from the date of admission of the application till the completion of the insolvency resolution process (the calm period) facilitates the resolution professional, the CoC and other stakeholders to effectively resolve the insolvency of the CD or of the individual. In the case of individual insolvency proceedings, there is also a provision for interim- moratorium. The waterfall mechanism under sections 53 and 178 of the Code clearly spells out significantly the paradigm shift in the order of priority in distribution of liquidation proceeds in case of liquidation and priority of payment of debts in case of bankruptcy, however, insolvency process cost or liquidation process cost to be the first priority.

THE ROLE OF INSOLVENCY PROFESSIONALS

An important component of the ecosystem is the IP who has been entrusted with a wide range of functions so as to effectively strive to maximise the value of assets of debtor during the resolution process. As the processes underlined in the Code, viz., CIRP or withdrawal of the CIRP or liquidation process is largely executed through IPs. He is the backbone of all such processes and success thereof hinges on the conduct and competence of the IP. He is the fulcrum of the process and link between the AA and CoC as also other stakeholders. As on August 31, 2019, there are 2734 IPs registered with the IBBI.

Under the scheme of the Code, an IP is a professional enrolled under section 206 of the Code with an IPA as its professional member and registered with the Board as an IP under section 207 after qualifying Limited Insolvency Examination. The Code provides for a two-tier regulatory regime for the professionals, the IBBI and the IPA which is regulated by the IBBI. The IPAs are mandated to promote the professional development⁹ and first-tier regulation of IPs and as also to promote good professional and ethical conduct among them. The IPA grants membership to persons who qualify Limited Insolvency Examination and complete pre-registration educational course, lays down standards of professional conduct for its members, is empowered to issue certificate of authorisation for assignments¹⁰ (such certificate to be effective after December 2019) and may suspend or cancel the membership of IPs on certain grounds as provided in the bye-laws. The IPs giving consent for the assignments and against

⁶ Section 23.

⁷ Section 12A.

⁸ Section 33(2).

⁹ Section 200.

¹⁰ IBBI (Insolvency Professional Agencies) Regulations, 2016.

whom no disciplinary proceedings are pending are on the panel of IPs recommended by IBBI which saves judicial time.

Pre-Registration Conduct

The regulations, in addition to the requirement of qualifying Limited Insolvency Examination and requisite experience of the relevant profession in terms of regulation 5 of the Insolvency and Bankruptcy Board of India (Insolvency Professionals) Regulations, 2016 and completion of pre-registration educational course for the purpose of registration with the Board, also provide that the applicant needs to be a fit and proper person and no disciplinary proceedings are pending against him for the purpose of registration with the Board. This ensures that a person with clean hands can enter this profession to manage the operation of the business of CD and conduct the insolvency resolution process.

In the matter of rejection of application for registration by the Board in XXX case on the ground that the applicant is not a fit and proper person as criminal proceedings were pending against him, the Court of the Special Judge, Central Bureau of Investigation, Greater Mumbai observed:

'What is material is that what others feel about the applicant who has been charge sheeted for offences such as criminal conspiracy, cheating
Does such a person inspire confidence of the stakeholders who can entrust him with property of lakhs of crores for management under corporate insolvency resolution process? Pendency of serious criminal proceedings against the applicant adversely impacts his reputation and makes him not a person fit and proper to become an IP.'

The IP may be appointed by the AA as an interim resolution professional, the resolution professional or liquidator or bankruptcy trustee. The BLRC in its final report, emphasised the role of an IP as follows:

'The Insolvency Professionals form a crucial pillar upon which rests the effective, timely functioning as well as credibility of the entire edifice of the insolvency and bankruptcy resolution process. ... In administering the resolution outcomes, the role of the IP encompasses a wide range of functions, which include adhering to procedure of the law, as well as accounting and finance related functions. The latter include the identification of the assets and liabilities of the defaulting debtor, its management during the insolvency proceedings if it is an enterprise, preparation of the resolution proposal, implementation of the solution for individual resolution, the construction, negotiation and mediation of deals as well as distribution of the realisation proceeds under bankruptcy resolution. In performing these tasks, an IP acts as an agent of the adjudicator. In a way the adjudicator depends on the specialized skills and expertise of the IPs to carry out these tasks in an efficient and professional manner.....This creates Role of Resolution Professionals in CIRP the positive externality of better utilisation of judicial time.'

It further states:

'The IP makes sure that assets are not stolen from the company and initiates a careful check of the transactions of the company for the last two years, to look for illegal diversion of assets. Such diversion of assets would induce criminal charges...
These IPs will be delegated the task of monitoring and managing matters of business by the Adjudicator, so that both creditors and the debtor can take comfort that economic value is not eroded by actions taken by the other.'

The UNCITRAL Legislative Guide on Insolvency Law spells out the role of an 'insolvency representative' as follows:

'[T]he insolvency representative plays a central role in the effective and efficient implementation of an insolvency law, with certain powers over debtors and their assets and a duty to protect those assets and their value, as well as the interests of creditors and employees, and to ensure that the law is applied effectively and impartially. Accordingly, it is essential that the insolvency representative be appropriately qualified and possess the knowledge, experience and personal qualities that will ensure not only the effective and efficient conduct of the proceedings and but also that there is confidence in the insolvency regime.'

The International Monetary Fund described the role of a liquidator and the administrator in effective implementation of the law as follows:

'As court-appointed officials, they have an obligation to ensure that the law is applied effectively and impartially. Moreover, since they normally have the most information regarding the circumstances of the debtor, they are in the best position to make informed decisions.'

The Code casts various duties upon the IP or resolution professional, viz., to make public announcement for inviting claims, receive and collate claims, take immediate custody and control of all the assets of the CD, preserving and protecting the assets of the CD, manage affairs of the CD including the continued business operations of the CD, to appoint authorised representative, if required, to give instructions to financial institutions, constitute CoC within 30 days of his appointment, to convene and conduct the meetings of the CD, raise interim finance, represent and act on behalf of the CD with third parties, prepare an information memorandum, appoint valuers, invite prospective resolution applicants to put forth their resolution plan and to take all such steps as may be required for an on-going concern.¹¹ However, the professional is required to seek approval of the CoC for certain acts, such as, to raise interim finance beyond certain limit, to change the capital structure of the CD, to create security interest over the assets of the CD, to make any change in the management of the CD and its subsidiary, etc.¹²

The role of an IP becomes very crucial and important in view of the provisions of section 20 of the Code. Its sub-section (1) provides that the interim resolution professional shall make every endeavour to protect and preserve the value of the property of the CD and manage the operations of the CD as a going concern. Further clause (d) of its sub-section (2) empowers the IP to issue instructions to personnel of the CD as may be necessary for keeping it as a going concern. Section 25 of the Code also casts similar duty on the resolution professional. The biggest challenge before the resolution professional or the liquidator is examination of the affairs of the CD and to identify who have contributed to its insolvency as also to examine whether there has been any preferential transactions or undervalued transaction or fraudulent transaction or extortionate transactions and, if so, to take action for avoidance of such transactions in accordance with the provisions of the Code.¹³ He shall comply with the provisions of the Code regulations made thereunder as also terms and conditions specified in the bye-laws of the IPAs of which he is a professional member and take reasonable care and

¹¹ Section 25

¹² Section 28.

¹³ Sections 43-51.

diligence while performing the duties.¹⁴

In this context, words of wisdom of *karma* in Fourth Chapter of the *Geeta* appears to be relevant for professionals:

**कर्मण्यकर्म यः पश्येदकर्मणि च कर्म यः।
स बुद्धिमान् मनुष्येषु स युक्तः कृत्स्नकर्मकृत्॥4.18॥**

It means he who sees inaction in action and action in inaction, he among men is intelligent. He is a perfect actor-doer of all *karmas*. This equally applies to IP while performing his duties under the Code and regulations.

CODE OF CONDUCT

A Code of conduct is generally derived from Codes of ethics. These ethical norms are benchmark of right actions at a given point of time which the society or the system expects from an individual and are responsible for evolution of the mankind and strengthening the legal system. All the religious scriptures prescribe a code of conduct for the followers. Ancient society in India was governed by the principles of Dharma which may mean, though not exactly, righteousness and subjected the king and the subject alike to the rule of law to ensure well-being of all, not only of human beings but the entire environment. These principles are found in teachings of *Bhagavad Geeta*, Old Testament, edicts of Buddha and Ashoka, etc. In addition to the ethical norms propounded by saints and sages in various religious scriptures, eminent scholars and statesmen also spelt out ethical norms in their principles and practices, e.g., Mahatma Gandhi gave new dimension to the national struggle based on truth, and non-violence and expressed in relation to *Ahimsa* as:

'vaishnav janto te kahiye jo peer parai jane re'

Jeremy Bentham, the great reformer, based the premise of principle of utility on the ethics of 'greatest happiness of the greatest number'.

The Indian Constitution also provides code of conduct for its citizens under Article 51A as 'Fundamental Duties' which forms the foundation of human dignity and national character. Further, the principles of natural justice are in the nature of code of conduct for every judicial and quasi-judicial authority. In *Tulsiram Patel v. Union of India*¹⁵, the Supreme Court held that the term natural justice means certain rules of conduct supposed so just that they are binding upon all mankind and observed:

'The principles of natural justice constitute the basic elements of fair hearing, having their roots in the innate sense of man for fair play and justice which is not the preserve of any particular race or country but is shared in common by all men.'

At present there is a code of conduct for every professional, be it Advocates, Chartered Accountants, Company Secretaries, IP, valuers, engineers, doctors, *vaidya*, government officers/ employees, etc. A professional is known by the practices he professes and code of conduct he adheres to.

¹⁴ Section 208

¹⁵ AIR 1985 SC 1416.

Post Registration Conduct

As far as the IPs are concerned, the code of conduct has been codified in writing and enforced with penalties in various countries. The code of ethics aims to help IPs or practitioners meet their professional obligations. In the United Kingdom (UK), the Code of Ethics for insolvency practitioners' details how the code should be applied in specific circumstances. It lays down five fundamental principles which guide how IPs should act in the course of their work: (i) the IPs should be straightforward and honest in all professional relationships(Integrity); IPs should not allow any bias or conflict of interest to cloud their decisions(Objectivity); IPs have a duty to maintain professional knowledge and skill based on the latest developments in practice, legislation and techniques (Professional competence and due care); IPs should respect the confidentiality of the information acquired as a result of professional and business relationships and not disclose such information to third parties (Confidentiality) and IPs should comply with relevant laws and regulations and conduct themselves with courtesy and consideration when performing their work (Professional behaviour).

The IBBI has notified the Insolvency and Bankruptcy Board of India (IPs) Regulations,2016 (Regulations). Regulation 7(2) of these Regulations provide for five primary commandments of conduct after registration with the Board. It provides that the registration of an IP is subject to the conditions that the IP shall (a) at all times abide by the Code, rules, regulations, and guidelines thereunder and the bye-laws of the IP agency with which he is enrolled; (b) at all times continue to satisfy the requirements under Regulation 4; (c) undergo continuing professional education, as may be required by the Board; (d) not outsource any of his duties and responsibilities under the Code, except those specifically permitted by the Board and abide by the Code of Conduct specified in the First Schedule to Regulations.

The First Schedule to the said Regulations provides detailed Code of Conduct for IPs which is briefly summarised as under:

Integrity and objectivity

- An IP must maintain integrity and act with objectivity in his professional dealings without any bias, conflict of interest, coercion, or undue influence of any party and not acquire assets of the debtor.

Independence

- An IP must maintain complete independence in his professional relationships and should conduct the insolvency resolution, liquidation or bankruptcy process, as the case may be, independent of external influences.
- He or his relative must not accept gifts or hospitality nor offer gifts or hospitality nor a financial or any other advantage to a public servant or any other person, which undermines or affects his independence as an IP.
- An IP must not engage in any employment when he holds a valid authorisation for assignment or when he is undertaking an assignment.
- An IP shall not engage or appoint any of his relatives or related parties, for or in connection with any work relating to any of his assignment until a period of one year has elapsed from the date of his cessation from such process.

Confidentiality

- An IP must ensure that confidentiality of the information relating to the insolvency resolution process.

Disclosure obligations

- An IP shall disclose the existence of any pecuniary or personal relationship with any of the stakeholders entitled to distribution under sections 53 or 178 of the Code, and the concerned corporate person/ debtor by making a declaration of the same to the applicant or committee of creditors.
- An IP must not conceal any material information or knowingly make a misleading statement to IBBI, the AA or any stakeholder, as applicable.
- An IP shall disclose the fee payable to him, the fee payable to the IP Entity, and the fee payable to professionals engaged by him to the IPA of which he is a professional member.
- An IP shall disclose all costs towards the insolvency resolution process costs, liquidation costs, or costs of the bankruptcy process, as applicable, must endeavour to ensure that such costs are not unreasonable.

Professional behaviour

- An IP must adhere to the time limits prescribed in the Code and the rules, regulations and guidelines thereunder for insolvency resolution, liquidation or bankruptcy process, as the case may.
- An IP must provide all information and records as may be required by the Board or the IPA with which he is enrolled and must co-operate and be available for inspections and investigations carried out by the Board or such IP agency.
- An IP must ensure that he maintains written contemporaneous records for any decision taken, the reasons for taking the decision, and the information and evidence in support of such decision.
- An IP must not conduct business which in the opinion of the Board is inconsistent with the reputation of the profession or brings disrepute to the profession.
- An IP must provide services for remuneration which is a reasonable reflection of the work necessarily and properly undertaken.

In addition to the above Code of Conduct, the Bye-laws of IPAs made in accordance with the IBBI (Model Bye-Laws and Governing Board of Insolvency Professional Agencies) Regulations, 2016, *inter alia*, provide that in the performance of his functions, a professional member shall discharge his functions with utmost integrity and objectivity; and be independent and impartial with the highest standards of professional competence and professional ethics, and perform duties subject to the timelines under the Code; maintain confidentiality of information obtained in the course of his professional activities unless required to disclose such information by law.

Orders

In view of the key role of the IP during CIRP and liquidation process, any non-cooperation by the personnel of the CD with the IP delays the time bound process. In the matter of Shivam

Water Treaters Pvt. Ltd., CD was not cooperating with the RP and not handing over the possession of the property to her. The NCLAT vide its order dated February 18, 2019 held that RP is discharging her duties as Court Officer and any non-compliance of the Court Officer will be deemed as Contempt of Court. However, any non-compliance of the provisions of the Code or regulations made thereunder or violation of the Code of Conduct on the part of IP affects the process and in some of the cases, disciplinary action has been taken by the IBBI against IPs. The Disciplinary Committee of IBBI, vide its Order dated November 12, 2018, observed as follows:

'An IRP or RP is appointed by the AA. He is an officer of the Court. He is duty bound to (i) conduct CIRP with fairness and diligence, (ii) confirm that the resolution plan does not contravene any of the provisions of the law for the time being in force, (iii) maintain absolute independence in discharge of his statutory duties, and (iv) assist the AA with the correct perspective of the law, including provisions of section 29A of the Code. The AA relies on the work of an IP, as an insolvency proceeding is mostly not adversarial in nature.'

In various cases, the AA has made remarks against IP for his failure to perform duties under the Code. In *Ankit Kumar v. Advance Power infra Tech Limited*,¹⁶ the AA vide its order dated May 6, 2019 observed:

'whether the corporate Debtor has undertaken fraudulent trading within the meaning of section 66 of the Code also not explored by the Resolution Professional in the case in hand. Though he has observed that there are certain preferential transactions carried on by the CD, no application also seems to have been filed u/s 44,45 & 46 of the Code by him.'

Due to these issues, AA did not appoint RP as liquidator in the said case.

Similarly, in *Tirupati Jute industries Limited*,¹⁷ the AA vide its order dated February 13, 2019, observed that RP did not give correct advise when he submitted K. L. Jute's plan for approval of CoC and held that in such a situation it would not be proper to appoint the present RP as the Liquidator.

Further, in *Madhucon Projects Limited*,¹⁸ the AA vide its order dated November 22, 2017, in relation to the exorbitant fee quoted by an IP, observed:

'...the Adjudicating Authority is of the considered view that remuneration quoted by the IRP is quite exorbitant and the same needs to be referred to IBBI. Though there are no prescribed set of Rules and Regulations/Guidelines at present with regard to the fee payable to the IRP/RP, the Adjudicating Authority is of the considered view that the fee quoted by the professionals should be reasonable, commensurate with work to be handled. In view of the above we recommend the matter to IBBI for taking appropriate action/remedial measure against the proposed IRP including disciplinary action if any, as deemed fit.'

In *Hahnemann Housing and Development Private Limited*,¹⁹ the AA vide order dated October 29, 2018 observed that it is quite unfortunate to take note that the RP has not taken any earnest effort to see that the landed properties of the Corporate Debtor are identified and its valuation is fixed by appointing professionals from qualified surveyors or revenue authorities. In *Apna Scientific Supplies Pvt. Ltd.*²⁰ AA vide order dated March 14, 2019 observed that in spite of three

¹⁶ CA (IB) No.528/KB/2019 in CP (IB) No. 990/KB/2018

¹⁷ CP(IB) No. 508/KB/2018 along with CA (IB) Nos.972/KB/2018, 974/KB/2018, 1013/KB/2018, 08/KB/2019, 24/KB/2019 & 83/KB/2019

¹⁸ CP (IB) SR No. 4322/9/HDB/2017

¹⁹ C.P. (IB) No. 275/KB/2018

²⁰ MA/154/2019 in CP 811/IB/2018

directions, there is no compliance by the IRP. The IRP is flouting the orders of the Tribunal wilfully, intentionally and avoiding personal appearance.

Various orders of the AA indicate that non compliance of the provisions of the Code and regulations and as also directions given in their orders has led many a time to the replacement of professional during the CIRP or disciplinary action against such professionals.

The institution of IP stands on conduct and capability of the professionals. The capability needs to be enhanced continuously because of evolving legal and regulatory framework as also jurisprudence and evolution of best practices including use of technology. Every function which an IP is required to perform under the Code requires highest level of professional excellence including financial engineering and value maximising management. The objectives of the Code cannot be achieved unless the resolution professional strives for excellence and follows the Code of Conduct in various processes under the Code for establishing fairness in the conduct of the processes in order to inspire confidence among all the stakeholders.

To conclude, in the words of *Gurudev* Rabindranath Tagore:

*'You can't cross the sea merely by standing and staring at the water.'*²¹

²¹Sir Rabindranath Tagore, The Geetanjali.