

Address by Chairman, IBBI



Dr. M. S. Sahoo
Chairman
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Dr. M. S. Sahoo, Chairperson, Insolvency and Bankruptcy Board of India (IBBI), was invited to address the 14th meeting of the Governing Board of the Indian Institute of Insolvency Professionals of ICAI (IIPI) on May 26, 2020. In his address, Dr. Sahoo shared his views on evolving ecosystem of insolvency and bankruptcy profession in the country and expectations of the regulator from Insolvency Professional Agencies (IPAs) and Insolvency Professionals (IPs) to ensure a world class robust resolution regime in India.

In continuation of his address, we also have views of CA. Atul Kumar Gupta, President, the Institute of Chartered Accountants of India (ICAI) and Dr. Ashok Haldia, Chairman, IIPI. Read on to know more...

IPAs in the Governance Hierarchy¹

I thank Mr. Ashok Haldia, Chairman, IIPI for giving me this opportunity to talk to you, a distinguished set of individuals. You are the who's who of the corporate and financial world and the IIPI is privileged to have you on its Board.

It was on 1st October, 2016 that IBBI was set up with a mandate to commence the corporate insolvency proceedings by 1st December, in just sixty days, by which it had to create the entire ecosystem comprising Insolvency Professionals Agencies (IPAs), Insolvency Professionals (IPs), rules and regulations for processes, and so on. This mandate could not have materialised if the Institute of Chartered Accountants of India had not promoted IIPI to join the insolvency ecosystem in November, 2016. I must congratulate you for the IIPI achieving a leadership position in terms of membership of about two third of IPs, with commensurate number of Authorisation for Assignments (AFAs) and number of assignments by its members.

Good Governance

The concept of IPA is, in fact, a very novel one. I have not seen a similar organisation in the Indian context except that it is comparable with the stock exchanges, which act as frontline regulators for the stockbrokers and regulate markets under regulatory oversight of the Securities and Exchange Board of India (SEBI). The COVID-19 pandemic impacted everyone, including regulators. It, however, did not interrupt the trading operations of the stock exchanges which underscores the resilience of the systems in place with them. The stock exchanges are now the envy of the regulator. There is similar scope for IPAs like IIPI to take a centre stage and become an envy of the IBBI

1. Address by Dr. M. S. Sahoo, Chairperson, IBBI at 14th Meeting of the Governing Board of IIPI held on 26th May, 2020.

and I sincerely wish it happens during my tenure with the regulator.

An IPA has broadly two sets of interests. One is public interest, as enumerated in section 202 of the Insolvency and Bankruptcy Code, 2016 (Code), encompassing the interests of the debtors, creditors, other stakeholders, the market, and the society. An IPA also pursues private interest, as enumerated in section 204 of the Code, encompassing the top and bottom lines of the business, the interests of professional members, shareholders, and employees. A measure - commercial or regulatory - undertaken by an IPA may not always further both the interests simultaneously. Or, an IPA may adopt measures that give precedence to one interest over the other. A big dilemma before you is: how does IIIPI balance public interests and private interests. There is no magic formula to do so. We faced similar problems in the space of stock exchanges for decades. We addressed this by demutualisation of stock exchanges in 2005. However, we have started the IPAs on a much sounder footing. Section 203 of the Code provides for governance norms for IPAs. There is limited presence of IPs in the Governing Board which has 50% independent directors. The IPAs have in-built features of demutualisation which were brought in the stock exchanges after 150 years of existence. An IPA is better structured to balance private and public interests, provided this remains in top of your mind, while taking decisions for or on behalf of IIIPI.

An Instrumentality of State

Given the interests of an IPA, it is simultaneously 'State' and a market participant. It regulates and develops the insolvency profession and has several responsibilities under section 200 read with section 204 of the Code. Let's visualise the IPA in the governance hierarchy. Citizens are ultimate principals in parliamentary democracies. They delegate their authority to their representatives who form the Parliament.

The Parliament further delegates some of its authority to the Government which further delegates the same to the Ministers. The Government and Ministers delegate the implementation to the Bureaucracy. Thus, in a normal chain of delegation, there are four delegates, namely, the Parliament, the Government, the Ministers, and the Bureaucracy. The delegation to independent regulatory agencies is relatively a new concept in the Indian context, beginning in 1992, with the establishment of SEBI. We consider bodies like SEBI, IRDAI, ICAI, ICSI, etc. as regulatory state, being the fifth layer in the governance hierarchy². Further delegation to IPAs constitutes the sixth layer. As IBBI is bound by a principal-agent contractual framework to deliver on its mandate to the Government, so also is an IPA.

In the hierarchy of principals and agents, IPAs are closest to the market. Because of this proximity, they have a better understanding of the market than the Government or IBBI has. As agents of IBBI, and indirectly of the Government, IPAs regulate the conduct of their constituents. It is possible that there is some transmission loss in terms of objectives or focus from one layer to the other in the hierarchy. Appropriate design of contracts minimises the loss by holding an IPA accountable while incentivising it to promote the interests of the principal. It is also important to minimise the perceived conflict of interests between the commercial aspirations and regulatory tasks of an IPA.

There are a series of judgements³ where it has been held that the stock exchange is an instrumentality of State under Article 12 of the constitution and is amenable to writ jurisdiction under Article 226. Similarly, an IPA is an instrumentality of State and performs statutory public duty cast on it under a statute. As envisaged in the report of the Bankruptcy Law Reforms Committee (BLRC), an IPA is a

2. Fabrizio Gilardi and Dietmar Braun (2006), "Delegation in Contemporary Democracies", Volume 43, Routledge/ECPR Studies in European Political Science, Routledge.

3. Delhi Stock Exchange and Anr. Vs. K.C. Sharma and Ors., 2002, Delhi High Court.

mini State. It discharges three sets of functions, namely, quasi-legislative, executive, and quasi-judicial. The quasi-legislative functions cover making byelaws to lay down standards and code of conduct, which are binding on all its members. The executive functions include monitoring, inspection, and investigation of professional members on a regular basis, addressing grievances of aggrieved parties, gathering information about their performance, etc. with the overarching objective of preventing malicious behaviour and malfeasance conduct by IPs. The quasi-judicial functions include dealing with complaints against members and taking suitable disciplinary actions.

Generally, there is a broad separation of powers among the agencies associated with law - the legislature makes the law; the executive and the judiciary respectively administer and enforce it. This provides a system of checks and balances for one another to prevent misuse of power. The Hon'ble Supreme Court⁴ made an interesting observation in the context of SEBI's powers: *"Integration of power by vesting legislative, executive and judicial powers in the same body (SEBI), in future, may raise a several public law concerns as the principle of control of one body over the other was the central theme underlying the doctrine of separation of powers"*. Though the Constitution of India does not envisage strict separation of powers, it does indeed make horizontal division of powers among the legislature, the executive, and the judiciary. In keeping with the spirit of the constitutional provisions, every regulator must ensure that its three wings exercise quasi-legislative, executive and quasi-judicial powers with independence and without intra-institutional bargaining and, thereby, avoid potential public law concerns prognosticated by the Hon'ble Supreme Court. This requires the three wings to operate at arm's length distance from one another, a system of mutual checks and balances to prevent any excess. The IBBI has created three separate wings, in charge of three separate whole-time

members to ensure that the wings exercise quasi-legislative, executive, and quasi-judicial powers with independence. The IIPI should also strive towards having such checks and balances, if not done already.

A primary function of a state agency like IPA is to protect the interest of consumers or users. This is evident from the long titles of the modern legislations such the SEBI Act, IRDAI Act, the Competition Act. Section 204 of the Code enjoins upon the IPA to redress the grievances of the consumers against its members. There is a considerable scope and an urgent need for IIPI to improve its performance in this regard.

Inter-se Competition

Though an IPA is an agency of State, it is not a monopolist like IBBI, SEBI, Competition Commission of India, etc. Like stock exchanges, IPAs compete among themselves focussing their unique selling propositions. As a market player, an IPA is selling two products. One is its membership. It is important that such membership enjoys a brand equity and brand loyalty and commands a premium in the market. I am told, in the context of RVOs in the US, members of a Valuation Professional Organisation (VPO) command 40% higher remuneration than those of other VPOs. The second is professional development services provided by IPAs to their members.

The BLRC envisaged that IPAs would be competing among themselves. You need to fight fiercely with your competitors at marketplace. You need to have a competitive strategy such as Philip Kotler's five forces model⁵ or any other model that can drive your business. You need to understand rivalry within your industry. Rivalries naturally develop between players competing in the same market. I do not see this yet happening among IPAs. You also need to consider forces like pressure from substitute products, bargaining power of suppliers, bargaining power of buyers, threat of new

4. Clariant International & Anr. Vs. SEBI, 2004, Supreme Court.

5. Competitive Strategy: Techniques for Analyzing Industries and Competitors, Philip Kotler, 1980.

entrants, etc. There is no entry barrier today either by law or by market power. Traditional entry barriers like economies of scale, the amount of investment, switching cost, etc. do not exist in the IPA space except that an IPA has to be a section 8 (not for profit) company and this has limited the entry to some extent. In UK, the Recognised Professional Bodies (RPBs) regulate the insolvency practitioners. However, the Insolvency Service (Government Department dealing with Insolvency) is empowered by law to act as an RPB itself and compete with other RPBs. There is currently a proposal for the Insolvency Service to takeover this responsibility from RPBs. So, you need to remain relevant and add value for your continued existence. You need to ensure that you are indispensable, and no one can replace you. You need to perform and demonstrate performance quarter after quarter as a listed company does.

While competing among yourselves, as a front-line regulator, you should ensure that your members set high standards which in turn would earn the confidence and trust of stakeholders. The ultimate objective is that the market value that the IPs, who are members of IPA "X", are the best and the first choice of stakeholders for provision of services under the Code. Further, every profession - CA, CS, or Advocate - has a reputation. It takes considerable effort and time to build reputation. The society and stakeholders form a view about a profession in its initial years. That view does not change for long, even if the profession behaves differently. You must build and safeguard the reputation of the insolvency profession now to ensure it becomes the most enviable profession in the country. By building reputation of your members and creating a brand loyalty, you would be discharging an important statutory duty that you have under section 204 of the Code to safeguard the rights, privileges, and interest of your members.

Best Practices

I have spent a long time in the financial markets. The SEBI Act, 1992, Regulations made by SEBI and case laws taken together constitute about one third of the total law governing securities markets, while two third of the law comes from the custom or the best practices. For instance, debit and credit rule (in accountancy) does not flow from any law; it flows from the custom. Likewise, IPs face complicated situations, for which there is no solution in rule book. The solution emerges from practice. The law at times adopts the best practices. Most often such practices acquire the force of law and guide the practitioners. I urge you to take the lead in developing best practices for situations for which rule book has no solution.

COVID-19 Pandemic

Let me briefly touch upon COVID-19 pandemic. The authorities have been extremely proactive to make the Code accommodative to deal with insolvencies. The Government, vide notification dated 24th March, 2020, one day before the lockdown, increased the threshold amount of default required to initiate an insolvency proceeding under the Code from Rs.1 lakh to Rs.1 crore, with the intent to prevent MSMEs from being pushed into insolvency for their inability to meet their repayment obligations due to business disruptions. Based on the announcement of the Finance Minister on 17th May, 2020, the work is on to amend the Code to suspend initiation of insolvency proceedings against corporate debtors in respect of any default arising during the COVID-19 period. This will prevent corporate persons which are experiencing distress largely on account of unprecedented situation being pushed into insolvency proceedings when it is difficult to find adequate number of resolution applicants to rescue them.

The market protagonists believe that suspension of the Code would deprive ailing entities to

find a resolution or allow unviable companies to continue. Currently, every company is struggling for its own survival. Who can rescue another ailing company? If all these are pushed into insolvency, many of them may face liquidation for want of resolution applicants to rescue them. Rescuing lives of companies being the prime objective of the Code, it cannot be used to take away their lives prematurely.

Further, the insolvency framework typically aims to: (i) rescue a viable firm, and (ii) liquidate an unviable firm. In the present circumstances, there are two policy choices: If insolvency framework is suspended, unviable firms would not be liquidated; and if it is not suspended, viable firms would be liquidated. The first choice fails to liquidate an unviable firm, which can be rectified in the following quarter or year. The second choice liquidates a viable one forever, which cannot be undone. Rescuing a viable firm is, therefore, far more important than failing to liquidate an unviable one during the current crisis. Additionally, the second choice provides a breathing space, when many companies, which are failing solely on account of COVID-19, would bounce back on their own as soon as normalcy restores. Or, they would recalibrate their operations and businesses to an 'all-new normal'. They may even explore innovative workouts for resolutions outside the Code.

Also underway is a tailor-made package for resolution of MSMEs. This would enable MSMEs to resolve their own distress, if they wish, even in COVID-19 times. Government has decided to enlarge the scope of MSMEs. The enterprises having investment in Plant and Machinery or Equipment up to Rs.50 crore and turnover up to Rs.250 crore would be considered MSMEs. With this definition, about 60% of companies would fall in the ambit of MSME. As the story unfolds further, I am sure, Government would step in with further appropriate measures. I believe, the IPAs can play a significant role in these circumstances. While contributing to policy formulation, they

must prepare their members as care givers for the persons in distress.

I thank Chairman, IIIPI and distinguished directors of Governing Board for this opportunity and wish IIIPI all the best in its future endeavours.

Thank you

Excerpts from Speech by Dr. Ashok Haldia Chairman, IIIPI

I extend a warm welcome to Dr. M. S. Sahoo, Chairperson IBBI

It's a privilege to have you with us in the Board meeting of IIIPI. Although IBBI has been closely interacting with IIIPI and monitoring & supervising their operations, we thought to gain from your wisdom in the areas of (i) IIIPI's functioning, (ii) the direction in which the insolvency regime is moving particularly in the wake of Covid-pandemic, (iii) the impact of some provisions of IBC getting suspended, and (iv) the manner in which IIIPI could better respond to the members requirements and regulatory expectations.

I also take this opportunity to introduce you to our Board members. Though you need no introduction, may I mention your illustrious background in the banking and finance sector, particularly your distinguished stints at the Ministry of Finance followed by SEBI, Competition Commission of India and at the helm of ICSI. Your contribution to shaping up the insolvency regime in such a short time frame is unparalleled. Under your guidance IBC has evolved into one of the most important legislations for the world to see and appreciate.

IIIPI, apart from being a wholly owned subsidiary of ICAI, is the largest IPA with over 61% share of membership across IPAs. Moreover 60 to 70% of cases under CIRP and liquidation have been dealt with by the members of IIIPI. Given the volume IIIPI is looking after, we have tried our best to stand up to our reputation and meet the