

## Insolvency and Bankruptcy Board of India

7<sup>th</sup> Floor, Mayur Bhawan, Connaught Place, New Delhi-110001

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To

All Registered Insolvency Professionals

All Registered Insolvency Professional Agencies

All Recognised Insolvency Professional Entities

All Registered Valuers

(By mail to registered email addresses and on the website of IBBI).

### **Subject: Mistakes committed by insolvency professionals in conduct of corporate insolvency resolution process**

Dear Madam / Sir,

The Central Government has been steering deep economic reforms to make India a great place to do business. It swiftly established a modern insolvency regime to revive companies in stress and thereby promote competition and innovation at marketplace, and enhance entrepreneurship and credit availability in the economy.

2. The Insolvency and Bankruptcy Code, 2016 (Code) provides a market process, popularly known as called corporate insolvency resolution process (CIRP), for time bound revival of viable corporate debtors (CD) and closure of unviable ones. An insolvency professional (IP) is a key driver of CIRP - he acts as interim resolution professional (IRP) in the initial days of CIRP and then as resolution professional (RP) till its completion. He runs the operations of the CD as going concern and assists the stakeholders to find out the best resolution plan, while protecting and preserving the value of assets of the CD and ensuring compliance with all the applicable laws to the business of the CD and the CIRP. The law facilitates and empowers the IP to discharge his responsibilities effectively.

3. The IBBI and Insolvency Professional Agencies (IPAs) have come across some mistakes being committed by a some of the IPs in conduct of CIRPs. These mistakes are costs to the CD and the economy, and often amount to contravention of provisions of the law. Most of these are probably unintentional and can be avoided with a little more care and diligence. This communication lists out a few such mistakes with a hope that these will not be committed by any IP, pre-empting the IBBI/IPA to initiate any disciplinary action.

**(a) Assignment without having Authorisation:** Regulation 7A of the IBBI (Insolvency Professionals) Regulations, 2016 (IP Regulations) requires that an IP shall not accept or undertake any assignment, including CIRP, unless he holds an authorisation for assignment (AFA) on the date of such acceptance or commencement of such assignment, as the case may be. The bye-laws of the IPAs provide that, if the AFA is not issued, renewed or rejected by the IPA within 15 days of the date of receipt of application, the authorisation shall be deemed to have been issued or renewed, as the case may be, by the IPA. The IBBI has made available an IT facility for the IPs to apply for the issuance or renewal of AFA and the IPAs to issue or renew AFAs, as the case may be, in a time bound manner. There are, however, instances where an IP undertook CIRP without having an AFA and in some cases, without even applying for an AFA, in contravention of the provisions of law.

**(b) Fee payable to IP:** The Code of Conduct for IPs under the IP Regulations require that an IP must provide services for remuneration which is charged in a transparent manner, and is a reasonable reflection of the work necessarily and properly undertaken. Regulation 33 of the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 (CIRP Regulations) requires that the applicant shall fix the expenses to be incurred on or by the IRP. Regulation 34 requires that the committee of creditors (CoC) shall fix the expenses to be incurred on or by the RP. Regulation 39D requires the CoC to fix the fee payable to the liquidator, in the event the CD proceeds for liquidation. It is, however, observed that in a few cases, the fee payable to an IP was not fixed beforehand and the IP drew a fee on his own without approval of such fee from the competent authority, in contravention of the provisions of law.

**(c) Application for cooperation:** A CIRP requires cooperation of the CD, and its promoters, suspended directors, and management. However, co-operation may not be forthcoming in all cases. Section 19 of the Code, therefore, enables the IRP/RP to file an application to the Adjudicating Authority (AA) in case of non-co-operation for direction to such persons to comply with the instructions of the IRP/RP and to co-operate with him. Since time is the essence of a CIRP, the IRP /RP must act with promptitude and file the application, wherever required, without any procrastination. There are instances where the IRP / RP failed to file such applications or filed it so late that it lost its purpose and effectiveness. Any delay in filing applications despite continuing non-cooperation may reflect undue influence of promoters on the IP, and endanger the life of the CD.

**(d) Public announcement:** Section 15 of the Code read with regulation 6 of the CIRP Regulations requires the IRP to make a public announcement of commencement of CIRP within three days of his appointment. Such announcement is required to be made in one English and one regional language paper with wide circulation at the location of the registered office and principal office of the CD. This enables the creditors to submit claims to the IRP and consideration of such claims by the authorised stakeholders while resolving stress of the CD. There are instances where the IRP did not make public announcement promptly on his appointment, or made it later, or made it in one newspaper, or made it in one English newspaper having circulation at the location of the CD. This not only puts the CIRP at risk, but also deprives the stakeholders of their legitimate rights.

**(e) Updating of list of claims:** Section 25(2)(e) read with regulation 13 of the CIRP Regulations mandates that the IRP/RP shall verify every claim as per time line and maintain a list of creditors containing their names along with the amount claimed by them, the amount of their claims admitted and the security interest, if any, in respect of such claims, update the list and display it on the website, if any, of the CD. There are instances where some IRPs/RPs did not display the list of creditors on the web site of the CD and in some cases, did not update it. This increases queries and complaints about the status of claims, impacts transparency and compromises interests of stakeholders.

**(f) Authority of CoC:** The Code read with Regulations has specified responsibilities of an IP and of the CoC in a CIRP. These require decisions on several matters by the CoC with the required majority of voting share. No creditor, whether secured or unsecured, irrespective of its voting power or share, or no pool of creditors such as Joint Lenders' Forum is a substitute of the CoC. It has been observed in a few cases that an IP took directions of a creditor having significant voting power or a pool of creditors. This compromises the independence of IP and amounts to contravention of the provisions of the Code.

**(g) Appointment of professionals:** It is the duty of the RP to preserve and protect the assets of the CD, including continuing its business operations. Section 25(2) of the Code empowers an RP to appoint accountants, legal or other professionals for this purpose. Clause 23B of the Code of Conduct under the IP Regulations prohibits an IP from engaging or appointing any of his relatives or related parties for or in connection with any work relating to any of his assignment. An IP is, therefore, required to satisfy himself that there is a need for services of a professional; such services are not available within the CD; the person is qualified to render professional service; the professional to be appointed is suitable for the purpose; the professional is not a relative or related party of the IP; the fee to be paid to the professional is reasonable; etc. He needs to apply his mind to these and other related aspects while appointing a professional. He must not appoint any person who is not a professional, or who is his relative or a related party, or who is choice of a stakeholder. He must not appoint a professional to provide services to a stakeholder, or a professional because a stakeholder wants that professional to be appointed. There are instances where the RP appointed a professional who is the choice of a stakeholder or a person who is not a professional for professional services. This compromises the independence of the IP as well as that of the professionals and imposes avoidable cost on the CD and other stakeholders.

**(h) Appointment of registered valuers:** Regulation 27 of the CIRP Regulations envisages estimation of fair value and liquidation value of the assets of the CD. These values serve as reference for evaluation of choices, including liquidation, and selection of the choice that decides the fate of the CD, and consequently of the stakeholders. A wrong valuation may liquidate an otherwise viable CD, which may be disastrous for an economy. Given the importance of valuation in CIRP, the CIRP Regulations require that fair value and liquidation value of the CD shall be determined by two registered valuers (RVs) and it is the duty of the RP to appoint RVs only. There are, however, a few instances where the RP appointed persons other than RVs for conduct of valuations and in some cases, appointed only one RV instead of two. This indicates lack of due diligence and sincerity of the IP and probably demonstrates *mala fide* intent in some cases to get a valuation done to subserve certain interests. This potentially risks the life of the CD and adversely affects the interests of stakeholders, and drives out qualified and regulated valuation professionals out of practice.

**(i) Payment for professional services:** An IP and every other professional he appoints are independent professionals. They need to be paid reasonable fee commensurate to their services and such fee must be agreed before the appointment. The IP or professional concerned must raise bills / invoices in his name towards such fee, and such fee must be credited to his bank account. Any payment of fee for the services of an IP or any other professional appointed by the IP to any person other than the IP or such other professional, as the case may be, does not form part of the insolvency resolution process cost (IRPC). There are, however, a few instances where fee was paid to a person other than the IP or the professional concerned. This impacts transparency and cleanliness of the process while diluting professional accountability.

**(j) Disclosure of fee and relationship:** The CIRP Regulations require the IRP / RP to make relationship and cost disclosures in the manner required by IBBI. It is the duty of an IP to disclose the fee payable to him as well as the fee payable to professionals engaged by him while performing the duties as an IP. It is also his duty to disclose the relationship he has with the professionals engaged by him. This ensures transparency and enables the stakeholders to take informed decisions. Failure to disclose these details creates a suspicion in the mind of stakeholders about impartiality and objectivity of the IP and possibly, conflict of interests, he may have.

**(k) Fee for authorised representatives:** Regulation 16A of the CIRP Regulations entitles an authorised representative (AR) of creditors in a class to receive the specified amount of fee for every meeting of the CoC attended by him. It is, however, observed that ARs in a few CIRPs were paid an amount different from what is permissible under the Regulations. It is also observed that an AR engaged others, whether professionals or not, and such other persons attended the meetings of the CoC with the AR. Engagement of other persons by an AR, payment for services of such other persons, attendance of such persons in the meetings of the CoC, and payment of a different amount than permissible under the Regulations to an AR are in contravention of the law by the IRP/RP as well as of the AR.

**(l) Representation in judicial proceedings:** Section 25(2)(b) of the Code mandates RP to represent and act on behalf of the CD with third parties, and exercise rights for the benefit of the CD in judicial, quasi-judicial or arbitration proceedings. There are instances where the IP failed to represent the CD in judicial proceedings. Failure to do so compromises the duties of the RP to preserve and protect the interests of the CD, in addition to compromising the objective of value maximisation of the Code.

**(m) Related party transactions:** Section 28 of the Code requires the RP to take prior approval of the CoC before undertaking any related party transactions during the CIRP. Any such transaction without approval of the CoC is void. There are instances where the IP failed to take approval of the CoC before undertaking such transactions. This puts the transaction at risk and compromises the objective of value maximisation through CIRP and may reflect the intention of the RP to give undue advantage to a related party.

**(n) Payment to creditors during CIRP:** The Code requires every creditor to submit claims as on insolvency commencement date (ICD) to the IRP. Section 14 of the Code prohibits settlement of any such claim during CIRP and requires the resolution plan to deal with them together in the manner decided by the CoC subject to section 30(2) of the Code. Section 53 of the Code provides a waterfall for distribution of liquidation proceeds if the CIRP yields liquidation. Therefore, the IRP / RP cannot clear the dues of any creditor during the CIRP, as this amounts to giving preferential treatment to one creditor over others and thereby alters the priority mandated under the Code. He cannot also allow any creditor, who is having custody of funds of the CD, to appropriate it towards its own dues. There are instances where the RP allowed payment of dues outstanding as on the ICD to some creditors during CIRP. This not only impacts the interests of remaining creditors but also may be seen as compromising independence and integrity of the IP.

**(o) Avoidance transactions:** The Code read with the CIRP Regulations casts a duty on the RP to file applications in respect of avoidance transactions (preferential, undervalued, extortionate and fraudulent transactions) for appropriate directions with a view to claw back the value lost in these transactions. He is required to form an opinion on such transactions within 75 days of the ICD and to file applications to the AA within 135 days of the ICD. There are instances where the RP failed to independently apply mind to such transactions and file applications in respect of them. In a few cases, he allowed himself to be directed by the CoC or stakeholders. This may reflect serious dereliction of duty and breach of trust in addition to depriving the stakeholders of their legitimate dues.

**(p) Supply of information:** The success of CIRP largely hinges on availability of information to relevant stakeholders, particularly the CoC and the resolution applicants (RAs). Section 29 of the Code casts a duty on the RP to provide access to all relevant information to prospective

RAs in physical and electronic form. Regulation 36 of the CIRP Regulations requires the RP to provide information memorandum in electronic form to each member of the CoC. However, in few instances, it has been observed that RPs did not provide the relevant information to prospective RAs and members of the CoC. This compromises the possibility of revival of the CD in contravention to the provisions of the Code.

**(q) Confidentiality undertaking:** The Code requires the RP to provide access to all relevant information of CD to the RA subject to the RA undertaking to comply with the confidentiality requirements. The CIRP Regulations require the RP to obtain an undertaking of confidentiality from every prospective RA and every member of the CoC before sharing the information memorandum. These also require the RP to obtain an undertaking of confidentiality from every member of the CoC before sharing with them the report of the RVs containing details of fair and liquidation value of the CD. There are instances where the RP shared the documents with the members of the CoC and/or prospective RAs without obtaining the required undertaking. This exposes the CD to risks such as insider trading or weakens its competitive position in the market. This may reflect intention of the IP to provide privileged access to some persons at the cost of others and compromise value maximisation.

**(r) Disclosure of information:** The Code read with Regulations requires disclosure of certain information such as commencement of CIRP and details list of creditors in public domain. These envisage supply of certain information like information memorandum, evaluation matrix, agenda of the meetings of the CoC, etc. to entitled persons, often after taking a confidentiality undertaking. The details of valuation are required to be disclosed to every member of the CoC in electronic form, on receiving a confidentiality undertaking. Thus, information and documents need to be disclosed or supplied to entitled persons, in the specified manner, at the specified time, after meeting the specified requirements. It has been observed that in a few cases, certain information meant for entitled stakeholders were disclosed in public domain, or certain information meant for public were not disclosed in public domain, or certain information were disclosed before or after the time specified in the law.

**(s) Window for views:** Regulation 16A (9) of the CIRP Regulations mandates that an AR shall circulate the agenda to creditors in a class, and may seek their preliminary views on any item in the agenda to enable him to effectively participate in the meeting of the CoC. The creditors have a time window of at least 12 hours to submit their preliminary views, and the said window must open at least 24 hours after the AR has sought preliminary views. Further, regulation 25(6) of the CIRP Regulations requires the AR to circulate the minutes of the meeting to creditors in a class and announce the voting window at least 24 hours before the window opens for voting instructions and keep the voting window open for at least 12 hours. It is observed that such timelines were not adhered to in a few cases and voting window remained open for a period shorter than that is provided in the Regulations or for unusually long periods. This may create suspicion about the intention of the IP and may deprive a creditor of its right to vote.

**(t) Circulation of minutes:** The CoC is the authority to decide various matters in a CIRP, including approval or rejection of a resolution plan. It takes decisions through its meetings and its decisions are reflected in the minutes of its meetings. The CIRP Regulations, therefore, require the RP to circulate the minutes of the meetings by electronic means to members of CoC and ARs, if any, within 48 hours of the conclusion of the meeting. There are instances where the IRP/RP failed to record and circulate minutes promptly or did it late. This may reflect poorly on the competence and integrity of the IP and cause delay in critical decisions.

**(u) Inclusion of costs in IRPC:** Section 5(13) of the Code read with regulation 31 of the CIRP Regulations specifies what is included in IRPC. It includes only those costs which are necessary for a CIRP. The law does not allow inclusion of any other cost in IRPC. A member of CoC may incur costs to travel to attend the meetings of the CoC; the CoC may incur costs to obtain a legal advice or in engaging a professional; the CD may have incurred a cost before ICD; the RP may pay a penalty for non-compliance with any law during CIRP; etc. There are instances where such costs were included in the IRPC. This may reflect undue influence of beneficiaries on the IP, in addition to causing diminution of value of the CD.

**(v) Compliance with applicable laws:** Section 17(2)(e) of the Code mandates the IRP/RP to comply with the requirements under any law for the time being in force on behalf of the CD. Any non-compliance has a cost to the CD and its stakeholders and attracts penal consequences. For example, a listed company has several continuing obligations under the securities laws. Failure to discharge these obligations compromises the interests of investors in securities. This amounts to contravention not only of securities laws, but also of the provisions of the Code. The IRP/RP is responsible for the non-compliance of the provisions of the applicable laws if it is on account of his conduct. There are, however, instances where an IRP/RP failed to comply with requirements of various laws. This reflects lack of competence and professionalism of the IP, compromises the interests of stakeholders, and burdens the CD with the liabilities for failure of the IP to make compliances.

**(w) Timeline:** The Code read with Regulations specifies timeline for each task in a CIRP, as well as overall timeline. It is the duty of the IRP/RP to ensure that every task in the CIRP is completed in time unless directed otherwise by a competent authority. There are instances where the IP failed to adhere to specified timelines. This endangers the life of the CD, compromises the interests of stakeholders, and frustrates the objectives of the Code.

**(x) Compliance with orders:** The AA issues directions from time to time to facilitate smooth conduct of CIRP, generally based on applications by the parties. The proceedings before the AA are judicial proceedings and its directions are orders of the Court. Any non-compliance with any of their orders may amount to contempt of court. There are a few instances where the RP failed to comply with directions of the AA. Such disregard of the order of the AA may jeopardise the CIRP, impact the interests of stakeholders and drain scarce judicial resources.

**(y) Maintenance of records:** Regulation 39A of the CIRP Regulations requires an IRP/RP to preserve a physical as well as an electronic copy of the records relating to CIRP of the CD. Further, regulation 7(2)(g) of the IP Regulations requires an IP to maintain records of all assignments undertaken by him under the Code for at least three years from the completion of such assignment. It has been observed that in a few cases an IP failed to produce complete records in respect of CIRPs conducted by him. This suggests the possibility of failure to comply with the relevant provisions of law as well as lack of transparency.

**(z) Co-operation with the Inspecting Authority:** The Code enables the IBBI and the IPA to monitor conduct and performance of the IPs. Inspection is a typical means of monitoring. The IBBI appoints an Inspecting Authority (IA) to conduct an inspection of an IP. It is the duty of the IP to give all assistance to the IA, produce all records in his custody or control, and furnish all statements and information which the IA may require. There are instances where an IP failed to cooperate with the IA, did not produce documents and records promptly and prolonged inspection on some excuse or the other. This may be construed as a hindrance to the functioning of the IBBI or the IPA, as the case may be, and compromise of interests of stakeholders.

4. This communication has been prepared, in consultation with the three Insolvency Professional Agencies, with the sole purpose of sensitising the IPs about some of the mistakes committed by some of them. The observations made herein are only indicative. An IP must refer to the Code, the Rules/Regulations/Circulars under the Code and relevant case laws and / or may seek professional advice if he intends to take any action or decision, in any matter dealt with in this communication.

Yours faithfully,

Sd/-

(Mayank Mehta)

Assistant General Manger

[mayank.mehta@ibbi.gov.in](mailto:mayank.mehta@ibbi.gov.in)

Tel: 011-23462831