

**Discussion Paper**

**Subject: Governance of Insolvency Professional Agencies and Information Utilities**

The institutional infrastructure under the Insolvency and Bankruptcy Code, 2016 (Code) envisages four key pillars, namely, the Adjudicating Authority (National Company Law Tribunal and Debt Recovery Tribunal), the Insolvency and Bankruptcy Board of India (IBBI), the Information Utilities (IUs), and the Insolvency Professionals (IPs). An IP plays a central role in resolution, liquidation and bankruptcy processes of companies, LLPs, partnership firms and individuals. The Bankruptcy Law Reforms Committee (BLRC), which conceptualised the Code, felt that regulations must ensure that IPs are competent to perform the variety of tasks they may be hired for and that IPs are fair and impartial, as also conflict of interests are minimised.

2. To this end, the BLRC recommended that the Insolvency Professional Agencies (IPAs) establish rules and standards for their members through bye-laws, create and update relevant entry barriers, and have mechanisms in place to enforce their rules and standards effectively. It observed: *“Thus, the Committee believes that a new model of “regulated self-regulation” is optimal for the IP profession. This means creating a two-tier structure of regulation. The Regulator will enable the creation of a competitive market for IP agencies under it. This is unlike the current structure of professional agencies which have a legal monopoly over their respective domains. The IP agencies under the Board will, within the regulatory framework defined, act as self-regulating professional bodies that will focus on developing the IP profession for their role under the Code. They will induct IPs as their members, develop professional standards and code of ethics under the Code, audit the functioning of their members, discipline them and take actions against them if necessary. These actions will be within the standards that the Board will define. The Board will have oversight on the functioning of these agencies and will monitor their performance as regulatory authorities for their members under the Code. If these agencies are found lacking in this role, the Board will take away their registration to act as IP agencies.”*

3. The BLRC was of the opinion that the regulatory structure be so designed that competition is promoted amongst the multiple IPAs to help achieve efficiency gains. Greater competition among the IPAs will in turn lead to better standards and rules and better enforcement. It visualised IPAs as mini State having the following functions:

*“1. Regulatory functions - drafting detailed standards and codes of conduct through bye-laws, that are made public and are binding on all members;*

*2. Executive functions - monitoring, inspecting and investigating members on a regular basis, and gathering information on their performance, with the overarching objective of preventing frivolous behaviour and malfeasance in the conduct of IP duties;*

*3. Quasi-judicial functions - addressing grievances of aggrieved parties, hearing complaints against members and taking suitable actions.”*

4. Section 205 of the Code empowers an IPA to make bye-laws consistent with the model bye-laws specified by the IBBI. Section 204 of the Code provides that an IPA shall perform the following functions:

(a) *Grant membership to persons who fulfil all requirements set out in its bye-laws on payment of membership fee;*

- (b) *Lay down standards of professional conduct for its members;*
- (c) *Monitor the performance of its members;*
- (d) *Safeguard the rights, privileges and interests of insolvency professionals who are its members;*
- (e) *Suspend or cancel the membership of insolvency professionals who are its members on the grounds set out in its bye-laws;*
- (f) *Redress the grievances of consumers against insolvency professionals who are its members; and*
- (g) *Publish information about its functions, list of its members, performance of its members and such other information as may be specified by regulations.*

5. The IBBI has notified: (a) the IBBI (Model Bye-Laws and Governing Board of Insolvency Professional Agencies) Regulations, 2016, and (b) the IBBI (Insolvency Professional Agencies) Regulations, 2016. In November, 2016, it registered three IPAs, namely, the Indian Institute of Insolvency Professionals of ICAI, the ICSI Institute of Insolvency Professionals, and the Insolvency Professional Agency of ICAI. These IPAs are not-for-profit companies registered under section 8 of the Companies Act, 2013 and have been promoted by the three professional institutes, namely, the Institute of Chartered Accountants of India, the Institute of Company Secretaries of India and the Institute of Cost Accountants of India respectively. All the three IPAs have adopted the model bye-laws. No new IPA has been registered since November, 2016. There seems to be no visible sign of competition among the existing IPAs. After long persuasion by the IBBI, only one of the IPAs has appointed a Managing Director.

6. The IPAs have responsibility to develop and regulate the profession of IPs. They carry out quasi-legislative, executive and quasi-judicial functions. While they are public utilities and front-line regulators, they must compete with one another in terms of service rendered by their members acting as IPs. They need autonomy in terms of regulatory responsibilities as well as their finances and must not suffer from any kind of conflict of interest. They need to have energy to deliver on the assigned tasks. The provisions relating to organisational structure, shareholding pattern, the board composition and the Managing Director need to be designed to enable an IPA to discharge its responsibilities effectively.

7. There is no exact parallel organisation to IPAs. The closest may be the stock exchanges regulated by the Securities and Exchange Board of India (SEBI). The stock exchanges regulate trading on their platform and their members, called brokers, who are registered with the SEBI. In view of their statutory regulatory responsibilities and their commercial obligations, SEBI regulates the stock exchanges through the Securities Contracts (Regulation) (Stock Exchanges and Clearing Corporations) Regulations, 2012. These regulations provide as under:

A. **Organisation:** A company limited by shares is eligible for recognition as a stock exchange.

**B. Shareholding**

i. At least fifty-one per cent of the paid-up equity share capital of a stock exchange is by public.

ii. No person resident in India shall at any time, directly or indirectly, either individually or together with persons acting in concert, acquire or hold more than five per cent of the paid-up equity share capital in a stock exchange.

iii. The following persons may, however, acquire or hold, directly or indirectly, either individually or together with persons acting in concert, up to fifteen per cent of the paid-up equity share capital of a stock exchange:

- (a) a stock exchange;
- (b) a depository;
- (c) a banking company;

- (d) an insurance company; and
- (e) a public financial institution.

iv. No person resident outside India, directly or indirectly, either individually or together with persons acting in concert, shall acquire or hold more than five per cent of the paid-up equity share capital in a stock exchange.

v. The following persons may, however, acquire or hold, directly or indirectly, either individually or together with persons acting in concert, up to fifteen per cent of the paid-up equity share capital of a stock exchange:

- (a) a foreign stock exchange;
- (b) a foreign depository;
- (c) a foreign banking company;
- (d) a foreign insurance company; and
- (e) a foreign commodity derivatives exchange.

vi. The combined holding of all persons resident outside India in the paid up equity share capital of a stock exchange shall not exceed, at any time, forty-nine per cent of its total paid up equity share capital.

vii. No person shall, directly or indirectly, acquire or hold equity shares of a stock exchange unless he is a fit and proper person.

### **C. Board Composition**

i. The governing board of a stock exchange shall include: (a) shareholder directors; (b) public interest directors; and (c) managing director.

ii. Subject to prior approval of the SEBI, the chairperson shall be elected by the governing board from amongst the public interest directors.

iii. The number of public interest directors shall not be less than the number of shareholder directors in a stock exchange.

iv. The managing director shall be an ex-officio director on the governing board and shall not be included in either the category of public interest directors or shareholder directors.

v. Any employee of a stock exchange may be appointed on the governing board in addition to the managing director, but such director shall be deemed to be a shareholder director.

vi. No trading member or their associates and agents shall be on the governing board of a stock exchange.

vii. At least one public interest director shall be present in the meetings of the governing board to constitute the quorum.

viii. No foreign portfolio investor shall have any representation in the governing board of a stock exchange.

ix. The appointment and re-appointment of all shareholder directors on the governing board of a stock exchange shall be with the prior approval of the SEBI.

x. The public interest directors on the governing board of a stock exchange shall be nominated by the SEBI.

### **D. Managing Director**

i. The appointment, renewal of appointment and termination of service of the managing director of a stock exchange shall be subject to prior approval of the SEBI.

ii. A stock exchange shall, subject to the guidelines issued by the Board from time to time, determine the qualification, manner of appointment, terms and conditions of appointment and other procedural formalities associated with the selection/ appointment of the managing director.

iii. The appointment of the managing director shall be for a tenure not less than three years and not exceeding five years.

iv. The managing director shall be liable for removal or termination of services by the governing board of the stock exchange with the prior approval of the SEBI for failure to give effect to the directions, guidelines and other orders issued by the SEBI, or the rules, the articles of association, bye-laws and regulations of the stock exchange.

v. The SEBI may *suo motu* remove or terminate the appointment of the managing director if deemed fit in the interest of securities market after giving a reasonable opportunity of hearing.

8. In order to promote competition, to provide for and strengthen the position of Managing Director and generally to further energise the governing board of the IPAs, it is proposed to broadly adopt the provisions relating to organisational structure, board composition, shareholding pattern and Managing Director from and similar to the provisions in the Securities Contracts (Regulation) (Stock Exchanges and Clearing Corporations) Regulations, 2012, as narrated in Para 7 above, subject to following modifications, namely,

i. There may be no limit on shareholding of Government or any statutory regulator in an IPA;

ii. Multilateral institutions may be allowed to hold shares up to 15% of paid up capital of an IPA;

iii. The term 'independent director' may be used in place of 'public interest director'. An individual may serve as an independent director of an IPA for a maximum of two terms of three years each or part thereof, or up to the age of seventy years, whichever is earlier. The second term may be subject to a satisfactory performance review of the first term by the governing board of the IPA. A cooling off period of three years may be applicable for an independent director to become a shareholder director in the same or another IPA;

iv. An independent director may be nominated by the IBBI from a list of names proposed by the IPA;

v. The chairperson may be elected by the governing board from amongst the independent directors.

vi. The restriction on foreign portfolio investor to have representation in the governing board may not be applicable.

vii. An IPA may have a Managing Director;

viii. The Managing Director shall be an *ex-officio* member of Membership Committee, Monitoring Committee, Grievance Redressal Committee and Disciplinary Committee;

ix. An IPA may lay down eligibility criteria for appointment of Managing Director. An individual having any of the following qualifications and experience may be eligible to be Managing Director:

a. CA, CS, CMA, LL. B. or Post Graduate in Economics/Business administration;

b. Proven track record in industry or regulatory capacity;

c. Industry experience of fifteen years in insolvency, banking, finance, insurance, securities or with a regulatory body, which may include at least 5 years as Managing Director or one level below the Board;

d. Not more than 55 years on the date of joining;

x. The Managing Director may be selected through open advertisement in all editions of at least one national daily newspaper;

xi. An individual may serve as Managing Director of an IPA for a maximum of two terms of up to 5 years each or up to the age of 65 years, whichever is earlier. After the first term, the appointment process for Managing Director may be conducted afresh; and

xii. Appointment and remuneration payable to a Managing Director may be approved by a Compensation Committee constituted by the Governing Board.

9. An Information Utility (IU), which is a utility, stores financial information that helps to establish defaults as well as verify claims expeditiously and thereby facilitates completion of

transactions under the Code in a time bound manner. The IBBI has notified the IBBI (Information Utilities) Regulations, 2017 to provide for its shareholding and governance. An IU has no comparable organisation whether in India or overseas. It is somewhat close to depositories which record allotment of securities or transfer of ownership of securities. Keeping in view the provisions in the SEBI (Depositories and Participants) Regulations, 1996 and the need to provide for and strengthen the position of Managing Director and generally to further energise the governing board of the IUs, it is proposed to amend the IBBI (Information Utilities) Regulations, 2017 relating to Board Composition, and Managing Director as under:

#### **A. Board Composition**

- i. The governing board of an IU may include: (a) shareholder directors; (b) independent directors; and (c) managing director;
- ii. The number of independent directors may not be less than the number of shareholder directors in an IU;
- iii. The independent directors on the governing board of an IU may be nominated by the IBBI from a list of names proposed by the IU;
- iv. An individual may serve as an independent director of an IU for a maximum of two terms of three years each or part thereof, or up to the age of seventy years, whichever is earlier. The second term may be subject to a satisfactory performance review of the first term by the Governing Board of the IU. A cooling off period of three years may be applicable for an independent director to become a shareholder director in the same or another IU;
- vi. At least one independent director may be present in the meetings of the governing board to constitute the quorum;
- vi. The chairperson may be elected by the governing board from amongst the independent directors;
- vii. The managing director may be an *ex-officio* director on the governing board and may not be included in either the category of independent directors or shareholder directors; and
- viii. Any employee of an IU may be appointed on the governing board in addition to the managing director, but such director may be deemed to be a shareholder director.

#### **B. Managing Director**

- i. The appointment, renewal of appointment and termination of service of the managing director of an IU may be subject to prior approval of the IBBI;
- ii. An IU may determine the qualification, manner of appointment, terms and conditions of appointment and other procedural formalities associated with the selection/ appointment of the managing director;
- iii. The appointment of the managing director may be for a tenure of not less than three years and not exceeding five years;
- iv. The managing director may be liable for removal or termination of services by the governing board of the IU with the prior approval of the IBBI for failure to give effect to the directions, guidelines and other orders issued by the IBBI, or the rules, the articles of association, bye-laws and regulations of the IU;
- v. The IBBI may suo motu remove or terminate the appointment of the managing director if deemed fit in the interest of IU or in public interest after giving a reasonable opportunity of hearing;
- vii. An IU may lay down eligibility for Managing Director. An individual having any of the following qualifications and experience may be eligible to be Managing Director:
  - a. CA, CS, CMA, LL.B. or Post Graduate in Economics/Business administration/ Information Technology/Computer Science;
  - b. Proven track record in industry or regulatory capacity;

- c. Industry experience of fifteen years in insolvency, banking, finance, insurance, securities, information technology or with a regulatory body, which includes at least 5 years as Managing Director or one level below the Board;
- d. Not more than 55 years on the date of joining;
- vii. The Managing Director may be selected through open advertisement in all editions of at least one national daily newspaper;
- viii. An individual may serve as Managing Director of an IU for a maximum of two terms of up to 5 years each or up to the age of 65 years, whichever is earlier. After the first term, the appointment process for Managing Director may be conducted afresh; and
- ix. Appointment and remuneration payable to a Managing Director may be approved by a Compensation Committee constituted by the Governing Board.

10. The existing IPAs and the IU may get one year to comply with the provisions proposed in Para 7, 8 and 9 above.

11. A note covering the above aspects was shared with the IPAs and discussed in the meeting with CEOs of the IPAs and the Managing Director of the IU on 7<sup>th</sup> August, 2018. This paper has considered their suggestions.

12. Comments and suggestions are invited from public, including stakeholders on the proposals at Para 7A, 7B, 7C, 7D, 8, 9A, 9B and 10 at id: **ipa@ibbi.gov.in** latest by **5<sup>th</sup> September, 2018**. In subject line of the email, please state: “Comments on Para 7A / Comments on Para 7B / Comments on Para 7C / Comments on Para 7D / Comments on Para 8 / Comments on Para 9 / Comments on Para 10A / Comments on Para 10B”.