

Regulating Insolvency Professionals under the IBC  
Tracing pathways to regulation based on a study of professional  
development

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**Abstract**

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# 1 Introduction

The *IBC 2016* was enacted on May 28, 2016 and created the first ever, non-sectoral law on bankruptcy in India. A key institution of the legal framework for bankruptcy was the creation of the profession of insolvency professionals, and a self-regulatory system to oversee their functioning. Insolvency professionals were envisaged to play a key role in the insolvency and bankruptcy processes, in charge of ensuring symmetry of information between debtors and creditors, the correct collection and evaluation of bids, satisfying the National Company Law Tribunal of compliance with due process and acting as a liquidator, among others. In this paper we attempt to analyse the regulation of the insolvency profession as it has evolved since the enactment of the law as well as the factors shaping the development of the profession with regard to a specific aspect, accountability.

A large number of cases have been filed before NCLTs under the *IBC 2016* since its enactment, and the website of the regulator (Insolvency and Bankruptcy Board of India) lists more than 1,700 IPs currently registered, and three Insolvency Professional Associations (IPAs) which are the self-regulatory organisations that each IP is enrolled with. There is therefore early evidence of the demand for the IBC as a legal remedy in general, and the role of IPs within that system of legal remedies. Burman and Roy, proposed that IPs be regulated indirectly via SROs to be regulated by the State in turn.<sup>1</sup> That paper located the need for a separate profession of IPs in the need for consumer protection, and as an exit from the problematic regulation of professionals who were likely to perform services envisaged for IPs, namely lawyers and accountants.

The IBC as it was passed, accepted some of these recommendations. The existing structure has the following broad characteristics:

- Unlike other professions in India, no single SRO has a legal monopoly over the development of the profession. At the time of writing, three SROs are regulating IPs and are in-turn regulated by the IBBI.
- The IBC clearly obliges the regulator (IBBI) to monitor the conduct of IPs and IPAs, including by creating a competitive market for IPAs.
- The IBC contains clearly defined objectives of regulation aimed at consumer protection.

This legal framework is exceptional in the manner in which a new profession is sought to be created. Academic literature on professions points to the historical and organic emergence of professions, with state recognition and regulation being an advanced stage in the development of the profession.<sup>2</sup> The IBC model on the other hand starts with the conferment of state recognition on professionals who meet standards of competency and eligibility based on Parliamentary law and accompanying regulations. The entire regulatory apparatus governing the IP profession has also been laid out in the primary law. This alone act as a useful point of departure in understanding the factors shaping the development of the IP profession.

In their proposals, Burman and Roy located the need for regulating insolvency professionals in a conception of market failures that could lead to sub-optimal outcomes in the bankruptcy process. Two primary concerns were those of information asymmetry and professional misconduct. These concerns were in turn located in specific contexts: the fact that many other professions arbitrage information asymmetry to earn premiums for services, and the failure of SROs in other professions to effectively regulate their members.

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<sup>1</sup>Anirudh Burman and Shubho Roy, “Building an Institution of Insolvency Practitioners in India”, in: *IGIDR Working Paper* WP-2015-033 (2015), ISSN: 1556-5068, DOI: 10.2139/ssrn.2725800, URL: <http://www.ifrogs.org/PDF/WP-2015-033.pdf> (visited on 03/26/2018).

<sup>2</sup>Andrew Abbott, *The System of Professions*, University of Chicago Press, 1988, URL: <http://www.press.uchicago.edu/ucp/books/book/chicago/S/bo5965590.html> (visited on 03/19/2018).

This paper builds on prior work by examining the specific context in which insolvency professionals are likely to proffer their services to consumers. It departs from the work of Burman and Roy by evaluating non-state sources of demand for quality in an IP’s work, as well as sources of accountability that are exogenous to the regulatory standards prescribed under the IBC (such as clients, courts and the changing nature of professional work due to market developments). We hypothesise that multiple sources of external accountability may act as effective self-regulating factors. These will in turn critically inform the need and nature of regulation by IBBI.

In addition, we also critically evaluate the regulation of the IP industry in India as it has evolved since the enactment of the law, in particular the role played by the insolvency professional agencies (IPAs). We highlight the points of departure from the regulatory edifice initially envisaged in the *The report of the Bankruptcy Law Reforms Committee Volume I: Rationale and Design* that had laid down the foundations of *IBC 2016* . This in turn may help throw light on what further needs to be done to strengthen the regulation as well as foster the development of the insolvency profession in India.

We review existing literature to study the historical development of professions in other societies and sectors to understand the structural and contextual factors that determine the path a profession might take towards its development. A preliminary reading of this literature indicates that state recognition generally acts primarily as an instrument to concentrate power in organised groups that professions have collectivised into. State recognition is a tool for excluding non-conformists. The IBC framework that requires the state to “regulate” the profession in its incipient stage will have to be studied in light of this literature.

This analytical framework will then be tested through conversations with IPs and IPAs as well as recent clients. The objective will be to understand the specific issues and factors that are shaping the profession of IPs at this early stage of their development and also contributing to the regulation of the profession. We will also analyse the few but important complaints of misconduct against IPs that have arisen in order to understand the extent to which regulation could have prevented such conduct. An important assertion this paper seeks to make is the need for careful contextualisation of the need for regulation, given the incipient stage of the IBC process in general.

## 2 Tracing the development of professions

The professional development of IPs is exceptional when compared to the development of many other professions. Literature shows that professions usually go through certain distinct stages of institutionalisation and formalisation. According to Abbott professions are organised bodies of experts who apply esoteric knowledge to specific cases. Professions develop when jurisdictions become vacant or are perhaps newly created. Jurisdictions provide the link between a profession and its work. Professionalisation is the process of pursuing, developing and maintaining monopoly over occupational jurisdictions. It refers to the institutionalisation of expertise and the process of organisation of a profession. It is also a process through which occupations seek status and recognition often by means of standardisation of education, training and qualification for practice. Legal recognition and state regulation generally come about at an advanced stage in process of professionalisation, after other forms of institutionalisation have taken place within the profession itself. State regulation typically comes about once a profession has acquired a certain degree of stability and maturity.<sup>3</sup>

In contrast, the profession of IPs was “invented” in India by the Committee , and introduced by the *IBC 2016* . To borrow the terminology from Abbott, the profession was created by the

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<sup>3</sup>Abbott, see n. 2, Page to be inserted.

state to fill up a vacant jurisdiction. The occupational jurisdiction of IPs itself is formalised in legislation along with the regulatory structure. The professional associations or IPAs have also been formed in the same manner. Therefore, all the stages in the initiation of a new profession, its formalisation and institutionalisation (a) happened at the same time, and (b) occurred in a top-down manner through state regulation rather than through organic market forces. This is a point of departure for the study of the IP profession due to its implications for the development of the profession. For example, many of the institutions that develop organically (self-regulatory bodies, rules of conduct, rules for membership) as a result of the internal discussions between members of the profession and its negotiations with other professions were created by legal mandate. This is likely to affect the degree to which the profession can monitor and discipline itself, since the profession was “fitted” into an institutional architecture rather than organising itself into one. It is also likely to shape professional attitudes since peer pressure could be a less important factor in professional development, than in some other professions.

State-led professional development is likely to be a major feature of the development of IPs. The bankruptcy regulator and the larger Indian state is likely to be a major arbiter between commercial necessities and demands on the profession on the one hand, and the interests of the profession on the other. As a consequence, the relative effects of state regulation and market forces is likely to be play a critical role in the development of IP. If IBBI is likely to be a major stakeholder in holding IPs responsible (directly, or via IPAs), it is also likely to be a source of risk and disruption to their professional development.

We therefore conduct our study with an emphasis towards understanding and conceptualising the role of state regulation vis-a-vis the profession of IPs.

### 3 Creating a new, regulated profession

The *IBC 2016* defines an insolvency professional as a person enrolled with an insolvency professional agency, and registered with the Insolvency and Bankruptcy Board of India.<sup>4</sup> Insolvency professionals were created under the *IBC 2016*, and did not exist as a distinct profession prior to its enactment. Prior to the enactment of the *IBC 2016*, the bankruptcy process was heavily overseen by the appropriate courts who oversaw procedural compliance, but also, critically, were required to second-guess business decisions in the insolvency process.

Lawyers were therefore heavily involved in the bankruptcy process. Accountants advised debtors and creditors, but had no formal role within the process. Burman and Roy point to the fact that these professions themselves are not appropriately regulated.<sup>5</sup> There was therefore a need to ensure that professionals formally engaged in the bankruptcy process be properly organised and regulated. This was necessary in view of the strict timelines in the bankruptcy process under the *IBC 2016* as well as the larger success of the Code.

Burman and Roy proposed that the primary objective of creating a regulated cadre of insolvency professionals is to protect consumers i.e. the distressed firms and creditors of such firms. The primary task of regulating such professionals should be left to Self Regulatory Organisations (SROs) such as the IPAs. The state should, in turn regulate these SROs to ensure that they are discharging their functions effectively. Direct regulation of the IPs by the state may be limited by constraints of state capacity. The authors viewed the SROs as agents of the state who would be able to absorb evolving best practices faster and in a more dynamic manner. Regulation must create:

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<sup>4</sup>Section 2(19) of the *IBC 2016*

<sup>5</sup>Insert PAGE NUMBER Burman and Roy, see n. 1.

- Entry barriers allowing for competent IPs
- Clear performance requirements for ensuring minimum service standards
- Penalties for deterring non-compliance
- Compensation and/or redress mechanisms for consumers.

It is also important to allow competition among the SROs. This can act as a potential check on interest-group capture by allowing for exit and also creates better incentives to attract better IPs. Thus the SROs would be the primary regulators of IPs. The state will set minimum standards, collect supervisory information about the conduct of IPs from the SROs, will make sure that the SROs are enforcing the law correctly against the IPs and will hold the SROs responsible for negligent or fraudulent behaviour of IPs.

### 3.1 BLRC

The *The report of the Bankruptcy Law Reforms Committee Volume I: Rationale and Design* acknowledged that 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 as envisaged in the *IBC 2016* :

*“The law must appoint a resolution professional as the manager of the resolution period, so that the creditors can negotiate the assessment of viability with the confidence that the debtors will not take any action to erode the value of the enterprise. The professional will have the power and responsibility to monitor and manage the operations and assets of the enterprise. The professional will manage the resolution process of negotiation to ensure balance of power between the creditors and debtor, and protect the rights of all creditors. The professional will ensure the reduction of asymmetry of information between creditors and debtor in the resolution process.”*<sup>6</sup>

This was considered important in light of other design principles, namely that the *IBC 2016* would facilitate assessment of a firm’s viability at an early stage, that business viability decisions be left to creditors, that courts ought to control process but not make business decisions, that a fixed moratorium period be given for debtors and creditors to negotiate without fear of debt recovery enforcement and that the resolution process be completed in a time bound manner in order to facilitate value maximisation.<sup>7</sup>

The Committee therefore recommended in its report that a new profession of insolvency professionals be established under the *IBC 2016*, and proposed that the profession be regulated indirectly by the state. Insolvency professional agencies (IPAs) were envisaged to regulate IPs and in turn be regulated by the overall regulator for the bankruptcy ecosystem.

More specifically, Committee suggested that the regulatory framework must impose entry barriers on the IPs and this should be based on registration. The recommended registration process was a layered one wherein:

*“Any person or individual who wants to practice as an IP will need to obtain membership of an approved, professional IP agency. Once the IP is the member of a professional IP agency, he will need to apply to be registered with the Regulator.”*

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<sup>6</sup>Bankruptcy Law Reforms Committee, *The report of the Bankruptcy Law Reforms Committee Volume I: Rationale and Design*, India, Nov. 4, 2015, URL: [http://ibbi.gov.in/BLRCReportVol1\\_04112015.pdf](http://ibbi.gov.in/BLRCReportVol1_04112015.pdf) (visited on 04/07/2018), see section 3.4.2.

<sup>7</sup>Ibid., see section 3.4.2.

The report further suggested that in order to become a member of an IPA the individual needs to be “fit and proper” and clear an IP exam. Each IPA can conduct its own IP entry exam. The report implied that only individuals can get registered as IPs. In context of the precise regulatory structure of the IP industry, Committee highlighted the inefficiencies of the existing self-regulating, professional bodies (such as Institute of Chartered Accountants of India (ICAI), Institute of Company Secretaries (ICSI) etc.) in regulating and disciplining their members. The report therefore recommended a new model of “regulated self regulation” for the IP profession. This would get manifested through a two tier structure of regulation i.e. the IPAs and the bankruptcy regulator.

*“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.”*

In their bye-laws the IPAs would lay down detailed grounds of suspension or cancelation of membership of the IPs and also publish the disciplinary actions taken by them against their members, on their respective websites, in order to maintain transparency.

The bankruptcy regulator in turn will exercise oversight on the functioning of the IPAs and if they are found lacking in their role as regulatory authorities, then their registration as IPAs will be taken away. Committee laid down a detailed framework for the crucial role played by the IPAs including their legislative, executive, and quasi-judicial functions.

### **3.2 IPs in IBC**

Following the recommendations of the Committee, *IBC 2016* provides broad guidelines about the registration, functions and obligations of the IPs and IPAs. While the Committee goes into the details of how the regulatory structure should be designed, including the regulatory functions of the IPAs, *IBC 2016* leaves the details to subordinate legislation. For example the law does not say anything about an IP entry exam or the exact process of delicensing an IP. According to the law, IPs who meet the specified criteria and possess the required qualifications as mentioned in the subordinate legislation, can get enrolled as members of IPAs and then get registered with the IBBI. IPs so registered will perform their duties in the context of both corporate and individual insolvency and bankruptcy cases as and when they are called upon to do so. While acting as IPs they are required to abide by a certain code of conduct as specified in the regulations of the IBBI and the bye-laws of the IPAs of which they are members.

According to the *IBC 2016*, the IPAs need to get registered with the IBBI following the procedure prescribed in the law. The IPAs so registered, will be responsible for the promotion of professional development of the IPs, and for the regulation of their conduct. The IPAs will draft detailed bye-laws to regulate the IPs who are their members. The IPAs will grant membership to the eligible IPs, lay down the minimum standards of professional and ethical conduct for the IPs in their bye-laws, monitor the performance of their members, safeguard their rights, interests and privileges, and redress the grievances of consumers against the IPs. IPAs will also have the power to suspend or cancel the membership of IPs on the basis of grounds specified in their bye-laws.

The *IBC 2016* has given a clear mandate to the IBBI for regulating the IPs and IPAs. It confers specific legal duties that the IBBI is required to discharge. Most of these duties require the IBBI to frame regulations regarding insolvency proceedings, roles and duties of IPs, IPAs and information utilities. With regard to the insolvency profession, the functions of IBBI

include specifying the minimum eligibility criteria for the registration of IPs and IPAs as well as the minimum standards for their professional and ethical conduct, outlining the curriculum of the examination through which the IPs will get registered, conducting audits, inspections and investigations of the IPs and IPAs and monitoring their performance. The IBBI can also use subordinate legislation to call for any information and records from the IPs and IPAs. Further, it needs to specify in its regulations a mechanism for the redressal of grievances against the IPs and IPAs. The law also requires IBBI to frame model bye-laws which will act as guidelines for the IPAs in their role as regulators of the IPs.

### 3.3 IBBI and IPAs: current regulatory structure

A study of the regulations issued so far by the IBBI shows that the regulator has framed regulations covering most items that it is required to. In fact, one of the key issues highlighted in the following sections of the paper is the haste with which the regulatory framework for IPs was created.

The regulatory structure has already undergone significant changes since its inception approximately two years ago. The creation of the profession and the regulatory ecosystem was expedited in 2016 in light of the large amount of non-performing assets in the banking system and the failure of existing legal mechanisms to resolve this issue. The Insolvency and Bankruptcy Board of India was established on October 1, 2016.

The first regulations regarding insolvency professionals came into force on November 29, 2016.<sup>8</sup> The *Insolvency and Bankruptcy Board of India (Insolvency Professionals) Regulations, 2016* (as they then existed) required a combination of prior experience, clearing a qualifying examination, as well as membership of pre-existing professional bodies (Institute of Chartered Accountants of India (ICAI), Institute of Company Secretaries of India (ICSI), Institute of Cost Accountants of India (ICWAI), and Bar Councils).<sup>9</sup> This was subsequently amended to include experienced management professionals as well.<sup>10</sup>

In March 2018, these regulations were amended to permit the recognition of Insolvency Professional Entities (partnership firms or companies where IPs hold majority of the shares or capital contributions) if such entities work exclusively to service its member or director IPs.<sup>11</sup>

Regulations regarding IPAs were notified on November 21, 2016.<sup>12</sup> Regulatory requirements stipulated high financial assurances, domestic ownership and control, and that the IPAs be not-for-profit companies.<sup>13</sup> IBBI also framed regulations regarding the bye-laws of IPAs, requiring them to write their internal bye-laws in conformity of the model bye-laws, and get them pre-approved by IBBI. The model bye-laws specified the composition of internal committees, duties of internal members, and the manner of conducting their monitoring and disciplinary functions vis-a-vis their members.<sup>14</sup>

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<sup>8</sup>See section 1(2) of the Insolvency and Bankruptcy Board of India, *Insolvency and Bankruptcy Board of India (Insolvency Professionals) Regulations, 2016*, 2016, URL: [http://ibbi.gov.in/webadmin/pdf/legalframework/2018/Apr/word%20copy%20Updated%20upto%2001.04.2018%20IP%20REGULATIONS\\_2018-04-11%2016:15:54.pdf](http://ibbi.gov.in/webadmin/pdf/legalframework/2018/Apr/word%20copy%20Updated%20upto%2001.04.2018%20IP%20REGULATIONS_2018-04-11%2016:15:54.pdf) (visited on 05/11/2018).

<sup>9</sup>See footnote 3 of the *Insolvency and Bankruptcy Board of India (Insolvency Professionals) Regulations, 2016*, containing the text of the now amended regulation 5

<sup>10</sup>See regulation 5(c)(iii) of the *Insolvency and Bankruptcy Board of India (Insolvency Professionals) Regulations, 2016*

<sup>11</sup>See Chapter V of the *Insolvency and Bankruptcy Board of India (Insolvency Professionals) Regulations, 2016*

<sup>12</sup>See regulation 1(2) of the Insolvency and Bankruptcy Board of India, *Insolvency and Bankruptcy Board of India (Insolvency Professional Agencies) Regulations, 2016*, 2016, URL: [http://ibbi.gov.in/webadmin/pdf/legalframework/2017/Jul/IPA%20REGULATIONS\\_professional\\_agencies.pdf](http://ibbi.gov.in/webadmin/pdf/legalframework/2017/Jul/IPA%20REGULATIONS_professional_agencies.pdf) (visited on 05/11/2018).

<sup>13</sup>See regulation 5 of the *ibid.*

<sup>14</sup>See regulation 5 of the *ibid.*



Initially, the three professional bodies, ICAI, ICSI and ICWAI were granted recognition as IPAs and were asked to perform associated functions. These bodies subsequently formed independent non-profit companies that have been recognised as IPAs by the IBBI. Membership of these bodies is open to persons outside the original membership of the parent IPA (a lawyer, chartered accountant or cost accountant can be enrolled as a member of any of the ICAI IPA, ICSI IPA or the ICWAI IPA).

We therefore see that the initial regulatory framework for IPs was established within less than two months of the establishment of the regulator, IBBI. This paper argues that this need to act quickly, along with the substantive regulatory framework created under the regulations has had a negative impact on professional development on balance. There are several points of departure between the original vision of the Committee, the regulations drafted by IBBI and what has finally been implemented by the IPAs.

To begin with, despite the regulatory failures of the existing SROs, the same entities were registered as IPAs by the IBBI, perhaps because of the haste with which the entire law had to be operationalised in order to urgently deal with the big insolvencies that had not been addressed for years and were increasingly contributing to the growing pile of non-performing assets in the banking sector. Moreover, IBBI in its regulations mandated that IPAs must be Section 8 companies under the Companies Act, 2013 as opposed to for-profit organisations. The entry barriers for eligible IPAs are also very high (minimum net worth of Rs 10 crore and paid-up share capital of Rs 5 crore). A combination of these restrictive regulations would have implied that the existing SROs were best placed to apply for an IPA registration.

Secondly, while Committee envisaged that each IPA could conduct its own entry-level IP exam, IBBI in its regulations mandated a centralised insolvency exam to be conducted by itself or any other designated agency.

Third, Committee and subsequently the law and IBBI's regulations required the IPAs to draft detailed bye-laws outlining the codes of conduct and standards to be followed by their IP members and also mentioning the eligibility criteria to qualify for IPA membership. In reality, all three IPAs ended up adopting the same code of conduct as drafted by the IBBI in the regulations for IPs. None of the IPAs has any additional eligibility criteria for the members other than the ones laid down by IBBI for IP registration. Two out of three IPAs have published their bye-laws on their websites and the bye-laws are also identical because they have simply adopted the model bye-laws given to them by IBBI. As a result, despite there being multiple IPAs, they all look identical in this respect.

Fourth, Committee envisaged that disciplinary actions taken by the IPAs against their members would be published on their respective websites. This recommendation was not included in the IBBI regulations and consequently this is not public knowledge. In fact one IPA mentions a list of IPs who have not paid membership fees despite notices being served and while this is included as a ground for cancellation of membership in the IPA's bye-laws, it is not clear whether any action has been taken against these IPs. However disciplinary action taken by the IBBI against some IPs has been published on IBBI's website. The reasons for this asymmetry between IPAs and IBBI in the exercise of their regulatory powers is unclear.

Finally, the details of how disciplinary actions are to be taken against IPs is also not clear. For instance, what is the sequence of events when an IP is found to have violated either the law or the regulations or the IPA's bye-laws? Is it the case that the IPA will be the first port-of-call, take a disciplinary action against an errant IP, report it to IBBI, and IBBI steps in for the more egregious cases or is it that all disciplinary actions against IPs are only taken by the IBBI? It seems that in reality the latter is being practiced because there are orders on IBBI's website about punishing errant IPs but nothing on the IPAs' websites. In that case it is not clear what

kind of regulation the IPAs are really doing.

In fact the domain of disciplinary actions against IPs remains vague. The law contains general guidelines about the process of delicensing of the IPs. It says that if sufficient cause exists then the IBBI can take away the registration of IPs. It is clear from both the Committee and *IBC 2016* that the IPAs do not have the power to take away the registration of IPs. They can only suspend or cancel the membership of IPs but it is not clear either from the law or from IBBI's regulations, whether losing an IPA membership tantamount to losing IP registration. The other way round however holds i.e. IPs whose registration has been canceled by IBBI will also lose their IPA membership. This can be an important point in the ability of the IPAs to effectively exercise regulatory powers on their members.

From the above it is apparent that IPAs do not really have a lot of regulatory powers over the IPs and there has been a significant divergence between the initial vision of the committee that proposed the tripartite regulatory structure for the IP industry and the actual regulatory framework that has emerged in reality. While the emphasis of the Committee and the *IBC 2016* was on market-determined self-regulation through IPAs, the regulatory structure adopted is one of state-led regulation with IPAs playing a secondary role.

Critically, most of the requirements of serving as an IP begin after registration with the IBBI, not the IPA. IPs are registered directly by the IBBI, but their registration is subject to the membership of their respective IPAs (among other conditions). The Committee had envisaged a system where the IPAs function as self-regulatory organisations, and therefore as gatekeepers of the profession. This would necessitate IPAs having a more pro-active role in the professional regulation of IPs than at present. The manner in which IPAs were created however, militated against these organisations developing the necessary internal motivations for regulating their members effectively.

As originally proposed, the regulatory ecosystem for IPs was to be shaped primarily by market forces, with IPAs existing to provide the institutional support for self-regulation, and the IBBI present to oversee the general functioning of the market, primarily through overseeing the functioning of IPAs. Significant changes to this proposed regulatory framework occurred in the different stages of the formulation and drafting of the *IBC 2016*, and in the precise manner in which the law was implemented.

It is important to note that the success or failures of IPs as a profession and IPAs as SROs have to be viewed in the context of state action as described above, in particular the interpretation of their roles and responsibilities under the *IBC 2016* by the IBBI. Incidences of incompetence, negligence or malpractice by IPs arise within this regulated ecosystem. It is also important to note that the current ecosystem is one created by law and regulation, and did not exist prior to the enactment of the *IBC 2016*. Misconduct by IPs is as much a government failure as a market failure.

How should this analysis inform regulation of IPs in the future? We posit that regulation can instead focus on filling in gaps in accountability mechanisms within the market. As our analysis in section 4 shows, market forces exert accountability on IPs in significant ways. This has benefits over any regulatory prescription since such accountability mechanisms are usually tailored to the specific time and context in which the IP provides his or her services. The specific parties to an insolvency transaction exert accountability on the IPs.

## 4 Factors shaping the accountability of IPs

The following are the non-state forces that can help shape the accountability of the IP profession:

1. The **nature of the work** of IPs is such that the IP is accountable to multiple entities despite having a single client in any one case. These entities are the committee of creditors in the insolvency resolution process, the courts or the NCLT, the debtor firm, interested third parties submitting the resolution bids etc.

This is different from other professions such as doctors and lawyers where the client alone holds the professionals accountable. Market forces impose accountability on the IP from many different sources, unlike other professions. The forces of market-driven accountability are therefore much stronger in the case of IPs than many other regulated professions.

In many if not most of the cases before IPs, affected parties are sophisticated consumers who can make informed decisions. This again, is different from many other professions where the profile of clients may vary drastically, and the majority of clients may not be able to judge the quality of the service the professional is providing. In the event that these market based accountability mechanisms fail, professional development facilitated by the IPAs can fill up the gaps and when IPAs too fail to perform their role, that is when the IBBI can step in.

2. **Inter-professional competition** can typically play an important role in enforcing accountability in professions. Competition from outsiders allows members practising a profession to associate amongst themselves to defend their practise, and it also provides fertile grounds for formulating common codes of conduct in opposition to outsiders who do not.

But in the case of IPs this may not work. This is because the exclusive domain of work of the IPs is very well defined in the primary law that created this profession and therefore one can argue that there is very little threat to the jurisdiction of IPs. There could however be internal competition from amongst IPs and this depends crucially on whether the IBBI registers more IPAs. In a way the IBBI has emerged as the gatekeeper in determining how the intra-professional competition among IPs will play out.

One mechanism for the IBBI to promote the development of the profession is therefore to ensure that competitive forces allow for greater associational behaviour among IPs, and new skills and approaches can inform the practice of insolvency resolution.

3. There is at present an immediate and urgent **demand for IPs** created by the insolvencies of several large firms. An important question in this regard is what happens when this wave of big insolvencies is over? Will a reduction in the demand for IPs make them more entrepreneurial? Things may also change with the notification of the personal insolvency related sections of IBC. This will create the demand for IPs with different profiles and expertise. Amendment to *IBC 2016* or enactment of a new law to resolve cross-border insolvencies will also play a role in expanding the jurisdiction of the IPs and may even trigger the entry of foreign insolvency professionals. The high demand for IPs can be an accountability diluting factor in the present exceptional environment (as can perhaps be seen in several cases of errant IP behaviour that have recently come to attention). At the same time regulatory intervention can distort the accountability arising out of market demand.

Thus there are fairly substantial market led mechanisms of accountability in the IP profession. At the same time IPs are a product of law, not market-forces. IBBI needs to evaluate the relative

strengths of different accountability mechanisms in the market. As the profession develops further, IBBI may need to exercise greater forbearance in favour of market led accountability mechanisms such as letting the IPAs play a more important role.

## 5 Role of state vs. market in professional development

The literature on professional development highlights the organic process through which market-based forces of accountability and competition incentivise professionals to associate, determine rules of membership and conduct and thereby create a self-regulatory framework for their profession. The regulatory framework created by IBBI has however limited the role that these market forces can play in promoting self-regulation in the IP profession. This limitation is best exemplified in the following features of the regulatory framework:

1. *High entry barriers*: The *IBC 2016* gives the IBBI the discretion to decide the eligibility requirements for IPs. The *Insolvency and Bankruptcy Board of India (Insolvency Professionals) Regulations, 2016* allow lawyers, chartered accountants, company secretaries and cost accountants to be IPs. IBBI has not put forward any rationale for explaining why persons with other qualifications or skills are not eligible to be IPs. This is in addition to the qualifying exam that every candidate must clear before being eligible to be registered as an IP. In addition, only professionals from these fields who have a minimum of ten years of experience are eligible.

Similar entry barriers exist with regard to IPAs in the form of net-worth requirements and domestic ownership, that have a tenuous relationship with the stated regulatory objectives under the *IBC 2016*. The IBBI has not published any documents explaining the linkage of these restrictions to its regulatory objectives.

2. *Limits on competition*: IPs have to be pre-existing professionals with a certain degree of experience. The regulatory framework limits the list of professionals who are eligible to become IPs. It is worth noting here that the original intent of Committee in proposing a new profession was to overcome the problems in service delivery of existing professions involved in the insolvency process in India. However, the existing regulatory framework does not permit persons with any new professional expertise to be considered eligible for work as an IP. Considering that the IBBI conducts qualifying examinations, this additional restriction on eligible qualifications is anti-competitive. Secondly, this has the effect of placing the primary responsibility of professional development on the IBBI rather than competitive forces.

Though the *IBC 2016* requires the IBBI to create a competitive system of IPAs, the specific historical context in which the law was enacted required some compromises. For one, the IBBI could not have waited for persons to come forward voluntarily to form IPAs. The IBBI had to encourage existing professional organisations to become IPAs. Since existing professional regulatory bodies (ICAI, ICSI, etc.) were asked to become IPAs, it is entirely possible that new IPAs may not come about barring the entry of new professional *skills* in the industry.

3. *State-led professional development*: The Committee envisioned professional development among IPs as largely market determined, with the IBBI playing the role of the overseer of the market. The mere existence of the IBBI has however made it the most powerful and effective institution in this market. As a statutory body responsible to Parliament, it is also the most accountable institution of the others that exist in this market. As a consequence, the development of the profession has so far been driven largely by IBBI.

The existing IPAs mostly seem to function as clubs and look identical to each other in terms of the codes of conduct and eligibility criteria for their members. It is difficult to understand what kind of regulatory roles they are really playing. Further, their Bye-laws are prescriptive regarding their governance structures. Detailed codes of conduct exist for IPs, and there is a rigidity to the membership of the IP profession (as limited by IBBI regulations).

This has important implications for how one should think about frameworks of accountability with respect to IPs. It is important to consider whether the issues in the functioning of IPs are due to professional negligence, or the overall market ecosystem as shaped by IBBI regulations. If both factors have a role, it is important to consider the relative impact of each. In the subsequent work in this paper we intend to argue that professional development requires a different regulatory approach from the regulation of other economic institutions such as utilities and market infrastructure.

## **6 Understanding professional development: a literature review**

In this section we plan to study the relevant literature on the development and regulation of other professions as well as the insolvency profession in other jurisdictions such as the UK and Canada. The objective here is to draw lessons about how IP regulation in India can be modified going forward so as to deliver better outcomes.

## **7 Analysis of current regulatory structure based on interviews**

So far our understanding of how the IPs are regulated today is based on readings of the law and subordinate legislation and the information available on the IPAs' websites. As a next step, we plan to supplement this through detailed interviews of existing IPs and IPAs with an objective to get a clearer picture of how the regulation of IPs is playing out in reality, especially the roles played by IBBI, IPAs and market forces.

## **8 Conclusion**

IP profession was created by IBC to fill up a vacant jurisdiction. The entire regulatory edifice of this industry has been clearly laid out in the law instead of evolving organically and gradually. This adds a certain rigidity to the manner in which IPs are regulated today. In this context we analyse the factors shaping the regulation as well as development of the IP profession in India and draw lessons for possible policy recommendations.

IPs play a critical role in IBC processes. These professionals need to be regulated because they act as agents of the state and because lack of trust in their services would lead to an erosion of trust of the overall insolvency resolution process. The BLRC laid down a tripartite regulatory structure wherein the IPs would be regulated by multiple, competitive SROs or IP agencies, who in turn would be regulated by the state. BLRC further envisaged that the IPAs would act as mini-states with well-defined legislative, executive, and quasi-judicial functions, rather than as clubs with no accountability. What we find so far in the nascent IP industry in India is that the IPAs are doing just the opposite. They are operating mostly as clubs whereas the actual function of regulating the IPs is being performed by the IBBI. This is effectively the same as having a single, national regulator who sets and enforces standards of conduct for all

the professionals in a sector, a flawed design that is prevalent in the existing professions of lawyers, doctors and accountants and one that has consistently proved to be inadequate. This is precisely the flaw in regulatory design that BLRC aimed to avoid when it recommended a framework of multiple SROs that would compete with each other.

If consumer trust in IPs is to be developed and maintained, IP SROs have to be mandated to ensure that disciplinary actions against errant members are conducted impartially and efficaciously. Today there are three IPAs registered with the IBBI and from the information available so far from their websites they do not seem to be faring too well on the regulatory functions that are expected of them. There are already a litany of allegations about misbehaviour by the IPs in less than two years and the IPAs seem to have no enforcement effort or outcomes.

We argue that this is primarily because of the way the IPAs were set up. Given the urgency with which the law had to be implemented there was little scope and time to create well designed and well functioning institutions to support the working of the law. As a result the IBBI ended up registering existing SROs as IPAs despite their legacy issues. The high entry barriers specified in the IBBI's regulations also seem to discourage the setting up of private IPAs. Consequently the IP industry now has three SROs which look identical to each other in terms of the codes of conduct and eligibility criteria for their members. One key feature of the BLRC's regulatory design was competition among the IPAs. It is unclear to what extent today's IPAs are competing against each other to get the best IPs as their members.

Over time as the profession evolves, it will devise its own norms and codes of conduct that are suited to the changing needs of the clients and these need to manifest themselves through the competitive model of multiple IPAs. State intervention can retard, if not inhibit this process. The primary role of the IBBI in this context should be to effectively shape the incentives of IPAs in order to produce the best possible outcome for the final clients. The IBBI needs to provide enough leeway for the IPAs to compete on parameters such as quality of members, entry requirements, codes of conduct and quality of grievance redress.

In summary, we argue that while there is a role for the state in regulating the IPs, market forces are also likely to contribute significantly to the development of the profession, especially in holding the IPs accountable. The constant interaction between state regulation and market forces will play a critical role in shaping the profession. The IBBI needs to evaluate the relative strengths of the different accountability mechanisms in the market. As the profession develops further, IBBI may need to exercise greater forbearance in favour of the market led accountability mechanisms and let the IPAs play a more important role in regulating the IPs.

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