CHAPTER – V

ROLE OF GOVERNMENT AND OTHER AGENCIES IN CORPORATE GOVERNANCE IN INDIA

5.1 Role of Government in Corporate Governance in India

Recent corporate scandals have led to public pressure to reform business practices and increase regulation. Of course, dishonesty, greed, and cover-ups are not new societal concerns. The public outcry over the recent scandals have made it clear that the status quo is no longer acceptable; the public is demanding accountability and responsibility in corporate behaviour. It is widely believed that it will take more than just leadership by the corporate sector to restore public confidence in our capital markets and ensure their ongoing vitality. It will also take effective government action, in the form of reformed regulatory systems, improved auditing, and stepped up law enforcement.

These responses make clear that the governance of corporations has become a central item on the public policy agenda. The recent scandals themselves demonstrate that lax regulatory institutions, standards, and enforcement can have huge implications for the economy and for the public. Of course, government responses to scandals should be well considered and effective. Regulatory reforms that overreact or that address symptoms while ignoring underlying causes can be costly and counterproductive. Government’s task is to restore corporate integrity and market confidence without stifling the dynamism that underlies a strong economy.¹

5.1.1 Role of Government in Prevention of Oppression and Mismanagement

Oppression and mismanagement is part and parcel of business. During the course of business, oppression of small/minority shareholders takes place by the majority shareholders who are in control of the company. Oppression is the exercise of authority or power in a burdensome, cruel, or unjust manner.² It can


also be defined as an act or instance of oppressing, the state of being oppressed, and the feeling of being heavily burdened, mentally or physically, by troubles, adverse conditions, and anxiety. The general rule is that the decisions of the majority shareholders in a company bind the minority. This has long been recognised in a landmark ruling "Foss v Harbottle"\(^3\) which is popularly recognised as the Rule in Foss v Harbottle or rule of majority. The directors are elected by the majority shareholders and therefore the directors become an instrument in the hands of majority shareholders. Mismanagement therefore occurs through this instrumentation. As far as oppression is concerned, the majority shareholders are required to respect the rights of minority shareholders. Whenever the rights of minority shareholders are violated it leads to oppression. The right of the majority to have their way has, however, been occasionally abused and the whip of the majority has often produced sullen effects prejudicial to the best interest of the shareholders. Sometimes a group of unscrupulous persons or a particular person may obtain control of the affairs of the company by purchasing majority shares and run the company in a manner prejudicial to the interest of the company or minority shareholders. In such a case, a proper balance of rights of the majority and minority shareholders is essential for the smooth functioning of the company.

Similarly, mismanagement of business is not uncommon. The term ‘Mismanagement’ has not been defined by the Companies Act. When the affairs of the company are being conducted in a manner prejudicial to the interest of the company or its members or against the public interest, it amounts to mismanagement. When we talk of mismanagement we mean mismanagement of resources. Mismanagement could mean siphoning of funds, causing losses due to rash decision, not maintaining proper records, not calling requisite meetings. Finer version of mismanagement could arise where the management does not act/react to a business situation leading to downfall of business. The oppression of minority or mismanagement calls for some remedial action. In such a case, the minority shareholders may apply to the National Company Law Tribunal for the winding up of the company on the ground that it is ‘just and equitable’ to do so or

\(^3\) (1843) 2 Hare 461.
apply for appropriate relief which is short of winding up. The shareholders may also apply to the central government for appropriate relief.4

5.1.2 Meaning of Oppression

As regards meaning of the term ‘oppression’ Lord Cooper observed in *Elder v. Elder & Watson Ltd.*5 “The essence of the matter seems to be that the conduct complained of should at the lowest involve a visible departure from the standards of fair dealing, and a violation of the conditions of fair dealing, and a violation of the conditions of fair play on which every shareholder who entrusts his money to the company is entitled to rely.”

As per the Supreme Court in *Kalinga Tubes Ltd. v. Shanti Prasad Jain*6 ‘oppression’ involves at least an element of lack of probity or fair dealing to a member in the matter of a property right as a shareholder. However, to constitute oppression the complainant member must show that he is suffering from oppression in the capacity of a member and not in any other capacity. Thus, in *Lundi Brothers Ltd.*,7 Re a minority shareholder was removed from his position as a working director. It was held that a complaint for oppression could not be entertained because he had suffered as director and not as a member. However, in *Naresh Trehan v. Hymatoo Agro Equipments Pvt. Ltd.*,8 it was held that in a family concern, removal of shareholder-director from directorship of the company was held to be an act of oppression.

The substance of the matter is that ‘oppression’ or ‘oppressive conduct’ means not keeping to the accepted standards of honesty and fairness and a lack of regard of other shareholders’ interest. More succinctly it has been stated that the complaining shareholder must be under a burden which is unjust or harsh or tyrannical. A persistent and persisting course of unjust conduct must be shown. In *Ramashankar v. S.I. Foundary*9 it was held that where allegations of this nature

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5 (1952) S.L.T. 112.
6 (1665) 35 Comp. Cas. 35.
7 [1965] 1 WLR 1050.
are made in the petition and substantiated, the company can even be ordered to purchase the minority’s shares at a fair value.

In Broadcast Station 2 G.B. Pty., Re it was held that one single and solitary instance of any act does not seem to answer the oppressive continuity of conducting the affairs of the company implicit in the construction of the language of sec. 397, viz., ‘the affairs are being conducted’. Where there is an isolated act of oppression, an injunction may be obtained under the general law.

In Needle Industries (India) Ltd. v. Needle Industries Newey (India) Holding Ltd., The Supreme Court observed in this regard: “The true position is that an isolated act, which is contrary to law, may not necessarily and by itself support the inference that the law was violated with a mala fide intention or that such violation was burdensome, harsh and wrongful. But a series of illegal acts following upon one another can, in the context, lead justifiably to the conclusion that they are part of the same transaction, of which the object is to cause or commit the oppression of persons against whom those acts are directed.”

The Supreme Court in Daleant Carrington Investment (P) Ltd. v. P.K. Prathapan, held that increase of share capital of a company for the sole purpose of gaining control of the company, where the majority shareholder is reduced to minority, would amount to oppression. The director holds a fiduciary position and could not on his own issue shares to himself. In such cases the oppressor would not be given an opportunity to buy put the oppressed.

5.1.3 Prevention of Oppression

Section 397(1) of the Companies Act provides that any member of a company who complains that the affair of the company are being conducted in a manner prejudicial to public interest or in a manner oppressive to any member or members may apply to the NCLT for appropriate relief. Sub-section (2) of Section 397 lays down the circumstances under which the tribunal may grant relief under Section 397, if it is of opinion that:

10 (1964-1965) N.S.W.R. 1648.
12 Supra n. 1 at 451-452.
the company’s affairs are being conducted in a manner prejudicial to public interest or in a manner oppressive to any member or members; and

to wind up the company would be unfairly and prejudicial to such member or members, but that otherwise the facts would justify the making of a winding up order on the ground that it was just and equitable that the company should be wound. The tribunal with the view to end the matters complained of, may make such order as it thinks fit.

5.1.4 Application to the National Company Law Tribunal

Section 397 of the Companies Act states the members of a company shall have the right to apply under Section 397 or 398 of the Companies Act. According to Section 399 where the company is with the share capital, the application must be signed by at least 100 members of the company or by one tenth of the total number of its members, whichever is less, or by any member, or members holding one-tenth of the issued share capital of the company. Where the company is without share capital, the application has to be signed by one-fifth of the total number of its members. A single member cannot present a petition under section 397 of the Companies Act. The legal representative of a deceased member whose name is again on the register of members is entitled to petition under Section 397 and 398 of the Companies Act.14

Under Section 399(4) of the Companies Act, the Central Government if the circumstances exist authorizes any member or members of the company to apply to the tribunal and the requirement cited above, may be waived. The consent of the requisite no. of members is required at the time of filing the application and if some of the members withdraw their consent, it would in no way make any effect in the application. The other members can very well continue with the proceedings.

5.1.5 Conditions for Granting Reliefs

To obtain relief under section 397 the following conditions should be satisfied:

I. There must be “oppression”- The Punjab and Haryana High Court in Mohan

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Lal Chandmal v. Punjab Co. Ltd\textsuperscript{15} has held that an attempt to deprive a member of his ordinary membership rights amounts to “oppression”. Imposing of more new and risky objects upon unwilling minority shareholders may in some circumstances amount to “oppression”.\textsuperscript{16} However, minor acts of mismanagement cannot be regarded as “oppression”. The Court will not allow that the remedy under Section 397 becomes a vexatious source of litigation.\textsuperscript{17} But an unreasonable refusal to accept a transfer of shares held as sufficient ground to pass an order under Section 397 of the Companies Act, 1956.\textsuperscript{18} Thus to constitute oppression there must be unfair abuse of the powers and impairments of the confidence on the part of the majority of shareholders.

**II. Facts must justify winding up**- It is well settled that the remedy of winding up is an extreme remedy. No relief of winding up can be granted on the ground that the directors of the company have misappropriated the company’s fund; as such act of the directors does not fall in the category of oppression or mismanagement.\textsuperscript{19} To obtain remedy under Section 397 of the Companies Act, the petitioner must show the existence of facts which would justify the winding up order on just and equitable ground.

**III. The oppression must be continued in nature** - It is settled position that a single act of oppression or mismanagement is sufficient to invoke Section 397 or 398 of the Companies Act. No relief under either of the section can be granted if the act complained of is a solitary action of the majority. Hence, an isolated action of oppression is not sufficient to obtain relief under Section 397 or 398 of the Act. Thus to prove oppression continuation of the past acts relating to the present acts is the relevant factor, otherwise a single act of oppression is not capable to yield relief.

**IV. The petitioners must show fairness in their conduct** - It is settled legal principle that the person who seeks remedy must come with clean hands. The members complaining must show fairness in their conduct. For example, Mere

\textsuperscript{15} AIR 1961 Punj. 485.
\textsuperscript{16} Re, Hindustan Cooperative Insurance Society Ltd.,(1961) 31 Comp. Cas. 193.
\textsuperscript{17} Lalita Rajya lakshmi v. Indian Motor Co.,AIR 1962 Cal. 127.
\textsuperscript{18} Gajabai v. Patni Transport Co.,(1965) 2 Comp. L. J. 234.
\textsuperscript{19} Palghat Exports Ltd. v. F.V. Chandran , (1994) 79 Comp. Cas. 213 Ker.
declaration of low dividend which does not affect the value of the shares of the petitioner was neither oppression nor mismanagement in the eyes of law.\textsuperscript{20}

**V. Oppression and mismanagement should be specifically pleaded** - It is settled law that, in case of oppression a member has to specifically plead on five facts:

\begin{itemize}
  \item a) what is the alleged act of oppression;
  \item b) who committed the act of oppression;
  \item c) how it is oppressive;
  \item d) whether it is in the affairs of the company; and
  \item e) whether the company is a party to the commission of the act of oppression.\textsuperscript{21}
\end{itemize}

5.1.6 **Judicial Decisions on Oppression**

It is analyzed that to constitute "oppression" and "mismanagement" facts of each case would be relevant. The oppression in one situation may not be in another. Given below are some of the judicial decisions, which could have persuasive value:

I. **Single act can constitute oppression:** A single act of oppression which has its continuous impact could also constitute oppression. It was held in *Sindhri Iron Foundry (P) Ltd.*,\textsuperscript{22} that "affairs are being conducted" has been judicially interpreted to include past and concluded act which has a continuous impact. It was held in *Tea Brokers Pvt. Ltd. v. Hemendra Prasad Baroah*,\textsuperscript{23} that a single act was capable of causing perpetual damage like removal from directorship and allotment of new shares was held to be oppressive.

II. **Acts have to be considered as part of a consecutive story:** In *Shanti Prasad Jain v. Kalinga Tubes Ltd.*,\textsuperscript{24} it was held that events of oppression have to be a part of consecutive story and not in isolation to constitute "oppressive" conduct of the majority.

\textsuperscript{21} Dinesh Sharma and another v. Vardeen Agrotech (P) Ltd. and others ,(2007) 1 Comp. L.J. 155 (CLB).
\textsuperscript{22} (1964) 34 Comp. Cases 510.
\textsuperscript{23} (1998) 5 Comp. L.J. 463 (Cal).
\textsuperscript{24} (1965) 35 Comp. Cases 351 also see Needle Industries (India) Ltd. and Others v. Needle Industries Newey (India) Holding Ltd. (1981) 51 Comp. Cases 743; G. Kasturi v. N. Murali (1992) 74 Comp. Cases 661 (Mad).
III. Acquisition of shares in market cannot constitute oppression: It was held in *Mohta Bros. (P) Ltd. v. Calcutta Landing and Shipping Company Ltd. and Others*\(^{25}\) that acquisition of shares in the market cannot constitute oppression to minorities.

IV. Lack of transparency, probity and fairness to gain majority control constitute oppression: In *Hemant Vakil and other v. RDI Print and Publishing (P) Ltd.*\(^{26}\) a group of shareholders gained management control by lack of transparency, probity and fairness where they increased the shareholding which was set aside and it was held to constitute oppression.

V. Issue/Allotment of shares - majority reduced to minority: In *Mrs. Rashmi Seth v. Chemin (India) Pvt. Ltd.*\(^{27}\) It was held that one of the ways a group of shareholders oppress other groups is to issue and allot shares to themselves in an illegal manner. Courts/Company Law Board has been very critical of these actions and has consistently held these to be oppressive in nature. These allotments have been set aside and status quo ante restored.

VI. Termination of distributorship agreement in which a shareholder is interested: The Company Law Board in *M. L. Thukral v. Kone Communication Ltd.*\(^{28}\) did not interfere in a matter concerning termination of distributorship agreement which it felt was the powers of Board of Directors and outside the purview of section 397/398.

VII. Omission to give notice and short notice of meeting: One of the common types of oppression/mismanagement is not sending notices to shareholders/directors and passing resolutions thereat. These have by and large being held to be "oppressive" to members and constitute mismanagement of companies. It will be interesting to note that "proofs" of sending notices by "UPC" were not relied upon by the Company Law Board as circumstances clearly pointed out to the contrary. The Company Law Board gave directions to end this

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\(^{25}\) (1969) 2 Comp. LJ. 157 (Cal).
\(^{26}\) (1993) 2 Comp. LJ. (CLB).
\(^{27}\) (1992) 3 Comp. Cases LJ. 89 (CLB).
oppression/mismanagement. But Company Law Board, in *Shantidevi P. Gaikwad v. Sangramsingh P. Gaikwad* held that the provisions in the act regarding length of notice are directory and not mandatory and giving of shorter notice will not invalidate the meeting or cause oppression.

**VIII. Issue of further capital and irregularity thereof:** The issue of further capital and impropriety in these issues have given rise to a lot of litigation under section 397/398. The Supreme Court in *Needle Industries (India) Ltd. v. Needle Industries Newey (India) Holdings Ltd.* held that where a group incidentally got control was not abuse of fiduciary powers of the directors but what would be objectionable would be the use of such powers merely for an extraneous purpose of gaining control. This case acts as a benchmark for many cases. In following cases, where minority has been converted to majority by way of new issues, the same is liable to be set aside on grounds that it was unfair, manipulative and oppressive.

**IX. Increase in directorship/Removal from directorship:** One of the common ways of controlling the board is to induct directors pertaining to one group. Similarly removal of directors pertaining to the other group is common. On this point Courts/Company Law Board has consistently held that where there is written agreement/oral understanding amongst the family members or groups, any new appointment or removal, which disturbs the parity amongst the family members or groups was held to be "oppressive" and liable to be set aside. This is in spite of the fact that proper procedure for appointment and removal under section 284 Companies Act 1956 has been followed. Courts/Company Law Board have time and again relied upon the principle of "quasi-partnership" as far as family owned private companies are concerned were participation of family members in the business is part and parcel of the management setup. But not all increase or removal of directors has been held to oppression.

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5.1.7 Prevention of Mismanagement

If a company is being run by the Board in their own interest overriding the wishes and interest of the majority of shareholders is deemed to be mismanagement held in *Re, Albert David*33. In *Asiatic Ltd. Re*34, Courts have also ruled that erosion of a company’s substratum abuse of fiduciary duties and misuse of funds in *Narain Das (K.) v. Bristol Grill (P.) Ltd.*35 Are all instances of mismanagement that come within the ambit of sec.398. Section 398(1) of the Companies act provides that any members of a company who complain:- that the affairs of the company are being conducted in a manner prejudicial to public interest or in a manner prejudicial to the interests of the company; or a material change has taken place in the management or control of the company, whether by an alteration in its Board of directors, or manager or in the ownership of the company’s shares, or if it has no share capital, in its membership, or in any other manner whatsoever, and that by reason of such change, it is likely that the affairs of the company will be conducted in a manner prejudicial to public interest or in a manner prejudicial to the interests of the company; may apply to the Company Law Board for an order of relief provided such members have a right so to apply as given below.

If, on any such application, the Company Law Board is of opinion that the affairs of the company are being conducted as aforesaid or that by reason of any material change as aforesaid in the management or control of the company, it is likely that the affairs of the company will be conducted as aforesaid, the court may, with a view to bringing to an end or preventing the matters complained of or apprehended, make such order as it thinks fit.

5.1.8 Who May Apply for Relief under Sec. 397/398

1. The following members of a company shall have the right to apply as above:

a) in the case of a company having a share capital, not less than one hundred members of the company or not less than one tenth of the total number of its

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33 (1964) CWN 163, 172.
34 (1994) 3 Comp LJ 294 (CLB).
members, whichever is less, or any member or members holding not less than
one-tenth of the issued share capital of the company, provided that the applicant or
applicants have paid all calls and other sums due on their shares;
b) in the case of a company not having a share capital, not less than one-fifth of
the total number of its members.
2. Where any share or shares are held by two or more persons jointly, they
shall be counted only as one number.
3. Where any members of a company, are entitled to make an application,
any one or more of them having obtained the consent in writing of the rest, may
make the application on behalf and for the benefit of all of them.
4. The Central Government may, if in its opinion circumstances exist which
make it just and equitable so to do, authorize any member or members of the
compny to apply to the Company Law Board, notwithstanding that the above
requirements for application are not fulfilled.
5. The Central Government may, before authorizing any member or members
as aforesaid, require such member or members to give security for such amount as
the Central Government may deem reasonable, for the payment of any costs
which the Court dealing with the application may order such member or members
to pay to any other person or persons who are parties to the application.
6. If the managing director or any other director, or the manager, of a
company or any other person, who has not been impleaded as a respondent to any
application applies to be added as a respondent thereto, the Company Law Board
may, if it is satisfied that there is sufficient cause for doing so, direct that he may
be added as a respondent accordingly.
5.1.9 Notice to be given to Central Government of application
According to section 400 The National Company law Tribunal must give
notice of every application made to it as above to the Central government, and
shall take into consideration the representations, if any, made to it by that
Government before passing a final order.
5.1.10 Right of Central Government to apply
Under section 401, The Central Government may itself apply to the
Company law Board for an order, or because an application to be made to the
National Company Law Tribunal for such an order by any person authorized be it in this behalf.

5.1.11 Powers of Central Government to prevent oppression or mismanagement

5.1.11.1 Appointment of directors by the Central Government:

The Central Government may appoint such number of persons as the National Company Law Tribunal may, by order in writing, specify as being necessary to effectively safeguard the interests of the Company or its shareholders or public interests, to act as directors thereof for such period not exceeding 3 years on any one occasion as it deems fit if the National Company Law Tribunal: On a reference being made to it by the Central Government; or on an application of not less than one hundred members of the company or of members of the company holding not less than one-tenth of the total voting power therein, is satisfied, after such inquiry as it deems fit to make, that it is necessary to make the appointment or appointments in order to prevent the affairs of the company being conducted either in a manner which is oppressive to any members of the company or in a manner which is prejudicial to the interests of the company or to public interest.

The verb ‘satisfy’, in the context in which it is used, means that there must be sufficient evidence and the standard of proof that is required is the proof which ordinarily satisfies any unprejudiced mind beyond reasonable doubt, objectively and not subjectively as held in Peerless General Finance & Investment Co. Ltd. v. Union of India.37

However, in lieu of passing order as aforesaid, the National Company Law Tribunal may, if the company has not availed itself of the option given to it of proportional representation to minority shareholders on the Board of the company, direct the company to amend its articles in the manner provided section 265 and make fresh appointments of directors in pursuance of the articles as so amended within such time as may be specified in that behalf by the National Company Law Tribunal.

In case the Central Government passes such an order it may, if thinks fit, direct that until new directors are appointed in pursuance of the order aforesaid,

36 Section 408(1) of the Companies Act, 1956.
37 (1991) 71 Comp. Cas. 300 (Cal.).
not more than two members of the company specified by the Company law Board shall hold office as additional directors of the company. The Central Government shall appoint such additional directors on such directions.

The person appointed as a director by the Central Government in accordance with the above provisions, need not hold any qualification shares or need to retire by rotation. However, his office as director may be terminated at any time by the Central Government and another person appointed in his place. No change in the constitution of the Board of Directors can take place after an additional director is appointed by the Central Government in accordance with these provisions unless approved by the National Company Law Tribunal. The Central Government in such cases may also issue such directions to the company as it may consider necessary or appropriate in regard to its affairs.

*Union of India v. Satyam Computers Services Ltd. & Ors.*

The Respondent Company indulged in grave financial mismanagement practices due to which its Chairman resigned. The Central Government applied to the CLB for the removal of the Board of directors and to appoint its directors to manage the respondent company.

“It was held that the petitioner has sufficient grounds to invoke the provisions of section 388B/397/398 and 408 of the Companies Act, 1956. The written admission of the second respondent, who is the chairman of the company, establishes beyond any shadow of doubt that there have been financial impropriety and jugglery of financial statements, with the view to mislead the stakeholders, employees and the public in general. It appears that a serious fraud has been perpetrated on the society as a whole. The manner in which the affairs of the company have been conducted has shaken the confidence of the public in the company as is evident from the fall in the share price of the company on 7.1.2009 from ` 188 to 38.40. As indicated above, the company is the fourth largest IT Company in India. It has clients in over 60 countries and also has over 53,000 employees and has nearly 3 lakh shareholders. Their interests along with the interests of the company have to be protected. The public interest at large is also at stake.”

The need of the hour is to be to create confidence in the minds of all those connected with the company in any capacity and also to assure that

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38 (2009) 1Comp LJ 308(CLB).
regulatory/judicial mechanism in India is alive and active to take immediate and positive steps in case of needs. The present state of affairs of the company is such, that there could not be a better case, wherein, this Board, in exercise of its powers under sections 388C/403 of the Act, is obligated under the law to regulate the affairs of the company on an urgent basis.

Therefore, in the interests of the members, employees, customers of the company and also in the larger public interest, the interim relief sought should be granted ex parte. Accordingly, it is directed/ordered, inter alia, as follows:

(i) the present board of directors stands suspended with immediate effect. None of the present directors shall represent himself to be a director of the company and shall also not exercise any powers as a director.

(ii) On the authority of this order, in the name and on behalf of the Board, the Central Government shall immediately constitute a fresh board of the company with not more than 10 persons of eminence as directors. The Central Government may also designate one of them as the chairman of the board. This board shall be entitled to exercise and discharge all powers vested in the board by the articles and the Act. The said constitution shall be notwithstanding anything contrary contained in the articles, the Act, listing agreement or any other law/regulations relating to the constitution of the board of a listed company. The said board will continue till further orders.

(iii) The newly constituted board shall meet within seven days of its constitution and take necessary immediate action to put the company back on the road.

(iv) It shall submit periodical reports to the Central Government, with a copy to this Board on the state of affairs of the company.

(v) The petitioner is permitted to file additional affidavits that may become necessary after further investigations/enquiries into the affairs of the company.39

5.1.11.2 Other Directions by the Central Government to the Company

Where the power of appointing directors is exercised by the Central Government in reference to a company, it may issue necessary directions to the company as to its affairs. Such directions may include the following:

(i) To remove an auditor already appointed and to appoint another auditor in his place, or

(ii) To alter the articles of the company.

Upon such directions being given, the appointment, removal or alteration, as the case may be, shall be deemed to have come into effect as if the provisions of this act in this behalf have been complied with without requiring any further act or thing to be done.

5.1.11.3 Report to the Central Government

The Central Government may require the persons appointed as directors to report to it from time to time with regard to affairs of the company. The Central Government must be careful while exercising power under section 408. The Central Government must take care to see that sec. 408 is not invoked lightly by the disgruntled shareholders to satisfy their own private ends. ‘Prejudice’ to the interests of a company will be judged by minimum standard of good management required of all companies as held in South India Viscose Ltd. v. Union of India.\(^{40}\)

5.1.11.4 Power of the Central Government to Remove Managerial Personnel

Section 388-B to 388-E empower the Central Government to remove managerial personnel from office on the recommendation of the National Company Law Tribunal. The Central Government may state a case against the managerial personnel of a company and refer the same to the Tribunal with a request that the Tribunal may enquire into the case and record a finding weather he is a fit or proper person to hold the office of director or any other office connected with the conduct and management of the company. At the conclusion of the hearing of the case, the National Company Law Tribunal shall record its findings. The person removed shall not hold the office of a director or any other office connected with the conduct and management of the company for a period of 5 years. The Central Government may, with the previous concurrence of the

\(^{40}\) (1982) 52 Comp. Cas. 247.
National Company Law Tribunal shall, remit or relax this period of 5 years. On the removal of a person from office, no compensation shall be payable to him for the loss or termination of the office. The company may, with the previous approval of the Central Government, appoint another person to the office in the place of the person removed.

5.1.12 The Companies Act 2013 on Oppression and Mismanagement

The Companies Act, 2013 provides for provisions relating to oppression and mismanagement under Sections 241-246 in the chapter XVI of the Companies Act. Section 241 provides that an application for relief can be made to the Tribunal in case of oppression and mismanagement. Section 244(1) provides for the right to apply to Tribunal under Section 241, wherein the minority limit is same as that mentioned in the companies Act, 1956. Under The Companies Act, 2013, the Tribunal may also waive any or all of the requirements of Section 244(1) and allow any number of shareholders and/or members to apply for relief. This is a huge departure from the provisions of The Companies Act, 1956 as the discretion which was provided to the Central Government to allow any number of shareholders to be considered as minority is, under the new Companies Act, 2013 been given to the Tribunal and therefore is more likely to be exercised.\(^{41}\) Class Action is one of the youngest additions to Indian jurisprudence particularly, in Indian Corporate Jurisprudence. Class Action aims to prevent Oppression and Mismanagement in Companies.\(^{42}\)

5.1.12.1 Application In Case Of Oppression & Mismanagement:\(^{43}\)

Any member, who has right to apply under Section 244, may apply to the Tribunal under Section 241. An application may be filed for a complaint that:

i. The affairs of the company have been or are being conducted in a manner prejudicial to the public interest, or in an manner prejudicial or oppressive to him or any other member or members, or in a manner prejudicial to the interests of the company; or


\(^{42}\) [http://aishmghrana.me/2013/06/14/oppression-mismanagement/](http://aishmghrana.me/2013/06/14/oppression-mismanagement/) (Visited on November 15, 2015).

\(^{43}\) Section 241 of Companies Act, 2013.
ii. The material change has taken place in the management or control of the company, whether by; An alteration in the Board of Directors, or Manager, or in the ownership of the company’s share, or If it has no share capital, in its membership, or in any other manner whatsoever, and that by reason of such change, it is likely that the affairs of the company will be conducted in a manner prejudicial to its interests or its members or any class of members. These changes should not be a change brought about by, or in the interests of, any creditors, including debenture holders or any class of shareholders of the company. The Central Government, if it is of the opinion that the affairs of the company are being conducted in a manner prejudicial to public interest, it may itself apply to the Tribunal.

5.1.12.2 Right to Apply

In case of company having sharing share capital: Not less than one hundred members of the company, or Not less than one – tenth of the total numbers of its members, whichever is less shall have right to apply under Section 241. However, any member or members holding not less than one – tenth of the issued share capital of the company, subject to the condition that the applicant or applicants has or have paid all calls and other sums due on his or their shares, shall also have right to apply under Section 241. In case of a company not having a share capital, not less than one – fifth of the total number of its members shall have right to apply under Section 241. Tribunal may, on an application made to it in this behalf, waive all or any of the requirements specified, so as to enable the members to apply under section 241. Where any members of a company are entitled to make an application, any one or more of them having obtained the consent in writing of the rest, may make the application on behalf and for the benefit of all of them.

5.1.12.3 Power of Tribunal

On any application made under Section 241, the Tribunal shall frame its opinion on two points:

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44 Ibid.
45 Section 242(1&3) of Companies Act, 2013.
(a) that the company’s affairs have been or are being conducted in a manner prejudicial or oppressive to any member or members or prejudicial to public interest or in a manner prejudicial to the interests of the company; and
(b) that to wind up the company would unfairly prejudice such member or members, but that otherwise the facts would justify the making of a winding-up order on the ground that it was just and equitable that the company should be wound up, the Tribunal may with a view to bringing to an end the matters complained of, make such order as it thinks fit. A certified copy of the order of the Tribunal under sub-section (1) shall be filed by the company with the Registrar within thirty days of the order of the Tribunal. This means the Tribunal has unlimited power under this Section. However, this Section asks the Tribunal to give particular details in its order.\textsuperscript{46}

5.1.12.4 Class Action Suits\textsuperscript{47}

Section 245 provides for class action to be instituted against the company as well as the auditors of the company. The Draft Companies Rules allow for this class action to be filed by the minority shareholders under Clause 16.1 of Chapter-XVI. This provision not only empowers the minority shareholder and/or members of the company but also the depositors. Unlike Section 399 of The Companies Act, 1956 which provides for protection to only shareholder/members of the company, Section 245 of The Companies Act, 2013 also extends this protection to the class of depositors as well. However, in the current scenario, the provision of representation of a class of members or depositors by a particular member or depositor lacks clarity.\textsuperscript{48}

Sub-section (1) of Section 245 provides, "such number of member or members, depositor or depositors or any class of them, as are indicated in sub-section (2) may, if they are of the opinion that the management or conduct of the affairs of the company are being conducted in a manner prejudicial to the interests of the company or its members or depositors, file an application before the Tribunal on behalf of the members or depositors for seeking all or any

\textsuperscript{46} Supra n. At 39.
\textsuperscript{47} Section 245 of Companies Act, 2013.
of the following orders …". Besides, there being a typographical error in this sub-section (1) with respect to indicating sub-section (2) instead of sub-section (3) which provides for the minimum number of members who can apply for class action there is also some confusion as to the class on whose behalf such class action can be instituted. While 'member has been defined in The Companies Act, 2013 as including the subscriber to the memorandum of the company, shareholders and person whose name is entered in the register of members; definition for depositor is not provided under The Companies Act 2013.

Further, section 245 does not empower the Tribunal with discretionary power to admit/allow any class suit wherein class of members or depositors are unable to comply with the minimum number of members/depositors requirement to be laid down in the Companies Rules. Also, on a close reading of Section 241 and Section 245 of The Companies Act, 2013, we can find duplication in protection provided to the members in case affairs of the company are conducted in a manner prejudicial to the interest of the company/members.

Upon careful examination of the provisions of The Companies Act, 2013 it can be ascertained that legislative intent in The Companies Act, 2013 is to safeguard the minority interest in a more comprehensive manner. However, the provisions of Companies Act, 2013 not only requires proper implementation upon addressing the present lacunas but also requires instilling confidence in the minority shareholders with respect to the institutional and regulatory mechanism which ensures that interest of minority shareholders shall be given due consideration. This dual approach towards enforcement of minority rights shall only guarantee proper administration of the corporate activities. Nevertheless, Ministry of Corporate Affairs' effort in preparation of a framework, which endeavours to empower minority shareholders, is commendable.  

5.1.13 **Amalgamation of Companies in National Interest**

Section 396 is intended to provide, at the instance of the Central Government, for the amalgamation of two or more companies in the national interest.

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49 Ibid.
5.1.13.1 Satisfaction of Central Government

Where the Central Government is satisfied that it is essential in the public interest that two or more companies should amalgamate, it may, by order notified in the Official Gazette, provide for the amalgamation of these companies into a single company.

5.1.13.2 Continuation of Legal Proceedings

The order of the Central Government may provide for the continuation by or against the transferee company of any legal proceedings pending by or against any transferor company. It may also contain such consequential, incidental and supplemental provisions as may be necessary to give effect to the amalgamation.

5.1.13.3 Preservation of Books and Papers of Amalgamated Company

Under section 396-A the books and papers of a company which has been amalgamated with, or whose shares have been acquired by, another company under secs.391-396 shall not be disposed of without the prior permission of the Central Government. Before granting any such permission the Central Government may appoint a person to examine the books and papers for the purpose of ascertaining whether they contain any evidence of the commission of an offence in connection with the promotion or formation, or the management of the affairs, of the first-mentioned company or its amalgamation or the acquisition of its shares. This provision is intended to prevent the practise of destroying incriminating accounts and records of the company which has been amalgamated with another company. The permission of the Central government has to be obtained before any such records are destroyed.

5.1.14 Petition for Winding up by The Central Government\(^{50}\)

Under section 243 the Central Government may cause to be presented to the NCLT, by any person authorised by it in this behalf, a petition for winding up of a company where it appears from the report of inspectors appointed to investigate the affairs of the company under sec.235 that the business of the company is being conducted with intent to defraud its creditors, members, or any other persons, or otherwise for a fraudulent or unlawful purpose, or in a manner

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\(^{50}\) Section 439(1)(f) of Companies Act, 1956.
oppressive of any of its members, or that the company was formed for any fraudulent or unlawful purpose.

5.1.14.1 Petition by the Central Government or a State Government

The petition may be filed where the company has acted against the interests of the sovereignty and integrity of India, the security of the state, friendly relations with foreign states, public order, decency or morality.

5.1.14.2 Winding up Petition by The Central Government under Companies Act, 2013

Under section 272 (1) Subject to the provisions of this section, a petition to the Tribunal for the winding up of a company shall be presented by any person authorised by the Central Government in that behalf; if the company has acted against the interests of the sovereignty and integrity of India, the security of the State, friendly relations with foreign States, public order, decency or morality; by the Central Government or a State Government.  

5.2 Role of Judiciary in Enforcing Corporate governance in India

The development of law relating to criminal liability has not only been similar to that in English Law, but also greatly influenced by the English law. At one point of time, corporations were viewed as convenient shield to evade liability. However under present penal structure, for an offence by the corporation, both the corporation and its officers can be made liable.

The United States Supreme Court in *New York Central & Hudson River Railroad Co. V. United States* stated the principle thus: - “it is true that there are some crimes which, in their nature, cannot be committed by corporations. But there is a large class of offences, of which rebating under the federal statute is one, wherein the crime consists in purposely doing the things prohibited by statute. In that class of crimes we see no good reason why corporations may not be held responsible for and charged with the knowledge and purpose of their agents, acting within the authority conferred upon them....”

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51 Clause (C) section 271 (1) of companies Act, 2013.
53 53 L ED 613.
54 supra n.1 at 40.
As in the Anglo-American system, the Indian legal framework allows for a significant role for the judiciary. For example, the primary corporate governance measures under the Companies Act are the statutory provisions protecting shareholders against "oppression" and "mismanagement." Shareholders can bring suit against a company's management or board of directors in cases of oppression and mismanagement, in order to protect shareholder interests. While Indian courts have developed extensive case law interpreting and applying the provisions of the Companies Act, these judicial judgments have not radically altered the state of corporate governance in India as Clause 49 has. In fact, some even argue that the lack of judicial action has meant that "India seems to have moved away from the common law tradition of changing the law on a case-by-case basis and toward the tradition of detailed rule-making backed by public enforcement mechanisms, which is usually associated with the civil law countries. The primary reason behind the lack of development of corporate governance standards through the judiciary is the failure of the Indian judicial system to effectively resolve corporate disputes. India's judicial process has long been the subject of criticism. According to a vocal critic of the Indian legal system, the judicial process involves countless delays, and when decisions are finally rendered by courts, they are often ignored. The defining feature of the Indian court system is the staggering delays involved in resolving a case by trial, which typically would take up to 20 years. Given the significant delays in bringing a suit, there is little incentive for shareholders to advocate for their rights through the courts. According to a recent report by the World Bank, the process under which cases brought pursuant to the Companies Act were adjudicated was similarly mired in delay and ineffectiveness. For example the Company Law Board (CLB), the primary judicial authority for enforcement of the Companies Act, experienced significant delays and a large backlog of cases. The delays at the CLB level were further compounded by the ability of parties to appeal CLB decisions to the High Courts and Supreme Court. The Companies (Second Amendment) Act, 2002, created a new National Company Law Tribunal (NCLT), along with its appellate body, the National Company Law Appellate Tribunal (NCLAT), to enforce the provisions of the Companies Act. The National Company Law Tribunal was also granted
jurisdiction with respect to matters previously distributed between several different government agencies, including management of "sick industrial companies" and the dismantling of unprofitable companies, a power that previously rested with the various Indian high courts.

Although the rulings of the Appellate Tribunal are still appealable to the Supreme Court of India under the new enforcement scheme, 22 the availability of a separate appellate body specifically tasked with handling appeals from the National Company Law Tribunal's rulings was intended to prevent the tremendous logjam of proceedings previously seen in the various high courts.

It is important to have a credible, independent and efficient judicial system to enforce corporate governance. A common problem, however, is the lack of judges’ and prosecutors’ expertise in corporate governance matters and financial market rules, plus a backlog attributable to the sheer volume of cases. While there may be a temptation to bypass the judicial system as much as possible, the complication is that the system is a foundation for public and private enforcement and is the ultimate legal authority in most jurisdictions. There are several solutions to the problem of a lack of judicial expertise or long, drawn-out cases filed in court. The first would be to ensure that regulators have additional powers, such as full investigative power, administrative alternatives including injunctions to stop and reverse actions short of or before going to court, and power to initiate enforcement actions against board members. This would reduce the burden on the courts to be involved in each step and improve timeliness for disposal of cases. The second solution would be to establish specialized business courts with the power to address civil and criminal breaches of securities laws. The advantage of specialized courts is that judicial officers’ knowledge and experience are continually enhanced. Indonesia’s experience with specialized courts dealing with corruption has contributed to the success of anti-corruption efforts by its Corruption Eradication Commission. The High Court in Malaysia has three new commercial courts to deal with banking, finance, insurance, admiralty and sale of goods cases, which has reduced time and costs for litigants. Empirical evidence shows that specialized business courts play an important role in providing a high level of minority-investor protection. Another solution is to improve court
procedures by encouraging judges to dispose of minor cases without unnecessary delays through setting key performance indicators for judges. It is important that judges’ decisions be well-written and published, to ensure their quality and integrity. Other methods to enhance quality would be to raise judges’ salaries, conduct performance management assessments established and monitored within the judiciary, and take steps to ensure their independence in order to insulate the judicial system from outside influence and interference. Regulators and ministries of justice should also work with judges and prosecutors to increase their knowledge of new laws and programs. Judges, prosecutors and the police should be given training to improve their understanding, which regulators can be facilitate through participation in international and domestic meetings, roundtable discussions, workshops and interagency task forces. Alternative dispute resolution (ADR) could also be explored. The Singapore International Arbitration Centre and the Hong Kong Market Misconduct Tribunal are examples of specialized entities that dispose of cases faster than conventional courts. Good practices Regulators in Thailand and Malaysia work closely with the Judges’ Organisation and the Judicial and Legal Training Institute in their respective jurisdictions to enhance judges’ knowledge on securities laws and related issues. Hong Kong’s Market Misconduct Tribunal is headed by a Chair who is a judge or former judge of the High Court. It determines whether market misconduct has occurred (insider dealing, false trading, price rigging, stock market manipulation, disclosure of information relating to prohibited transactions and disclosure of false or misleading information inducing transactions in securities and futures contracts. A recent Supreme Court of India Bench Mark judgement has announced that companies can be tried and punished. The Supreme Court has held that “a corporate body can be tried and punished with fine for committing financial irregularities including tax violations. Companies could no more claim immunity from persecution and courts could impose fines on them even though they cannot be sentenced.55 Legal analysts feel that companies could be tried and punished for committing financial irregularities, including tax violation. It was further held that

55 Supreme Court of India – Justice K.G. Balakrishnan, D.M Dharmadhikari and Arun Kumar-Times of India, New Delhi, Friday 6th May, 2005.
since these cases had an adverse impact on the economy as well as society, it was necessary that these companies face prosecution along with those who perpetrated the crime. Therefore there is always need for transparency and professionalism in corporate governance.\textsuperscript{56}

Having investigated a case of serious fraud, it then remains for the evidence to be presented to the relevant prosecution agency. It is at this point that serious fraud cases often founder, as prosecutors may believe that the evidence presented to them is inadequate or that the chances of success are insufficient to justify the time and expense involved in a lengthy trial. In 1992 the High Court of Australia in the case of \textit{Dietrich v The Queen}\textsuperscript{57} ruled that, unless exceptional circumstances exist, where a genuinely indigent accused person is unrepresented by counsel at a trial for a serious offence, the trial will be considered to be unfair and should be adjourned until legal representation is made available. Few individuals are able to afford the costs associated with a long and complex criminal trial. Defendants charged with serious fraud are often able to arrange their financial circumstances in such a way as to make them appear indigent and thus able to take advantage of the Dietrich ruling. The effect may well be that a long and complex investigation will be stayed indefinitely. Because many fraud offences do not involve face-to-face interactions in their commission, it is possible for offenders and victims to be located in more than one jurisdiction. More sophisticated conspiracies may involve individuals in three or more jurisdictions within Australia or overseas. Few remedies are available to the unfortunate individual who might fall victim to such activities. Even if one is able to mobilise the law, the chances of locating the fraudsters, obtaining extradition, mounting a prosecution, or recovering compensation may be impossible. Even where a perpetrator has been identified, two problems arise in relation to the prosecution of offences which have an international aspect: first, the determination of where the offence occurred in order to decide which law to apply; and, secondly, obtaining evidence and ensuring that the offender can be located and tried before a

\textsuperscript{56} \url{http://www.oecd.org/daf/ca/Public-Enforcement-Corporate-Governance-Asia.pdf} (Visited on July 10, 2015).
\textsuperscript{57} (1993) 67 ALJR 1.
court. Both these questions raise complex legal problems of jurisdiction and extradition.\(^{58}\)

While deciding a matter related to telecom, the Supreme Court in *Cellular Operators Association of India and Others v. Union of India and Others*\(^{59}\) made certain observations regarding the working of Telecom Regulatory Authority of India (TRAI) and Telecom Dispute Settlement Appellate Tribunal (TDSAT). These observations, mutatis mutandis, apply to other regulatory bodies and appellate tribunals also, and are as follows:

“\(\text{The regulatory bodies exercise wide jurisdiction. They lay down the law. They may prosecute. They may punish. Intrinsically, they act like an internal audit. They may fix the price, they may fix the area of operation and so on and so forth. While doing so, they may, as in the present case, interfere with the existing rights of the licensees. Statutory recommendations made by it are normally accepted by the Central Government, as a result of which the rights and obligations of the parties may seriously be affected. It was in the aforementioned premise the Parliament thought of creating an independent expert tribunal which, if an occasion arises therefore, may interfere with the finding of fact, finding of law or a mixed question of law and fact of the Authority. Succinctly stated, the jurisdiction of the tribunal is not circumscribed in any manner whatsoever.}\)"

The Supreme Court of India in *Sahara India Real Estate Corporation Limited and others v. Securities and Exchange Board of India and Another*\(^{60}\) held that On August 31, 2012, the Supreme Court held that Securities Exchange Board of India had jurisdiction over the Optionally Fully Convertible Debentures (OFCDs) issued by two companies of the Sahara group and directed Sahara to repay the investors, through Securities Exchange Board of India, as the money had been collected without following the regulatory and legal norms. Securities Exchange Board of India was ordered to verify the veracity of investors and make the payment. The court gave ten days to Sahara to submit the details of investors to Securities Exchange Board of India and three months to make the payment.

The Supreme Court observed in *Clariant v. SEBI*\(^{61}\) in 2004:

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“The Board exercises its legislative power by making regulations, executive power by administering the Regulations framed by it and taking action against any entity violating these regulations and judicial power by adjudicating disputes in the implementation thereof. The only check upon exercise of such wide ranging power is that it must comply with the Constitution and the Act. In that view of the matter, where an expert Tribunal has been constituted, the scrutiny at its end must be held to be of wide import. The Tribunal, another expert body, must, thus, be allowed to exercise its own jurisdiction conferred on it by the statute without any limitation.”

The Supreme Court in *Jyoti Harshad Mehta and Ors. V. Custodian*, upheld the conviction of stock broker, Harshad Mehta, (who died during the pendency of the appeal in the Apex Court) by a Special Court in Mumbai in the 1992 security scam case. A bench comprising Justice M. B. Shah, Justice B. N. Agrawal and Justice Arijit Pasayat by a majority of 2:1 also upheld the conviction of Pramod Kumar Manocha and Vinayak Deosthali but reduced the sentence to the period already undergone by them. Further the Bench also upheld the acquittal of Ambuj Jain and Ram Narayan Popli.

The case of the Central Bureau of Investigation was that the accused had hatched a criminal conspiracy to divert surplus funds of Maruti Udyog deposited in Canara Bank to the account of Harshad Mehta in the ANZ Grindlays Bank in Delhi and then to UCO Bank in Mumbai. While Justice Shah acquitted all the accused, the majority judgment by Justice Agrawal and Justice Pasayat said that keeping in mind that the scam took place more than ten years ago, the lengthy trial and the death of Harshad Mehta during the pendency of the appeal, "We feel custodial sentence for the period already undergone (which we are told was for a number of months) would meet the ends of justice."

The Bench said, "While fixing the quantum of the sentence, we have duly considered the fact that in the instant case, the amounts have been paid back." However, it refused to alter the amount of fine imposed on the accused convicted in the scam.

The Bench said that "Unfortunately, in the last few years, the country has seen an alarming rise in white collar crimes which have affected the fibre of the
country's economic structure. These are nothing but private gain at the cost of public and lead to economic disaster."

*HB Stockholdings Limited V. Securities and Exchange Board of India*\(^{63}\)

Securities Exchange Board of India investigated, this case and it was evident that bank and promoter funds were used to rig the markets. Parekh was arrested in March that year and was in custody for 53 days. In the aftermath of the scam, many gaping loopholes in the market were plugged. The trading cycle was now reduced from one week to one day. Badla was banned and operators could not carry forward trade in its primitive form. Forward trading was formally introduced in the form of exchange-traded derivatives to ensure a well-regulated futures market. Broker control over stock exchanges was demolished.

In *Jay Bee Properties Private Limited and Ors. v. Pawan Kumar Budhia and Ors*\(^{64}\) the High Court of Calcutta observed that the transfer of shares in a third company pursuant an order sanctioning a scheme of amalgamation does not require compliance with the provisions of Section 108(1) of the Act of 1956 and the transferee of the shares pursuant to an order sanctioning a scheme of amalgamation is entitled to cite such shareholding to meet the qualification under Section 399 thereof any time after the order sanctioning the scheme becomes effective. As a consequence, the appeal and the application, APO No. 227 of 2014 and ACO No. 119 of 2014, are dismissed. The appellants will pay costs assessed at Rs. 2 lakh, half of it to the petitioners before the Company Law Board and the rest to the West Bengal State Legal Services Authority within four weeks from date. Such payment of costs would be a condition precedent to the appellants herein being entitled to a defence on merits in the proceedings under Sections 397 and 398 of the Act of 1956 before the Company Law Board.

As to other allegations of siphoning and not holding meetings and not holding Annual General Meeting in compliance of the statutory provisions, the same cannot become a ground unless such violations are coupled with oppression and misconduct. However, I have not seen any material that R2

\(^{63}\) MANU/SB/0039/2013.

\(^{64}\) MANU/WB/1066/2015.
did something not to hold meetings, it is clear from the correspondence in between
the petitioner and R2, the petitioner part is more in not holding Board meetings.
On seeing the pleadings and letters he has written to R2, it appears that the
petitioner has vindictive attitude towards R2, therefore sought relief to make R2
responsible for punishments and penalties, if letter of R2 to the petitioner is seen,
it is the petitioner who withheld records with him and not allowing R2 to proceed
any further in the company.

_Darius Rutton Kavasmaneck vs. Gharda Chemicals Limited_65 it was held
by the court that there no oppression in the present case. t is held to be a public
company, its shares are freely transferable and the Articles would not hold good as
they are contrary to the statute. Holding that violation of such an clause in the
Articles is not an act of oppression, the petition came to be dismissed.

In _Union of India v. Satyam Computers Services Ltd. & Ors_66 A special
court sentenced B. Ramalinga Raju, founder of the erstwhile Satyam Computer
Services Ltd, and nine others to seven years of rigorous imprisonment, convicting
them in India’s biggest corporate fraud case after a marathon. It was observed that
the case involved grave offences affecting the reputation of the corporate system
of the country as a whole and the economy of the country. Justice demands that
courts should impose punishment fitting to the crime so that the courts reflect
public abhorrence of the crime.

In May 2011, the Supreme Court has given a very fair judgment, with far-
reaching implications both for the government and India Inc., in the _Reliance
Industries Limited (RIL) vs RNRL_67 gas pricing case. It has established
unequivocally that the production sharing contract between the government and
RIL overrides any private memorandum of understanding arrived at between two
individuals. In short, it refused to give sanctity to the Memorandum of
Understanding (MoU) signed between the two Ambani brothers. This principle
had to be established in the interest of corporate governance or it would have

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65 [2015]188CompCas291(SC).

66 (2009) 1Comp LJ 308(CLB).
created havoc in the corporate world with promoters of public limited, quoted companies coming together and signing MoUs without a care for the shareholders and other stakeholders in the company. The second important aspect of the judgment is that the natural resources of a country belong to the government and the government has the right to price it and prioritize the beneficiaries. While it is a well-known fact, even internationally, that natural resources belong to the government, the government as a monopoly has the sacred responsibility to put the interest of the nation before everything else when deciding on its use and sale price. It will be the government that will decide at what price it should market it, and to whom it should market it.

A lack of specialized courts to try commercial cases is a major obstacle to effective enforcement. The Companies Act 2013 provides for the establishment of Special Courts for the speedy trial of offences under the Companies Act. Section 436 provides that all offences under the Companies Act shall be subject to trial only by the Special Court established for the area where the offence is committed. The Act also empowers the Special Courts to try “in fast track” any offence under the Companies Act that is punishable with imprisonment for a term not exceeding three years. The India-OECD Policy Dialogue also highlighted the need for these courts to try corporate offences and noted that the provisions in the Companies Act 2013 are expected to speed up the enforcement machinery dealing with abusive RPTs.

To prevent corporate scams and enforce corporate governance, specialized business courts should be established and staffed with adequately remunerated judges and prosecutors trained specifically in capital market laws and procedures, to enable them to prosecute and dispose of complex cases efficiently. If there are no specialized courts, panels of judges with proper expertise should be set up within the ordinary court systems. The judiciary should be independent, with integrity and respect for the transparency of the judicial process. Decisions should be published. Ongoing training should be a permanent feature to build credibility and competence of the judicial process.
5.3 Role of Stock Exchange Board of India in Corporate Governance

Recently, corporate governance has gained significant attention and focus around the world. One of the main reasons for this renewed focus has been major corporate failures and lack of corporate governance standards. In India, myriad initiatives have been taken in the past by the Ministry of Corporate Affairs and Stock Exchange Board of India to ascertain that those entrusted with the responsibility of governing shareholder wealth are adequately regulated and made accountable. Over the past years, there have been many reforms in the corporate governance framework starting from constitution of the Kumar Mangalam Committee (1999), introduction of Clause 49 in the listing agreement (2000), revision in Clause 49 on recommendations of the Narayana Murthy Committee (2006), issue of voluntary guidelines on corporate governance (2009), issue of guiding principles on corporate governance (2012) based on recommendation of the Adi Godrej Committee, enactment of the revised Companies Act (2013) and finally the new corporate governance norms by Securities Exchange Board of India (2014).

There is a move towards increased transparency on conducting board matters and articulated several changes in the roles and responsibilities of the board, board committees and independent directors. This also indicates the intent of the regulators to align with the global standards on corporate governance.68

Prior to the establishment of Stock Exchange Board of India, stock exchanges were under the administrative control of the Stock Exchange Division of Department of Economic Affairs (DEA). The stock exchange division was responsible for the administration of the Securities Contract Regulation Act, 1956, which governed the business of buying, selling and dealing in securities69. Since

69 The Securities Contracts (Regulation) Act, 19565 defines ‘securities’ in section 2 (h) and is as follows:
“2 (h) “Securities” include— (i) Shares, scrips, stocks, bonds, debentures, debenture stock or other marketable securities of a like nature in or of any incorporated company or other body corporate; (ia) Derivative; (ib) Units or any other instrument issued by any collective investment scheme to the investors in such schemes; (ic) Security receipt as defined in clause (zg) of section 2 of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002. (id) units or any other such instrument issued to the investors under any mutual fund
the empowerment of the Securities and Exchange Board of India (SEBI) through an Act of Parliament in 1992, Securities Exchange Board of India has come up with a number of initiatives aimed at regulating and developing the Indian securities market and improving its safety and efficiency. These initiatives have made an impact on nearly every aspect of the market. Some of those initiatives have transformed the market fundamentally. There is a growing network of financial intermediaries that operate in a highly competitive environment while being governed by a tight set of norms.

India has one of the most sophisticated new equity issuance markets. Disclosure requirements and the accounting policies followed by listed companies for producing financial information are comparable to the best global regimes.

The Indian securities market is among the safest and the most efficient trading destinations internationally. The Indian corporate governance code is compared to the Sarbanes-Oxley Act of the USA. India has one of the fastest growing and well-developed asset management businesses in the world, with state-owned as well as private sector players. That said, the Indian market is often hostage to some scam or the other from time to time.

Securities Exchange Board of India (SEBI) was set up in 1988 to regulate the functions of securities market. Securities Exchange Board of India promotes orderly and healthy development in the stock market but initially Securities Exchange Board of India was not able to exercise complete control over the stock market transactions. It was left as a watch dog to observe the activities but was found ineffective in regulating and controlling them. As a result in May 1992, Securities Exchange Board of India was granted legal status. Securities Exchange Board of India is a body corporate having a separate legal existence and perpetual succession.

scheme; Explanation.—For the removal of doubts, it is hereby declared that "securities" shall not include any unit linked insurance policy or scrips or any such instrument or unit, by whatever named called, which provides a combined benefit risk on the life of the persons and investment by such persons and issued by an insurer referred to in clause (9) of Section 2 of the Insurance Act, 1938 (4 of 1938). (ie) any certificate or instrument (by whatever name called), issued to an investor by any issuer being a special purpose distinct entity which possesses any debt or receivable, including mortgage debt, assigned to such entity, and acknowledging beneficial interest of such investor in such debt or receivable, including mortgage debt, as the case may be (ii) Government securities, (iia) Such other instruments as may be declared by the Central Government to be securities; and (iii) Rights or interests in securities.”
5.3.1 Reasons for Establishment of Stock Exchange Board of India

Stock Exchange Board of India was established to strengthen the oversight of the securities market in India in the wake of a securities scam that surfaced in 1992. With the growth in the dealings of stock markets, lot of malpractices also started in stock markets such as price rigging, ‘unofficial premium on new issue, and delay in delivery of shares, violation of rules and regulations of stock exchange and listing requirements. Due to these malpractices the customers started losing confidence and faith in the stock exchange. So government of India decided to set up an agency or regulatory body known as Securities Exchange Board of India (SEBI). Since the establishment of Securities Exchange Board of India, the Indian securities market has grown in terms of volume of transactions.

5.3.2 The Statutory Sources of Stock Exchange Board of India’s Authority

Stock Exchange Board of India was brought into existence by the Securities and Exchange Board of India Act, 1992 (the SEBI Act, hereafter), which came into effect on January 30, 1992. The preamble to the act describes the purpose of the Act in broad terms as “an act to provide for the establishment of a Board to protect the interests of investors in securities and to promote the development of, and to regulate, the securities market and for matters connected therewith or incidental thereto”. The provisions of the Stock Exchange Board of India Act, 1992 define its role in more specific terms. These broadly relate to

(i) Regulating the business in stock exchanges and any other securities markets

(ii) Registration and regulation of a range of financial intermediaries and trade participants

(iii) Prohibiting practices that are considered to be unhealthy for development of the securities market such as insider trading and fraudulent and unfair trade practices for promoting and regulating self regulatory organizations

(iv) Promoting investors education and training of intermediaries of securities markets

(v) Inspection and calling for information from various regulated entities referred to in (ii) above

70 S 11(2) of SEBI Act, 1992.
(vi) Conducting research
(vii) Collecting fees or other charges for carrying out the purposes of this section and
(viii) Performing such other functions as may be prescribed.

The Stock Exchange Board of India Act leaves open the room for Stock Exchange Board of India to perform such other functions as may be prescribed.\(^{71}\) The Stock Exchange Board of India Act empowers Stock Exchange Board of India to make rules and regulations governing various aspects of the functioning of the securities market.\(^{72}\) A wide range of powers has also been delegated by the Central Government to Stock Exchange Board of India under the Securities Contract Regulation Act, 1956.\(^{73}\) Stock Exchange Board of India pronounces regulations proactively and sometimes in response to developments that potentially challenge the functioning of the market mechanism.

Several of the functions that Stock Exchange Board of India discharges are based on powers that it draws from the Securities Contract Regulation Act, 1956 (14 of 1956) (SCR Act, hereafter) and the rules made there under, the Securities Contract Regulation Rules, 1956 (SCR Rules, hereafter). The object of the SCR Act is to provide for the regulation of stock exchanges and of securities dealt in on them with a view to preventing undesirable speculation in them. It also seeks to regulate the buying and selling of securities outside stock exchanges through its various provisions. Two amendments in 1995 and 1999\(^{74}\) brought about several important changes to the scope and the administration of the SCR Act, resulting in the current form of the law.

Securities Exchange Board of India also draws some of its authority from the Companies Act,\(^{75}\) which empowers Securities Exchange Board of India to administer a number of provisions of the Companies Act.\(^{76}\) These sections pretty

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\(^{71}\) S 11(m) of the SEBI Act, 1992.
\(^{72}\) S 11, S 11A and S 30 of the SEBI Act, 1992.
\(^{73}\) S 29A of Securities Contract Regulation Act, 1956.
\(^{75}\) S 55A of the Companies Act.
\(^{76}\) The sections identified are Sections 55 to 58, 59 to 84, 108, 109, 110, 112, 113, 116, 117, 118, 119, 120, 121, 122, 206, 206A and 207 of the Companies Act. The sections of the Companies Act broadly (not in seriatim) relate to issuance and contents of the prospectus and responsibility
much govern the capital mobilization process (issuance of capital), liquidity creation process (transfer) and the realization of return (dividend), the three important aspects of the issuer’s relationship with investors.

5.3.3 **Purpose and Role of Securities Exchange Board of India**

Securities Exchange Board of India was set up with the main purpose of keeping a check on malpractices and protects the interest of investors. It was set up to meet the needs of three groups.

I. **Issuers:** For issuers it provides a market place in which they can raise finance fairly and easily.

II. **Investors:** For investors it provides protection and supply of accurate and correct information.

III. **Intermediaries:** For intermediaries it provides a competitive professional market.

5.3.4 **Objectives of Stock Exchange Board of India**

The overall objectives of Stock Exchange Board of India are to protect the interest of investors and to promote the development of stock exchange and to regulate the activities of stock market. The objectives of Stock Exchange Board of India are:

I. To regulate the activities of stock exchange.

II. To protect the rights of investors and ensuring safety to their investment.

III. To prevent fraudulent and malpractices by having balance between self regulation of business and its statutory regulations.

IV. To regulate and develop a code of conduct for intermediaries such as brokers, underwriters, etc.

5.3.5 **Functions of Securities Exchange Board of India**

The Stock Exchange Board of India performs functions to meet its objectives. To meet three objectives Stock Exchange Board of India has three important functions. These are:

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of those authorizing the issuance of the prospectus, procedure for issuance and allotment of shares and debentures, payment of brokerage and commission, buyback of shares, issue of shares at a premium or discount, further issue of capital (rights or otherwise), issue and redemption of preference share capital, administration of share capital, transfer of shares, provisions and payment of dividend.
I. **Protective Functions:**

These functions are performed by Stock Exchange Board of India to protect the interest of investor and provide safety of investment. As protective functions Stock Exchange Board of India performs following functions:

(i) **It Checks Price Rigging:**

Price rigging refers to manipulating the prices of securities with the main objective of inflating or depressing the market price of securities. Stock Exchange Board of India prohibits such practice because this can defraud and cheat the investors.

(ii) **It Prohibits Insider trading:**

Insider is any person connected with the company such as directors, promoters etc. These insiders have sensitive information which affects the prices of the securities. This information is not available to people at large but the insiders get this privileged information by working inside the company and if they use this information to make profit, then it is known as insider trading, e.g., the directors of a company may know that company will issue Bonus shares to its shareholders at the end of year and they purchase shares from market to make profit with bonus issue. This is known as insider trading. Securities Exchange Board of India keeps a strict check when insiders are buying securities of the company and takes strict action on insider trading.

(iii) **Securities Exchange Board of India prohibits fraudulent and Unfair Trade Practices:**

a) Securities Exchange Board of India does not allow the companies to make misleading statements which are likely to induce the sale or purchase of securities by any other person.

b) Securities Exchange Board of India undertakes steps to educate investors so that they are able to evaluate the securities of various companies and select the most profitable securities.

c) Securities Exchange Board of India promotes fair practices and code of conduct in security market by taking following steps:
i. Securities Exchange Board of India has issued guidelines to protect the interest of debenture holders wherein companies cannot change terms in midterm.

ii. Securities Exchange Board of India is empowered to investigate cases of insider trading and has provisions for stiff fine and imprisonment.

iii. Securities Exchange Board of India has stopped the practice of making preferential allotment of shares unrelated to market prices.

II. Developmental Functions:
These functions are performed by the Securities Exchange Board of India to promote and develop activities in stock exchange and increase the business in stock exchange. Under developmental categories following functions are performed by Securities Exchange Board of India:

(i) Securities Exchange Board of India promotes training of intermediaries of the securities market.

(ii) Securities Exchange Board of India tries to promote activities of stock exchange by adopting flexible and adoptable approach in following way:

a) Securities Exchange Board of India has permitted internet trading through registered stock brokers.

b) Securities Exchange Board of India has made underwriting optional to reduce the cost of issue.

c) Even initial public offer of primary market is permitted through stock exchange.

III. Regulatory Functions:
These functions are performed by Securities Exchange Board of India to regulate the business in stock exchange. To regulate the activities of stock exchange following functions are performed:

(i) Securities Exchange Board of India has framed rules and regulations and a code of conduct to regulate the intermediaries such as merchant bankers, brokers, underwriters, etc.

(ii) These intermediaries have been brought under the regulatory purview and private placement has been made more restrictive.
(iii) Securities Exchange Board of India registers and regulates the working of
stock brokers, sub-brokers, share transfer agents, trustees, merchant
bankers and all those who are associated with stock exchange in any
manner.
(iv) Securities Exchange Board of India registers and regulates the working of
mutual funds etc.
(v) Securities Exchange Board of India regulates takeover of the companies.
(vi) Securities Exchange Board of India conducts inquiries and audit of stock
exchanges.

5.3.6 **The Organisational Structure of Securities Exchange Board of India**
1. Securities Exchange Board of India is working as a corporate
   sector.
2. Its activities are divided into five departments. Each department is
   headed by an executive director.
3. The head office of Stock Exchange Board of India is in Mumbai
   and it has branch office in Kolkata, Chennai and Delhi.
4. Stock Exchange Board of India has formed two advisory
   committees to deal with primary and secondary markets.
5. These committees consist of market players, investors associations
   and eminent persons.

5.3.7 **Objectives of the two Committees are**
1. To advise Stock Exchange Board of India to regulate
   intermediaries.
2. To advise Stock Exchange Board of India on issue of securities in
   primary market.
3. To advise Stock Exchange Board of India on disclosure
   requirements of companies.
4. To advise for changes in legal framework and to make stock
   exchange more transparent.
5. To advise on matters related to regulation and development of
   secondary stock exchange.
These committees can only advise Stock Exchange Board of India but they cannot force Stock Exchange Board of India to take action on their advice.\textsuperscript{77}

\textbf{5.3.8 \hspace{1em} Stock Exchange Board of India and Corporate Governance}\\

Stock Exchange Board of India has set out corporate governance provisions that are intended to drive in a minimum standard of corporate governance among listed companies in India. This is issued as a part of the Listing Agreement that each listed company signs with the stock exchange under the title ‘Clause 49’. Clause 49 remains the most significant corporate governance reform and established a new corporate governance regime. A certificate of compliance on terms contained in Clause 49 is required to be signed by the director and auditors/ company secretary of the company is to be annexed to the annual report. Some elements of the role of the Board of Directors of a company collectively and that of directors individually have been dealt with under the Companies Act, long before corporate governance emerged as the hot topic that it is currently.\textsuperscript{78} Securities Exchange Board of India’s initiatives starting with the deliberations of two committees in succession\textsuperscript{79}, culminated in the introduction of Clause 49 in the listing agreement. The main items covered under Clause 49 are:\textsuperscript{80}

\textit{5.3.8.1 Clause 49}\\

Clause 49 of the Equity Listing Agreement consists of mandatory as well as non- mandatory provisions. Those which are absolutely essential for corporate governance can be defined with precision and which can be enforced without any legislative amendments are classified as mandatory. Others, which are either

\textsuperscript{77} \hspace{1em} \url{http://www.yourarticlelibrary.com/education/sebi-the-purpose-objective-and-functions-of-sebi/8762/} (Visited on July 13, 2015).

\textsuperscript{78} The Companies Act has provisions governing the constitution of the board of directors of a company (Section 255 to Section 266), disqualification of directors (Section 274), restrictions on maximum number of directorships (Section 275 to Section 278), remuneration of directors (Section 309 to Section 311), vacation of office by directors (Section 283 and Section 284), procedure to be followed in the case of business in which directors are interested (section 299 to Section 302), powers of the board (section 291 to section 293). Further, Section 211 requires that the accounts presented to shareholders will be authenticated by the directors of the company and Section 224 states that the accounts will have to be audited.

\textsuperscript{79} The two committees were headed by Mr Kumar Mangalam Birla and Mr. N R Narayanamurthy respectively.

desirable or which may require change of laws are classified as non-mandatory. The non-mandatory requirements may be implemented at the discretion of the company. However, the disclosures of the compliance with mandatory requirements and adoption (and compliance) / non-adoption of the non-mandatory requirements shall be made in the section on corporate governance of the Annual Report. Gist of Cause 49 is as follows:

I. **Mandatory provisions comprises of the following**

   Composition of Board and its procedure - frequency of meeting, number of independent directors, code of conduct for Board of directors and senior management;
   a) Audit Committee, its composition, and role
   b) Provision relating to Subsidiary Companies
   c) Disclosure to Audit committee, Board and the Shareholders
   d) CEO/CFO certification
   e) Quarterly report on corporate governance
   f) Annual compliance certificate

II. **Non-mandatory provisions consist of the following**

   a) Constitution of Remuneration Committee
   b) Despatch of Half-yearly results o Training of Board members
   c) Peer evaluation of Board members
   d) Whistle Blower policy

   As per Clause 49 of the Listing Agreement, there should be a separate section on Corporate Governance in the Annual Reports of listed companies, with detailed compliance report on Corporate Governance. The companies should also submit a quarterly compliance report to the stock exchanges within 15 days from the close of quarter as per the prescribed format. The report shall be signed either by the Compliance Officer or the Chief Executive Officer of the company.

Apart from Clause 49 of the Equity Listing Agreement, there are certain other clauses in the listing agreement, which are protecting the minority share holders and ensuring proper disclosures

a) Disclosure of Shareholding Pattern
b) Maintenance of minimum public shareholding (25%)
c) Disclosure and publication of periodical results

d) Disclosure of Price Sensitive Information

e) Disclosure and open offer requirements under SAST

In Companies Act, 1956, Stock Exchange Board of India has been given power only to administer provisions pertaining to issue and transfer of securities and non-payment of dividend. Apart from the basic provisions of the Companies Act, every listed company needs to comply with the provisions of the listing agreement as per Section 21 of Securities Contract Regulations Act, 1956. Non-compliance with the same, would lead to delisting under Section 22A or monetary penalties under Section 23 E of the said Act. Further, Stock Exchange Board of India is empowered under Section 11 and Section 11A of Stock Exchange Board of India, Act to prescribe conditions for listing. However, Section 32 of the Stock Exchange Board of India Act, 1992 states that the provisions of the Stock Exchange Board of India Act, 1992 shall be in addition to, and not in derogation of, the provisions of any other law for the time being in force. Considering the emergence of code of best Corporate Governance practices all over the world (like Cadbury Greenbury and Hampel Committee reports), in 1999, Stock Exchange Board of India constituted a Committee on Corporate Governance under the Chairmanship of Shri Kumar Mangalam Birla, to promote and raise the standard of Corporate Governance in respect of listed companies. Stock Exchange Board of India’s Board, in its meeting held on January 25, 2000, considered the recommendations of the Committee and decided to make the amendments to the listing agreement on February 21, 2000 for incorporating the recommendations of the committee by inserting a new clause in the Equity Listing Agreement – i.e. Clause 49. Subsequently, after Enron, WorldCom, and other corporate governance catastrophes, Stock Exchange Board of India felt that there was a need to improve further the level of corporate governance standards in India and constituted a second corporate governance committee chaired by Mr. Narayana Murthy, of Infosys Technologies Limited. Based on the recommendations of the aforesaid Committee, Stock Exchange Board of India issued a circular on August 26, 2003 revising Clause 49 of the Listing Agreement. Based on the public comments received thereon and the revised recommendations of the Committee,
certain provisions of the regulatory framework for corporate governance were modified and relevant amendments were made to Clause 49 of the Listing Agreement. The revised clause 49 superseded all the earlier circulars on the subject and became effective for listed companies from January 01, 2006. It is applicable to the entities seeking listing for the first time and for existing listed entities having a paid up share capital of Rs. 3 crores and above or net worth of Rs. 25 crores or more at any time in the history of the company.

5.3.8.2 Recent policy steps taken by Securities Exchange board of India for ensuring better governance in listed companies

The introspection that followed the Satyam episode\textsuperscript{81} has resulted in some major changes in Indian corporate governance regime. Some of the recent steps taken in this regard are as follows:

I. Disclosure of pledged shares: It is made mandatory on the part of promoters (including promoter group) to disclose the details of pledge of shares held by them in listed entities promoted by them. Further, it was decided to make such disclosures both event-based and periodic.

II. Peer review: In the light of developments with respect to Satyam Securities Exchange Board of India carried out a peer review exercise of the working papers (relating to financial statements of listed entities) of auditors in respect of the companies constituting the NSE – Nifty 50, the BSE Sensex and some listed companies outside the Sensex and Nifty chosen on a random basis.

III. Disclosures regarding agreements with the media companies: In order to ensure public dissemination of details of agreements entered into by corporate with media companies, the listed entities are required to disclose details of such agreements on their websites and also notify the stock exchange of the same for public dissemination.

IV. Maintenance of website: In order to ensure/enhance public dissemination of all basic information about the listed entity, listed entities are mandated to maintain a functional website that contains certain basic information about them, duly updated for all statutory filings, including agreements entered into with media companies, if any.

\textsuperscript{81} Union of India v. Satyam Computers Services Ltd. & Ors (2009) 1Comp LJ 308(CLB).
V. **Compulsory dematerialization of Promoter holdings:** In order to improve transparency in the dealings of shares by promoters including pledge / usage as collateral, it is decided that the securities of companies shall be traded in the normal segment of the exchange if and only if, the company has achieved 100% of promoter’s and promoter group’s shareholding in dematerialized form. In all cases, wherein the companies do not satisfy the above criteria, the trading in securities of such companies shall take place in trade for trade segment;

VI. **Peer reviewed Auditor:** It has been decided that in respect of all listed entities, limited review/statutory audit reports submitted to the concerned stock exchanges shall be given only by those auditors who have subjected themselves to the peer review process of ICAI and who hold a valid certificate issued by the ‘Peer Review Board’ of the said Institute;

VII. **Approval of appointment of ‘CFO’ by the Audit Committee:** In order to ensure that the CFO has adequate accounting and financial management expertise to review and certify the financial statements, it is mandated that the appointment of the CFO shall be approved by the Audit Committee before finalization of the same by the management. The Audit Committee, while approving the appointment, shall assess the qualifications, experience & background etc. of the candidate.

VIII. **Disclosure of voting results:** In order to ensure wider dissemination of information regarding voting patterns which gives a better picture of how the meetings are conducted and how the different categories of investors have voted on a resolution, listed entities are required to disclose the voting results/patterns on their websites and to the exchanges within 48 hours from the conclusion of the concerned shareholders’ meeting.

IX. **Enabling shareholders to electronically cast their vote:** In order to enable wider participation of shareholders in important proposals, listed companies are mandated to enable e-voting facility also to their shareholders, in respect of those businesses which are transacted through postal ballot by the listed companies.
X. **Manner of dealing audit reports filed by listed entities:**

Securities Exchange Board of India has approved a mechanism to process qualified annual audit reports filed by the listed entities with stock exchanges and Annual Audit Reports where accounting irregularities have been pointed out by Financial Reporting Review Board of the Institute of Chartered Accountants of India (ICAI-FRRB). In order to enhance the quality of financial reporting done by listed entities, it has been, inter-alia, decided that:

Deficiencies in the present process would be examined and rectified.

Securities Exchange Board of India would create Qualified Audit Report review Committee (QARC) represented by ICAI, Stock Exchanges, etc. to guide Securities Exchange Board of India in processing audit reports where auditors have given qualified audit reports.

Listed entities would be required to file annual audit reports to the stock exchanges along with the applicable Forms (Form A: 'Unqualified' / 'Matter of Emphasis Report'; Form B: 'Qualified' / 'Subject To' / 'Except For Audit Report'). After preliminary scrutiny and based on materiality, exchanges would refer these reports to Securities Exchange Board of India /QARC

Cases wherein the qualifications are significant and explanation given by Company is unsatisfactory would be referred to the ICAI-FRRB. If ICAI-FRRB opines that the qualification is justified, Securities Exchange Board of India may mandate a restatement of the accounts of the entity and require the entity to inform the same to the shareholders by making the announcement to stock exchanges.

5.3.8.3 Certification course and training for independent directors

Securities Exchange Board of India has established National Institute of Securities Markets (NISM), a public trust, to add to market quality through educational initiatives. School for Corporate Governance, NISM, jointly works with the Global Corporate Governance Forum of International Finance Corporation in conducting workshops on various aspects of corporate governance. Apart from that NISM is conducting certified course for various market participants. A separate course for independent directors may be devised by NISM for independent directors covering their role, liabilities, expectations from various stake holders, internal controls, risk management systems, business models and
independent directors may be mandated to clear such courses, before their appointment. Apart from conducting induction courses, NISM may also conduct training/review courses for independent directors.

5.3.8.4 Provision for regulatory support to class action suits

Presently, Regulation 5 (2) of Securities Exchange Board of India (Investor Protection and Education Fund) Regulations, 2009 mentions that Investor Protection and Education Fund created by Securities Exchange Board of India may, inter-alia, be used for aiding investors’ associations recognized by Securities Exchange Board of India to undertake legal proceedings (not exceeding seventy-five per cent. of the total expenditure on legal proceedings) in the interest of investors in securities. Though there are provisions for oppression and mismanagement, there is no express recognition of class action suits in Companies Act, 1956. However, Clause 245 of the Companies Bill, 2012 expressly provides for class action suits and Clause 125 provides for re-imbursement of expenses incurred in class action suits from the Investor Education and Protection Fund of Ministry of Corporate Affairs.

5.3.8.5 Stock Exchange Board of India consultative paper on Corporate Governance

In early 2012, Securities Exchange Board of India released a consultative paper on “Review of Corporate Governance Norms in India”. To improve the governance standards of companies in India, the report had provided a broad framework in the form of (i) overarching principles of corporate governance, and (ii) proposals. The objective of the concept paper was to attract a wider debate on the governance requirements for the listed companies so as to adopt better global practices. An attempt was made to ensure that the additional cost of compliance with the proposals did not outweigh the benefits of listing, while at the same time the need to boost the confidence of the investors on the capital market was recognized. Establishment of the NSE Centre for Excellence in Corporate Governance National Stock Exchange has continually endeavoured to organize new initiatives relating to corporate governance in recognition of the important role that stock exchanges play in enhancing the corporate governance standards. To encourage best standards of corporate governance among the Indian corporate
and to keep them abreast of the emerging and existing issues, the National Stock Exchange set up in December, 2012, a Centre for Excellence in Corporate Governance (NSE CECG). This is an independent expert advisory body comprising eminent domain experts, academics and practitioners. The Committee meets from time to time to discuss corporate governance issues and developments. The ‘Quarterly Briefing’, a note that offers an analysis of one emerging or existing corporate governance issue, is a product emerging from these discussions.

5.3.8.6 Enforcement of Corporate and Securities laws

In India, Corporate and securities laws in India are enforced through the many different arms of the government. Securities and Exchange Board of India enforces matters arising under the Securities & Contracts (Regulation) Act 1956 and the Securities & Exchange Board of India Act 1992, as well as the regulations and rules promulgated under these Acts. Securities & Exchange Board of India’s decisions can generally be appealed in the first instance to the Securities Appellate Tribunal (SAT), the High Court, and then potentially to the Supreme Court of India.\(^82\) Both the Securities & Contracts (Regulation) Act, 1956 and the Securities & Exchange Board of India Act 1992 contain provisions and regulations that are relevant to corporate governance. Perhaps the most important is Section 23E of the Securities & Contracts (Regulation) Act 1956, which states that a violation of the Stock Exchange Listing Agreement (SELA) can result in severe financial and criminal penalties for the directors and the firms involved.\(^83\) The Stock Exchange Listing Agreement contains Clause 49 which is the watershed corporate governance provision in India. Violations of Clause 49 can be enforced by Stock Exchange Board of India under Section 23E of the Securities & Contracts (Regulation) Act, 1956. The crucial matter is then whether these provisions have been enforced. Although it is well known that a number of firms are not complying with the provisions of Clause 49, the first (and to date, the only) time

\(^{82}\) Sections 15T, 15U and 15Z of the Stock Exchange Board of India Act (1992).

\(^{83}\) Sec. 23 E. (SECURITIES CONTRACTS (REGULATION) ACT, 1956), Penalty for failure to comply with provision of listing conditions or delisting conditions or grounds. If a company or any person managing collective investment scheme or mutual fund, fails to comply with the listing conditions or delisting conditions or grounds or commits a breach thereof, it or he shall be liable to a penalty not exceeding twenty-five crores rupees. (Inserted by the Securities Laws (Amendment) Act, 2004, Sec 11, w.r.e.f. 12-10-2004).
Stock Exchange Board of India initiated investigation proceedings was in September 2007 (Stock Exchange Board of India Press Release, 2007). This was more than seven years after the initial enactment of Clause 49, and nearly two years after all firms which were subject to Clause 49 were to have complied with its provisions. The proceedings were primarily initiated against firms owned by the Indian government, and to date no sanctions have been imposed. In addition to Clause 49, there are a number of other Stock Exchange Board of India regulations that could address governance issues, such as insider trading, and other forms of unfair trading practices; the failure of a firm to address investor grievances sent to the firm by Stock Exchange Board of India or a stock exchange; and violations of certain provisions in the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, as amended in 2010 (“Takeover Code”). Stock Exchange Board of India has brought enforcement actions under some of these rules, but often the issues are not at the core of governance concerns, but are at the periphery (Stock Exchange Board of India Annual Report, 2008–09). However the presence of active Stock Exchange Board of India enforcement in primarily noncore governance areas suggests that Stock Exchange Board of India could be a useful source of enforcement and could provide credible deterrence related to governance issues if it became more active in enforcement. Ministry of Company Affairs Although Stock Exchange Board of India is the primary enforcement agency for violations of securities laws, the primary agency for the investigation of company laws is the Ministry of Company Affairs (Ministry of Company Affairs Annual Report, 2005). The ministry acts mainly through its investigations divisions, serious fraud

84 Violations of Clause 49 can also lead to de-listing, but that has yet to happen in India. Clause 49 requires the inclusion of independent directors on corporate boards, defines independence (although with amendments over the years), and lays out some specific duties and obligations of the independent directors.


86 Section 23C of the SCRA (1956), and Section 15C of the SEBI Act (1992). Enforcement of Corporate Governance in India: Steps Forward 163.

87 See Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, as amended in 2010 (“Takeover Code”) Sections 45(5) and 45(6).
investigation office (SFIO), regional directors, and registrars of companies. The investigative authority is broad, but the provisions for which cases can be brought are limited to those mentioned in this paper, especially the criminal provisions.  

5.3.9 Provisions of Stock Exchange Board of India Act, 1992

Stock exchange board of India Act, 1992 Act, was passed to provide for the establishment of a Board to protect the interests of investors in securities and to promote the development of, and to regulate, the securities market and for matters connected therewith or incidental thereto. The Act extends to the whole of India and came into force on the 30th day of January, 1992

5.3.9.1 Composition of the Board

The Board shall consist of a Chairman and two members from amongst the officials of the Ministries of the Central Government dealing with Finance and Law; one member from amongst the officials of the Reserve Bank of India, and two other members, to be appointed by the Central Government.

5.3.9.2 Removal of member from office

The Central Government shall remove a member from office if such member is, or at any time has been, adjudicated as insolvent, is of unsound mind and stands so declared by a competent court, has been convicted of an offence which, in the opinion of the Central Government, involves a moral turpitude or has, in the opinion of the Central Government, so abused his position as to render his continuation in office detrimental to the public interest; Provided that a reasonable opportunity of being heard in the matter should be given to the member before removal.

5.3.9.3 Functions of Board

Subject to the provisions of this Act, it shall be the duty of the Board to protect the interests of investors in securities and to promote the development of, and to regulate the securities market, by such measures as it thinks fit. The Board perform the following functions:


89 constituted under section 3 of the Reserve Bank of India Act, 1934 (2 of 1934).

90 Sec.4 (Stock Exchange Board of India Act, 1992).

91 Sec. 6 (Stock Exchange Board of India Act, 1992).
(a) regulating the business in stock exchanges and any other securities markets;

(b) registering and regulating the working of stock brokers, sub-brokers, share transfer agents, bankers to an issue, trustees of trust deeds, registrars to an issue, merchant bankers, underwriters, portfolio managers, investment advisers and such other intermediaries who may be associated with securities markets in any manner;

(c) registering and regulating the working of the depositories, [participants] [93] custodians of securities, foreign institutional investors, credit rating agencies and such other intermediaries as the Board may, by notification, specify in this behalf;

(d) registering and regulating the working of [venture capital funds and collective investment schemes] [94], including mutual funds;

(e) promoting and regulating self-regulatory organisations;

(f) prohibiting fraudulent and unfair trade practices relating to securities markets;

(g) promoting investors' education and training of intermediaries of securities markets;

(h) prohibiting insider trading in securities;

(i) regulating substantial acquisition of shares and take-over of companies;

(j) calling for information from, undertaking inspection, conducting inquiries and audits of the [stock exchanges, mutual funds, other persons associated with the securities market.] [95] intermediaries and self-regulatory organisations in the securities market;

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(k) performing such functions and exercising such powers under the provisions of [***]\textsuperscript{96} the Securities Contracts (Regulation) Act, 1956 (42 of 1956), as may be delegated to it by the Central Government;

(l) levying fees or other charges for carrying out the purposes of this section;

(m) conducting research for the above purposes;

(n) calling from or furnishing to any such agencies, as may be specified by the Board, such information as may be considered necessary by it for the efficient discharge of its functions;\textsuperscript{97}

(o) performing such other functions as may be prescribed.

(p) Notwithstanding anything contained in any other law for the time being in force while exercising the powers under clause (i) of sub-section (2), the Board shall have the same powers as are vested in a civil court under the Code of Civil Procedure, 1908 (5 of 1908), while trying a suit, in respect of the following matters, namely:

(i) the discovery and production of books of account and other documents, at such place and such time as may be specified by the Board;

(ii) summoning and enforcing the attendance of persons and examining them on oath;

(iii) inspection of any books, registers and other documents of any person referred to in section 12, at any place.\textsuperscript{98}

5.3.9.4 Matters to be disclosed by the companies

Without prejudice to the provisions of the Companies Act, 1956 (1 of 1956), the Board may, for the protection of investors, specify, by regulations, the matters relating to issue of capital, transfer of securities and other matter incidental thereto; and the manner in which such matters, shall be disclosed by the companies.\textsuperscript{99}

\textsuperscript{96} The words, brackets and figures “the Capital Issues (Control) Act, 1947 (29 of 1947) and” omitted by the Securities Laws (Amendment) Act, 1995, w.e.f. 25-1-1995.

\textsuperscript{97} Inserted by the Securities Laws (Amendment) Act, 1995, w.e.f. 25-1-1995

\textsuperscript{98} Inserted by the Securities Laws (Amendment) Act, 1995, w.e.f. 25-1/1995.

5.3.9.5 Penalty for failure to furnish information return etc.

If any person, who is required under this Act or any rules or regulations made thereunder, to furnish any document, return or report to the Board, fails to furnish the same, he shall be liable to a penalty not exceeding one lakh and fifty thousand rupees for each such failure; or to file any return or furnish any information, books or other documents within the time specified there for in the regulations, fails to file return or furnish the same within the time specified there for in the regulations, he shall be liable to a penalty not exceeding five thousand rupees for every day during which such failure continues; or is required to maintain books of account or records, fails to maintain the same, he shall be liable to a penalty not exceeding ten thousand rupees for every day during which the failure continues. \(^{100}\)

5.3.9.6 Penalty for failure by any person to enter into agreement with clients

If any person, who is registered as an intermediary and is required under this Act or any rules or regulations made there under to enter into an agreement with his client, fails to enter into such agreement, he shall be liable to a penalty not exceeding five lakh rupees for every such failure. \(^{101}\)

5.3.9.7 Penalty for failure to redress investors' grievances

If any person, who is registered as an intermediary, after having been called upon by the Board in writing to redress the grievances of investors, fails to redress such grievances, he shall be liable to a penalty not exceeding ten thousand rupees for each such failure. \(^{102}\)

5.3.9.8 Penalty for insider trading

If any insider who, either on his own behalf or on behalf of any other person, deals in securities of a body corporate listed on any stock exchange on the basis of any unpublished price sensitive information; or communicates any unpublished price sensitive information to any person, with or without his request for such information except as required in the ordinary course of business or under any law; or counsels, or procures for any other person to deal in any securities of

\(^{100}\) Sec.15A. (Stock Exchange Board of India Act, 1992).

\(^{101}\) Sec. 15B. (Stock Exchange Board of India Act, 1992).

\(^{102}\) Sec.15C. (Stock Exchange Board of India Act, 1992).
anybody corporate on the basis of unpublished price sensitive information, shall be liable to a penalty not exceeding five lakh rupees.\textsuperscript{103}

5.3.9.9 Penalty for non-disclosure of acquisition of shares and takeovers

If any person, who is required under this Act or any rules or regulations made thereunder, fails to disclose the aggregate of his share holding in the body corporate before he acquires any shares of that body corporate; or make a public announcement to acquire shares at a minimum price, he shall be liable to a penalty not exceeding five lakh rupees.\textsuperscript{104}

5.3.9.10 Offences by companies

(1) Where an offence under this Act has been committed by a company, every person who at the time the offence was committed was in charge of, and was responsible to, the company for the conduct of the business of the company, as well as the company, shall be deemed to be guilty of the offence and shall be liable to be proceeded against and punished accordingly:

Provided that nothing contained in this sub-section shall render any such person liable to any punishment provided in this Act, if he proves that the offence was committed without his knowledge or that he had exercised all due diligence to prevent the commission of such offence.

(2) Notwithstanding anything contained in sub-section (1), where an offence under this Act has been committed by a company and it is proved that the offence has been committed with the consent or connivance of, or is attributable to any neglect on the part of, any director, manager, secretary or other officer of the company, such director, manager, secretary or other officer shall also be deemed to be guilty of the offence and shall be liable to be proceeded against and punished accordingly.\textsuperscript{105}

\textsuperscript{103} Sec. 15G. (Stock Exchange Board of India Act, 1992).

\textsuperscript{104} Sec. 15H. (Stock Exchange Board of India Act, 1992).

\textsuperscript{105} Sec. 27. (Stock Exchange Board of India Act, 1992).
Power to make regulations

(1) The Board may, [***] with the previous approval of the Central Government, by notification, make regulations consistent with this Act and the rules made thereunder to carry out the purposes of this Act.

(2) In particular, and without prejudice to the generality of the foregoing power, such regulations may provide for all or any of the following matters, namely:

(a) the times and places of meetings of the Board and the procedure to be followed at such meetings under sub-section (1) of section 7 including quorum necessary for the transaction of business;

(b) the term and other conditions of service of officers and employees of the Board under sub-section (2) of section 9;

(c) the matters relating to issue of capital, transfer of securities and other matters incidental thereto and the manner in which such matters shall be disclosed by the companies under section 11A;

(d) the conditions subject to which certificate of registration is to be issued, the amount of fee to be paid for certificate of registration and the manner of suspension or cancellation of certificate of registration under section 12.)

Thus, Stock Exchange Board of India drafts regulations in its legislative capacity, conducts investigations and authorizes enforcement action in its executive function, passes rulings and orders in its judicial capacity. Though this makes it very powerful, there is an appeal process to ensure fairness and accountability through a Securities Appellate Tribunal. Securities Appellate Tribunal was formed in 1995 to act as a form of justice to appeal against the orders passed by Stock Exchange Board of India Board or the adjudicating officer appointed under Stock Exchange Board of India Act, 1992.

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106 Sec. 30. (Stock Exchange Board of India Act, 1992).
107 The words “with the previous approval of the Central Government” omitted by the Securities Laws (Amendment) Act, 1995, w.e.f. 25-1-1995.
108 Substituted by the Securities Laws (Amendment) Act, 1995, w.e.f. 25-1-1995 for the following: “(c) the amount of fee to be paid for registration certificate and manner of suspension or cancellation of registration certificate under sub-sections (2) and (3) of section 12.”