CHAPTER VI

CONCLUSION AND SUGGESTIONS

Protection of the interest of investors is the paramount duty of a company which ultimately rests on its Board of directors. It paves the way for long term sustainability of the company in modern period and in fact, it is one of the main features of good Corporate Governance. A company is an entity distinct alike its shareholders and directors. Being an artificial person it cannot act without the help of a human agency. The business of the company is either conducted by the majority of shareholders of the company in the general meeting or by the agents appointed by the company (i.e. again the majority of the shareholders acting collectively in the general meeting). The operating procedure for companies might be described in terms of an hour glass in form. At the base are the shareholders who elect the Board of directors and delegate certain powers to them.

Capital is the first requirement for the establishment as well as to run successfully of any public company so, often; it is coined as backbone for the company. It is also required for further extension and joint venture process of the company. Any kind of liquidity (capital) crunch will force the company to become sick and it ultimately may lead to winding up of such company. An investor, who invests money, will always have desire, to safety of his investments, liquidity of his investments and a good return with least or at no risk. Sometimes, due to unsound Corporate Governance which results into various scams, he suffers huge loss. He feels helpless in such situation. To avoid such situation several legislations were enacted against bad Corporate Governance and to protect the investors. The Companies Act sets the code of conduct for the administration of corporate sector. It also prescribes rules for the formation of a company, rising of capital through
issuance, allotment of shares and disclosures to be made in public issues. The Act has also empowered the Central Government for the establishment of National Company Law Tribunals and a National Company Law Appellate Tribunal, to exercise and discharge such powers and functions as may be conferred on it by the Act or any other law for the time being in force.

Another important legislation for the protection of investors is Securities Exchange Board of India (SEBI) Act, 1992. This Act gave the legal status to Securities Exchange Board of India (SEBI). The main function of SEBI is the protection of the investors’ interest and the healthy development of Indian financial markets. Accordingly, it has made several regulations to check and control the securities market. It is entrusted with quasi-legislative, quasi-judicial and quasi-executive power. There are several other legislations which also aim to protect the interest of investors, which have been briefly discussed in Chapter I.

Despite several legislations to protect the rights of the investors, still many scams and serious frauds in capital market are taking place like insider trading, sudden stake selling, cartelization, falsified the bank accounts to inflate the balance sheet with balances that did not exist etc. which have shaken the confidence of domestic as well as foreign investors in India. They feel insecure to invest money in the capital market. It means there are some loopholes either in the provisions of these legislations or in the implementation of the Act/procedures. Keeping in view of this aspect, provision related with inspection, investigation and audit as enshrined in the Companies Act, 2013 as well as SEBI Act, 1992 were dealt to find out the lacunae.

Though there were several provisions in the Companies Act, 1956 for protection of the interests of the shareholders, but it did not keep pace with the changing business environment. The new Companies Act addresses a number of investors concerns and seeks to provide a more generous environment for minority shareholders especially in the light of scams took placed such as Satyam Computer scam, Sahara case etc.
The provision of inspection, investigation and audit of the documents and papers of the company in the Companies Act, 2013 and SEBI Act, 1992, ensure the sound functioning of a company in accordance of the above legislations. This paves in finding any abnormality in Corporate Governance, which, further, ensures the protection of the investors. This chapter has also stated the purpose of the research along with its aim and objectives, meaning, definition and objectives of investment.

In chapter II, the meaning of investors, types of investor and a brief study on various protections available to them, civil and criminal liabilities of company and its directors, establishment and role of investor’s education and protection fund under Companies Act, 2013 has been dealt. Role of SEBI as regulator of capital market, the investor’s protection measures under the Security and Exchange Board of India (SEBI) Act, 1992 and through various regulations and fourth research question i.e., whether the security and exchange board of India (SEBI) is able to check fraudulent or unlawful conduct of the company in order to protect the rights and interests of investors has been tested.

An individual or any entity who commits money to investment products with the hope of financial return is called an investor. Group of such individual may be members or shareholders or creditors or debenture-holders or other depositories of the company. Normally, an investor is regarded as a blind person and he does not know any activities made by the company. Investor cannot guide the fortune or destiny of the company in which he has invested money. An investor to that extent is quite fragile and is exposed to certain risks because the utilizer of his money can commit mistakes. Normally they are contributing the funds for fruitful purpose of the company and they are exposing him to the business decisions that the company has taken or will take. Sometimes they may lose their hard earned money due to mismanagement of the company so they need protection for their investment.

Various protections which are available to investors under the Companies Act, 2013 as well as SEBI Act, 1992, have been dealt in this chapter. Memorandum of
Association (MOA) and Articles of Association (AOA) of the company provides numerous protections to its members. Since the AOA constitute a contract between the company and its member, the provision mentioned in the AOA is mandatory. Such rights includes right to have his name in the Register of members, to vote at the meeting of members, to receive dividends when declared, to exercise the right of pre-emption, return of capital on winding-up or on reduction of share capital of the company etc. Since MOA provides the Object Clause of the Company, the member has a right to bring action to restrain the company from doing an *ultra vires* act. Prospectus of the company provides important disclosures and on the basis of that investors do the investment.

In order to protect the interests of the investors and give them an active control over the management, the law as regards the company’s meeting etc., giving more rights to shareholders and ensuring their exercise by the shareholders was drastically changed and various statutory provisions were made to make it difficult for the directors to secure the hurried passage of controversial issues (by stating that certain important matters could only be transacted by the general meeting of the shareholders), and as far as possible to encourage shareholders to considered carefully any proposals required by law to be put before the shareholders by the directors (by making provisions regarding notices, resolutions etc. in the Companies Act itself). Although the BODs was declared the primary executive organ of the company, its authority was restricted to the management of the regular business affairs of the company, unless extensive powers are expressly conferred by either the Article or the Act. The fundamental changes in the character of the organisation of the company, winding up of the company, variation of shareholder’s right etc. now cannot be made by the BODs, unless expressly authorised to do so, because such matters do not relate to ‘ordinary business’. In many cases the Board has to take consent of the shareholders in general meetings and certain transaction are required by the statute to be made by concurrent authorization of the shareholders and BODs.
As stated above, the corporate world has adopted the rule of majority in decision making process and in management of the companies but **oppressed minority** has got right to move to the Tribunal. Whenever the affairs of the company have been or are being conducted in a manner prejudicial to public interest or in a manner prejudicial or oppressive to any other member or members, an application can be made to the Tribunal under section 241(1) (a) of the Act. Alternatively, an application can be made to the Tribunal under sub-clause (b) of this section on the grounds that the material change, not being a change brought about by, or in the interests of, any creditors, including debenture holders or any class of shareholders of the company, 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 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 its interests or its members or any class of members.

Section 241 of the Act provides that the requisite number of members, who must sign the application to apply to the Tribunal. In the case of a company having a share capital, the application must be signed by not less than one hundred members of the company or not less than one-tenth of the total number of its members, whichever is less, or 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. In the case of a company not having a share capital, the application must be signed by not less than one-fifth of the total number of its members. The Tribunal has got several powers to regulate the affairs of the company.

A new, much awaited, significant provision in the form of Section 245 is provided in the Act of 2013 which empowers to bring **class action** by members or depositories against the mis-management or conduct of the affairs of the company which is conducted in a manner prejudicial to the interests of the company or its members or depositors. The requisite number of members in case of a company
having a share capital, not less than one hundred members of the company or not less than such percentage of the total number of its members as may be prescribed, whichever is less can apply to Tribunal for seeking all or any of the following remedial action to restrain the company from committing an act which is *ultra vires* the articles or memorandum of the company or to restrain the company from committing breach of any provision of the company’s memorandum or articles.

Another significant protection available to investors is in the form of **inspection, inquiry, investigation and audit**. Since this is the main objective of this research so it has been discussed in detail from chapters III to V.

In the light of Section 125 of the Act, **Investor Education and Protection Fund (IEPF)** for the protection and education of investors have been established. The main objective of IEPF is to equip the investors with better knowledge of protection against frauds. This fund is managed by a committee that consists of the Secretary, Company Affairs, as well as members from RBI, SEBI (Board) and experts on investor protection. The Board ensures maintenance of proper and separate accounts and other relevant records in relation to the fund. Accordingly, Board has made regulations for investors’ protection and education fund, 2009, with a view to strengthen its activities for protection of investors. Board also deals with the redressal of investors’ grievances related with capital market. Section 11(2) of the SEBI Act gave wide power to Board to implement the legislators’ desire of investor protection.

Section 11C of the SEBI Act has empowered the Board to investigate when there is reasonable ground to believe that the transactions in securities are being dealt with in a manner detrimental to the investors or the securities market; or any intermediary or any person associated with the securities market has violated any of the provisions of this Act or the rules or the regulations made or directions issued by the Board there under, it may, at any time by order in writing, direct any person (Investigating Authority) specified in the order to investigate the affairs of
such intermediary or persons associated with the securities market and to report thereon to the Board.

SEBI has got wide powers to regulate the securities market and to protect the interest of investors in primary market as well as secondary market. The Board has powers to regulate the functioning of stock broker, sub brokers or other intermediaries, so that investor’s money cannot be lost by malpractices or in other way. The Board had issued guidelines for the protection of the investors through the Securities and Exchange Board of India (Disclosure and investor protection) Guidelines, 2009 replacing Guidelines of 2000. These guidelines have been issued by the Board in pursuance of section 11 of the SEBI Act, 1992. SEBI has always been emphasizing on the importance of disclosure standards for corporate in disseminating relevant and correct information of public issues to the investors.

SEBI has also issued Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Markets Regulations, 2003, to ensure fair, efficient, and transparent markets which are closely linked to protecting investors from unfair, manipulative, or fraudulent practices, including synchronized trading, front-running, mis-selling etc.

SEBI has also passed regulation “Prohibition of Manipulative and Deceptive Devices, Insider Trading and Substantial Acquisition of Securities or Control.” Section 12 A of Chapter VA of SEBI Act, which was inserted by Amendment Act, 2002, prohibits any person who directly or indirectly uses or employs, in connection with the issue, purchase or sale of any securities listed or proposed to be listed on a recognized stock exchange, any manipulative or deceptive device or contrivance in contravention of the provisions of this Act or the rules or the regulations. This also prohibits engagement in any act, practice, course of business which operates or would operate as fraud or deceit upon any person, in connection with the issue, dealing in securities, in contravention of the provisions of this Act or the rules or the regulations.
SEBI has viewed insider trading a very serious offence and regarded it as against the investor’s interests. To prevent this, SEBI has made Prohibition of Insider Trading) Regulation, 2003 which will soon replaced by another regulation in 2015. If a person found guilty of insider trading, he can be sent to prison for up to 10 years or be required to pay a fine of up to Rs.25 crore or thrice the amount of profits made.

SEBI is empowered to adjudicate and stipulate penalties in case of contravention of its provision, rule and regulation. Section15A to 15HB of chapter VIA of the SEBI Act prescribes penalties for the violation of the provisions of the Act, rules and regulation made there under. Section 15I to 15JB provides the power of SEBI for adjudication.

Section 15HA prescribes that if any person indulges in fraudulent and unfair trade practices relating to securities, he shall be liable to a penalty which shall not be less than five lakh rupees but which may extend to twenty-five crore rupees or three times the amount of profits made out of such practices, whichever is higher.

SEBI is also empowered to inspect the Stock Exchanges to review of market operations, organizational structure and administrative control to ascertain as to whether - (a) It provides a fair, equitable, transparent and growing market to the investors, (b) Its organization system and practices are in accordance with the Securities Contracts (Regulation) Act, 1956 [SC(R) Act], 1956 and rules framed there under, (c) It has implemented the directions, guidelines and instructions issued by SEBI/ Government of India from time to time and (d) It has complied with the conditions, if any, imposed on it at the time of renewal / grant of its recognition under section 4 of the SC(R) Act, 1956.

During the year 2013-14, SEBI did comprehensive inspections at ten stock exchanges, namely Bombay Stock Exchange, MCX-SX Stock Exchange, Pune Stock Exchange, Jaipur Stock Exchange, United Stock Exchange, Interconnected Stock Exchange, Bhubaneswar Stock Exchange, Calcutta Stock Exchange, Vadodara Stock Exchange and Madhya Pradesh Stock Exchange. In addition,
during 2013-14, compliance inspections were carried out at Pune Stock Exchange, OTC Exchange and Uttar Pradesh Stock Exchange. The compliance inspections of exchanges were carried out for the purpose of renewal of recognition of stock exchange. Further, inspections were carried out prior to the commencement of various segments at respective stock exchanges. In 2013-14, inspections were conducted before the commencement of debt segment at NSE and BSE, currency derivative segment at BSE and SME segment at MCX-SX.

SEBI has also did comprehensive inspection of Depositories, 350 market intermediaries, stock brokers and 217 sub brokers and reviewed the market operations, organizational structure and administrative control to ascertain as to whether these are providing a fair, equitable, transparent and growing market to the investors, during 2013-14.

Thus, SEBI is empowered by SEBI Act, 1992 and various amendments in the Act from time to time, to protect the investors’ interest and promote healthy development of Indian financial markets.

Chapter III has dealt the first research question i.e., whether the inspection of company’s documents will serve to check fraudulent or unlawful conduct of the company in order to protect the rights and interests of investors? This chapter described that the inspection of books of account and other books and paper of a company is necessary to know the fairness and transparent functioning of the company accordance with the Act.

Inspection is a useful instrument and the preliminary step for finding out the true and fair view of the state of company’s affairs. Every company is required to maintain the books of account, registers, annual returns and other records at the registered office of the company. Therefore a company should prepare its annual report as per the section 92 of the Companies Act, 2013 and it should be duly signed by the company secretary or director if there is no company secretary. This annual reports are also required to be filed at ROC within 60 days from the completion of AGM.
In case of non-compliance, section 94(5) of the Act has prescribed punishment with fine which shall not be less than rupees fifty thousand but which may be extended up to rupees five lakh. The Act has also prescribed to maintain the books of account and other relevant paper in electronic form. Section 400 also clarifies that the electronic form shall be exclusive, or in the alternative or in addition to the physical form.

Inspection of books of account and other books and paper of a company can be done by the ROC or inspector duly appointed by the Central Government under section 206 or any other person/authority as mentioned in the Act. They enjoy with certain powers as mentioned in the section 206 (5) of the Act, during inspection. They also have the power to summon and enforce the attendance of persons and examine them on oath as are vested in a civil court, during inspection. They can also seize the doubtful documents during inspection.

Investor of a company can also inspect such documents and records during office hours without paying any fee and they can also take the extracts or copies of it. Inspection of such documents of a company enables the investors to check the true affairs of the company. They would like to see that their investments are safe and also being used for the intended purpose. If the investors are not satisfied with affairs of the company, they may sell out the shares of that company which may ultimately lead into reduction of company’s capital. Therefore, companies are bound to maintain the proper books of account and records according to the provision of the Act in order to sustain and prosper further. This will help in prevention of fraud which ultimately provides better protection of the rights and interests of investors.

Here, it is also to be noted that the inspection under section 206 and 207 is not an investigation, though it may lead to one, in case, anything wrong or objectionable or fraudulent. The right to inspection is limited to books of account and other books and paper only. The inspector cannot under the guise of this right, undertake a roving inquiry into all the affairs of the company. Persons inspecting are merely
report making authority. They are required to submit an inspection report to the Central Government after completion of inspection.

Now, it is on the discretion of the Central Government to order for further investigation into the affairs of the company (section 210), in case the affairs of the company are not in consonance with the Act. Meantime, such default company will get time to destroy, mutilated, alter, falsified or secreted of such documents. Therefore, to prevent such occurrences, it is suggested that inspectors should be empowered to start investigation *suo motto* along with the submission of report to Central Government and recommendation for further investigation into the affairs of the company by giving his reasons in support. Accordingly, insertion of subsection (2) is suggested in Section 208 of the Companies Act, 2013, in this regard.

Draft proposal of subsection (2) is indicated in *bold italic* font

**208. Report on inspection made**

(1) The Registrar or inspector shall, after the inspection of the books of account or an inquiry under section 206 and other books and papers of the company under section 207, submit a report in writing to the Central Government along with such documents, if any, and such report may, if necessary, include a recommendation that further investigation into the affairs of the company is necessary giving his reasons in support.

(2) *When there is reasonable ground to belief that serious nature of fraud has occurred, the Registrar of inspector shall start investigation *suo moto* along with submission of inspection report to the Central Government and recommendation of investigation as mentioned in sub section (1).*

The Calcutta High Court has held in *Indra Prakash Karnani v. Registrar of Company* [(1985) 57 Comp. Cas. 662 (Cal)] that Registrar of the Companies has right to inspect the books of account and if he is prevented from rendering inspection of accounts, the directors of the company may be prosecuted. A prior prosecution of company is not a pre-condition for prosecution of director of the
company and he is entitled to demand inspection of the books of accounts even in his office under clause (iii) of subsection (5) of section 209-A of the Act of 1956 [Now, 206(3) (c) of the Act of 2013]. However, it can be made at any time during business hours.

In *Bajoria B.M. v. Union of India* [(1972) 42 Comp. Cases 338 (Del)], the Delhi High Court held that the power of inspection is different from an investigation under the Act and that is not necessary for the Registrar before filling a complaint on the basis of inspection of accounts to give to a company a copy of the inspection report. In this way the courts of India are also vigilant in implementation of the powers of inspector or ROC for the inspection of documents and other records of the company so that the investors can be protected against any intended corporate frauds.

**Chapter IV** has described the provision related to investigation and how it serves as a means of protection of investors and also tested the second research question. Though investors are the real owners of a company but the power of management of the company is vested in the Board of directors. This may, sometimes, lead to abuse of power by few directors. Lord Acton has said in this regard that ‘Power corrupt; absolute power corrupt absolutely’. Hence, to avoid monopoly of Board of directors, the Central Government reserves its right to investigate the affairs of the companies, especially in the cases of alleged frauds or the oppression of the minority shareholders, to protect their interests.

Investigation of a company is the process to examine the management of the company’s affairs to find out whether the company is functioning according to the provisions of the Company Act and other relevant laws of the country. Investigation of the affairs of a company is the investigation of all its business affairs i.e. profits and losses, assets including goodwill, contracts and transactions, investments and other property interests and control of subsidiary companies too.

The purpose of investigation is to discover something which is apparently not visible to the naked eye or on the face of it. An order of investigation can, *inter
alia, be made when the Tribunal is of opinion that the persons in management are guilty of fraud, siphoning off of funds, misfeasance, mismanagement or other misconduct in carrying on the day to day affairs of the company.

The Central Government is empowered to appoint inspectors to investigate the affairs of such companies, which are not complying the provision of the Companies Act, 2013, either, on its own if it is of the opinion that such investigation is required on the report of the Registrar or Inspector under section 208(i.e. report on inspection made) or in public interest that has pointed out the huge financial irregularities. The Central Government is also empowered to order investigation into the affairs of a company on intimation of a special resolution passed by a company that its affairs are required to be investigated, or the Tribunal has passed order in the public interest.

Investigation may be also carried out when there is allegation 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 any person concerned in the formation of the company or the management of its affairs have in connection therewith. The Tribunal may pass an order that the affairs of a company ought to be investigated by an inspector appointed by the Central Government. If such an order is passed by the Tribunal, it is necessary for the Central Government to appoint inspector(s) to investigate the affairs of the company in respect of such matter.

The Central Government is also empowered to investigate the ownership of a company when satisfied that there is good reason, in public interest, to know the persons who are financially interested in the company and who control the policy or materially influence it. The Central Government, on the order of the Tribunal, appoints one or more inspectors to investigate and report on matters relating to the company and its membership for the purpose of determining the true persons who are or have been financially interested in the success or failure, whether real or apparent, of the company or who are or have been able to control or to materially
influence the policy of the company. In the case of a company intended to operate in modern welfare State, the concept of public interest takes the company outside the conventional sphere of being a concern in which the shareholders alone are concerned. It emphasises the idea of the company functioning for the public good or general welfare of the community [N.R. Murthy v. Industrial Development Corporation of Orissa Ltd (1977)]. Now, under sub-clause (c) of Section 210(1) of the Companies Act, 2013, the Central Government has discretion to order an investigation into the affairs of company in public interest.

In Union of India v. Mukta Arts Ltd [(2007) 137 Comp. Cas. 648 (CLB)], it was held that investigation into the affairs of a company can be ordered when the inspection report has pointed out the huge financial irregularities.

The Supreme Court of India has observed in Sri Ramdas Motor Transport Ltd. v. Tadi Adhinarayana Reddy [AIR 1997 SC 2189] that the writ jurisdiction is not appropriate Forum to invoke the investigation of affairs of a company. The power to appoint an inspector to investigate the affairs of the company has to be exercised by the Central Government after preliminary scrutiny by the Registrar of Companies or the CLB (now, Tribunal) under section 234, 235 and 237 of the Companies Act, 1956 (now, section 206, 210 and 213 of the Act of 2013). The investigation cannot be executed on the basis of allegations made by one shareholder.

Thus, the main objective of investigation is to redress the issue of mismanagement of a company and to protect the interest of members/shareholders, debenture holders, creditors and other investors of the company. The Central Government may also define the scope of the investigation by inspector with respects to the matters or the period to which it is to extend or otherwise.

Inspector(s), appointed by the Central Government to investigate the affairs of a company, they enjoy certain powers for the smooth function during investigation which includes power to carry out investigation into affairs of the company and its related subsidiary companies, to compel directors and its officers for the
production of documents, to examine them on oath, to take down notes of
examination in writing, seizure of documents, to seek support from other
authorities etc.

Inspector is required to prepare and submit a report to the Central Government.
Under Section 223 of the Companies Act, 2013, the inspector, if so directed by the
Central Government, shall submit interim reports to that Government, and on the
conclusion of the investigation, shall submit a final report to the Central
Government. Employees of the company are protected against dismissal or
discharge or removal or reduction of rank or change of the terms of employment to
his disadvantage during investigation.

On receipt of such report, the Central Government studies the report and if the
company is not functioning in accordance with the provisions of the Companies
Act and detrimental to the investors, the follow up action taken may be initiation of
criminal prosecution against such company or recovery of loss or property or
damages or order for winding up of such company. There are various criminal
liabilities has been provisioned in the Companies Act, 2013.

Under Section 211 of the Companies Act, 2013, the Central Government has, now,
constituted the Serious Fraud Investigation Office (SFIO) in the ministry of
corporate affairs. This is a specialized, multi-disciplinary organization to deal with
serious cases of corporate fraud. This was also a major recommendation made by
the Naresh Chandra Committee which was set up by the Government on 21 August
2002 on corporate governance.

Headquarters of this office is located in New Delhi, with field offices located in
major cities throughout India. The SFIO is headed by a Director not below the rank
of a Joint Secretary to the Government of India having knowledge and experience
in dealing with the matters relating to corporate affairs and also consist of experts
from various disciplines. The SFIO will only deal with investigation of corporate
frauds characterized by complexity and having inter- departmental and multi-
disciplinary ramifications. SFIO enjoys all the powers as provided to inspector
during investigation. In addition, he has also the power to arrest the accused, if authorised by the Central Government.

Therefore, investigation of the affairs of the company is an important means of protection of the interest of the investors. Investigation by Inspectors/SFIO may reveal the occurrence of various corporate frauds in speedy manner. SFIO is involved, when the Central Government finds that there is allegation of serious fraud in the company. The Central Government is empowered by the Companies Act, 2013 to investigate all the matters pertaining to frauds occurred in any company where the investors lost their hard earned money. An inspector can examine on oath any person involved in the fraud and may thereafter be used in evidence against him. In this work of inspector, the officers of the Central Government, State government, police or statutory authorities are duty bound to provide necessary assistance to him. An inspector/SFIO also enjoys all the powers as are vested in a civil court under the Code of Civil Procedure, 1908, while trying a suit during investigation. But it is also expected from them to work honestly and in responsible way in the investigation.

Since SFIO is a Government agency and its officials are appointed by the Central Government so there is strong apprehension for its unbiased and unfair working. Therefore, it is suggested that inspector/SFIO should conduct fair investigation of any alleged corporate fraud and then they should submit the detail report to the Central Government, otherwise the share price of the company will fall sharply in a single day, in reaction, merely on this bad news, which will result into huge loss, again, to investors.

In A. Ravishanker Prasad v. Prasad Production Pvt. Ltd(2007), the Andhra Pradesh High Court has also held that the order of investigation should not be ordered on mere suspicion or surmises.

In the Act, there is no provision, as such, by which the SFIO can suo moto investigate into a case where an alleged serious fraud has been committed. The SFIO lacks a proactive approach in this regard. The SFIO has to wait for the
Central Government’s order for the reference to be made to it. So, if there appears to be any fraud SFIO is toothless for taking any action against that particular company on its own motion. Therefore, SFIO should also be empowered to investigate *suo moto* like in the UK where the director of the Serious Fraud Office can *suo moto* investigate into a case.

It is suggested that SFIO should also be given power to initiate prosecution or imposing penalties when finds that the company is involved in fraud, like Serious Fraud Office (SFO) of U.K., which is an independent department which investigates and also prosecutes serious and complex fraud and corruption cases.

The appointment of the officers of the SFIO is on transfer and deputation basis which may be changed and permanent appointment may be made solely for the purpose of this agency. The efficiency of the agency may also be impeded due to frequent transfers of its personnel. It is submitted that in order to maintain continuity a permanent and tenure based structure should be made. The members of SFIO should not be transferred to other government departments.

57th Annual Report on the working and administration of the Companies Act, 1956, in pursuance of Section 638 of the Companies Act, 1956 (now, section 461 of the Act of 2013) for the year ended March 2013, disclosed that total 46 cases were referred to Serious Fraud Investigation Office (SFIO) under section 235/237 of the Companies Act, 1956 (now, section 210/213 of the Act of 2013), by the Ministry of Corporate Affairs, where the size of the alleged fraud was estimated to be at least Rs. 50 crores or more in each cases, for further investigation. The Ministry has received 22 investigation reports from SFIO during the period the financial year 2012-13 and prosecutions have been launched in various courts.

The report also states that total 139 cases were referred to SFIO for investigation up to 31 March 2013. Out of these, SFIO has submitted investigation report in 104 cases to the Ministry of Corporate Affairs till 31 March 2013. In 10 cases the order for investigation were either stayed or
quashed/withdrawn as on 31 March 2013 and the remaining 25 cases are under investigation.

The report, further, states that a total of 49950 prosecutions launched under the Companies Act, were pending in various courts as on 31 March 2012 and 6062 prosecutions were instituted during the year 2012-13 against 3293 companies and their officers. Thus, in all 56012 prosecutions were pursued in the courts during 2012-13. Out of these 6542 prosecutions were disposed of and 49470 were pending at the end of the year.

In Chapter V, the third research question has been tested i.e., whether audit of books of account and vouchers of the company will serve to check fraudulent or unlawful conduct of the company in order to protect the rights and interests of investors. This chapter has described the provision of audit and how it can serve as an important means to protect the interests of investors.

The audit is intended for the protection of the investors and the auditing is expected to examine the accounts maintained by the directors with a view to inform investors of the true financial position of the company. The investors of the company are mainly depend upon the good faith and efficiency of the auditor appointed to check the accounts and certify the balance sheet of the company, the auditors do have a chance to make a detailed check of the accounts, call for the information and satisfy themselves that the accounts have been properly maintained and the balance sheet are fairly drawn up.

The auditors are, therefore, under duty to safeguard the rights of investors vis-a-vis the activities of the directors in the purported exercise of their powers in dealing with assets of the company. They are also known as watchdog. It doesn’t mean that an auditor owes duty only towards the company to which he has been appointed. He has also ethical duty to report the cases of fraud to concerned authorities promptly when detected. He is not expected to be a detective nor is he required to approach his work with a suspicious or pre-conceived impression that there is something wrong. He is watchdog but not a blood hound. However, if
there is anything that excites, suspicion in him, he should examine into the matter. But in the absence thereof, he is only required to be reasonably cautious and careful.

Auditors also play a major role in ensuring transparency and accountability in the corporate world, thus they are also, often, called as gatekeepers, eye and ear of the company. It is also equally true that a fraud may be discovered pertaining to a particular period after the auditor has completed his audit, it does not necessarily mean that the auditor has been negligent or that he has not performed his duties completely. He checks and verifies the books and accounts and vouchers of the company as presented before him. If he has conducted his audit by applying due care and skill in consonance with the accepted professional standards expected, the auditor would not be held responsible for not having discovered that fraud. Therefore it is expected that the auditor should be vigilant in conducting audit of the company.

The shareholders of a company place a very high trust on the auditor's report, which apparently shows the true and fair view of the accounts of a company. The auditors should perform their duties with utmost care and vigilance to ensure that there are no illegal or improper transactions. It is very important for auditor to use their professional skills and make a reasonable examination of the accounts to see that the dealings are not illegal or improper and it is their duty to uncover such activities. As audit has revealed many corporate frauds in the past so it is an important means to protect the interests of investors.

It is suggested that severe civil liabilities should be imposed to auditors or auditing firm in cases of their involvement in corporate fraud if overlooked the account or abetted in the occurrence of fraud. An auditor also performs his duties as an agent of the shareholders, so he is expected to safeguard their interests. He must exercise his reasonable care and diligence in the performance of his duties. If he fails to do so and in consequence the principal suffers any loss, he may be liable to compensate loss caused to the company resulting from his negligence. If an
auditor of a company contravenes any of the provisions of section 139, section 143, section 144 or section 145, of the Companies Act, 2013, he will be held liable with fine which shall not be less than twenty-five thousand rupees but which may extend to five lakh rupees under S.147 (2) of the Act. It is suggested to increase the maximum civil liability of an independent auditor up to rupees twenty five lakh and in case of an audit firm up to rupees one crore.

It is also suggested that criminal liability of an auditor to be made severe. If an auditor has contravened provisions of audit as incorporated in the Companies Act knowingly or willfully with the intention to deceive the company or its shareholders or creditors or tax authorities, he should be punished with imprisonment for a term which may extend to one year and with fine as prescribed in Section 147 of the Companies Act. In order to make more deterrent effect, it is suggested that the punishment may be increased for a term which may be extended to three years in place of present term of one year.

Provision of statutory duty of auditors towards third parties/society is lacking in the Companies Act, 2013. They have contractual relationship with the management of appointing company. Under privities of the contract, they are not answerable to any third party including the shareholders of the company. Therefore it is suggested that provision should be made in the Act, for the auditors of public companies to meet the requirement of its shareholders. This will bring transparency in the system and also create accountability of an auditor to the investors of the company.

It is, further, suggested that duration of appointment of an independent auditor and an audit firm should be made equal. Section 139 (2) of the Act has prescribed for compulsory rotation of the auditors for the listed companies and certain class or classes of companies. Under this section, such companies shall not appoint an individual as auditor for more than one term of five consecutive years whereas an audit firm shall not be appointed for than two terms of five consecutive years. After the expiry of the period as aforesaid the auditors are required to be
rotated. It is suggested that Audit firm should also be appointed for five years instead of two terms of five consecutive years, in order to ensure auditor’s independence and also to prevent any kind of nexus that may develop between the company and auditors of audit firm, in long run.

It is also suggested that **internal audit mechanism to be made more strengthened** and it should also be done by the competent persons. If possible, such work should be entrusted to outside auditors. It also suggested that internal audit should not be done by the departmental people.

The Companies Act, 2013 has minimised several lacunae and provides effective control over arbitrariness of the directors of the companies. This Act did make two pronged attack on the problem, the first one is that shareholders were bedecked with effective weapons for exercising effective control over the BODs and realizing their rights and secondly the directors were restored to their rightful place of power and responsibility in the management of companies. Now the relationship between directors and shareholders has become healthier; much of the humbug and malpractices which were found in managerial actions have gradually disappeared. Directors have started concentrating on the managerial tasks for which they are primary appointed. Now they are not considered paternal guardian of shareholders. The suppliers of capital (shareholders) have started taking interest in the company’s affairs and they are able to know, in realistic terms, the current worth of their investment.

Finally, it is concluded that after detail study of the provisions of inspection, investigation and audit in the Companies Act, 2013 as well as in the Security and Exchange Board (SEBI) Act, 1992 and various judicial pronouncements, it is observed these provisions are sufficient to protect the interests of the investors in India and if all the above suggestions are incorporated, it will be more foolproof to prevent occurrence of corporate frauds in India and investors will not be in fear while making investment either in primary market of secondary market.

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