GUIDELINE ANSWERS

PROFESSIONAL PROGRAMME

(New Syllabus)

JUNE 2021 Session

MODULE 3

THE INSTITUTE OF
Company Secretaries of India
भारतीय कम्पनी सचिव संस्थान
IN PURSUIT OF PROFESSIONAL EXCELLENCE
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(Under the jurisdiction of Ministry of Corporate Affairs)
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In answers to the questions based on case study, the students may write any other alternative answer with valid reasoning.

The Guideline Answers contain information based on the Laws/Rules relevant for the Session. Students are expected to be well versed with the amendments in the Laws/Rules made upto **six** months prior to the date of examination.

C O N T E N T S

PROFESSIONAL PROGRAMME EXAMINATION

JUNE 2021

CORPORATE FUNDING & LISTINGS IN STOCK EXCHANGES

Time allowed : 3 hours *Maximum marks : 100*

NOTE : *Answer ALL Questions.*

PART A

Question 1

A Ltd. has been sanctioned Working Capital Limit of ₹ 2 crore from its banker at 11% p.a. Its tangible Net Worth is ₹6 Crore and its account is classified as a Standard Asset by banks/institutions. Till date company has not obtained any Credit Rating. Analysing the current trend of lower interest rate, CEO of A Ltd., Mr. X proposed to raise more funds by way of Commercial Papers (CPs) on the following terms :

(i) The period of the CPs shall be of 2 years.

(ii) The denomination of each CP shall be ₹ 1 Lakh and will be issued at Par Value.

(iii) The CPs shall be issued to retail investors.

(iv) The CPs shall be issued in Dematerialised Form only.

(v) The quantum of issue of CPs shall be of ₹ 4 Crore.

(vi) The trading of CPs will be purely on OTC basis.

You as Company Secretary of the A Ltd. have been asked to submit a Report advising the management on the following matters :

(a) Whether company is eligible for issuing Commercial Papers or not ?

(b) Whether company can issue CPs for ₹4 Crore and that too in Dematerialised form only for the period of 2 years or not ?

(c) Whether company can issue CPs to Retail Investors at Par Value in denomination of ₹ 1 Lakh each and trading shall be possible purely on OTC basis or not ?

(5 marks each)

Answer 1(a)

Yes, A Ltd. is eligible for issuing Commercial Papers (CPs) as it meets the following conditions, as issued by Reserve Bank of India

(1) the tangible net worth of the company, as per the latest audited balance sheet, is not less than ₹ 4 crore;

(2) company has been sanctioned working capital limit by bank/s or Financial Institutions; and

(3) the borrowal account of the company is classified as a Standard Asset by the financing banks/ institutions.

However, A Ltd. shall obtain credit rating for issuance of CPs from any one of the SEBI registered Credit Rating Agencies.

The minimum credit rating shall be 'A2' [as per rating symbol and definition prescribed by the Securities and Exchange Board of India (SEBI)] The company shall also appoint an Issuing and Paying Agent for issuance of CPs.

Answer 1(b)

CP can be issued in denominations of ₹ 5 lakh and multiples thereof. The amount invested by a single investor should not be less than ₹ 5 lakh (face value). Therefore, the Company can issue CPs for ₹ 4 crore.

While option is available to company to issue/hold CP in dematerialised or physical form, issuers and subscribers are encouraged to opt for dematerialised form of issue/ holding. However, banks, Financial Institutions (FIs) and Primary Dealers (PDs) are required to make fresh investments and hold CP only in dematerialised form.

CP can be issued for maturities between a minimum of 7 days and a maximum of up to one year from the date of issue. The maturity date of the CP should not go beyond the date up to which the credit rating of the issuer is valid. The Company therefore, can issue CPs for a period of 1 year or up to the period for which credit rating will be valid.

Answer 1(c)

Commercial Paper can be issued in denominations of ₹ 5 lakh and multiples thereof. The amount invested by a single investor should not be less than ₹ 5 lakh (face value). Hence, company cannot issue CPs in denomination of ₹ 1 lakh.

CP may be issued to individuals, banking companies, other corporate bodies (registered or incorporated in India) and unincorporated bodies, Non-Resident Indians and Foreign Institutional Investors (FIIs). The initial investor in CP shall pay the discounted value and not the par value and that too by means of a crossed account payee cheque to the account of the issuer through Issuing and Paying Agent (IPA).

Though CPs can be traded on OTC but all trades shall be reported within 15 minutes of the trade to the reporting platform of Clearcorp Dealing Systems (India) Ltd. (CDSIL).

Additionally, the SEBI has prescribed framework for listing of Commercial Papers. Post listing, CPs will be available for trading on stock exchange's trading platform.

Attempt all parts of either Q. No. 2 or Q No. 2A

Question 2

(a) The promoters of Z Ltd. holds 78 percent shares of the Equity Share capital of the company. The promoters are intending to reduce their holding to meet the provisions of regulatory authorities of minimum public subscription by way of Qualified Institutional Placement (QIP). Total Issued Share Capital of the Z Ltd. is ₹ 10 Crore consisting of 1 crore shares of ₹ 10 each. As a Company Secretary advise the Z Ltd. on the following points :

(i) What is minimum quantity the promoters should offer under the QIP ?

(ii) Provisions regarding the approval of shareholders.

(iii) Rules regarding the listing of these shares with the Stock Exchange.

(b) PQR Ltd. is listed on SME platform. The company has excellent performance in terms of turnover and profit during last few years. It is interested in migrating to the Main Board.

Prepare a note on the same.

(c) Enumerate the rules for distribution of cash flows by InvIT.

(5 marks each)

OR (Alternate question to Q. No. 2)

Question 2A

Distinguish between the following :

(i) Overdraft and Cash Credit Account

(ii) Buyers' Credit and Suppliers' Credit

(iii) Letter of Credit Limit and Bank Guarantee Limit.

(5 marks each)

Answer 2(a)

(i) Every listed company is required to maintain public shareholding of at least twenty-five per cent as per the Securities Contracts (Regulation) Rules, 1957 and therefore, balance can be held by promoter / promoter group. In the given case the promoters can offer shares up to 3% of 1 crore shares i.e. 3 lakh shares of ₹ 10 each under QIP.

(ii) No resolution is required to be passed by the Shareholders in case the QIP is through an offer for sale by the promoters for compliance with minimum public shareholding requirements.

(iii) Since the shares offered are in offer for sale and hence, already listed, no further listing is required.

Answer 2(b)

Under the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018, an issuer, whose specified securities are listed on a SME Exchange and whose post issue face value capital is more than ten crore rupees and up to twenty five crore rupees, may migrate:

- its specified securities to Main Board if its shareholders approve such migration by passing a special resolution through postal ballot to this effect; and
- if such issuer fulfils the eligibility criteria for listing laid down by the Main Board.

However, the special resolution shall be acted upon if and only if the votes cast by shareholders other than promoters in favour of the proposal amount to at least two times the number of votes cast by shareholders other than promoter shareholders against the proposal which means that resolution shall be approved by majority of minority.

Where the post issue face value capital of an issuer listed on SME exchange is likely to increase beyond twenty five crore rupees by virtue of any further issue of capital by the issuer by way of rights issue, preferential issue, bonus issue, etc. the issuer shall first migrate its specified securities listed on SME exchange to Main Board and seek listing of specified securities proposed to be issued on the Main Board subject to the fulfilment of the eligibility criteria for listing of specified securities laid down by the Main Board.

However, no further issue of capital by the issuer shall be made unless:

- the shareholders of the issuer have approved the migration by passing a special resolution through postal ballot wherein the votes cast by shareholders other than promoters in favour of the proposal amount to at least two times the number of votes cast by shareholders other than promoter shareholders against the proposal;
- the issuer has obtained in- principle approval from the Main Board for listing of its entire specified securities on it.

Answer 2(c)

With respect to distributions made by the InvIT and the Holding company (Holdco) and/or SPV,

(i) not less than 90% of net distributable cash flows of the SPV shall be distributed to the InvIT/ Holdco in proportion of its holding in the SPV subject to applicable provisions in Companies Act, 2013 or Limited Liability Partnership Act, 2008;

(ii) not less than 90 % of net distributable cash flows of the InvIT shall be distributed to the unit holders;

(iii) such distributions shall be declared and made not less than once every six months in every financial year in case of publicly offered InvITs and not less than once every year in case of privately placed InvITs and shall be made not later than 15 days from the date of such declaration;

(iv) subject to above condition, such distribution shall be in the manner as mentioned in the offer document or placement memorandum.

Answer 2A(i)

Overdraft : Overdraft means allowing the customer to draw cheques over and above credit balance in his account. Bank overdraft is line of credit that overs the transaction if the bank account balance drops below zero. Overdraft is normally allowed to Current Account customers and in exceptional cases Savings bank account holders are also allowed to overdraw their account. High rate of interest is charged on daily debit balance of overdraft account as these are clean advances i.e. banks do not have any securities to fall back if these facilities are not repaid. There are two types of overdraft accounts as prevalent in Banks i.e. (i) Temporary overdraft or clean overdraft and (ii) Secured overdraft.

Temporary overdrafts are allowed purely on personal credit worthiness of the customer concerned and it is meant for the customer to meet some urgent commitments on rare

occasions. Allowing a customer to draw against his cheques sent in clearing known as "against clearing" also falls under this category. Secured overdraft is allowed up to a certain limit against some tangible security like bank deposits, LIC policies, National Saving Certificates, shares and other similar assets. Secured overdraft is most popular with traders as lesser operating cost, simple application and document formalities are involved in this facility.

Cash Credit Account : A cash credit facility is a short-term finance to a borrower company, having a tenure of up to one year which can be renewed for further period by the bank on the basis of projected sales and satisfactory operation in the account during the period of finance. Cash credit facility is extended in two forms viz. Open Cash Credit and Key Cash Credit. Open Cash credit account is a running account just like a current account where the borrower is allowed to maintain debit balance in the account up to a sanctioned limit or drawing power whichever is lower.

The Cash Credit facility is offered to borrowers normally either against pledge (Key Cash Credit) or hypothecation of stocks of raw materials, semi - finished goods and finished goods and Book Debts (Receivables). This type of limit is offered mainly to traders who find it difficult to maintain stock register and submitting periodic stock statements. In the case of Key Cash Credit, the borrower lodges the stocks in his godown and the key of the godown will be handed over to the bank. By this process, the goods lodged in the godown are pledged to the bank and the bank will allow the customer to draw funds against the value of the goods less margin. This is known as Drawing Power. The pledged goods are allowed to be removed by the borrower on remitting into his CC account the amount equivalent to value of the goods. The bank would release further funds to the borrower within the Drawing Power (DP)/sanctioned limit on borrower depositing (pledge) more stock in the godown. Therefore, such facility is called Key Cash Credit. Cash Credit limits are also sanctioned to a borrower against security of term deposits, LIC policies, National Saving Certificates or Gold Jewels.

Answer 2A(ii)

Buyers' Credit : It refers to loans for payment of imports into India arranged by the importer from overseas bank or financial institution. Imports should be as permissible under the extent of Foreign Trade Policy of the Director General of Foreign Trade (DGFT). For the overseas exporter the transaction becomes a cash sale.

Suppliers' Credit : Suppliers' credit relates to the credit for imports into India extended by the overseas supplier. In this case too, imports should be as permissible under the extent of Foreign Trade Policy of the DGFT. Usually this type of facility is availed for import of Capital goods. The importer pays an agreed amount of down payment and the balance amounts are paid in instalments over a deferred period. Interest rates for the transactions are decided at the initial contracting stage and are included in the instalments payable by the importer.

Answer 2A(iii)

Letter of Credit Limit : Letter of credit (LC) is a method of settlement of payment of a trade transaction and is widely used to finance purchase of raw material, machinery etc. It contains a written undertaking by the bank on behalf of the purchaser to the seller to make payment of a stated amount on presentation of stipulated documents and

fulfilment of all the terms and conditions incorporated therein. Letters of credit thus offers both parties to a trade transaction a degree of security. The seller can look forward to the issuing bank for payment instead of relying on the ability and willingness of the buyer to pay.

Bank Guarantee Limit : Appraisal of proposals for Bank guarantees is done with same diligence as in the case of fund-based limits. Whenever an application for the issue of bank guarantee is received, Bank examine & satisfy the following aspects:

a) The need of the bank guarantee & whether it is related to the applicant's normal trade/business.

b) Whether the requirement is one time or on the regular basis.

c) The nature of bank guarantee i.e., financial or performance.

d) Applicant's financial strength/ capacity to meet the liability/ obligation under the bank guarantee in case of invocation.

e) Past record of the applicant in respect of bank guarantees issued earlier, e.g., instances of invocation of bank guarantees, the reasons thereof, the customer's response to the invocation, etc.

f) Present outstanding on account of bank guarantees already issued.

g) Margin

h) Collateral security offered.

Question 3

(a) International Monetary Fund (IMF) plays a vital role in the global economy. Explain its mission and activities.

(b) What do you understand by Green Debt Securities ? Explain.

(c) Prepare a flow chart for issuance of Non-convertible Redeemable Preference Shares under SEBI (Non-convertible Redeemable Preference Shares) Regulations, 2013.

(5 marks each)

Answer 3(a)

The International Monetary Fund (IMF) is an organization of 189 countries, working to foster global monetary cooperation, secure financial stability, facilitate international trade, promote high employment and sustainable economic growth and reduce poverty around the world. Created in 1945, the IMF is governed by and accountable to the 189 countries that make up its near-global membership.

The IMF's primary purpose is to ensure the stability of the international monetary system, the system of exchange rates and international payments that enables countries (and their citizens) to transact with each other. The Funds mandate was updated in 2012 to include all macroeconomic and financial sector issues that bear on global stability.

The IMF assists countries hit by crises by providing them financial support to create breathing room as they implement adjustment policies to restore economic stability and growth. The IMF's fundamental mission is to ensure the stability of the international monetary system which it does so in three ways:

(i) keeping track of the global economy and the economies of member countries:

(ii) lending to countries with balance of payments difficulties; and

(iii) giving practical help to members.

It also provides precautionary financing to help prevent and insure against crises. The IMF's lending toolkit is continuously refined to meet countries' changing needs.

Answer 3(b)

A Debt Security shall be considered as "Green or Green Debt Securities", if the funds raised through issuance of the debt securities are to be utilised for project(s) and/ or asset(s) falling under any of the following broad categories:

(i) Renewable and sustainable energy including wind, solar, bioenergy, other sources of energy which use clean technology etc.;

(ii) Clean transportation including mass/public transportation etc.;

(iii) Sustainable water management including clean and/or drinking water, water recycling etc.;

(iv) Climate change adaptation;

(v) Energy efficiency including efficient and green buildings etc.;

(vi) Sustainable waste management including recycling, waste to energy, efficient disposal of wastage etc.;

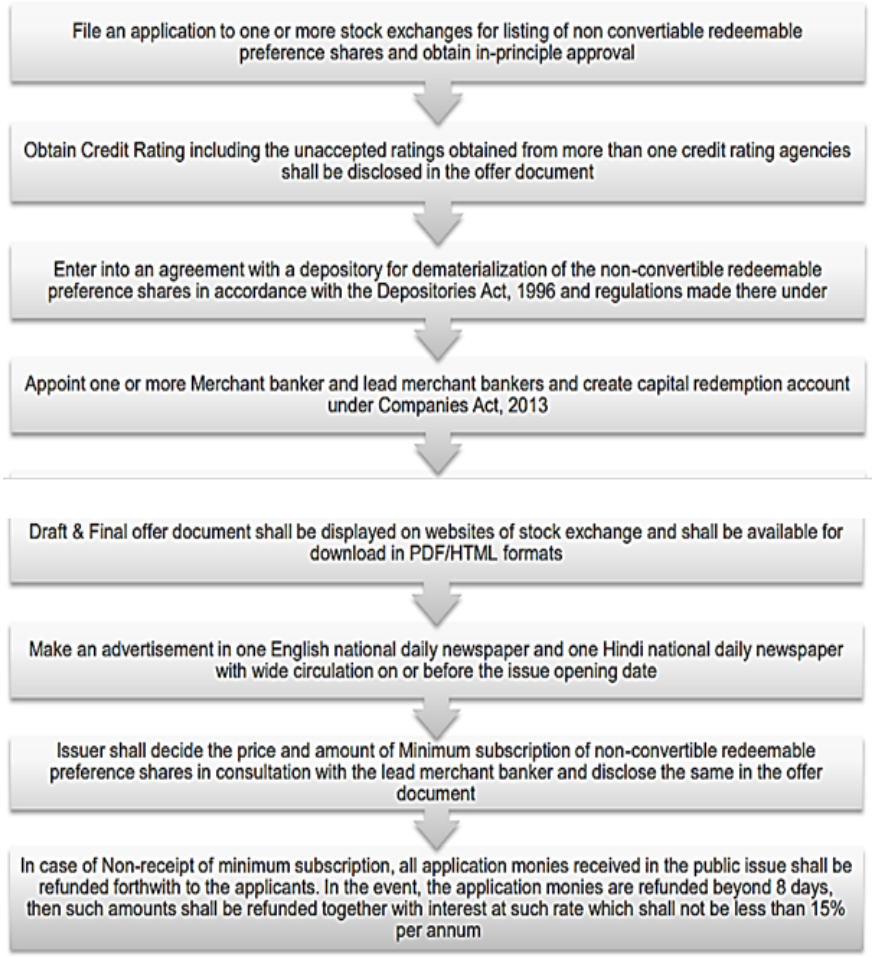
(vii) Sustainable land use including sustainable forestry and agriculture, afforestation etc.;

(viii) Biodiversity conservation;

(ix) Any other category as may be specified by SEBI, from time to time.

Answer 3(c)

Flow Chart for Issuance of Non-Convertible Redeemable Preference Shares under the SEBI (Non-Convertible Redeemable Preference Shares) Regulations, 2013 is as under:



Question 4

(a) *Whether investment by Angel Funds are restricted by any specific guidelines. Discuss.*

(b) *Discuss the rules relating to pricing and lock-in under Employees Stock Purchase Scheme (ESPS) including exception if any, thereof.*

(c) *Mention the Regulatory Framework in India for Issue of ADR/GDR/FCCBs/ FCEBs.*

(d) *Explain the conditions for Listing of Non-convertible Redeemable Preference Shares issued on private placement basis on a recognized stock exchnage.*

(e) The following data pertains to XYZ Ltd. :

	₹
Projected Sales	*20,00,000*
Creditors	*3,00,000*
Bank Borrowings	*3,30,000*
Current Assets	*7,40,000*

Assess the Working Capital requirement of XYZ Ltd. using the method given by Nayak Committee.

(3 marks each)

Answer 4(a)

1) Yes, investment by Angel funds are governed by the SEBI (Alternative Investment Funds) Regulations, 2012. Angel funds shall invest in venture capital undertakings which:
   (i) complies with the criteria regarding the age of the venture capital undertaking/ start-ups issued by Ministry of Commerce and Industry, Government of India or such other policy made in this regard which may be in force;
   (ii) have a turnover of less than twenty five crore rupees:
   (iii) are not promoted or sponsored by or related to an industrial group whose group turnover exceeds three hundred crore rupees.

   For the purpose of this clause, "industrial group" shall include a group of body corporates with the same promoter(s)/promoter group, a parent company and its subsidiaries, a group of body corporates in which the same person/ group of persons exercise control, and a group of body corporates comprised of associates/subsidiaries/holding companies. For the purpose of this clause, "group turnover" shall mean combined total revenue of the industrial group.
   (iv) are not companies with family connection with any of the angel investors who are investing in the company.
2) Investment by an angel fund in any venture capital undertaking shall not be less than twenty five lakh rupees and shall not exceed ten crores rupees.
3) Investment by an angel fund in the venture capital undertaking shall be locked-in for a period of one year.
4) Angel Funds shall not invest in associates.
5) Angel funds shall not invest more than twenty-five per cent of the total investments under all its schemes in one venture capital undertaking, the compliance of which shall be ensured by the Angel Fund at the end of its tenure.
6) An angel fund may also invest in the securities of companies incorporated outside India subject to such conditions or guidelines that may be stipulated or issued by the Reserve Bank of India and SEBI from time to time.

Answer 4(b)

The company may determine the price of shares to be issued under an Employee Stock Purchase Scheme, provided they conform to the provisions of accounting policies as prescribed under the SEBI (Share Based Employee Benefit) Regulations, 2014. Shares issued under an ESPS shall be locked-in for a minimum period of one year from the date of allotment.

However, in case where shares are allotted by a company under an ESPS in lieu of shares acquired by the same person under an ESPS in another company which has merged or amalgamated with the first mentioned company, the lock-in period already undergone in respect of shares of the transferor company shall be adjusted against the lock-in period required under this sub-regulation.

If ESPS is part of a public issue and the shares are issued to employees at the same price as in the public issue, the shares issued to employees pursuant to ESPS shall not be subject to lock in.

Answer 4(c)

Capital can be raised from international capital market in foreign currency by accessing foreign capital market. Funds raised through foreign currency are called as euro equity or debt. Indian companies are allowed to raise capital in the international market through the issue of GDR/ADR/FCCB/FCEB and through External Commercial Borrowings.

Issuance of ADR/GDR/FCCBs/FCEBs are regulated by the following regulations in India:

- The Foreign Currency Convertible Bonds and Ordinary Shares (Through Depository Receipt Mechanism) Scheme, 1993
- Foreign Currency Exchangeable Bonds Scheme, 2008
- Depository Receipts Scheme, 2014
- Notifications/Circulars issued by Ministry of Finance (MoF), GOI.
- Consolidated FDI Policy.
- RBI Regulations/Circulars.
- Companies Act and Rules thereunder.
- SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015.

Answer 4(d)

An issuer may list its non-convertible redeemable preference shares issued on private placement basis on a recognized stock exchange subject to the following conditions as provided under the SEBI (Issue & Listing of Non-Convertible Redeemable Preference Shares) Regulations, 2013:

a) the issuer has issued such non-convertible redeemable preference shares in compliance with the provisions of the Companies Act, 2013 rules prescribed thereunder and other applicable laws;

b) credit rating has been obtained in respect of such non-convertible redeemable

preference shares from at least one credit rating agency registered with the SEBI. Where credit ratings are obtained from more than one credit rating agencies, all the ratings shall be disclosed in the offer document;

c) the non-convertible redeemable preference shares proposed to be listed are in dematerialized form;

d) the disclosures as provided in Regulation 18 of the SEBI (Non-Convertible Redeemable Preference Shares) Regulations, 2013 have been made;

e) the minimum application size for each investor is not less than ten lakh rupees;

f) the issuer shall create a capital redemption reserve in accordance with the provisions of the Companies Act, 2013;

g) the issuer shall not issue non-convertible redeemable preference shares for providing loan to or acquisition of shares of any person who is part of the same group or who is under the same management, other than to subsidiaries of the issuer, and

h) where the application is made to more than one recognised stock exchange, the issuer shall choose one of them as the designated stock exchange.

The issuer shall comply with conditions of listing of such non-convertible redeemable preference shares as specified in the Listing Agreement with the stock exchange where such non-convertible redeemable preference shares are sought to be listed.

Answer 4(e)

Net Working Capital = Current Assets - Current Liabilities i.e Bank Borrowings & Creditors

Net Working Capital = ₹ 7,40,000 - ₹ 6,30,000 = ₹ 1,10,000

(i) Minimum Working Capital required i.e 25% of Sales = 25% of 20,00,000 = ₹ 5,00,000

(ii) Margin or Minimum Borrower's contribution i.e. 5% of projected sales = 5% of 20,00,000 = ₹ 1,00,000

(iii) Margin or Net Working Capital whichever is higher to be deducted from 25% of Sales i.e. ₹ 5,00,000 – ₹ 1,10,000 = ₹ 3,90,000

So, maximum permissible finance as per Nayak Committee's recommendation in the case under consideration shall be ₹ 3,90,000.

PART B

Question 5

(a) Discuss the procedural requirements which a listed entity needs to delegate to a Share Transfer Agent to deal with unclaimed shares.

(b) Explain the conditions and procedure to be adopted by a listed company to change its name as per Regulation 45 of SEBI (LODR) Regulations 2015.

(c) List out the standard material contracts to be attached with the copy of Offer Document delivered to ROC for an IPO.

(d) SEBI has given a good recognition to the Company Secretaries. Discuss this statement in light of SEBI Regulations 2015. (5 marks each)

Answer 5(a)

The listed entity may delegate the following procedural requirements to a share transfer agent so as to deal with unclaimed shares:

i. Reminders to be sent

(1) The listed entity shall send at least three reminders at the address registered as per the following criteria:

(a) For shares in physical form, reminders shall be sent to the address given in the application form as well as last available address as per listed entity's record.

(b) For shares in demat form, reminders shall be sent to the address captured in depository's database or address given in the application form, in case of application made in physical form.

ii. Procedure in case of non-receipt of response to reminders

(1) For shares in demat form, the unclaimed shares shall be credited to a Demat Suspense Account' with one of the Depository Participants, opened by the listed entity for this purpose.

(2) For shares in physical form, the listed entity shall transfer all the shares into one folio in the name of "Unclaimed Suspense Account and shall dematerialise the shares held in the Unclaimed Suspense Account with one of the Depository Participants.

(3) The listed entity shall maintain details of shareholding of each individual allottee whose shares are credited to such demat suspense account or unclaimed suspense account, as applicable.

(4) The demat suspense account or unclaimed suspense account, as applicable shall be held by the listed entity purely on behalf of the allottees who are entitled to the shares and the shares held in such suspense account shall not be transferred in any manner whatsoever except for the purpose of allotting the shares to the allottee as and when he/she approaches the listed entity. Provided that all such shares, in respect of which unpaid or unclaimed dividend has been transferred under Section 124 (5) of the Companies Act, 2013, shall also be transferred by the listed entity in accordance with Section 124 (6) of the Companies Act, 2013 and rules made thereunder.

iii. Procedure in case of claim by allottee

As and when the allottee approaches the listed entity, the listed entity shall, after proper verification of the identity of the allottee either credit the shares lying in the Unclaimed Suspense Account or demat suspense account, as applicable, to the demat account of the allottee to the extent of the allottee's entitlement, or deliver the physical certificates after re-materialising the same,

depending on what has been opted for by the allottee, Provided that the rematerialising of the physical certificates shall be done only in case where the shares were originally issued in physical form.

Answer 5(b)

- Listed Entity is allowed to change its Name, subject to compliance with the following conditions as prescribed in the SEBI (LODR) Regulations, 2015:
  - at least 1 year has elapsed from the last Name change;
  - at least 50% of the Total Revenue in the preceding 1 year period has been accounted for by the new activity suggested by the new name; or
  - the amount invested in the new activity project is at least 50% of the Assets of the listed entity.
- If any listed entity has changed its activities which are not reflected in its name, it shall change its name in line with its activities within a period of six months from the change of activities in compliance of provisions as applicable to change of name prescribed under Companies Act, 2013.
- On receipt of availability confirmation and, before filing the request for change with the Registrar of Companies (ROC), the company shall seek approval from Stock Exchange (SE) before making final application to ROC for name change.
- The company shall submit a certificate from Chartered Accountant (CA) stating compliance with conditions as mentioned above.

Answer 5(c)

Under the SEBI Regulations as well as the provisions of the Companies Act, 2013, the copies of standard material contracts and documents for inspection are required to be attached to the copy of offer document delivered to ROC and said documents are also required to be made available for inspection at registered office of the Company from draft offer document stage till the closure of the IPO.

The standard material contracts to be attached with copy of Offer Documents are as follows:

1. Offer/Issue Agreement between Company, the Merchant Banker and Selling Shareholders (if any).
2. Memorandum of Understanding or Agreement between Company and the Registrar to the Issue.
3. Bankers to the Issue Agreement between Company, Merchant Banker and the Banker to the Issue.
4. Underwriting Agreement between Company, Merchant Banker & other Underwriters (if any).
5. Market making agreement between Company, the Lead Managers and the Marker Maker to the Issue (If applicable).

6. Syndicate Agreement between Companies, Merchant Banker & Syndicate Members.
7. Copy of Tripartite agreement entered into between Company, CDSL and the Registrar to the Issue.
8. Copy of Tripartite agreement entered into between Company, NSDL and the Registrar to the Issue.

Answer 5(d)

The SEBI has recognized the significant role played by a Company Secretary as a Governance Professional under the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 and recognized the role to be played by a Company Secretary under various provisions of such Regulations, which are mentioned below:

1. Regulation 6 provides that every listed entity shall appoint a qualified company secretary as the compliance officer.
2. Regulation 7 (3) requires that the listed entity shall submit a compliance certificate duly signed by Company Secretary and authorised representative of the share transfer agent certifying that all activities in relation to physical and electronic share transfers facility are maintained either in house or by Registrar to an issue and share transfer agent registered with the SEBI.
3. Recognition as Senior Management under Regulation 16.
4. Company Secretary is treated as Key Managerial Personnel under Regulation 2(1)(o).
5. Regulation 24A mandates that every listed entity and its material unlisted subsidiaries incorporated in India shall undertake Secretarial Audit and shall annex with its Annual Report, a Secretarial Audit Report, given by a Company Secretary in Practice.
6. Regulation 40 (9) requires that the share transfer agent and/ or the in-house share transfer facility, as the case may be, produces a certificate from a practising Company Secretary within one month of the end of each half of the financial year, certifying that all certificates have been issued within thirty days of the date of lodgement for transfer, sub-division, consolidation, renewal, exchange or endorsement of calls/allotment monies.
7. Regulation 40(2) provides that a listed entity may delegate the power of transfer of securities to a committee or to compliance officer or to the registrar to an issue and/or share transfer agent(s)
8. Schedule V of the Regulation requires compliance certificate from either the auditors or practising Company Secretaries regarding compliance of conditions of corporate governance to be annexed with the directors' report.
9. As per Schedule V of the Regulation, a certificate from a Company Secretary in practice that none of the directors on the board of the company have been debarred or disqualified from being appointed or continuing as Directors of Companies by SEBI/ Ministry of Corporate Affairs or any such Statutory Authority.

Attempt all parts of either Q. No. 6 or Q. No. 6A

Question 6

(a) Write a detailed note on NASDAQ.

(5 marks)

(b) List out the documents to be submitted to Stock Exchange at the time of approval of finalization of basis of allotment in India.

(5 marks)

(c) Prepare a Checklist of documents for listing of securities issued pursuant to the Rights Issue.

(5 marks)

(d) Explain the procedure of Due Diligence as expected to be carried by a Merchant Banker for an IPO.

(5 marks)

OR (Alternate question to Q. No. 6)

Question 6A

(i) Discuss the various segments of Main Market of London Stock Exchange.

(ii) Regulatory Authorities require that the company must maintain the Asset Cover in respect of Debentures issued. Discuss this statement in context of provisions of SEBI (LODR) Regulations 2015.

(iii) Prepare quarterly and annually compliance calendars for listed SMEs.

(iv) Discuss the various parameters to be covered for a successful Road Show for raising funds via an IPO.

(5 marks each)

Answer 6(a)

NASDAQ began primarily as a U.S.based equities exchange. Today, NASDAQ is recognized around the globe as a diversified worldwide financial technology, trading and information services provider to the capital markets, with more than 3,500 colleagues serving businesses and investors from over 50 offices in 26 countries across six continents – and in every capital market.

There are three distinct markets within NASDAQ: the NASDAQ Global Market (NGM), the newly created NASDAQ Global Select Market (NGSM) and the NASDAQ Capital Market (NCM). The NGSM mandates the highest initial listing requirements of any market in the world, while its maintenance requirements are identical to those of the NGM. The NGM, in turn, has more stringent quantitative listing and maintenance requirements than does the NCM. The quantitative listing and maintenance criteria applicable to non-Canadian foreign private issuers for the NGM, NGSM and NCM are identical to those of US domestic and Canadian issuers. Foreign Private Issuers (FPI) (including Canadian issuers) may, however, elect to follow home country practice in lieu of compliance with the NASDAQ corporate governance requirements.

1. **Global Select Market (NGSM)**

   The NASDAQ Global Select Market has the highest initial listing standards of any exchange in the world. It is a mark of achievement and stature for qualified companies.

2. **Global Market (NGM)**

   The NASDAQ Global Market lists companies with an overall global leadership and international reach with their products or services.

3. **Capital Market (NCM)**

   NASDAQ Capital Markets are focused on its core purpose for those companies listed -capital raising

Answer 6(b)

The documents that needs to be submitted to Stock Exchange at the time of approval of finalisation of basis of allotment in India are as under:

1) Copy of Prospectus filed with the ROC (also in soft copy CD) along with letter from all the merchant bankers involved in the issue specifying details of amendments/ changes made in Red Herring Prospectus (which were subsequently incorporated in Prospectus). To submit the same in track changes mode also.
2) Proceeding details / minutes of basis of allotment, verified and signed by R & T Agent, BRLM (Responsible for post issue) and the Issuer along with the reasons for exception to rejection cases.
3) Category wise, summary of list of "technical rejection" cases Specifying - Application No., Category, Name & Add., Pan, DP ID, CL ID, Quantity, price Amount and reason for rejection along with photo-copies of Application forms.
4) Confirmation from registrar regarding withdrawal of applications received, considered in the basis, indicating date and time (should not be more than 12 hours from time of submission of basis).
5) Statements giving branch wise/bank wise/city wise/state wise/zone wise details of the total collections with a breakup of ASBA fund received at the various participating bank branches in response to the public issue / offer for sale.
6) Category wise, Bid lot wise, two copies of Calculation sheet of proposed basis of allotment of equity shares to the Qualified Institutional Buyers, Non-Institutional Bidders and Retail Bidders, Reserved category etc. duly signed by RTA, BRLM & Issuer.
7) Photo copy of the final certificate issued by the controlling branch of ASBA bankers giving branch wise details of collections received.
8) Undertakings from the company, lead managers and the registrars & transfer agents in respect of the basis of allotment.
9) Copy of the statutory advertisement released in respect of the public issue / offer for sale, opening and closing of the issue, price revision, if any etc. up to the stage of basis of allotment.

10) Auditors certificate with regard to the promoters contribution, if applicable.

11) Declaration from the Managing Director / Company Secretary that there is no injunction / prohibition order of a competent court of law on the issue or on a part of any particular category of the issue.

12) Confirmation that:

- Only Qualified Institutional Buyers as mentioned under the definition in Regulation 2 (zd) of the SEBI (Issue of Capital and Disclosure Requirements), Regulations, 2018 are proposed to be allotted equity shares under QIB category.
- No QIB has Bid and proposed to be allotted equity shares under non-QIB or retail category.

13) List of all prospective allottees (valid) along with number of shares applied, amount paid, bank account details, PAN number, Demat account details etc. (in soft copy CD)

14) If Approval from the SEBI is sought for relaxation in PAN mismatch applications, then copy of the SEBI approval letter as well as the true copy of request letter to the SEBI, should be submitted.

Answer 6(c)

The company should submit the letter of application along with the following documents/ formalities:

1) Listing Application for all types of securities issued on rights basis should be submitted.

2) Certified copy of the resolution passed by the Board of Directors for allotment of securities on Right Basis.

3) Shareholding pattern for pre and post issue as per the format prescribed under Regulation 31 of the SEBI (Listing Obligations and Disclosure Requirements), Regulations, 2015 for all types of securities issued on Rights basis.

4) A certified copy of Basis of Allotment as approved by Designated Stock Exchange should be filed.

5) Auditors/Practicing CA/CS certificate that allotment has been done as per basis of allotment approved by the designated stock exchange.

6) The total number of securities allotted in the physical category and in Demat (CDSL & NSDL Separately) with category wise distinctive numbers should be filed.

7) An undertaking from the Managing Director/Compliance Officer certifying that all the documents filed by the Company with the Exchange are same/similar/ identical in all respect with the documents filed by the Company with Register of Companies/SEBI/RBI/FIPB in respect of the allotment/enlistment of the aforesaid rights share on the Exchange, and that the company has complied with all the

legal and statutory formalities and no statutory authority has restrained the company from issuing and allotting the securities on rights basis.

8) Undertaking from the Compliance Officer of the issuer as per the following format:

- "The company or its promoters or whole time directors are not in violation of the provisions of Regulation 24 of the SEBI Delisting Regulations, 2009".
- "We hereby confirm that the company, its promoters, its directors are not in violation of the restrictions imposed by SEBI"

9) Undertaking from the Compliance Officer of the issuer as per the following format:

"Neither the issuer nor any of its promoters or directors is a wilful defaulter as defined under the SEBI (Issue of Capital and Disclosure Requirements), 2018";

OR

"<Name of the issuer> (<name>, the promoter(s) of the issuer / <name> the director(s) of the issuer is a wilful defaulter as defined under the SEBI (ICDR) Regulations, 2018 and disclosures in this regard has been made at <place of disclosure> as per the format given in said regulation."

10) Annual Listing fees

Answer 6(d)

The SEBI Regulations requires a Merchant Banker, amongst other things, to exercise due diligence, ensure proper care and exercise independent professional judgment. The SEBI Regulations requires Merchant Banker to maintain records and documents pertaining to due diligence exercised in pre-issue and post-issue matters. Furthermore, the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018 require due diligence certificate to be issued by the Merchant Banker.

A Merchant Banker for an IPO is expected to:

i. carry out the procedures to demonstrate that it had no reasonable ground to believe and did not believe that there were material misstatements or omissions in the Offer Documents which could have had an impact on an investment decision;

ii. have detailed discussions with the management and key customers, suppliers (where practicable) and the Issuer's auditors with respect to the business and associated risks and financial reporting statements;

iii. identify procedures such that disclosures in the Offer Document that are material to an investment decision are backed by appropriate documentation, such as corporate and secretarial records or certificates of the Issuer or third parties and independent third party reports; and

iv. inform the Issuer that it may be required to provide documents that have been reviewed for an Issue, post completion of the Issue in instances of receipt of clarifications or questions from the SEBI or other regulatory agencies or other persons.

It must be clearly understood that due diligence is the backbone of any primary market offering. The risk that the Merchant Banker runs for any lapse in conducting due diligence is not restricted only to any regulatory action but extends to reputational risk with the investors & Issuers.

Though Merchant Bankers are supposed to carry out diligence and comply with all the requirements of applicable regulations, the Company and the Management is responsible for the contents of offer document and have to declare and certify that all the information in the offer document is true and fair. Offer document being a legal document defined under the Companies Act as well as applicable regulations, responsibility of the management is final. Companies need to prepare and be ready for the process of the diligence.

Answer 6A(i)

The London Stock Exchange is one of the world's most international capital markets, home to approximately 2,200 companies from more than 70 countries around the world. More than 500 of these companies are international.

The Main Market is the flagship market for larger, more established companies, and is home to some of the world's largest and best known companies. The Main Market of London Stock Exchange has four segments that cater for a range of businesses and securities.

- *Premium* : Part of the FCA's (Financial Conduct Authority (FCA) is a financial regulatory body in the United Kingdom) Official List, this segment is home to some of the world's largest corporations that are subject to the highest standards of regulation and governance.
- *Standard* : Subject to European Union (EU) minimum standards and part of the Official List, open to shares and debt securities.
- *Specialist Fund Segment* : Designed for highly specialised investment entities that wish to target institutional, highly knowledgeable investors or professionally advised investors only.
- *High Growth Segment* : A new addition to the Main Market offering, this segment is specifically designed for equity securities of high growth, revenue generating businesses that are over time seeking to become Premium listed companies.

Answer 6A(ii)

Regulation 54 of the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 deals with Asset Cover for Non-convertible Debt securities which provides that the listed entity shall maintain 100% asset cover or asset cover as per the terms of offer document/Information Memorandum and/or Debenture Trust Deed, sufficient to discharge the principal amount at all times for the non-convertible debt securities issued.

Such entities are also required to disclose to the stock exchange in quarterly, half-yearly, year-to-date and annual financial statements, as applicable, the extent and nature of security created and maintained with respect to its secured listed Non-convertible Debt securities.

Answer 6A(iii)

Quarterly Compliances

S.No.	*Regulation Reference*	*Frequency*	*Period Covered*	*Timelines*
1.	Regulation 13(3) of the SEBI (Listing Obligation and Disclosure Requirements) Regulations, 2015 – Statement Grievance Redressal Mechanism	Quarterly	April-June, July-September, October December, January-March	Within 21 days from the end of Quarter
2.	Regulation 76 of the SEBI (Depositories and Participants) Regulations, 2018-Reconciliation of Share Capital Audit Report	Quarterly	April-June, July-September, October-December	Within 30 days from the end of the quarter

Annual Compliances

Sr. No.	*Regulation Reference*	*Frequency*	*Period Covered*	*Date by which to be filed*
1.	Regulation 14 of the SEBI (Listing Obligation and Disclosure Requirements) Regulations, 2015– Listing Fees	Annually	April-March	30th April
2.	Regulation 34(1) of the SEBI (Listing Obligation and Disclosure Requirements) Regulations, 2015 – Annual Report	Annually	April-March	Not later that the day of commencement of dispatch to its shareholder

Answer 6A(iv)

At road shows, generally series of information presentations are organised in selected cities around the world with analysts and potential institutional investors. It is, in fact, a conference by the issuer with the prospective investors. Road show is arranged by the lead manager by sending invitation to all prospective investors.

Management needs to prepare for proposed Road shows and Investor Meets in advance. Adequate representation of promoters & key managerial person should be available for various meets, Road shows etc. Often there is a need to undergo training for the representatives of the Company about their conduct & behaviour during these road shows. IPO bound Companies prepare a 'Corporate Film' which includes brief about the Company, its past and also take investors through the present set up, practices followed by the Company, overview of proposed expansion, brief information of

management, financials of the Company including various financial ratios & parameters and basis of IPO price. Besides this a short and concise Press Note about the Company and its IPO is required to be released for publications. The Road show generally comprises of a press meet and meeting with Brokers and Investors/Analysts. Press Conference is aimed at giving information to the press for publication in their papers/newspapers for dissemination of information to the investors whereas 'Brokers, Investors/Analysts Meet' aims at giving detailed information to the market participants about the Company enabling them to understand the details and take it further to the ultimate investors. Many a times IPO bound Companies also organize site/plant visit for the market participants enabling them to take a view of manufacturing facilities and other administrative set up of the Company. Managements are required to take into consideration all the above factors while preparing for marketing of an IPO.

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MULTIDISCIPLINARY CASE STUDIES

Time allowed : 3 hours *Maximum marks : 100*

NOTE : *Answer ALL Questions.*

Question 1

Read the following case study and answer the questions given at the end :

As the world is speedily inclining towards pure and organic products, the most ancient science of medicine, healthcare, personal care, food and beverages, Ayurveda is reliving its glory. Many recent studies and report clearly explain that the revival of Ayurveda is not restricted to India and China but spreading across all continents, Ayurveda is successful in creating domino impact all across the globe.

As per a market research, the Indian Ayurveda market is all set to register 16% growth (CAGR) till 2025. At present, the size of the domestic market is ₹30,000 Crores, and Ayurveda's market penetration is increasing in both rural and urban areas. A 2019 report also conveys that 77% of Indian households are using Ayurvedic products as against 69% in 2015. The major chunk of the domestic revenue (75%) comes from the sale of Ayurveda products whereas services/consulting contribute only 25% to the total business. The industry whose market size was USD 3.4 billion in 2015 is expected to reach USD 9.7 billion by 2022. Growing awareness among masses about potential side effects of present day modern medicine, healthcare, personal care, food and beverages on various media platforms has compelled them to switch to natural safer, and holistic alternative, Ayurveda. The future of Ayurveda is looking fabulous as more and more players are entering the market with innovative products, quality packaging, and strategic marketing activities. Earlier, Ayurvedic companies failed to impress customers with presentation and promotional activities, but the new generation of entrepreneurs is smartly working on these aspects to partake in growing market competition.

One of the major companies in Indian Ayurvedic Industry, Ashwamedha Rudrapeeth Limited (ARL) was founded by Rudra and his friend. ARL is consumer product giant that is beating the world's most recognised FMCG companies in India. ARL has managed to expand an empire so big that it is shaking the fast-moving consumer goods industry in India to its core. It is no mean achievement for someone like Rudra, who does not have any formal education on brand and marketing could beat world class brand in a very short span of 10 years. The answer lies at the core of building a brand – being "Purpose" driven. The objective of ARL was to develop a holistic approach to improve the quality of life of all beings, world over. It was conceived with the objective of amalgamating the ancient wisdom of the Science of Ayurveda with the modern scientific techniques of industrial management. Its intention was to distribute quality, tested and hygienic products with wide ranging effects to the largest section of populace at reasonable prices enabling the common citizen to avail their benefits. It also aimed to establish Ashwamedha Ayurveda as a science based, inventional, problem-solving, natural and trusted for healthy lives.

Rudra and his friend knew that they have created a captive market with their efforts

since last one and a half decade, which values health, yoga, pranayama and above all, Rudra has become brand ambassador for ARL. This captive market is health conscious, looks out for affordable products, believes in the philosophy of swadeshi (home grown) and above all considers Rudra as their idol. When Ashwamedha Ayurveda launched its products in the Indian retail sector, this captive market was among the first to buy and use its products. This captive market developed instant loyalty to Brand Ashwamedha. The role of this captive market was not only limited to buying, using and spreading good word of mouth about ARL products but they also became partners with ARL by becoming their franchisees. In the initial days' majority of the franchisees established by ARL came from this captive market. These franchisees along with the distribution of products also advertised and promoted ARL products in their respective regions, hence establishing brand Ashwamedha firmly into the mind of local populace. When compared to an FMCG multinational which uses a traditional distribution channel, ARL followed a different distribution strategy, effective in catapulting it to its present position. Presently, Ashwamedha's turnover stands close to ₹7000 Crore with a mammoth goal of reaching close to ₹10,500 Crore in Financial Year ending 2023 and close to ₹21,000 Crore by Financial Year ending 2025. Ashwamedha Ayurveda's value creation and delivery strategy encompassing both the Strategic and Tactical Marketing is instrumental in making it a force to reckon with in the Indian FMCG industry.

ARL's target segment comprise of health-conscious people who prefer "value for money" natural products. ARL has products targeted at children (health drinks) and elderly people (some ayurvedic preparations). Almost all products of ARL are affordable (at a price 15%-30% lower than the competition), hence the income segmentation strategy has worked.

Initially, the products were targeted at lower and middle-income groups but with the present turnover of close to a billion dollars this fiscal, it is evident that ARL's products have buyers not only from the lower income and middle-income segments but also from health conscious upper-middle and upper-income segments. These two segments have found value in ARL's natural and ayurvedic products. ARL's market targeting strategy is that of "Selective Specialization" as they cater to a large segment in their market but not the entire market. The company is planning to venture into packaged cow milk, 'Khadi' and animal feed this year. Ashwamedha uses natural ingredients and herbs to manufacture its products. They have state of the art Research and Development (R&D) facility, involved in the latest research on products which can benefit their target market. It has few star products in its product portfolio. Ashwamedha's cow ghee, Shampoo, Hair care and oral care products have a combined tumover more than ₹1500 Crore. One of the reasons Ashwamedha Ayurveda has been able to garner market share so rapidly is because of low lead times between the product concept and product launch. Ashwamedha Ayurveda's R & D team has been able to produce high quality products at low price in short duration. Ashwamedha Ayurveda's products are generally economically priced except for Ashwamedha Cow Ghee. This is sold at a premium in the market, every other product has a market penetration pricing strategy. The pricing strategy has helped Ashwamedha establish itself in the marketplace. Established brands which did not consider it as a competition initially, are now forced to sit and take note of it. Its core values are driven by Rudra's beliefs and hence there is no difference between the two. What drives Rudra, drives brand Ashwamedha Ayurveda.

Ashwamedha uses multiple distribution channels to cater to the market. Company has 2 Lakh outlets in India. ARL has a strong presence in the market through its 1200 Chikitsalayas, 2500 Arogya Kendras. For Rural market they have got 7000 stores in villages and 5600 marketing vehicles which roams across all villages. ARL also plans to establish 250 mega stores in tier 1 and tier 2 cities in next 3 years. ARL also has a tie-up with behemoths of modern retail Groups, which carry its entire product range in their exclusive retail chain across all stores in the country. ARL has embraced the e-commerce mode of retailing products through Ashwamedhaayurved.net and has a strong presence in the modern retail format. Rudra through his Yoga Camps not only talks about the different Yoga postures and their benefits in curing the diseases but also about the Ashwamedha Ayurved products aiding in a healthy lifestyle and a disease-free life. This is one of the most potent promotion tools used by ARL. Word of mouth communication certainly has a higher believability factor compared to other mediums of advertising. Rudra has created a strong community of loyalists through the efforts of Ashwamedha Yogapeeth Trust and Yoga Camps, which speak very high of Rudra and Ashwamedha products. Recently, Ashwamedha Ayurveda has seen a spurt in its promotional outlay. Ashwamedha Ayurveda has its channel on YouTube which features more than 1000 videos on Yoga and on product information.

Ashwamedha has made disruptive progress in the FMCG sector. Within a span of less than 10 years, it has displaced ayurvedic market leaders and has become synonymous with ayurvedic products. Rudra's charisma has pushed Ashwamedha to grow over 10 times in a span of less than 10 years. The FMCG giants are also taking steps to check its advancements. However, now it has gained public attention in the market and there is overwhelming demand for its products, it will be difficult for them to win back their lost market shares.

Questions :

(a) A successful business strategy is a combination of multiple elements. Explain.

(b) What do you understand by SMART objectives ? Elucidate in background of ARL's objectives.

(c) 'Focus on quality and quantity of offerings while assuming that customers will seek out and buy reasonably priced, well-made products'. Comment.

(d) "A communication strategy is designed to help you and your organization communicate effectively and meet core organizational objectives". Is the communication strategy of Ashwamedha Ayurveda effective ?

(10 marks each)

Answer 1(a)

When preparing a strategy for success, a business needs to be clear about what it wants to achieve. It needs to know how it is going to turn its dreams into realities in the view of cut-throat competition and Political, Economic, Sociological, Technological, Legal and Environmental factors that are always in a constant state of flux and exert substantial impact on business organisations on a continuous basis.

In light of the aforesaid facts, setting clear and specific aims and objectives is vital

for a business to compete and attain success. It is also imperative for a business organisation to be conversant with the market dynamics, i.e., a same market may provide varying business opportunities to various players dealing in the same product.

The multiple elements that assist in formulation of a successful business strategy are as under:

1. Vision

It is to be noted that without the Vision there is no strategy. The so-called "Vision Statement" is one of the central components of a good strategy. One should clearly think long-term. Where should the journey of the company go and above all explain the vision of the company, where it should be in 3, 5 or more years.

2. Mission

In contrast to the Vision of a company, the Mission statement is the description of what we represent as a company. It describes what makes us unique and how to make customers happy with what the company do.

Often Vision and Mission statement are combined into one. But we should clearly distinguish between describing where we are now, what we represent and what we are doing to move towards the Vision in the future.

3. Core Values- the values of a company

By looking at the core values, one can quickly define what values we represent as a company and what values we avoid. This is almost like a guide on how to work to achieve business goals. From the given case study, the core values of Ashwamedha Rudrapeeth Limited is evident from its intention to distribute quality, tested and hygienic products with wide ranging effects to the largest section of populace at reasonable prices enabling the common citizen to avail their benefits.

It also aimed to establish Ashwamedha Ayurveda as a science based, inventional, problem-solving, natural and trusted for healthy lives.

4. Branding

One of the most powerful tools that organisations have is branding. A brand is a name, design, symbol or major feature that helps to identify one or more products from a business or organisation.

The reason that branding is powerful is that the moment a consumer recognises a brand, the brand itself instantly provides a lot of information to that consumer. This helps them to make quicker and better decisions about what products or services to buy.

Rudra and his friend knew that they have created a captive market with their efforts since last one and a half decade, which values health, yoga, pranayama and above all, Rudra has become brand ambassador for ARL (Ashwamedha Rudrapeeth Limited). This captive market is health conscious, looks out for affordable products, believes in the philosophy of swadeshi (home grown) and above all considers Rudra as their ideal.

When Ashwamedha ayurved launched its products in the Indian retail sector, this captive market was among the first to buy and use its products. This captive market developed instant loyalty to Brand Ashwamedha.

5. Product positioning

Product positioning is the process of determining the position of a new product in the minds of consumers. It includes analyzing the market and competitors' positions, defining the position of a new product among the existing ones, and communicating the brand's product image. Managing a brand is part of product positioning. The positioning of a product is a process where the various attributes and qualities of a brand are emphasised to consumers. When consumers see the brand, they distinguish the brand from other products and brands because of certain attributes or qualities of the concerned product.

Ashwamedha Ayurveda's value creation and delivery strategy encompassing both the Strategic and Tactical Marketing is instrumental in making it a force to reckon with in the Indian FMCG industry.

Answer 1(b)

Well-constructed objectives are SMART objectives. They must be:

- Specific
- Measurable
- Achievable or Agreed
- Realistic
- Time-related

Specific

Specific answers the questions "what is to be done?" "how will you know it is done?" and describes the results (end product) of the work to be done. The description is written in such a way that anyone reading the objective will most likely interpret it the same way. To ensure that an objective is specific is to make sure that the way it is described is observable.

Measurable

Measurable w/Measurement answers the question "how will you know it meets expectations?" and defines the objective using assessable terms (quantity, quality, frequency, costs, deadlines, etc.). It refers to the extent to which something can be evaluated against some standard. An objective with a quantity measurement uses terms of amount, percentages, etc.

Achievable

Achievable answers the questions "can the person do it?" "Can the measurable objective be achieved by the person?" "Does he/she have the experience, knowledge or capability of fulfilling the expectation?" It also answers the question "Can it be done giving the time frame, opportunity and resources?" These items should be included in the SMART objective if they will be a factor in the achievement.

Relevant

Relevant answers the questions, "should it be done?", "why?" and "what will be the impact?" Is the objective aligned with the Company's implementation plan?

Time-oriented

Time-oriented answers the question, "when will it be done?" It refers to the fact that an objective has end points and check points built into it. Sometimes a task may only have an end point or due date. Sometimes that end point or due date is the actual end of the task, or sometimes the end point of one task is the start point of another. Sometimes a task has several milestones or check points to help you or others assess how well something is going before it is finished so that corrections or modifications can be made as needed to make sure the end result meets expectations.

ARL's demonstrate the intention of the management to enhance the business whilst maintaining the quality. The following are the key objectives:

- Develop a holistic approach to improve the quality of life of all beings, world over.
- To amalgamate the ancient wisdom of the Science of Ayurved with the modern scientific techniques of Industrial Management.
- Distribute quality, tested and hygienic medicines with wide ranging cures to the largest section of populace at reasonable prices enabling the common citizen to avail their benefits.
- Establish Ashwamedha Ayurved as a science based, inventional, problem-solving, natural and trusted for healthy lives.

These objectives are in essence aligned with the requirements of SMART.

Answer 1(c)

With so many options available to customers, one may wonder whether or not quality still matters. The answer is a resounding "yes," and quality isn't just about offering a product or service that exceeds the standard, but it's also about the reputation gained for consistently delivering a customer experience that is “above and beyond.”

It is to be noted that managing quality is crucial for small businesses. Quality products help to maintain customer satisfaction/loyalty and reduce the risk and cost of replacing faulty goods. Companies can build a reputation for quality by gaining accreditation with a recognized quality standard.

Meet Customer Expectations

Regardless of the industry, customers aren't going to choose solely based on price, but often on quality. In fact, studies have shown that customers will pay more for a product or service that they think is of high quality and either meet or exceeds the standards. It is well accepted fact that customers expect quality products from the business organisations.

Quality is Critical to satisfy a Customer

Quality is a key differentiator in a crowded / competitive market. It's the reason that Apple can price its iPhone higher than any other mobile phone in the industry - because the company has established a long history of delivering superior products.

If customer's expectations are not met they will quickly look for alternatives. Thus, quality is critical to satisfy customers and retaining their loyalty in order to ensure their long-term association with the products as well as the business organisation offering the products. Quality products make significant contribution to long-term revenue and profitability also.

Quality assist in building Reputation

Quality reflects on a company's reputation. The growing importance of social media means that both customers and prospective customers can easily share favourable opinions as well as criticisms regarding the product quality. In the current scenario, various online forums like, social media platforms, product review sites, social networking sites etc. have provided ample opportunities to the customers to express their good and bitter experiences regarding the quality of the products.

A product enjoying strong reputation due to its superior quality can thrive despite being the market is highly competitive. On the contrary, poor quality product most often fails in the market leading the product recall and negative publicity about the product, thereby exerting a debilitating impact on the reputation of the business organisation.

Meet or Exceed Industry Standards

Adherence to recognized quality standards may be essential for dealing with certain customers or complying with pertinent legislations. Public-sector companies, for example, may insist that their suppliers achieve accreditation with quality standards. If a business organisation sell products in regulated markets, such as health care, food or electrical goods, it must comply with health and safety standards formulated to protect consumers.

Accredited quality control systems play a crucial role in complying with various standards. Accreditation can also help an organisation to win new customers in the existing market or enter new markets by giving prospective customers a surety that the business organisation or the company possess the ability to sell quality products.

Effective Cost Management

Poor quality results into increase in costs. If a company do not have an effective quality-control system in place, it may have to incur costs on two fronts, i.e., first in analysing the root causes of the production of poor quality products and second in retesting of the poor quality or defective products in order to ensure that when they are resold in the market they conform to the prescribed quality standards.

It is to be noted that in case defective products increases the cost of the company substantially, i.e., first the replacement cost of the defective product and second paying of compensation to the aggrieved customer.

Thus, a business which focuses on producing quality products at reasonable price will command customer loyalty and brand image. The same is reflected by Ashwameda Ayurved.

Answer 1(d)

Drawing up a communications strategy is an art, not a science and there are lots of different ways of approaching this task. A communication strategy shall focus on the following:

- Objectives
- Audience identification
- Messages
- Tools and activities
- Resources and timescales
- Evaluation and amendment

Objectives

Company's objectives are the key to the success of communications strategy. It should ensure that communications strategy is organisationally driven rather than communications driven. Communications activity is not an end in itself and so must be aligned with organisational objectives. Aligning communications and organisational objectives will also help to reinforce the importance and relevance of communications and thereby make a convincing case for the proper resourcing of communications activity within the organisation.

Audience identification

The management needs to identify those audiences with whom company needs to communicate to achieve its organisational objectives. The best audiences to target in order to achieve an objective may not always be the most obvious ones, and targeting audiences such as the media may not always help in achieving the objectives.

Messages

Strategic orientation and consistency are keys to organisation's messages. A comprehensive case covering all the key messages, emphasising the different elements of the case for different audiences can assist phenomenally in drafting an ideal message. Communications is all about storytelling requiring usage of interesting narrative, sharing of experience and creating imagination.

Tools and activities

Identify the tools and activities that are most appropriate for communicating the key messages to the audiences. These may be suggested by the audiences also. For example, an annual report is a useful tool in corporate communications whereas an email newsletter is suitable for internal communications. It is essential that an organisation tailor its tools and activities keeping in view time, human and financial resources available to the management.

Resources and timescales

A company should always deliver what it promises and so it must take utmost care

of not communicating promises which it cannot fulfil. Thus, resources and timescales needs to be used in such a manner that legitimate expectations are set.

Evaluation and amendment

Consider performing a communications audit to assess the effectiveness of the organisation's strategy with both internal and external audiences.

Effective communication is vital for any strategy to be successful. Ashwamedha Rurdrapeeth Limited's success is due to how well it communicated its objectives to consumers to help them consider how yoga is beneficiary in curing the diseases. It developed different forms of communication to convey the message 'disease free life' to all its customers.

The communication strategy employed by Ashwamedha Rurdrapeeth Limited is multi-pronged and were done through:

- Promoting Ayurveda as part of day to day life-style
- Organizing yoga camps
- Franchisees/open stores across locations including villages
- Be synonymous with Ayurveda and good health
- Promote yoga as part of daily life
- Rudra's youtube videos

Question 2

(a) Pentagon Medical Marketing India Private Limited was incorporated in December 2006. The Company was profitable initially, however in few years there were internal issues and the Board decided to apply for Striking off with Registrar of Companies (ROC). An application was made for striking off its name under the Fast Track Exit Scheme, 2011, which was processed by ROC, Ahmedabad. The ROC sent a notice to the Company and Income-tax authorities seeking objections, if any within a stipulated period. Later, ROC struck off the name of the Company, as no objections were received by it within the stipulated period. Later, on the Income-Tax Authoritres filed an appeal to the NCLT seeking restoration of the name of the company on the ground that the tax dues against the company were not determined.

Comment briefly in background of decided case law(s). (6 marks)

(b) CO2 Technologies Limited provides various fintech and software innovation solutions. The Company was engaged by Energy Infra Exchange Limited, an exchange for carbon credits in India. The founder and chairman of CO2 Technologies Limited, Ziruch was convicted of fraud. Upon investigation, it was found that the fraud committed by Ziruch perpetrated through multiple layers impacting both the Company and Energy Infra Exchange Limited. Taking into consideration the provisions of the Companies Act, the Government of India ordered compulsory amalgamation of the CO2 Technologies Limited and Energy Infra Exchange Limited.

Evaluate in background of decided case law(s). (6 marks)

Answer 2(a)

The facts of the present case are similar to the case of *PR. Commissioner of Income Tax, Delhi* vs. *Registrar of Companies, Delhi & Ors. [NCLAT].*

In the instant case, the Report-cum-Affidavit filed by ROC and supported by Annexures - I and II satisfactorily establishes that the procedure laid down for striking off the name of Company from Register of Companies (ROC) has been observed in letter and spirit. In the face of the material on record corroborated by contemporary record, no exception can be taken as regards compliance of the procedural aspect laid down in the Guidelines governing FTE of the Company.

Though, in terms of the Guidelines, decision of the ROC in respect of striking off the name of Company from its Register is final, it is open to this Appellate Tribunal to examine whether the fundamental principles of jurisprudence have been observed in compliance. Whether the Company resorted to FTE with malafide intention of defrauding the Creditors would be a consideration having a bearing on the application of FTE Guidelines for defunct companies but before dwelling upon the question of Revenue being a Creditor qua the Company on the material date, it would be of primary importance to find whether the Company was 'defunct company' within the meaning of FTE Guidelines. Nil asset and liability was a *sine-qua-non* for a company to fall within the ambit of a 'defunct company'.

It was therefore incumbent upon the Revenue, in the first instance to lay proof before the Tribunal or even before this Appellate Tribunal that the Company was possessed of assets besides having liabilities. Unfortunately, the Revenue has not even made any feeble attempt at disclosing any details of the assets, movable and immovable, that the Company possessed and liability, if any, on the material date. Liability to pay Income Tax would necessarily depend on assets besides trade and business activity culminating in profit or loss. The proof in regard to possession of assets by the Company and owing of any liabilities by it as also in regard to factum of any income from legitimate sources assessable to Income Tax being abysmally absent, no fault can be found in regard to striking off the Company by ROC under FTE which has been duly notified in the 'Gazette of India'.

Striking off the Company which was a Private Company, from the Register of Companies, indisputably does not absolve its erstwhile Directors who are liable as provided under Section 179 of the Income Tax Act, 1961 to pay the amount of Tax leviable in respect of income of any previous year. Why, in presence of such mechanism within the legal framework available to Revenue, insistence is on restoration of Company without laying any proof of its being possessed of any assets and liabilities and without any evidence of the Company being in operation, is a question that can be best answered, though has not been answered by the Revenue.

The appeal is dismissed leaving the Revenue to pursue appropriate legal remedy in the light of observations in this judgment.

Answer 2(b)

The facts of the present case is similar to the case of 63, *Moons Technologies Ltd (formerly Financial Technologies (India) Ltd.* v. *Union of India & Ors (Bombay High Court).*

There is sufficient material on record on basis of which the Central Government has subjectively satisfied itself that the amalgamation is essential in public interest to facilitate recoveries of dues from defaulters from pooling human and financial resources of Financial Technology India Limited (FTIL) and National Spot Exchange Limited (NSEL). Despite claims by NSEL that it has the means to and it has been rigorously pursuing recoveries, the fact remains that the position of recoveries is not very promising and may further deteriorate if only NSEL has to fend for itself. In such matters, it is not sufficient that some decrees or attachment orders are obtained. This is also not an issue of mere recoveries but this is an issue of investor confidence in the very functioning of stock and commodity exchanges.

If the Central Government, were not to act in a situation of this nature, investor confidence would certainly be a casualty. Such a situation then, has a cascading effect, which is by no means conducive to the national economy.

The Central Government, in making the impugned order has balanced the interests of the two companies, its shareholders, creditors and employees on one hand and the interests, not only of the investors who may have claims, but also, of the investing public, which is required to be given the confidence that the Central Government will act to see that a holding company does not take shelter behind its wholly owned subsidiary and thereby shirk responsibility in the wake of such an unprecedented payment crisis. The three grounds or reasons stated in the impugned order, in our opinion, were sufficient to arrive at the subjective satisfaction that it was essential in public interest to order the amalgamation of the two companies. This is not a case of exercise of powers for any extraneous considerations or alien purposes.

Question 3

(a) Swadha Shareholding Limited, is a company incorporated under the Companies Act and functioned as a clearing house for BSE Ltd. and having its own depository participant services. SEBI conducted an inspection of the Company's books of accounts to examine whether it had put in place systems and processes to comply with the Circulars issued by SEBI relating to the Anti Money Laundering (AML) policy to be adopted, amongst others. SEBI issued a Show Cause Notice to the Company alleging violation of AML policy under the Prevention of Money Laundering Act, 2002, as to why adjudication proceedings should not be initiated against the appellant for violation of the said requirements. The Company submitted that it had belatedly complied with the requirements of AML policy.

Is the Company's submission valid ? Justify with reasons.

(6 marks)

(b) In the year 2018-19 there were more than 10 Initial Public Offers (IPOs) in the Indian Stock Market. Certain IPOs were marred by controversies including irregular allotment of shares. It was brought to the notice of the Securities and Exchange Board of India (SEBI) that several serious irregularities/illegalities had been committed by certain High Networth Individuals who manipulated the business by purchasing large chunk of shares through unscrupulous methods (benami/fictitious demat account holders) in these Companies to manipulate the price in the market.

Comment in the background of judicial pronouncements.

(6 marks)

Answer 3(a)

The facts mentioned are similar to a case between BOI Shareholding Limited (Appellant) and the SEBI (Respondent) filed before the Securities Appellate Tribunal (SAT).

In the case, an appeal was filed challenging the order of the Adjudicating Officer ('AO') of SEBI whereby a penalty of ₹ 40 Lakh has been imposed on the appellant under Section 15HB of the SEBI Act read with Section 19G of the Depositories Act, 1996 for delayed implementation of the SEBI Circulars / Guidelines relating to anti-money laundering (AML) policy.

The submission of the SAT was that they have perused the records produced before it. In the Master Circular on Anti-Money Laundering (AML)/ Combating the Financing of Terrorism (CFT) dated December 31, 2010 issued by SEBI, it was noted by SAT that all the registered intermediaries were directed to comply with the requirements contained therein on an immediate basis. Similarly, subsequent amendments made on January 24, 2013 also required adoption on immediate basis though the Circular dated March 12, 2014 does not specify the implementation time schedule. However, following the spirit of the basic policy, the SAT was of view that implementation has to be done at the earliest. From the evidence produced before SAT it was made clear that the appellant has implemented all the requirements of the AML/CFT policy as specified in the SEBI Circulars though belatedly. The SAT also noted that for delayed implementation / violation, the SEBI has imposed varying penalty including no penalty in some cases. However, under the Section 15HB of the SEBI Act read with Section 19G of the Depositories Act, 1996 the penalty imposable for each violation shall not be less than ₹ 1 Lakh which may extend to ₹ 1 Crore rupees. Accordingly, the minimum penalty imposable in case of six violations committed by the appellant should be in tune with the statutory provisions relating to the penalty.

Given the fact that, though belatedly, the appellant has implemented all the required policies and procedures on AML/CFT policy as stipulated under the various circulars of SEBI and by the penalty precedent set by SEBI itself, SAT was of the view that the penalty of ₹40 Lakh imposed on the appellant is excessive. SAT, therefore, reduced the amount of penalty imposed on the appellant to ₹ 6 Lakh.

Keeping in mind the outcome of the SAT in the above case, it can be established that though the delay in implementation is violation of the provisions of the SEBI Act, 1992, however, on justified submission by Swadha Shareholding Limited to the SEBI, the quantum of penalty can be reduced or waived-off.

Answer 3(b)

The facts mentioned are similar to a case between the SEBI (Appellant) and Opee Stock-Link Ltd & Anr (Respondents) filed before the Hon'ble Supreme Court.

Investigations was made by the officials of the SEBI and in pursuance of the said investigation it was revealed that in the matter of the IPO of the two companies, Jet Airways Limited and Infrastructure Development Finance Company Limited, shares which were meant for Retail Individual Investors (RIIs) had been cornered through hundreds of benami/fictitious demat account holders.

As *modus operandi* was quite similar in applications for shares made in respect of both the companies and parties concerned are common. The reference was made to the issue of Jet Airways India Limited. It was found by the SEBI that respondent in that case in Appeal No. 20 of 2009 before the SAT had received 12,053 shares out of which 3272 shares were transferred before the day of listing of shares of the company with the stock exchange, 3598 shares on the day of listing and 5183 shares after the day of listing. The said shares were purchased through off market transactions from 553 demat account holders, who had been allotted shares of the said company. The shares of the company were listed on 14th March, 2005.

The said 553 demat account holders sold the shares to the said respondent at the rate of ₹ 1170/- per share, though the market value of the said shares was much more than ₹ 1170/ per share. The said shares were thereafter sold by the said respondent at a higher price. Upon investigation, it was also found that most of those 553 demat account holders were not genuine persons.

The Whole Time Member (WTM) of the SEBI came to the conclusion that the dealings of the respondents were not fair and were in violation of the Act as well as the Regulations, and imposed penalty on the respondents. On appeal, SAT set aside the order of the WTM. The SEBI thereafter, challenged the order of SAT before the Hon'ble Supreme Court.

The Hon'ble Supreme Court did not find any substance in the submissions made on behalf of the respondents to the effect that the price of the shares of Jet Airways India Ltd. paid by the respondents to the demat account holders was reasonable. Even according to the submission made by the learned counsel, value of the said shares, during the said period varied from ₹ 1172/- to ₹ 1339/- and in such circumstances, nobody would believe that all the demat account holders would sell their shares at the same rate, viz. ₹ 1170/- per share to the respondents. These transactions are, therefore, definitely of fishy nature.

The submission to the effect that no Retail Individual Investor had made any complaint to the SEBI is not at all relevant because the SEBI need not act only on the basis of a complaint received. If from its independent sources, the SEBI, after due enquiry comes to know about some illegality or irregularity, the SEBI has to act in the manner as it acted in the instant case. The fact, however, remains that because of the undue advantage which the respondents got, some small investors or RII must have not got the shares, which they ought to have been allotted.

In the instant case, not one or a few, but several demat holders had given one particular address and it is also pertinent to note that upon initiation of an inquiry at the instance of the SEBI, most of the demat accounts had been closed by the demat account holders.

The submission was also to the effect that the shares could have been sold before they were listed with a stock exchange and such a sale cannot be said to be an illegality.

The submission made to the effect that the Tribunal is a final fact-finding authority cannot be disputed. According to the learned counsel, the facts found by the SAT should not be disbelieved by this Court. However, for coming to a definite conclusion contrary to the findings arrived at by the lower authority, the appellate authority, in the

instant case, the SAT, ought to have recorded specific reasons for arriving at a different conclusion, but the Hon'ble Supreme Court did not find any sound reason for coming to a different conclusion in the impugned order. On the other hand, the Hon'ble Supreme Court found detailed discussion for coming to a particular conclusion in the order, which was passed by the Whole Time Member of the SEBI and therefore, the Hon'ble Supreme Court did not see any reason for the SAT to disturb the said finding without mentioning any strong and justifiable reason for coming to a different conclusion.

Keeping in mind the outcome of the judgement of the Hon'ble Supreme Court in the above case, it can be established that the SEBI can initiate action in the manner as stated above to know about some illegality or irregularity even if SEBI comes to know from its independent sources and on the basis of evidence or submission, SEBI can take necessary steps or actions.

Question 4

(a) Ala Technologies India Limited is engaged in the business of IT consulting, software development services and sale of proprietary software under its coined trademark/ tradename "Quickthink" since 2003. It had registered its trademark 'Quickthink' in India in 2010 under Class 9.

In the year 2012, Hermaan, a disgruntled employee quit the Company and started his own software venture and started a domain name 'Quickthink.in'. In the year 2015, the Company's management became aware of the domain name registered by Hermaan, when one of its employees accidentally, noticed the website and informed the Management. Immediately, Ala Technologies filed a complaint against Hermaan. Will the Company succeed ? (6 marks)

(b) Surapad was a clerical level employee working with a public sector bank in Calicut. He was convicted of an offence involving moral turpitude and dismissed from service. He approached the employee staff union for support. A case was filed in higher Court by the staff union challenging the dismissal. Evaluate in background of judicial pronouncement(s). (6 marks)

Answer 4(a)

The facts of the given case are similar to *ThoughtworksInc* v. *Super Software Pvt. Ltd & Anr [Del]*

The Petitioner was able to show that no sooner than he came to know of the above domain name, it took prompt action by filing a complaint with NIXI. More importantly, the learned Arbitrator appears to have come to an erroneous conclusion that the trademark "ThoughtWorks" did not belong to the Petitioner. Again, no opportunity was afforded to the Petitioner. The impugned domain name contains only the Petitioner's trademark and yet no finding was returned on whether there was any similarity. The decision in Stephen *Koenig* v. *Arbitrator*, National Internet Exchange of India &Anr 186 (2012) DLT 43, which was subsequently upheld by the Division Bench of this Court because of the fact that a mere delay in lodging the complaint would not disentitle the aggrieved party from proceeding against the 'squatter".

The Court is satisfied that in the present case, the learned Arbitrator failed to apply his mind to the facts on record. Indeed, a copy of the trademark registration certificate

of the Petitioner was enclosed with the complaint and yet the learned Arbitrator failed to have noticed this fact. In any event, the complaint itself contained details of its various registrations. If there was any doubt, the learned Arbitrator ought to have sought a clarification from the Petitioner on this aspect as well. Importantly, no finding was returned on whether the use of the domain name by Respondent No. 1 would lead to confusion and deception. With the domain name taking up the entire name of the Petitioner, there could be no doubt that the use of such domain name by the Respondent would be deceptively confusing and erroneously indicate a connection of Respondent No. 1 with the Petitioner when there is none.

For all of the aforementioned reasons, the Court is satisfied that the impugned Award is opposed to the fundamental policy of India as it has numerous glaring errors which appear on the face of the Award. Consequently, the Court sets aside the impugned Award and allows the petition but, in the circumstances, with no order as to costs.

The situation given is similar to this case mentioned above. Accordingly, Ala Technologies may succeed in the complaint filed against Hermaan.

Answer 4(b)

The facts of the given case are similar to the *State Bank of India & ORS* vs. *P. Soupramaniane.*

In this case, it was observed by the Supreme Court that we do not agree with the reasons given by the High Court for setting aside the order of discharge and directing the reinstatement of the Respondent in service. A show cause notice was issued to the Respondent in which it was categorically mentioned that the Respondent cannot continue in service after his conviction in a criminal case involving moral turpitude in view of Section 10(1) (b) (i) of the Banking Regulation Act, 1949. After considering the explanation of the Respondent, an order of discharge was passed. The High Court is not right in holding that no reasons had been given by the bank for discontinuing the Respondent from service. The High Court committed an error in holding that the order of discharge should be set aside on the ground that the provision of law under which the Respondent was discharged was not mentioned in the order. Yet another reason given by the High Court for interference with the order of discharge is that the criminal court released the Respondent on probation only to permit him to continue in service. The release under probation does not entitle an employee to claim a right to continue in service. In fact the employer is under an obligation to discontinue the services of an employee convicted of an offence involving moral turpitude. The observations made by a criminal court are not binding on the employer who has the liberty of dealing with his employees suitably.

Though we do not agree with the reasons given by the High Court for setting aside the order of discharge of the Respondent from service, it is necessary to examine whether Section 10 (1) (b) (i) of Banking Regulation Act is applicable to the facts of the case. Conviction for an offence involving moral turpitude disqualifies a person from continuing in service in a bank. The conundrum that arises in this case is whether the conviction of the Respondent under Section 324 IPC can be said to be for an offence involving moral turpitude.

There can be no matter of doubt about certain offences which can straightaway be termed as involving moral turpitude e.g. offences under the Prevention of Corruption of

Act, NDPS Act, etc. The question that arises for our consideration in this case is whether an offence involving bodily injury can be categorized as a crime involving moral turpitude. In this case, we are concerned with an assault. It is very difficult to state that every assault is not an offence involving moral turpitude. A simple assault is different from an aggravated assault. All cases of assault or simple hurt cannot be categorized as crimes involving moral turpitude. On the other hand, the use of a dangerous weapon which can cause the death of the victim may result in an offence involving moral turpitude. In the instant case, there was no motive for the Respondent to cause the death of the victims. The criminal courts below found that the injuries caused to the victims were simple in nature. On an overall consideration of the facts of this case, we are of the opinion that the crime committed by the Respondent does not involve moral turpitude. As the Respondent is not guilty of an offence involving moral turpitude, he is not liable to be discharged from service.

For the aforementioned reasons, we affirm the judgment of the High Court. The Appeal is dismissed accordingly.

In the given situation, there is no doubt that the conviction is for an offence involving moral turpitude and conviction for an offence involving moral turpitude disqualifies a person from continuing in service in a bank.

Therefore, the challenge of the staff union may not succeed.

Question 5

(a) Vivardhan Industries Limited (VIL) had taken loan of Rs. 60 Crore from India Bank Limited. Due to slowdown in the economy and other external factors, the Company incurred huge losses and could not repay a portion of the loan taken from the Bank. The Bank filed an application before Debt Recovery Tribunal (DRT) Trivandrum against the VIL for recovery of dues through the sale of VIL's property under SARFAESI Act. The Company preferred an appeal before Debt Recovery Appellate Tribunal (DRAT) by depositing a sum of Rs. 5 Crore as it is a prerequisite for filing an appeal before the Appellate Tribunal. Subsequently, VIL sought to withdraw appeal and sought refund of deposit.

Will VIL succeed in its claim of refund of deposit ? (6 marks)

(b) Kitchenise is an online sale portal which displayed Hypersteel India Private Limited's, steel products on its portal at a discounted price. Aggrieved by this Hypersteel displayed a caution notice on its website ('Caution Notice') alleging that the its products sold by the Kitchenise through its website are without its authorization and are counterfeit.

Further, the Caution Notice stated that the Hypersteel will not honour warranties on its products sold through the Kitchenise's website and any purchase made from these websites shall be at customers' own risk. Kitchenise served a legal notice to Hypersteel for withdrawal of the Caution notice. Comment in the background of decided case law(s). (6 marks)

Answer 5(a)

The facts of the present case are similar to the case of *AXIS Bank V SBS Organics Pvt. Ltd. & Anr [Supreme Court of India].*

An appeal under Section 18 of The Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (hereinafter referred to as 'SARFAESI Act") before the Debt Recovery Appellate Tribunal (hereinafter referred to as "DRAT') can be entertained only if the borrower deposits 50% of the amount in terms of the order passed by the Debt Recovery Tribunal (hereinafter referred to as 'DRT) under Section 17 of the Act or fifty per cent of the amount due from the borrower as claimed by the secured creditor, whichever is less. The Appellate Tribunal may reduce the amount to twenty-five per cent. What is the fate of such deposit on the disposal of the appeal is the question arising for consideration in this case?

Being a pure legal issue, it may not be necessary for us to refer to the factual position in detail. The first respondent, being a borrower and aggrieved by the steps taken by the secured creditor, filed Securitization Application No. 152 of 2010 before the Debt Recovery Tribunal. Ahmedabad. Though, initially an interim relief was granted, the same was vacated by order dated 20.01.2011. Therefore, the first respondent moved the Debt Recovery Appellate Tribunal, Mumbai under Section 18 of the SARFAESI Act. In terms of the proviso under Section 18 the first respondent made a deposit of ? 50 lakhs before the Appellate Tribunal. During the pendency of the appeal before the DRAT, Securitisation Application itself came to be finally disposed of before the Debt Recovery Tribunal at Ahmedabad, setting aside the sale. Realising that the appeal did not survive thereafter, the first respondent sought permission to withdraw the same and also for refund of the deposit of ? 50 lakhs. Permission was granted, however, making it subject to the disposal of the appeal. As the appeal itself was being withdrawn, the first respondent moved the High Court of Gujarat at Ahmedabad by way of Writ Petition (Special Civil Application). Aggrieved by the observation that the withdrawal would be subject to the result of the appeal. The same was disposed of by order dated 05.03.2015 by the learned Single Judge, setting aside the said condition and permitting the first respondent herein to withdraw the amount unconditionally. Aggrieved, the appellant-Bank filed an intra-Court appeal. That appeal was dismissed by order dated 01.04.2015 by a Division Bench, and thus aggrieved, the Bank has come up in appeal before the Supreme Court.

Any person aggrieved by the order of the DRT under Section 17 of the SARFAESI Act, is entitled to prefer an appeal along with the prescribed fee within the permitted period of 30 days. For preferring an appeal, a fee is prescribed, whereas for the Tribunal to 'entertain the appeal, the aggrieved person has to make a deposit of fifty per cent of the amount of debt due from him as claimed by the secured creditors or determined by the DRT, whichever is less. This amount can, at the discretion of the Tribunal, in appropriate cases, for recorded reasons, be reduced to twenty-five per cent of the debt.

In the case before us, the first respondent had in fact sought withdrawal of the appeal, since the appellant had already proceeded against the secured assets by the time the appeal came up for consideration on merits. There is neither any order of appropriation during the pendency of the appeal nor any attachment on the pre-deposit. Therefore, the deposit made by the first respondent is liable to be returned to the first respondent. Though for different reasons as well, we endorse the view taken by the High Court. Thus, there is no merit in the appeal. It is accordingly dismissed. We make it clear that the dismissal of the appeal is without prejudice to the liberty available to the appellant to take appropriate steps under Section 13(10) of the SARFAESI Act read with Rule 11 of the Security Interest (Enforcement) Rules, 2002.

Answer 5(b)

The facts of the present case are similar to the case of [*Jasper Infotech Pvt. Ltd. (Snapdeal)* v. *Kaff Appliances (India) Pvt. Ltd [CCI*].

On a consideration of the aforesaid material, the main issue that arises for determination by the Commission in the present matter is whether the allegation of the Informant against the Opposite Party (OP) with regard to imposition of resale price maintenance, in contravention of the provisions of Section 3(4) (e) read with Section 3(1) of the Act, is established on the basis of the facts and evidence on record.

Upon a bare perusal of the provisions and the material available on record, it is evident that the Informant's online portal, i.e. Snapdeal, is offering an online distribution service to various distributors/dealers. It may also be relevant to highlight that the Commission has earlier held, though not in a case involving similar issues, that online retail portals are a part of distribution channel. The Commission, in *Deepak Verma* v. *Clues Network (Case No. 34/2016, order dated 26.07.2016)*, while determining the dominance of an online retail portal, held that online and offline are not two different relevant markets, but are two different channels of distribution to the same relevant market. Similarly, in the case of Confederation of *Real Estate Brokers Association of India* v. *Magicbricks.com & Ors.*(Case No. 23/2016, order dated 03.05.2016), while determining the relevant market, the Commission held that online and offline services of brokers cannot be distinguished. Both are alternative channels of delivering the same service.

The Commission, therefore, observes that in the instant case also, when the distributors/ dealers are using the services of Informant while selling the products of the OP, it ipso facto becomes a part of distribution/vertical chain and thus, it would be incorrect to state that the Informant is only a market place facilitating interaction of the buyers and sellers online. It is not necessary in such evolving markets that any entrant in the downstream level of the value chain should join at the behest of the manufacturer or with its explicit concurrence. What may be relevant is to examine as to whether such player provides any active service to the end customer in availing the product or service involved, which given the facts of the present case can be answered in affirmative.

Based on the material available on record, the Commission is of the view that in the present case there was no Appreciable Adverse Effect on Competition (AAEC). Further, the presence of a large number of dealers who were competing with each other suggests a fair degree of intra-brand competition. The data collected by the DG showed that there were 1,422 dealers selling OP's kitchen appliances all over India during the relevant time period who were found to be competing for the turnover linked incentives. Discounts were variable in nature and linked to the target being achieved. Since incentives were variable, the net landing price for each dealer was also different. This enabled different dealers to offer different prices to customers for the same product. Moreover, competition among distributors was found to be even stiffer as they were exclusively dealing with the OP's products.

Thus, the Commission is of the view that *vis-à-vis* the dealers the evidence did not reveal the existence of any price restriction or minimum Resale Price Maintenance (RPM). As regards the Informant, though the existence of Caution Notice, Legal Notice and Email has been established, it has not been conclusively established that they were

used as instruments for imposing a minimum RPM on the Informant. Further, since vertical agreements falling under Section 3(4) read with Section 3(1) are subjected to rule of reason analysis, even if there exists a price restriction by the OP, AAEC needs to be established. As highlighted above, the actual impact of the conduct of OP did not demonstrate any adverse effect on competition. Furthermore, the existence of intra brand competition among dealers/distributors negate the anti-competitive impact of the OP's alleged conduct. Thus, no contravention of the provisions of Section 3(4) (e) of the Act is found against the OP, in the facts and circumstances of the present case.

For the foregoing reasons, the Commission is of the view that the evidence on record does not establish a case of contravention against the OP within the provisions of Section 3(4) (e) read with Section 3(1) of the Act. Hence, the case is hereby directed to be closed.

Question 6

Amrut is a Director (Finance) of a Mutual Fund Company. The Board had requested Amrut to work towards introducing effective internal control systems and enhance inter-departmental and stakeholder relationship. He was given the liberty to choose his own team for this work. He recruited a deputy, Kalpa, who, was technically competent but seemed to have attitudinal issues. Some of his team members informed him, that Kalpa prefers to hold back information and her behavior is at times rude towards the team. However, no staff has formally complained or yet left the organization.

As such there was friction between Amrut and Kalpa. She seems to ressent any suggestions that he provides and is not open to feedback. She has implied, several times, that she feels she is being unfairly harassed and bullied.

Amrut discussed this situation informally with the Managing Director. Although he has found Kalpa awkward and defensive, and he knows that another director also considers her somewhat abrasive, he has identified nothing that would warrant disciplinary action. Kalpa informs Amrut that she has been shortlisted for a role as Director (Finance) at another Mutual Fund house. Quietly, Amrut felt elated at the prospect that she might be leaving. The following day he receives a letter from Kalpa's prospective new employer. Kalpa had given his name as referral without informing him. The letter asks questions concerning the ability of the candidate to work in team, to motivate volunteers and to accept advice.

For several reasons, Amrut would very much like Kalpa to be offered the position with the other employer. However, he is concerned that an honest response to the enquiries would jeopardize his desire of keeping her out of the organization, as such a response can only be negative.

Based on the above fact, answer the following :

(a) Explain in detail what is the dilemma Amrut is going through.

(b) As a Company Secretary and Compliance Officer what would be your suggestion to Amrut, for further course of action ? (6 marks each)

Answer 6(a)

Amrut seems to be going through an ethical dilemma.

An ethical dilemma is a moral situation in which a choice has to be made between two equally desirable or undesirable alternatives. It can be understood as a dilemma (ethical paradox or moral dilemma) being a problem in the decision-making process between two possible options, neither of which is absolutely acceptable from an ethical perspective.

Dilemmas may arise out of various sources of behaviour or attitude, as for instance, it may arise out of failure of personal character, conflict of personal values and organizational goals, organizational goals versus social values, etc. A business dilemma exists when an organizational decision maker faces a choice between two or more options that will have various impacts on (i) the organization's profitability and competitiveness; and (ii) its stakeholders. In situations of this kind, one must act out of prudence to take a better decision.

The ethical dilemma consideration takes us into the grey zone of business and professional life, where things are no longer black or white and where ethics has its vital role today. A dilemma is a situation that requires a choice between equally balanced arguments or a predicament that seemingly defies a satisfactory solution.

Examples

Some examples of ethical dilemma include:

- Taking credit for others' work
- Offering a client a worse product for your own profit
- Utilizing inside knowledge for your own profit

Ethical dilemmas are extremely complicated challenges that cannot be easily solved.

Ethical Dilemmas in Business

Ethical dilemmas are especially significant in professional life, as they frequently occur in the workplace. Some companies and professional organizations adhere to their own codes of conduct and ethical standards. Violation of the standards may lead to disciplinary sanctions.

Almost every aspect of business can become a possible ground for ethical dilemmas. It may include relationships with co-workers, management, clients, and business partners.

People's inability to determine the optimal solution to such dilemmas in a professional setting may result in serious consequences for businesses and organizations. The situation may be common in companies that value results the most.

Fundamental Ethical Issues : In the present case, Amrut is going through fundamental ethical issue. The most fundamental or essential ethical issues that businesses must face are integrity and trust. A basic understanding of integrity includes

the idea of conducting business affairs with honesty and a commitment to treating every customer fairly. When customers think a company is exhibiting an unwavering commitment to ethical business practices, a high level of trust can develop between the business and the people it seeks to serve.

In order to solve ethical problems, companies and organizations should develop strict ethical standards for their employees. Every company must demonstrate its concerns regarding the ethical norms within the organization. In addition, companies may provide ethical training for their employees.

Answer 6(b)

A compliance officer, or compliance manager, ensures a company functions in a legal and ethical manner while meeting its business goals. They are responsible for developing compliance programs, reviewing company policies, and advising management on possible risks.

As a Company Secretary / Compliance Officer, the following course of action could be advised to Amrut to settle the moral / ethical dilemma before him:

- **Analyse the available options** : List the alternative courses of action available.
- **Consider the consequences** : Think carefully about the range of positive and negative consequences associated with each of the different paths of action available.
  - Who/what will be helped by what is done?
  - Who/what will be hurt?
  - What kinds of benefits and harms are involved and what are their relative values?
  - What are the short-term and long-term implications?
- **Analyse the actions** : Actions should be analysed in a different perspective i.e. viewing the action per se disregard the consequences, concentrating instead on the actions and looking for that option which seems problematic. How do the options measure up against moral principles like honesty, fairness, equality, and recognition of social and environmental vulnerability? In the case you are considering, is there a way to see one principle as more important than the others?
- **Make decision and act with commitment** : Now both parts of analysis should be brought together and a conscious and informed decision should be made. Once the decision is made, act on the decision assuming responsibility for it.
- **Evaluate the system** : Think about the circumstances which led to the dilemma with the intention of identifying and removing the conditions that allowed it to arise.

In the case study presented, Amrut should set aside his personal desires and provide an honest and fair feedback to the new organisation which would enable them to take a proper decision on hiring or non-hiring of Kalpa. In giving the feedback, Amrut should not

allow his personal vendetta to taint his mind, rather he should analyse Kalpa's attitude and behaviour in a non-partial manner leaving the choice with Kalpa and the new organisation to decide where she should work going forward. On the other hand, being the Director (Finance) and the team head he should discuss the issues he and the other team members faced while working with Kalpa to afford her the opportunity to present her side of the facts and take corrective action wherever required.

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BANKING – LAW & PRACTICE
(Elective Paper 9.1)

Time allowed : 3 hours *Maximum marks : 100*

NOTE: *Answer **ALL** Questions.*

Question 1

Case Study :

Smart Agro Foods Ltd. is a listed entity at BSE and NSE. It started its operations since September, 2015. The Company is engaged in the business of trading of agriculture commodities. It was enjoying a working capital cash credit limit of ₹100 lakh and from West Bank Ltd. In the month of January, 2017, the company decided to expand its business activity and to undertake the manufacturing and processing of agro commodities. The expansion plan included manufacturing of tomato catch-up, bakery biscuits & cakes and packaged sweets of Rasgulla & Gulabjamun. For this ambitious expansion plan the company came out with IPO in June, 2017 to raise the money for purchase of land and erection of factory site at Telangana, Jadhpur and Bikaner. The issue was successfully completed and the company purchased the land and erected the factory buildings at the above three places.

To meet out the cost of plant and working capital at these places the company availed consortium loans from three banks, including the present banker. The various credit facilities sanctioned by the consortium of three banks in April, 2019 were as under :

(₹ in Lakh)

Credit Facility	*West Bank Ltd.*	*Jodhpur Bank Ltd.*	*Bikaner Bank Ltd.*	*Total*
Cash Credit (existing)	*100*	*---*	*---*	*100*
New Cash Credit Limit	*75 (For Tomato Catch-up Division)*	*50 (For Bakery and Cake Division)*	*50 (For Sweets Division)*	*175*
Term Loan (For Purchasing of Automatic Plant for Manufacturing)	*40 (For Tamoto Catch-up Division)*	*25 (For Bakery and Cake Division)*	*30 (For Sweets Division*	*95*
Total	***215***	***75***	***80***	***370***

The company has offered the following securities for its cash and term loan to the bankers :

(₹ in Lakh)

Security	*West Bank Ltd.*	*Jodhpur Bank Ltd.*	*Bikaner Bank Ltd.*
Hypothecation of Book Debts	*200#*	*60#*	*65#*
Hypothecation of Plant & Machinery	*40*	*50+25=75*	*50+30=80*
Value of Land and Building	*1200 (At Telangana Industrial Area where Tomato Ketch-up is manufactured)*	*1500 (At Jodhpur Industrial Area where Baker and cakes are manufactured)*	*1000 (At Bikaner Industrial Area where Sweets are manufac-tured)*
# It represents the average of the book debts during the FY 2019-20.			

The comapny's performance during the FY 2019-20 was satisfactory. However, with the beginning of the FY 2020-21 the manufacturing activity got slow down due to nationwide closure on account of COVID-19 and migration of the workers. On account of this the company was not able to pay the instalments of the term loans to all the three bankers as well as the transactions in the cash credit account were also stopped and the company was not able to service the interest charged in the cash credit account. As a result, the accounts were classified by the bankers as Non-performing accounts (NPA).

The West Bank Ltd. is the Consortium Leader. By the end of the June, 2020 quarter the accounts of the company were showing problems. From July, 2020 to Sept., 2020 the company could not deposit the EMI of term loan, no stock statements were submitted in cash credit accounts and no interest on outstanding amount of cash credit could be deposited. The accounts were classified as Sub-standard in the books of all the banks.

The bankers insisted for recovery of the dues. The company pleaded that security pledged/ hypothecated/mortgaged with the bankers is much more than the amount outstanding in the various loan accounts. The bankers did not accept the plea, continuously pressurised the company to pay the dues of the bankers else will take legal recourses available under various lows such as, Recovery of Debts and Bankruptcy Act, 1993, Insolvency and Bankruptcy Code, 2016 (IBC) and Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (SARFAESI).

Based on the above facts, answer the following questions:

(a) Explain the meaning of Non-Performing Accounts (NPA). When banks can

classify the Term loans and Cash credit accounts as Non-Performing Accounts (NPA) ? (8 marks)

(b) In the above question, the bankers have classified the accounts as Sub-standard. Explain the classification of NPAs. What is meant by re-structuring of Bank Loans ? (6+2 marks)

(c) If in the above case, the company is able to pay the EMI of term loan and maintain transactions, pay interest and submit stock statements in the account with West Bank Ltd. only and for other two banks, it could not pay the EMI and interest :

(i) In such a situation, whether the West Bank Ltd. should classify the accounts as NPA since other bankers have classified the account as NPA ?

(ii) What would be your answer, if only term loan EMI with West Bank Ltd. are paid by the company and the Cash Credit accounts remains irregular. Whether in that case only the CC accounts be classified as NPA or whole of the credit facility should be classified as NPA ?

(iii) The company pleaded that the Security tendered to the banks amounts to much higher than of the outstanding in the loans accounts. (2+3+3 marks)

(d) How the NPA is to be recognised in:

(i) Cash Credit account and

(ii) Term Loans Account? (4+4 marks)

(e) If any loan or advances is classified as NPA, what provisions have to made by the bankers in their books and how to treat such provisions? (8 marks)

Answer 1(a)

An asset, including a leased asset, becomes non-performing when it ceases to generate income for the bank.

A Non-Performing Asset (NPA) is a loan or an advance where:

i. Interest and /or instalment of principal remain overdue for a period of more than 90 days in respect of a term loan.

ii. The account remains 'out of order' in respect of an Overdraft / Cash Credit for more than 90 days. Regular / ad hoc limits not been renewed within 180 days from the due date / date of ad hoc sanction.

iii. The bill remains overdue for a period of more than 90 days in the case of bills purchased and discounted.

iv. The instalment of principal or interest thereon remains overdue for two crop seasons for short duration crops (maturing within one year).

v. The instalment of principal or interest thereon remains overdue for one crop season for long duration crops (maturing after one year) (other agriculture loans 90 days norms are applicable).

vi. The amount of liquidity facility remains outstanding for more than 90 days, in

respect of a securitization transaction undertaken in terms of guidelines on securitisation dated 1st February, 2006.

vii. In respect of derivative transactions, the overdue receivables representing positive mark-to-market value of a derivative contract, if these remain unpaid for a period of 90 days from the specified due date for payment.

viii. If minimum amount due, indicated in monthly Credit Card Statement is not paid fully within 90 days from the due date of the bill.

ix. Loans guaranteed by State Govt. the normal rules are applicable. Where guaranteed by Central Govt. loans will continued to be standard category and no provision shall be made.

In case of interest payments, banks should, classify an account as NPA only if the interest due and charged during any quarter is not serviced fully within 90 days from the end of the quarter.

Accounts with temporary deficiencies

In addition, an account may also be classified as NPA Accounts with temporary deficiencies. The classification of an asset as NPA should be based on the record of recovery. Bank should not classify an advance account as NPA merely due to the existence of some deficiencies which are temporary in nature such as non-availability of adequate drawing power based on the latest available stock statement, balance outstanding exceeding the limit temporarily, non-submission of stock statements and non-renewal of the limits on the due date, etc. In the matter of classification of accounts with such deficiencies banks may follow the following guidelines:

i. Banks should ensure that drawings in the working capital accounts are covered by the adequacy of current assets, since current assets are first appropriated in times of distress. Drawing power is required to be arrived at based on the stock statement which is current. However, considering the difficulties of large borrowers, stock statements relied upon by the banks for determining drawing power should not be older than three months. The outstanding in the account based on drawing power calculated from stock statements older than three months, would be deemed as irregular.

   A working capital borrowal account will become NPA if such irregular drawings are permitted in the account for a continuous period of 90 days even though the unit may be working or the borrower's financial position is satisfactory.

ii. Regular and ad hoc credit limits need to be reviewed / regularised not later than three months from the due date / date of ad hoc sanction. In case of constraints such as non-availability of financial statements and other data from the borrowers, the branch should furnish evidence to show that renewal /review of credit limits is already on and would be completed soon. In any case, delay beyond six months is not considered desirable as a general discipline. Hence, an account where the regular / ad hoc credit limits have not been reviewed / renewed within 180 days from the due date/date of ad hoc sanction will be treated as NPA.

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and insurance policies need not be treated as NPAs as long as adequate margin is available in the account. Advances against gold and other securities are not covered under this exemption.

Answer 1(b)

Classification of NPAs

Banks are required to classify non-performing assets further into the following three categories based on the period for which the asset has remained non- performing and the realisability of the dues:

- Substandard Assets.
- Doubtful Assets.
- Loss Assets.

Standard asset is one which does not show any problems and does not carry more than normal business risk.

Substandard Assets

A substandard asset would be one, which has remained NPA for a period less than or equal to 12 months. Such an asset will have well defined credit weaknesses that jeopardize the liquidation of the debt and are characterized by the distinct possibility that the banks will sustain some loss, if deficiencies are not corrected.

Doubtful Assets

An asset would be classified as doubtful if it has remained in the substandard category for a period of 12 months. A loan classified as doubtful has all the weaknesses inherent in assets that were classified as substandard, with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently known facts, conditions and values- highly questionable and improbable.

Three sub-categories are as under:

1. Doubtful up to one year;
2. Above one up to three years; and
3. Above three years.

Loss Assets

A loss asset is one where loss has been identified by the bank or internal or external auditors or the RBI inspection but the amount has not been written off wholly. In other words, such an asset is considered uncollectible and of such little value that its continuance as a bankable asset is not warranted although there may be some salvage or recovery value.

Restructuring

When a lender gives concession to the borrower, for economic or legal reasons relating to the borrower's financial difficulty it is called Restructuring. It normally involves:

Modification of terms of the Advances / Securities, including alteration of repayment period /repayable amount / the amount of instalments /rate of interest.

- Sanction of additional credit facility.

- Roll over of credit facility.
- Enhancement of existing Credit Limit.
- Compromise Settlement.

Banks may restructure standard, sub-standard and doubtful category accounts. Standard assets are to be classified as sub-standard assets on restructuring. NPAs upon restructuring continue to be in the same asset classification.

Answer 1(c)

(i) Advances under consortium arrangements

Yes. West Bank would classify the asset as Standard whereas the other two banks would classify them as NPAs on account on the following grounds:

Asset classification of accounts under consortium should be based on the record of recovery of the individual member banks and other aspects having a bearing on the recoverability of the advances. Where the remittances by the borrower under consortium lending arrangements are pooled with one bank and / or where the bank receiving remittances is not parting with the share of other member banks, the account will be treated as not serviced in the books of the other member banks and therefore, be treated as NPA. The banks participating in the consortium should, therefore, arrange to get their share of recovery transferred from the lead bank or get an express consent from the lead bank for the transfer of their share of recovery, to ensure proper asset classification in their respective books.

(ii) Asset Classification to be borrower-wise and not facility-wise

Even if term loan account is regular but other accounts of the borrower are irregular then entire advances of the borrower will be treated as NPA on account of the following RBI guideline:

All the facilities granted by a bank to a borrower will have to be treated as NPA and not the particular facility/investment or part thereof which has become irregular (except loans against deposit, insurance policies NSCs).

(iii) Security Cover is more than outstanding loans

The pleadings of the borrower will not be taken in to account as, the RBI has advised that the availability of security or net worth of borrower /guarantor should not be taken into account for the purpose of treating an advance as NPA or otherwise.

Answer 1(d)

(i) NPA in Cash Credit account

The Cash Credit account shall be classified as NPA if it remains 'out of order'.

Out of Order status : An account should be treated as 'out of order', if the outstanding balance remains continuously in excess of the sanctioned limit / drawing power for 90 days. In cases where the outstanding balance in the

principal operating account is less than the sanctioned limit / drawing power, but there are no credits continuously for 90 days as on the date of Balance Sheet or credits are not enough to cover the interest debited during the same period, these accounts should be treated as 'out of order'.

Overdue : Any amount due to the bank under any credit facility is 'overdue' if it is not paid on the due date fixed by the bank.

(ii) NPA in Term Loan

The Term Loan account shall be classified as NPA if the interest and / or instalment of principal remain overdue for a period of more than 90 days in respect of a term loan.

Answer 1(e)

Provisioning Norms

The primary responsibility for making adequate provisions for any diminution in the value of loan assets, investment or other assets is that of the bank managements and the statutory auditors. The assessment made by the inspecting officer of the RBI is furnished to the bank to assist the bank management and the statutory auditors in taking a decision in regard to making adequate and necessary provisions in terms of prudential guidelines.

In conformity with the prudential norms, provisions should be made on the non-performing assets on the basis of classification of assets into prescribed categories. Taking into account the time lag between an account becoming doubtful of recovery, its recognition as such, the realisation of the security and the erosion over time in the value of security charged to the bank, the banks should make provision against substandard assets, doubtful assets and loss assets as below:

Loss Assets

Loss assets should be written off. If loss assets are permitted to remain in the books for any reason, 100 percent of the outstanding should be provided for.

Doubtful Assets

i. 100 percent of the extent to which the advance is not covered by the realisable value of the security to which the bank has a valid recourse and the realisable value is estimated on a realistic basis.

ii. In regard to the secured portion, provision may be made on the following basis, at the rates ranging from 25 percent to 1.00 percent of the secured portion depending upon the period for which the asset has remained doubtful:

Period for which the advance has remained in 'doubtful' category	*Provision requirement (%)*
Up to one year	25
One to three years	40
More than three years	100

With a view to bringing down divergence arising out of difference in assessment of the value of security, in cases of NPAs with balance of Rs.5 crore and above stock audit at annual intervals by external agencies appointed as per the guidelines approved by the Board would be mandatory in order to enhance the reliability on stock valuation. Collaterals such as immovable properties charged in favour of the bank should be got valued once in three years by valuers appointed as per the guidelines approved by the Board of Directors.

Substandard Assets

A general provision of 15 percent on total outstanding should be made. Sub-standard (unsecured) 25%, sub-standard unsecured (infrastructure) 20%.

In addition to the above the banks are also required to maintain provisions on standard assets, details of which are as under:

Standard Assets

The provisioning requirements for all types of standard assets stands as below.

Banks should make general provision for standard assets at the following rates for the funded outstanding on global loan portfolio basis:

(i) Farm Credit to agricultural activities and Small and Micro Enterprises (SMEs) sectors at 0.25 per cent;

(ii) Advances to Commercial Real Estate (CRE) Sector at 1.00 per cent;

(iii) Advances to Commercial Real Estate - Residential Housing Sector (CRE - RH) at 0.75 per cent;

(iv) Housing loans extended at teaser rates, provisioning will be 2.00 per cent in view of the higher risk associated with them. The provisioning on these assets would revert to 0.40 per cent after 1 year from the date on which the rates are reset at higher rates if the accounts remain 'standard'. On restructured advances it will be 5%;

(v) All other loans and advances not included in (a) (b) and (c) above at 0.40 percent.

Question 2

(a) When the RBI can remove managerial and other persons from the services of the Bank?

(b) Whether RBI has powers to supersede the Board of directors of a Banking Company ? If so, what are the powers and duties of Administrator ?

(6 marks each)

Answer 2(a)

As a measure of control over management and other persons of a banking company, Section 36AA of the Banking Regulation Act confers powers to RBI, to remove managerial and other persons from office, under certain circumstances.

If the RBI is satisfied that in the public interest or in the overall interest of the banking

company as well as to protect the interests of depositors it is necessary to remove a managerial person, it can remove by a written order with effect from any specified date any Chairman, Director, Chief Executive Officer (by whatever name called) or other officer or employee of the banking company. Before removal, such persons who are being removed would be given a reasonable opportunity to make a presentation to RBI, against the said order.

Pending the consideration of the representation from persons facing removal, in the opinion of RBI any delay in the interim would harm the interests of the bank or its depositors, order such persons not to take part either directly or indirectly in the management of, the banking company. Persons who are facing an order of removal from RBI, within thirty days from the date of communication of the order, can appeal to the Central Government against the order. After considering the appeal, the Central government may take a decision and communicate the same to the concerned persons who have made the appeal and its decision would be final in the matter. The decision of the Central Government cannot be questioned in any Court.

Such persons who are facing removal order from RBI, cease to be whole- time Chairman, Managing Director or Director or any other employees as the case may be of the banking company and cannot directly or indirectly, be concerned with or take part in the management of, any banking company for period not exceeding five years.

On the removal of a person from office under this section, that person shall not be entitled to claim any compensation for the loss or termination of office.

Answer 2(b)

Under Section 36 ACA of Banking Regulations Act, 1949, Reserve Bank of India (RBI) has powers to supersede the Board of Directors of a Banking Company in certain cases.

If RBI is of the opinion that it is necessary in the interests of a banking company or its depositors and in consultation with Central Government, through a written order, supersede the Board of Directors of such banking company for a period of not exceeding six months (subject to a maximum period of 12 months) or as specified in the order.

Appointment of Administrator

Upon superseding the Board of Directors, the RBI (after due consultation with the Central Government) will appoint, an Administrator (not an officer of the Central Government or a State Government) who has experience in law, finance, banking, economics or accountancy for such period as it determines. The Administrator so appointed, is bound to follow directions issued by the RBI in this regard. Consequent to the supersession of the Board of Directors, the Chairman, Managing Director and other Directors have to vacate their offices. No person shall be entitled to claim any compensation for the loss or termination of his office.

Powers and Duties of Administrator

The Administrator will exercise all powers, discharge functions and perform duties that are applicable under the provisions of the Companies Act or the Banking Regulation Act or any other applicable law in force, until the Board of Directors is reconstituted.

The Administrator appointed shall vacate office immediately after the Board of Directors of such banking company has been reconstituted.

Committee to assist the Administrator

The RBI in consultation with Central government may also appoint a committee of three or more persons who holding meetings. The RBI will specify salary and allowances payable to the Administrator and the members of the committee constituted and the same to be borne by the concerned banking company.

Question 3

(a) From the following data, calculate the amount to be credited in the Customer's account. Sight Bill tendered for USD 5,00,000 on 10th November, 2020 drawn under the Letter of Credit issued by the UK Bank.

Interbank USD Rate : 73.2600

Exchange Margin : 0.10%

Interest Rate : 7%

Interest Period : 15 Days

Rounding off to nearest multiples of 0.0025.

(b) What is position of a Chief Compliance Officer (CCO) in a Bank and also describe his duties and responsibilities ? (6 marks each)

Answer 3(a)

Spot Rate as given	73.2600
Less : Exchange Margin of 0.10%	0.0733
Total	**73.1867**
Rounded off to nearest multiples of 0.0025	73.1875
USD 5,00,000 @ 73.1875	3,65,93,750.00
Less : Interest @7% for 15 Days (365 days in a Year)	1,05,269.69
Net Payable	**3,64,88,480.31**
Net Payable (Rounded off to nearest multiples of rupees)	**3,64,88,480.00**

Answer 3(b)

As part of robust compliance system, banks are required, inter-alia, to have an effective compliance culture, independent corporate compliance function and a strong compliance risk management programme at bank and group level. Such an independent compliance function is required to be headed by a designated Chief Compliance Officer (CCO) selected through a suitable process with an appropriate 'fit and proper' evaluation/selection criteria to manage compliance risk effectively. The CCO shall be a senior executive of the bank, preferably in the rank of a General Manager or an equivalent position, not below two levels from the Chief Executive Officer (CEO).

- The CCO is required to have a good understanding of industry and risk management, knowledge of regulations, legal framework, and sensitivity to expectations of supervisors.
- There should not be any vigilance case or adverse observation from the Reserve Bank of India pending against the candidate identified for the appointment as CCO.
- The CCO shall have an overall experience of at least 15 years in the banking or financial services, out of which minimum 5 years shall be in the Audit/ Finance / Compliance/Legal/Risk Management functions. The candidate identified for appointment as the CCO should not be more than 55 years of age.
- The CCO shall have the ability to independently exercise judgment. He should have the freedom and sufficient authority to interact with regulators/supervisors directly and ensure compliance.

Duties and Responsibilities

These shall include at least the following activities:

(i) To apprise the Board and senior management on regulations, rules and standards and any further developments.

(ii) To provide clarification on any compliance related issues.

(iii) To conduct assessment of the compliance risk (at least once a year) and to develop a risk-oriented activity plan for compliance assessment. The activity plan should be submitted to the Audit Committee of the Board of Directors (ACB) for approval and be made available to the internal audit.

(iv) To report promptly to the Board /ACB / MD & CEO about any major changes / observations relating to the compliance risk.

(v) To periodically report on compliance failures / breaches to the Board /ACB and circulating to the concerned functional heads.

(vi) To monitor and periodically test compliance by performing sufficient and representative compliance testing. The results of the compliance testing should be placed to Board / ACB / MD & CEO.

(vii) To examine sustenance of compliance as an integral part of compliance testing and annual compliance assessment exercise.

(viii) To ensure compliance of Supervisory observations made by RBI and/or any other directions in both letter and spirit in a time bound and sustainable manner.

(ix) Assessment of policies and procedures.

(x) Research on banking laws and consumer protection law.

(xi) Conducting audit and inspection.

(xii) Compliance to Risk Management Unit.

Question 4

(a) Banks have full autonomy to adopt any lending practices. They may provide loans and advances to any Sector or any Industry. Write a brief note on statutory restrictions on lending under Banking Regulation Act, 1949. (6 marks)

(b) From the following information, calculate :

(i) Market Value at given YTM and

(ii) Duration of the Bond.

Bond Face Value ₹1,000/-.

Coupon : 7%.

Maturity : 5 Years

YTM : 9%.

Present Value Interest Factor for an Annuity @ 7% / 5 Years = 4.1002.

Present Value Interest Factor for Single Cash Flows @ 7%.

1st Year	*0.9346*
2nd Year	*0.8734*
3rd Year	*0.8163*
4th Year	*0.7629*
5th Year	*0.7130*

(6 marks)

Answer 4(a)

Under Banking Regulation Act, 1949, there are statutory restrictions on banks for lending. Brief of such restrictions are as under:

Advances against bank's own shares : In terms of Section 20(1) of the Banking Regulation Act, 1949, a bank cannot grant any loans and advances on the security of its own shares.

Advances to bank's Directors : Section 20(1) of the Banking Regulation Act, 1949 lays down the restrictions on loans and advances to the Directors and the firms in which they hold substantial interest.

Advances to Companies for Buy-back of their Securities : As per provisions of the Companies Act, 2013, companies are permitted to purchase their own shares or other specified securities out of their free reserves / securities premium account or from the proceeds of any shares or other specified securities subject to compliance of statutory conditions. In view of the above, banks should not provide loans to companies for buy-back of shares / securities.

Granting loans and advances to relatives of Directors : Without prior approval of the Board or without the knowledge of the Board, no loans and advances should be granted to relatives of the bank's Chairman/ Managing Director or other Directors, Directors

(including Chairman / Managing Director) of other banks and their relatives, Directors of Scheduled Co-operative Banks and their relatives, Directors of Subsidiaries / Trustees of Mutual Funds / Venture Capital Funds set up by the financing banks or other banks.

Restrictions on Grant of Financial Assistance to Industries Producing / Consuming Ozone Depleting Substances (ODS) : Banks should not extend finance for setting up of new units consuming / producing the Ozone Depleting Substances (ODS). No financial assistance should be extended to small/medium scale units engaged in the manufacture of the aerosol units using Chlorofluorocarbons (CFC) and no refinance would be extended to any project assisted in this sector.

Restrictions on Advances against Sensitive Commodities under Selective Credit Control (SCC) : With a view to prevent speculative holding of essential commodities with the help of bank credit and the resultant rise in their prices. Reserve Bank of India issues directives from time to time to all commercial banks, stipulating specific restrictions on bank advances against specified sensitive commodities. Banks and their subsidiaries should not undertake financing of 'Badia' transactions. Banks should not extend bridge loans against amounts receivable from Central / State Governments by way of subsidies, refunds, reimbursements, capital contributions, etc. subject to certain exemptions like financing against receivables from Government by exporters (viz. Duty Draw Back and IPRS).

Answer 4(b)

(i) The Market Value at YTM of 9%

= 70 (4.1002) + 1000 (0.7130)

= 287.014 + 713

= 1000.014

(ii) Duration of bond is calculated as under:

Year	*Cash Flow*	*PV Factor @7%*	*Present Value @7%*	*Proportion of Bond Value*	*Proportion of Bond value X time years*
1	70	0.9346	65.4220	0.0654	0.0654
2	70	0.8734	61.1380	0.0611	0.1222
3	70	0.8163	57.1410	0.0571	0.1713
4	70	0.7629	53.1410	0.0534	0.2136
5	1070	0.7130	762.9100	0.7628	3.814
			1000.0140		4.3865

Hence, the Duration of the Bond is 4.3865 years.

Question 5

(a) Describe the definition of Adjusted Net Worth (ANW) and Risk Management as per the revised Guidelines issued by the RBI in August, 2020 for Core Investment Companies. (6 marks)

(b) 'Time Deposits of Bank' and 'Certificate of Deposits' are one and the same. Do you agree with it ? If your answer is 'YES' mention the points of similarity and if your answer is 'NO' mention the points which differentiate a 'Certificate of Deposits' from 'Time Deposits of Bank'. (3 marks)

(c) On the basis of the following information, calculate the Discounted Value of Certificate

Deposit.

Face Value ₹ 50,00,000/-.

Number of Days : 91 Days.

Rate of Interest : 7% (3 marks)

Answer 5(a)

Adjusted Net Worth (ANW)

While computing Adjusted Net Worth (ANW), the amount representing any direct or indirect capital contribution made by one Core Investment Company (CIC) in another CIC to the extent such amount exceeds ten per cent (10%) of Owned Funds of the investing CIC shall be deducted. All other terms and conditions for computation of ANW remain the same.

The deduction requirement shall take immediate effect for any investment made by a CIC in another CIC after date of issue of RBI circular. In cases where the investment by a CIC in another CIC is already in excess of 10 per cent as on the date of RBI circular, the CIC need not deduct the excess investment as on the date of RBI circular from owned funds for computation of its ANW till March 31, 2023.

Risk Management

The parent CIC in the group or the CIC with the largest asset size, in case there is no identifiable parent CIC in the group, shall constitute a Group Risk Management Committee (GRMC). The GRMC shall report to the Board of the CIC that constitutes it and shall meet at least once in a quarter. The composition of GRMC shall be as under:

(i) The GRMC shall comprise minimum of five members, including executive members.

(ii) At least two members shall be independent directors, one of whom shall be the Chairperson of the GRMC.

(iii) Members shall have adequate and commensurate experience in risk management practices.

The GRMC will have the following responsibilities:

(i) Analyse the material risks to which the group, its businesses and subsidiaries are exposed. It must discuss all risk strategies both at an aggregated level and

by type of risk and make recommendations to the Board in accordance with the group's overall risk appetite.

(ii) Identify potential intra-group conflicts of interest.

(iii) Assess whether there are effective systems in place to facilitate exchange of information for effective risk oversight of the group.

(iv) Assess whether the corporate governance framework addresses risk management across the group.

(v) Carry out periodic independent formal review of the group structure and internal controls.

(vi) Articulate the leverage of the Group and monitor the same.

Based on the analyses and recommendations of the GRMC, CICs shall initiate corrective action, where necessary. Chief Risk Officers (CROs), appointed in CICs shall initiate such corrective action.

All CICs with asset size of more than Rs.5,000 crore shall appoint a CRO with clearly specified roles and responsibilities.

CICs shall submit to the Board, a quarterly statement of deviation certified by the Chief Executive Officer /Chief Financial Officer, indicating deviations in the use of proceeds of any funding obtained by the CIC from creditors and investors from the objects / purpose stated in the application, sanction letter or offer document for such funding.

Answer 5(b)

No. I do not agree. 'Time Deposits of Bank' (TD) and 'Certificate of Deposits' (CD) are quite different. The following points are unique to the CD only:

(i) CD is a money market instruments in the form of a negotiable usance promissory note but TD of bank is not a negotiable instrument.

(ii) It is issued at a discount to face value either in dematerialised form or as a Usance Promissory Note, against funds deposited by an investor with a bank or other eligible financial institution for a specified time period.

(iii) CDs are issued by scheduled commercial banks and select AIFIs as per RBI directions but bank TDs are issued by all types of banks.

(iv) Regional Rural Banks and Local Area Banks cannot issue CDs.

(v) CDs can be issued between 7 days and not exceeding one year, from the date of issue. AIFIs can issue CDs for a minimum period of 1 year and a maximum of 3 years, from the date of issue but TD can be issued for more than one year.

(vi) Minimum amount of CD issue will be for a face value of Rs.1 lac to an investor and it will be issued in multiples of Rs. 1 lac but no such restrictions in bank TD.

(vii) CDs can be issued to individuals (excluding minors), corporations, companies (including banks and PDs), trusts, funds, associations, etc.

(viii) Non-Resident Indians (NRIs), can subscribe to CDs on non-repatriable basis only. Such CDs cannot be transferred to another NRI in the secondary market.

(ix) Premature cancellation not allowed but in case of bank TD it is allowed.

(x) Loan against collateral of CD not permitted exception; holder is Mutual funds, but loan against bank's own deposits are allowed.

In view of the above facts, "Time Deposits of Bank" and "Certificate of Deposits" are not the same.

Answer 5(c)

The formula for calculation of discounted value of Certificate of Deposit (CD) is:

Discounted Value of CD= [36,500*Face Value] / [36,500 + (No. of Days * Interest)]

By putting the value in the formula, we get:

Discounted Value of CD = (36,500 * 50,00,000) / [36,500 +(91*7)]

= (36,500 *50,00,000) / [36,500 + 637]

= (36,500 *50,00,000) / 37,137

= 49,14,236.48

Rounded off to nearest Rupees comes to Rs.49,14,236/-.

Question 6

(a) Ms. Rashmi, after completed Bachelor's Degree in Dental Surgery, want to open a Dental Clinic. For establishing dental clinic, she needs some funds for purchasing of necessary equipment and furniture and other establishment. The estimated amount may be around ₹ 7 lakh for Dental Clinic. She somewhere heard about the MUDRA, but do not know much about it. She approached the Bank branch to avail the credit facility.

How the Bank branch will consider the proposal of Ms. Rashmi and under which scheme she can be financed and what are the benefits of the Scheme.

(b) "The Documents taken by Banks for a Credit Facility do not have prepetual life". Explain the statement in detail and what the various modes to revive the Loan documents are. (6 marks each)

Answer 6(a)

The bank branch can provide credit facilities to Rashmi, as under:

(i) *Refinance Scheme for Banks/NBFCs* : Under this scheme the refinance is available for term loan and working capital loan up to an amount of 10 lakh per unit. The Banks and Financial institutes provide credit facilities to the applicants under the categories (i) Shishu : covering loans upto 50,000/-, (ii) Kishor : covering loans above 50,000/- and upto 5 lakh, and (iii) Tarun : covering loans above 5 lakh and upto 10 lakh. In order to encourage women entrepreneurs, the financing banks / Micro Finance Institutes may consider extending additional facilities, including interest reduction on their loan.

Since the estimated amount is around Rs. 7 lacs for dental clinic of Ms. Rashmi, banks can finance under "Tarun" scheme.

(ii) *MUDRA Card* : Banks can also provide a MUDRA card to Ms. Rashmi for working capital finance. MUDRA Card is a debit card issued against the MUDRA loan account for working capital portion of the loan. The borrower can make use of MUDRA Card in multiple withdrawal and credit, to manage the working capital limit in a most efficient manner and keep the interest burden minimum.

Benefits of MUDRA Schemes:

(a) *No collateral required* : The Pradhan Mantri MUDRA Yojana loan is an unsecured type of business loan that means the loan borrower does not require to pledge their valuable assets as collateral to the lender. Under this scheme the government is the credit guarantee for the borrower.

(b) *Rate of interest are affordable* : Applicants can avail business loans for small amounts at nominal interest rates from eligible Banks / Financial institutes.

(c) *Lower interest rates for women applicants* : In order to encourage women entrepreneurs, the lending Institutes provide reduction in interest rates to women applicants.

(d) *Multipurpose use* : Credit facility sanctioned under MUDRA scheme can be utilised for fund or non-fund based needs of the business.

Answer 6(b)

Limitation period is the time limit within which the parties to a legal agreement, can take action in a Court of law to enforce their legal rights. A suit cannot be filed for recovery on the strength of a time barred document. Hence, if the documents are time barred, the bank's right of legal remedy is lost (expiry of limitation period does not take away the right of recovery of the debt, as it bars only the remedy of filing a suit). There are certain rights like lien, set-off, selling the securities which are pledged where remedy through Court is not required. As such there is no limitation period for these rights. In computing limitation for any suit, the date from which such period is to be reckoned, shall be excluded. The suit can be filed on the 'anniversary day'. The limitation period can not be shortened or lengthened by mutual agreement.

A limitation period can be extended (to revive the loan documents) in following ways.

(i) *Acknowledgement of Debt* : It is an acceptance of liability by the party liable by Letter of Acknowledgement of Debt (LAD), balance confirmation letter or even ordinary letter. It can be in form of signing of a balance sheet by authorized person. It has to be before expiry of limitation period.

(ii) *Part Payment* : A credit entry by itself will not save limitation. If a debtor makes a part payment before expiry of limitation period, himself or if it is made by his authorized agent a fresh limitation period starts from the date of such payment. The pay in-slip has to be filled in by the debtor himself or signed by him or his agent. It cannot be signed by any other person including employee of the debtor.

(iii) *Obtaining fresh set of documents* : When the bank obtains the fresh set of documents, fresh period of limitation starts from the date of execution of the fresh documents. A time barred debt can be revived under Section 25(3) of Indian Contract Act, 1872 only by fresh promise in writing and signed by the borrower or his authorized agent. A promissory note / fresh documents executed for the old or a barred debt will give rise to a fresh cause of action and a fresh limitation period will start from the date of such documents.

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INSURANCE – LAW & PRACTICE

(Elective Paper 9.2)

Time allowed : 3 hours *Maximum marks : 100*

NOTE: *1. Answer ALL Questions.*

2. Suitable assumptions, if considered necessary, may be made while answering a question. However, such assumptions must be stated clearly.

Question 1

'A' was issued a Life Insurance 'Jeevan Anand' Policy No. 12345678 with sum assured of ₹5,00,000. B his spouse was a nominee under the said Policy. The date of commencement of the Policy was 4.12.2012. Unfortunately, on 26.9.2015, due to unknown reasons A committed suicide. B lodged a claim with the Divisional Manager of XYZ Insurance Co. Ltd., but the same was rejected, vide letter dated 24.6.2016, on the ground that the deceased concealed material facts at the time of buying the insurance policy. B filed an appeal before the Zonal Manager of XYZ Co. Ltd. against the order of the Divisional Manager of XYZ Co. Ltd.

The Zonal Office upheld the repudiation decision of the Divisional Office and dismissed the Appeal, vide order dated 9.11.2016. B then filed an Appeal before the Claims Disputes Redressal Committee, XYZ Co. Ltd. of India, no decision was taken by the aforesaid Committee for quite a long time. B then filed a complaint before the National Consumer Redressal Commission, New Delhi.

The Complaint was contested by XYZ Co. Ltd. stating that after the death of the deceased life assured (for brevity 'DLA'), a claim was lodged which was immediately examined and it was found that the DLA was suffering from Bipolar Disorder (a mental illness) and had taken treatment from different places and this material information had been deliberately suppressed by him while taking the Policy. In the proposal form made on 2.2.2012, while filling the questionnaire regarding his medical condition, he answered in the negative. However, the deceased remained hospitalised at Neuro Psychiatry and Drug Deaddiction Rehabilitation Centre during 2008 to 2009 and later in 2015. Hence, the claim of the Respondent (B) was repudiated, vide letter dated 24.6.2016, pleading that there was no deficiency in service or unfair trade practice on the part of the Insurer and prayed for dismissal of the Complaint. XYZ Co. Ltd. further stated that the Consumer Courts at District and State levels erred in interpreting section 45 of the Insurance Act, 1938. According to section 45 of the Act, which has been amended w.e.f. 26.12.2014, Policy is not to be questioned on ground of misstatement after three years. It was further stated that the State Commission and District Forum failed to appreciate the law laid down by this Commission in other cases. In one of the case, the Policy was questioned after two years and the Hon'ble Commission had observed that as the insured made untrue declaration, as such the orders of the Fora below were set aside and the Consumer Complaint was dismissed. The Insurance company submitted that the insured was under solemn obligation to make true and full disclosure of information which was

within his knowledge, in the proposal form and withholding of such information or making misstatement was a fraudulent act and breach of principle of utmost good faith and the insurer was justified in repudiating the claim under the provisions of section 45 of the Insurance Act, 1938. It was further submitted that both the consumers forums at District as well as State Level erred in appreciating that life insurance agents do not act as an agent of XYZ Co. Ltd. The agents work on commission basis, and there was no relationship of employer-employee or master-agent between the XYZ Ltd. and the agents. It also submitted that in various cases Hon'ble Supreme Court has held, ''It is settled law that terms of the policy shall govern the contract between the parties, they have to abide by the definition given therein and all those expressions appearing in the policy should be interpreted with reference to the terms of policy and not with reference to the definition given in other laws. It is a matter of contract and in terms of the contract the relation of the parties shall abide and it is presumed that when the parties have entered into a contract of insurance with their eyes wide open, they cannot rely on definition given in other enactment. XYZ Co. Ltd. also mentioned that in the said judgement, Hon'ble Supreme Court also observed that, ''In interpreting documents relating to a contract of insurance, the duty of the court is to interpret the words in which the contract is expressed by the parties, because it is not for the court to make a new contract, however reasonable, if the parties have not made it themselves.''

The District Forum directed the Petitioner to pay ₹5,00,000 being death claim of the deceased to the Complainant and ₹25,000 as Compensation for deficiency in service, unfair trade practice and mental agony suffered by the Respondent along with ₹ 10,000 towards cost of litigation. The above order was to be complied within 30 days of its receipt by the Petitioner (Insurance Company). Thereafter, they shall be liable for an interest @ 12% p.a. from the date of institution of this Complaint, till it is paid, apart from cost of litigation. Being aggrieved by the order of the District Forum, the Petitioner filed an Appeal before the State Commission. The State Commission, vide order dated 28.11.2017, dismissed the Appeal and upheld the order passed by the District Forum. It stated that the A took the life insurance policy on 4.12.2012, whereas he died on 26.9.2015 i.e. after a period of more than two and a half years from the date of commencement of the policy. Being aggrieved by the order passed by the State Commission, the Petitioner Insurance company filed the Revision Petition before this Commission (National Commission).

According to B, the deceased was asked to simply put his signature on the proposal form and rest of the columns and answers were filled by the insurance agent. The entire proposal form was filled in the handwriting of the insurance agent. The deceased cannot be made responsible for concealing information, filed by the insurance agents.

The National Commission heard the Learned Counsel for the Insurer Petitioner as well as B the Respondent.

The Respondent's contention was that the insured was simply asked to append his signature and all other answers were filled in by the agent, in his own handwriting. The deceased cannot be held responsible for concealing any facts. This aspect is well covered by judgment in LIC Vs. Bina Joshi where the entries filled by agents, the policy holders were not blamed for concealing information.

It is very clear that as per Section 45 of the Act in force when the proposal was made and Policy taken, no Insurance Policy can be repudiated after two years on the

grounds of concealment/suppression of facts. The amendment to Section 45 providing a period of three years came later in 2014. The present case is covered by this section before its amendment and the deceased died after more than two years nine months after taking the Policy.

In view of the above, National Consumer Commission confirmed the orders of the State Commission and the District Forum and dismissed the Revision Petition filed by XYZ Co. Ltd.

From the information given above, answer the following questions :

(a) What types of Consumer Courts are available for insurance complaints ? Explain powers of the lowest consumer court.

(b) Was the National Consumer Commission justified in its decision ? Give reasons for your answers citing relevant case laws if any.

(c) Explain the provisions of Section 45 of Insurance Act, 1938 and how do these provisions affect the assured after the amendment of 26.12.2014 ?

(d) Would the decisions of the Consumer Forums have been different if the assured had committed suicide before 03.12.2014 ?

(e) Explain the procedure of claims in case of different types of life insurance policies.

(8 marks each)

Answer 1(a)

The 'Consumer Protection Act' provides for a three tier Consumer Disputes Redressal Agencies Consumer forum and their jurisdictions which are as under:

(1) District Consumer Disputes Redressal Forum established by the State Government in each district of the State. The State Government may establish more than one District Forum in a district. It is a district level Court that deals with cases valuing up to Rs.20 lakh/ Rs.1 crore as per Consumer Protection Act, 2019.

(2) State Consumer Disputes Redressal Forum established by the State Government takes up cases valuing up to Rs. 1 crore /from Rs. 1 crore to Rs. 10 Crore as per Consumer Protection Act, 2019.

(3) National Consumer Disputes Redressal Commission established by the Central Government, which works as a national level Court and deals with amounts more than Rs. 1 crore / Rs. 10 crore as per Consumer Protection Act, 2019.

None of the above forum can entertain a complaint unless it is filed within two years from the date on which the cause of action had arisen. Notwithstanding the above, a complaint may be entertained after the period of two years, if the complainant satisfies the concerned forum that he had sufficient cause for not filing the complaint within such period and the reason for condonation of the delay is recorded by the concerned forum.

Filing of complaints : A complaint may be filed by the consumer to whom the goods are sold or services are provided. Any recognized consumer association with one or more consumers with same interest can also file compliant.

Power of Civil Court vested to District Forum are as under:

The District Forum shall have the powers of Civil Court while trying a suit in respect of the following matters:

(i) The summoning and enforcing attendance of any defendant or witness and examining the witness on Oath.

(ii) The discovery and production of any document or other material object producible as evidence.

(iii) The reception of evidence on affidavit.

(iv) The requisition of the report of the concerned analysis or test from the appropriate laboratory of from any other relevant source.

(vi) Any other matter which may be prescribed.

Answer 1(b)

The decision of the District, State and National Consumer Commission was justified on the following grounds:

Life Insurance Policy cycle starts with solicitation of insurance business by a Distributor. A Distributor can be an Individual Agent, Corporate Agent, Insurance Broker, Web Aggregator etc. Once they convince the Customer to buy an insurance product which suits the needs of the customer, an application form also known as the Proposal form is filled by the customer. The customer is required to give personal details like Name, Date 'of birth, address, Gender, Name of the nominee and other details about personal health, family history details. Since the insurance contracts are based on the principles of utmost good faith, the customer also termed as proposer is expected to disclose about the status of his/her health completely in the Proposal form. Under life insurance, up to a certain limit, Proposal forms are underwritten without any medical examination which are called Non-medical Proposals. In the present case the policy given to Mr. A under non-medical proposals. The Insurance Company had issued the Policy document based on the proposal form. The Policy document is the evidence of the insurance contract which mentions all the terms and conditions of the insurance. The insured buys not the policy contract, but the right to the sum of money and its future delivery.

In the present case the assured, 'A' was issued policy after the proposal form was properly filled and signed by him with all the necessary documents as required for the issuance of policy. As per requirement the premium was paid in time and the policy was in force on the date of the death of the assured.

The order of the National Commission is justified on the following grounds:

(i) The reasons for suicide of Mr. A are not known and the same was committed after more than 2 years of issuance of policy.

(ii) The Section 45 of the Insurance Act, 1938 provides that a policy of life insurance can not be called in question by an insurer after the expiry of two years from the date on which it was effected on the ground that a statement made in the proposal for insurance or any other document leading to the issue of the policy was inaccurate or false.

(iii) B's contention was that the insured was simply asked to append his signature and all other answers were filled in by the agent, in his own handwriting. The deceased cannot be held responsible for concealing any facts. This aspect is well covered by judgment in *LIC* vs. *Bina Joshi* where the entries filled by agents, the policy holders were not blamed for concealing information.

(iv) In *L.I.C. of India* vs. *Promila Malhotra (N.CD.R.C.) 2003(2) ALT 11*, it was observed that more than two years had elapsed between the date of issue of policy and the date of death, the policy could not be called in question by the insurer on the ground that the statement made in the proposal form or any report of the medical officers, or referee or friend of the insured or in any other document of the company leading to issue of policy, was inaccurate or false unless the insurer showed that such information was on a material matter and it was fraudulently made by the policy-holder. The onus of proving all these facts was with the Insurer.

Thus, based on the above reasons District, State as well as National Consumer Commission was justified in its decision asking the insurer to pay the sum assured with interest and costs.

Answer 1(c)

Section 45 of the Insurance Act, 1938 provides the remedy to a Life Insurer for breach of the condition of utmost good faith (uberrima fidei) on the part of the life assured. It gives the right to the Life Insurer to repudiate a claim under a Life Insurance Policy if there was a misstatement, concealment or misrepresentation on any fact which was material to consideration of the risk by a Life Insurer.

Section 45 as it stood before the Insurance Laws (Amendment) Act, 2015 gave powers to cancel a policy or repudiate on the establishment of misstatements, concealment or misrepresentation by the Life assured any time after the issue of the policy. However, after a period of 2 years from taking the policy or reinstatement of a lapsed Policy, only if fraud is established on the part of the life assured, cancelling a policy or repudiation of the claim was possible. However, in the amended Section 45 by the above amendment act, a 3 year time limit has been fixed for any cancellation of policy or repudiation of claim on the above grounds. After the passage of the Amendment Act (which was preceded by an Insurance Laws Amendment Ordinance on 26 December 2014), no Life insurer can call in question a life insurance Policy (cannot cancel or repudiate a policy) on any ground whatsoever (whether for misrepresentation, concealment or misstatement on the grounds of fraud or even otherwise), after a period of 3 years from the date of taking the Life insurance policy (3 years from the date of commencement of Policy) or 3 years from the date of reinstatement of a lapsed Policy whichever is later.

However, within the above 3 years period, Life insurance companies are well within their right to call such policies in question if they are able to prove with documentary evidence that such misstatements etc., were material to the Underwriter for consideration of the risk and could have significantly impacted the decision of the Underwriter. Where Fraud is established, premiums paid till the date of such cancellation or repudiation can be forfeited. However, where the mis-statements were proved to be unintentional, premiums paid by the Life assured till the date of cancellation or repudiation will have to be refunded.

Amended Section 45 states that no policy of life insurance shall be called in question

for any reason whatsoever after a period of 3 years from the date of commencement, date of issuance, date of reinstatement, date of rider, whichever is later. Within 3 years, claim can be repudiated on the grounds of fraud, misrepresentation (or) on the grounds of incorrect misrepresentation (no fraud). Refund of premium mandated where repudiation is on the grounds of incorrect misrepresentation. Grounds and materials based on which repudiation made to be communicated to the Claimant.

For ULIPs, repudiated within 3 years from the date of revival, Fund value on the date of revival + premiums collected upon reinstatement + premiums collected subsequent to revival to be refunded.

In the case of Money back policies where repudiation happens due to misrepresentation at the time of reinstatement, premiums from the date of reinstatement of a lapsed policy, till the date of repudiation to be refunded after adjusting any Survival Benefits, if any, paid after the date of revival. No repudiation possible if the reinstatement was made just by paying arrears of premium with or without interest, but without any Declaration of Good Health.

No repudiation possible if the facts alleged to have been misrepresented by the Life assured were within the knowledge of the Agent who had sourced the Policy from the Customer.

Answer 1(d)

The decisions of the consumer forums, if 'A' had committed suicide before 03.12.2014.

The Policy was issued to the assured 'A' with effect from 04.12.2012. If A had committed suicide on or before 03.12.2014 it would have fallen in the limit of suicide or death within 2 years of issuance of policy. This is considered as early claim. In such case, the insurance company would have conducted an investigation by a senior employee of the insurer of outsourced to a third party investigator. This is a requirement if the assured dies or commits suicide within 2 years of issuance of policy to rule out the possibility of any moral hazard or non-disclosure of any existing illness. If the insurance company would have proved any of the moral hazard on the part of the assured the consumer forums also might have allowed the repudiation of the claim and would have decided in favour of the insurer. However this is dependent upon proof by insurer of any moral hazard while taking the policy.

Answer 1(e)

The main purpose of taking an insurance policy is that it should come in use in the times of crises. Selection of the right policy from a good life insurance company with a healthy claim settlement ratio is the main requirement for buying a life insurance. The main function of an insurance company is to ensure easy and timely settlement of a valid claim in return for the premium paid by the insurer/ policy holder.

The procedure of claims in case of life insurance policies can be described as under:

I. The Death claim settlement process is as under:

Step One: Intimation to the insurance company about the Claim

The nominee should inform the insurance company as soon as possible to enable

the insurance company to start with the claim process. The details required for intimation are policy number, name of the insured, date of death, cause of death, place of death, name of the nominee etc. The claim intimation form can be obtained from the nearest insurance company branch or even by downloading it from the insurance company website. Alternatively, many insurance companies also have online forms these days on their website for claim intimation.

Step Two: Documents required

The nominee will be asked to furnish the following documents:

- Death certificate;
- Age of the life insured (if not already given);
- Original Policy document;
- Any other document as per requirement of the particular insurer or case related.

For early death claims i.e. the claim that has arisen within three years of the policy being in force the company will do extra investigation to ensure it is a genuine claim. They might do the following:

- Check with the hospital if the deceased was admitted to hospital.
- In case of an air crash confirmation from the airline authorities check if the policy holder was a passenger on the plane.
- In case of death from medical causes, the insurance company will ask the hospital to provide doctor's certificate, treatment records etc. If the policy holder dies due to murder, suicide, accident then police FIR report, panchanama, post mortem report etc. shall be required.

Step Three: Submission of required Documents for Claim Processing

For quicker claim processing, it is essential that the nominee submits complete documentation as early as possible and any other documents that the company needs to pass the claim.

Step Four: Settlement of Claim

As per the Regulation 8 of the Insurance Regulatory Development Authority of India (IRDAI) (Policy holder's Interest) Regulations, 2002, the insurer is obligated to settle a claim within 30 days of receipt of all necessary documents including extra documents sought by the insurer. If the claim requires further investigation, the insurer needs to complete its procedures within 6 months from receiving the written intimation of claim.

II. Maturity & Survival Claims

The payment made by the insurance company on completion of term of policy or maturity date is called maturity payment. The amount payable consists of sum assured plus any bonus/incentives.

The insurance company informs the policy holder in advance by sending bank discharge form for filling details in it. The form needs to be returned back to the

insurance company with original policy document, ID proof, Cancelled Cheque and copy of pass book.

III. Rider Claims

Different riders can be attached to the base life insurance policy for enhanced protection. The riders can be accidental rider, critical illness rider, waiver of premium rider etc. For different riders, different claim proceedings are required. Some riders may be valid with the death claim like accidental death rider or some riders need to processed standalone like waiver of premium rider in case of disability.

IV. For Critical Illness Rider

Necessary medical documents such as first diagnosis report, Doctor's report, etc. are required. For Accidental disability rider - copy of FIR, Certificate of disability by the treating doctor, doctor's report etc. are required.

In many cases, life insurance claims have been delayed or denied due to lack of proper documentation or simply because the proper claim process was not followed. Hence, it is recommended that the claimant should be aware of the claim process in order to have a hassle-free claim settlement process during the emotionally draining time especially while filing a death claim.

Question 2

ABC Insurance Limited received a proposal on 1st April, 2019 from M/s MC Pvt. Co. Ltd., a proprietary firm to take a fire and allied insurance policy. The proposer was a chemical manufacturer and their plant was commissioned in November, 2017. The proposal required coverage for :

Building	:	*₹80 lakhs*
Plant and Machinery	:	*₹95 lakhs*
Stocks	:	*₹1.6 crores*

The insurance company issued fire and allied perils policy without carrying out any inspection.

M/s. MC Co. Ltd. sent a communication on 24th September, 2019 intimating about a major fire accident in the factory in the early morning hours of 24th September. This intimation though email received by the insurance company on 24th September was followed by a detailed letter and claim form claiming full loss of the stocks of ₹ 1.4 crores in stock on that day and also damage to the Plant and Machinery estimated at ₹20 lakhs. The stocks were all hazardous chemicals. The claim form stated that the Fire originated in the control room and spread to the machinery and stocks. The fire brigade report also stated the probable cause of the fire also as accidental.

ABC Insurance Limited deputed XYZ Surveyors to survey and assess the loss. The surveyors submitted the report assessing the losses as under :

Particular	*Assessed loss*
Plant and Machinery	*₹22 lakhs*
Stocks	*₹1.3 crores*

The insurance company immediately on receipt of the first intimation from the insured deputed its claim officer R an engineer to the factory at about 11 am of 24th September, 2019. R could meet S son of the proprietor of the firm G who was out of the factory during that time. R observed that the fire had been extinguished by that time. He also observed that the electrical wiring on the wall was at a safe distance from the machinery and stock. The insurance company while processing the claim asked for various documents from the insured which included copies of invoices, bank statements, books of accounts, electricity bills and other relevant papers from the date of inception to the date of fire. On the scrutiny of the documents submitted it was found that the purchases of the raw materials and sales of finished goods were quite high but the bank transactions were too small not justifying the volume of sales and purchases and stocks. The electricity bills were also too small as compared to the level of operations claimed by sales and purchases. Even one of the electricity bills had a remark 'premises closed'. These facts aroused suspicion in the minds of officials of the insurance company. The insurance company deputed N, a Chartered Accountant to investigate the claim.

N submitted the investigation report on 5th December, 2019. The main observations from her report were :

(i) Most of the purchases invoices were from non-existent parties.

(ii) The GST registration numbers mentioned on the invoices were fake.

(iii) The GST authorities confirmed that the numbers were fake.

(iv) One of the customers mentioned in the sales invoices confirmed that he never purchased any goods from M/s MC Co. Pvt. Ltd. and he showed a letter from M/s MC Co. Ltd. that their plant was closed and not in operation, so no supplies could be made due to non-production for long. Copy of the letter was submitted with the report.

ABC Insurance Limited sent a letter to M/s MC Pvt. Co. Ltd. on 8th December, 2019 repudiating the claim. The insursance company also complained to IRDAI for alleged misconduct on the part of the surveyors.

However it did not lodge any police complaint against M/s MC Co. Ltd. for the alleged or attempted fraud. It however, confidentially circulated brief particulars of the claim among members of the general insurers' association.

As an insurance expert you are required to comment on the following with reasons :

(i) The Insurance Company had deputed a Chartered Accountant for investigating the claim in detail. What are the reasons that led to investigation ? Is the Insurance company justified in repudiating the claim ? How will the insurer justify in the Consumer Court ? (6 marks)

(ii) Comment on the role of surveyor in this case. Did he discharge his duty ? What in your opinion should be the Regulation action for such surveyors ? (6 marks)

Answer 2(i)

The insured M/s MC Pvt. Co. Ltd. had submitted the documents containing fake registration numbers. It prima facie seems that the insured by doing so is trying to defraud the insurance company. Since the purchases and sales figures do not match with the accounts submitted and the invoices for purchases are fake it all indicates that

the insured only wanted to get the insurance claim by forging the documents and defrauding the insurance company. Citing these documents the insurance company deputed Chartered Accountant to investigate the claim.

The following are the reasons that led to investigation of the claim:

(i) The insured claimed that the loss occurred due to fire which originated in the control room from there it spread to machinery and stocks. The fire brigade report also confirmed this. However-, claim officer of the insurance company on his visit to the factory found that the electrical wiring on the wall was at a safe distance from the machinery and stocks. As per his observations it seemed that the fire was not accidental.

(ii) The documents submitted include the bank statements which did not show many transactions and the figures submitted for purchase and sales were much higher as compared to the banking transactions.

(iii) Electrical bills of the factory were of too small amounts as compared to the volume of operations claimed by the insured. One of the electrical bills also had a remark that the premises was closed.

All these discrepancies led the officers of the insurance company to believe that there was some mala fide intentions on part of the insured to make the claim.

The insurance company was justified in investigating the claim as there were various reasons indicating that the claim made by the insured M/s MC Pvt. Co. Ltd. was not a bona fide claim. There were many documents submitted by the insured which were deviating and leading to believe that the claim could be a fraudulent claim from the insured.

In case the insured approached the Court.

As seen from the facts of the case, the insured M/s MC Pvt. Co. Ltd. intimated for the fire at the factory and loss resulting therefrom. He has filed claim form showing a total loss of

Machinery	₹ 22 Lakhs
Loss of Stock	₹ 1.30 crores.

He had shown that loss being caused due to fire which resulted from electrical wiring problem and that causing loss to machinery and stock.

However after investigation by a Chartered Accountant on the claim the insurance company has repudiated the claim, but in case the insured decides to file a complaint with the consumer forum then the insurance company can submit all the required documents as under:

(i) Invoices of purchases and sales submitted by the insured.

(ii) Bank statement submitted by the party.

(iii) Electrical bills of the factory from the insured including the electrical bill showing the remark "premises closed".

(iv) Confirmation from the sales tax authorities that the registration numbers mentioned on the purchases were fake and the suppliers mentioned in the records were non-existent.

(v) Confirmation from one of the buyers mentioned in the sales invoices that they never purchased any goods from the insured and even the insured showed its inability to supply saying the plant was closed.

(vi) Report on observation made by the claims officer of the insurance company showing that the electrical wiring on the wall was on a safe distance from the machinery and stock storage. This observation helped to arrive at the conclusion that the loss as claimed could not occur due to accidental fire.

(vii) Report of investigation submitted by the Chartered Accountant. This report would show detailed working on the amounts of purchases, sales up to the date of fire and closing stock as at the date of fire.

All the above would show that:

(a) There was no accidental fire at the premises of the insured.

(b) The loss was too small an amount as compared to the amount of claim.

Hence, based on the above documents and reports and working the insurance company would be able to justify the repudiation of the claim.

Answer 2(ii)

The primary responsibility of a Surveyor or a Loss Assessor is to estimate the liability of the loss incurred by the Policyholder who has taken the insurance cover, to enable the insurance company arrive at the amount to be indemnified to the Policyholders under the terms of insurance contract. The following are the specific duties and responsibilities as enshrined in the regulations.

(i) *Declaration of conflicts of interest* : In case the surveyor is interested in the subject matter under loss assessment or in the policyholder whose subject matter is being assessed, he must declare the conflict to the insurer and stay away from the assessment exercise. For example, if the Surveyor is the son of Policyholder whose car has been damaged in a fire accident, such a Surveyor cannot assess the loss of the car of his father, in view of the conflict of interest. He must declare the relationship to the insurer concerned and not conduct the survey proceedings in such cases.

(ii) Maintenance of confidentiality and neutrality in the loss assessment exercise. He has to keep the interests of both the insurer and the policyholder in mind.

(iii) He must investigate the cause and circumstances of the loss in question.

(iv) He must personally conduct a spot survey and comment upon excess insurance or under insurance.

(v) Advise the insurer about loss minimization or loss control efforts or security and safety measures which can be adopted to ensure that the incident of loss is reduced or avoided in future.

(vi) Pointing out discrepancy in policy wordings, if any.

(vii) Satisfying the queries of the insured or the insurer in connection with the claim or loss.

(viii) Recommending applicability of depreciation and the percentage and quantum.

(ix) Commenting on salvage and its disposal.

In the case cited, the surveyor has assessed the loss of stock into as claimed by the insured. However looking to the facts of the case there were many discrepancies in the documents submitted by the Insured. Prima facie it was evident that the insured has falsified the claim and the loss was too negligible as compared to the amount of claim.

However the report submitted by the surveyor to the insurance company shows the amount of loss as amount claimed which shows that the surveyor has not carried out his responsibilities properly, it looks like that the surveyor has erred in fulfilling his duties in proper manner. The surveyor has failed in discharge of his duty. The Regulator Insurance Regulatory Development Authority of India (IRDAI) has all the right to cancel the licence of the surveyor and as an example, restrict or debar the surveyor from any professional work for a period of 3 years. But the regulator in many cases of intermediaries have undertaken such action in the cases of agents and brokers. The licence of these agents and brokers are cancelled in case they are involved in malpractices. The licence of the surveyor should also be cancelled.

Question 3

(a) A company RST Limited has the following policies of fire from the insurers for its stocks at its manufacturing unit :

Standard Policy A = ₹50,00,000

Standard Policy B = ₹30,00,000

Declaration Policy C = ₹1,00,00,000

A fire took place on 15th July, 2020. The value of stocks at the time of fire was ₹ 1,50,00,000. The loss of stocks due to fire was assessed at ₹15,00,000. Calculate the claim amount under each of the three policies. State the principle of Insurance, governing the above claim settlement process. (6 marks)

(b) Distinguish between "Agent" and "Broker". What actions does the Regulator take when there is a breach in their code of conduct ? (6 marks)

Answer 3(a)

Calculation of claims under the policies:

$$\text{Share of loss} = \frac{\text{Insured Value x Loss}}{\text{Value of Property}}$$

$$\textbf{Standard Policy A} = \frac{50,00,000 \times 15,00,000}{1,50,00,000}$$

$$= \textbf{5,00,000}$$

Standard Policy B = $\frac{30,00,000 \times 15,00,000}{1,50,00,000}$

= **3,00,000**

Policy C (Declaration Policy) = $\frac{1,00,00,000 \times 15,00,000}{1,50,00,000}$

= **10,00,000**

However the excess of loss remaining is = 15,00,000 - (5,00,000 + 3,00,000)

= **7,00,000**

So the claim from policy C = 7,00,000

The principle of insurance gearing the above claim settlement process is the "Principle of Contribution" which is a corollary to the principle of "Indemnity". The principle of Indemnity advocate that the insured must be compensated for actual loss. The insurance policy should make good actuate loss as per the principle of indemnity.

However, when more than one policy is taken for a risk, all the policies must practically contribute to the loss payments on the basis of the coverage that they have committed on the policy. Therefore, the three companies have paid a loss of ₹15,00,000 in proportion to the sum assured in the policies. This suggest the principle of contribution.

Answer 3(b)

The main features of distinction between Agents and Brokers can be tabulated as under:

Features	*Agents*	*Broker*
Representation	Insurance agents represent only one company, and they sell products in the company's line up. In addition to selling policies, agents also focus on improving the brand image of the company they represent.	Brokers typically sell insurance products belonging to different companies in the market. They do not have any allegiance to a particular company and sell products based on the requirements of customers.
Training	Since insurance agents represent a particular company, they receive in- house training from their respective companies on various products offered.	Brokers are not trained by any specific companies. Since they sell a wide range of products. There are external courses that can be taken by brokers before they start selling insurance products.
Licensing	Agents who have received training must obtain a license as per the regulations put forth by the Insurance Regulatory	Brokers must be licensed by the IRDAI in order to operate in the market. They are expected to meet a certain level of business

	and Authority Development of India (IRDAI).	regulations before they can get the broker license.
Accountability	An insurance company is accountable for the actions of its agents. IRDAI has the right to penalise an insurance company for any wrongdoings of its insurance agents.	Brokers have bigger accountability as they are not backed by any specific company. Brokers are bound to offer multiple products to their clients and disclose the prices of these products. Brokers can get sued for any misleading information they provide to their clients.
Knowledge	Insurance agents have in-depth knowledge in the products offered by their own companies. Although they are not required to know about all products in the market, they may have some knowledge about their competitor's products just for the sake of comparison.	Insurance brokers are required to have knowledge about multiple products in the market. They are bound to explain various products that seem best fit for the requirements of their clients. Also, they are accountable for the information they provide to customers. Hence, extensive knowledge about multiple products is a mandatory requirement for brokers.
Compensation	The commissions offered to agents are typically higher than that of brokers. The income earned by agents are relatively stable as they provide service under the wing of only one company. Companies may pay extra compensation based on the performance of agents.	Brokers sell multiple products, and commissions are based on the sale they make. Brokers must advise their clients about the products they sell and charge a fee from the companies. Based on the type of policies sold, brokers could experience variations in their income.
Personalised service	Agents may be able to provide personalised service to their clients since they have a limited customer base for the products they sell. Moreover, agents represent the image of a company and they act accordingly to ensure personalised service.	Brokers offer good service for their clients with the help of their professional knowledge. However, the wide customer base they have might prevent them from offering personalised service to their clients.
Volume of business	For insurance agents, the volume of business is limited	Brokers, on the other hand, have access to multiple insurance

since they deal with the products of only one company.	products in the market, and their volume of business is often much higher.

The Regulator IRDAI has prescribed very straight guideline for the Agents and Brokers regarding their code of conduct in the interest of the policy holder. In case these intermediary agents or brokers are found guilty of misconduct or misselling, the IRDAI can cancel the licences of the agents / brokers and de-bar them from doing business.

Question 4

(a) What is Nomination ? Explain the difference between Nomination and Assignment citing relevant sections and provisions of the Act. Which of these clause can be used for Estate Planning by an individual ?

(b) Differentiate between surrender value and paid up value. Which is a better option for a policyholder to exercise, if he wants to discontinue the policy ?

(6 marks each)

Answer 4(a)

Nomination is a facility that enables a policyholder to nominate an individual who can claim proceeds of the policy upon the demise of the policyholder. Nomination is dealt with under Section 39 of the Insurance Act, 1938 which lays down that the policy holder who holds a policy of insurance on his own life, may nominate the person or persons to whom the money secured by the policy shall be paid in the event of death. Where the nominee is a minor, a major should be appointed to receive the money secured by the policy in the event of death of the policy holder during the minority of the nominee.

Difference between Nomination and Assignment

S. No.	*Nomination*	*Assignment*
1.	Nomination is appointing some, person(s) to receive policy benefits only when the policy has a death claim.	Assignment is transfer of rights title and interest of the policy to some person(s).
2.	By merely nominating someone the right, title and interest of the insured over the policy is not transferred straight forward to that nominated person and remains with the insured person only.	The insurer is bound to pass over the benefits, claims and / or interests to the assigned person(s). Even during the time the insured is alive (or even prior to the death of the insured person). Since the policy benefits are assigned till the time the assignment is revoked once again.
3.	Nomination is done at the instance of the Insured.	Along with the instance of the insured, consent of insurer is also required.
4.	It can be changed or revoked several times.	Normally assignment is done once or twice during the policy period.

		Assignment can be normally revoked after obtaining the "no objection certificate" from the concerned Assignees.
5.	No attestation is prescribed in case of nomination.	Attestation is required in case of assignment.

An insurance policy's maturity amount can be deemed to be an individual's estate. Therefore a life insurance policy can be used to transfer the sum assured amounts mentioned in the policy to anybody by either making that person a beneficiary under the policy through nomination. On the other hand, the policy benefits can also be assigned or transfer through a will by the insured. Thus, through nomination or assignment the policy proceeds can be transfer to people. Thus both these clauses can be used to make the policy proceeds as a part of Estate of an individual.

Answer 4(b)

Paid up Value - When one stops paying premiums after a certain period, the policy continues but with lower sum assured. This sum assured is called the paid up value. The paid up value also refers to the value of a life insurance policy which lapses after acquisition of surrender value, but is not surrendered, the policy does not lose any benefits. The sum assured shall be redeemed in the same rate as the number of years the premium actually paid been to the total number of years for which the premium are payable. However, the policy is not eligible for any future bonuses.

Surrender Value - Surrender is voluntary termination of a Policy contract only by the Policyholder. More the number of premiums paid, more is the surrender value. Surrender value factor is a percentage of paid up value plus bonus. If the Policy has acquired surrender value, then surrender value is paid to the Policyholder and the contract comes to an end.

Under Traditional products, the rules for Surrender value are as follows:

(i) No Surrender Value for Term, Health & Annuity products.

(ii) For Premium Paying Term (PPT) of 10 years or more, surrender value gets acquired after paying 3 years' premiums.

(iii) For PPT less than 10 years, surrender value gets acquired after 2 years premium.

(iv) Minimum amount payable as Guaranteed Surrender value (Non-single):

- 30% of premiums paid (less survival benefits paid) if surrendered in second and third policy years;
- 50% if surrendered between fourth and seventh;
- 90% of surrendered in last 2 years (for less than 7 year);
- Beyond 7 year term, to be decided in file & use document (which gives the product features including policy benefits and premiums payable) to be filed by the Life insurer with the Regulator.

If a policy holder want to discontinue his policy, he can opt for the paid up value of the policy, as in paid up value option policy remains valid and sum assured reduced in the same ratio as the number of years the premiums actually paid bears to the total number of years for which premiums are payable and surrender value option the policy is terminated.

Question 5

(a) What are the features of Sovereign Gold Bonds ? And how does the scheme help in the economic welfare of the country ?

(b) What is a Reinsurance Contract ? How is it helpful as a Risk Management ? Examine for an Insurance Company. (6 marks each)

Answer 5(a)

Sovereign Gold Bonds : Sovereign Gold Bond Scheme launched by Government, under Gold Monetisation Scheme. Under the scheme, the issues are made open for subscription in tranches by Reserve bank of India (RBI) in consultation with Govt. of India. RBI Notifies the terms and conditions for the scheme from time to time.

The salient features of Sovereign Gold Bonds are as under:

(i) They are issued by Reserve Bank India on behalf of the Government of India.

(ii) The Bonds are denominated in multiples of gram(s) of gold with a basic unit of 1 gram.

(iii) The tenor of the Bond is 8 years with exit option in 5th, 6th and 7th year, which can be exercised on the interest payment dates.

(iv) Minimum permissible investment is 1 gram of gold.

(v) The maximum limit of subscribed is 4 KG for individual, 4 Kg for HUF and 20 Kg for trusts and similar entities per fiscal year (April-March) notified by the Government from time to time. A self declaration to this effect obtained by the issuing authority.

(vi) In case of joint holding, the investment limit of 4 KG is applied to the first applicant only.

(vii) RBI issue Press Release stating issue price of the Bond before new issue.

(viii) Presently the price of Bond is fixed in Indian Rupees on the basis of simple average of closing price of gold of 999 purity published by the India Bullion and Jewellers Association Limited (IBJA) for the last 3 business days of the week preceding the subscription period.

(ix) Payment for the Bonds is through cash payment (up to a maximum of Rs. 20,000) or demand draft or cheque or electronic banking.

(x) The Gold Bonds issued as Government of India Stocks under Government Security Act, 2006. The investors get Holding Certificate for the same. The Bonds are eligible for conversion into Demat form.

(xi) The redemption price is Indian Rupees based on simple average of closing price of gold of 999 purity of previous 3 working days published by IBJA.

(xii) The investors can be compensated at a fixed rate of 2.50 per cent per annum payable semi- annually on the nominal value.

(xiii) Bonds can be used as collateral for loans. The Loan-To-Value (LTV) ratio is to be set equal to ordinary gold loan mandated by the Reserve Bank from time to time. The lien on the bond shall be marked in the depository by the authorised banks.

(xiv) Bonds will be tradable on stock exchanges within a fortnight of the issuance on a date as notified by the Reserve Bank of India.

The Sovereign Gold Bonds scheme will reduce the massive gold imports into the country every year. Gold imports are the second biggest commodity imports into India after oil.

As such, reduction in gold imports will positively affect the larger economy by reducing the Current Account Deficit (CAD).

Answer 5(b)

Reinsurance is a risk transfer mechanism where under an insurance company passes on the risk on an insurance policy to another entity called Reinsurer for a consideration under a Reinsurance treaty (contract).

Under reinsurance one direct insurance company (also called Ceding company) transfers (cedes) part of the risk to another insurance company (called Reinsurer). This helps in reducing the liability of the direct insurer to a large extent. If there is no reinsurance, it could result in a dent in the financial position of an insurance company, especially when a natural calamity happens. Some of the global reinsurance companies who have opened reinsurance offices in India include Swiss Re., Munich Re., RGA, Hannover Re. etc. The Indian Reinsurer is GIC Re. (General Insurance Corporation of India). Reinsurers have their teams which comprise of competent technical professionals who are experts in Actuarial, Claims, Underwriting etc. Reinsurers take a proportion of the premium paid by the Policyholder and promises to pay the proportionate amount of any claims insured under the Policy.

Treaty reinsurance represents a contract between the ceding insurance company and the reinsurer who agrees to accept the risks of a predetermined class of policies over a period of time. When insurance companies underwrite a new policy, they agree to take on additional risk in exchange for a premium.

Question 6

S from Indore, purchased a Jeep Compass from its Authorised Dealer in Mumbai 24th April, 2019 for a sum of ₹21,24,000. The vehicle bearing registration No. MP-09-UA-1413 was insured comprehensively from 24th April, 2019 to 23rd April, 2020 with ABC Insurance Company. S went to RNT Marg for some official work on 23rd May, 2019 where he parked and locked the car in a parking area. He returned to the parking area at about 5 PM. To his surprise, he found the vehicle missing. He searched for the car frantically and on not finding it, lodged an FIR with the M. G. Road police station for the missing car. Next day, he also informed the insurance company in writing about the said theft of the vehicle. Despite vigorous efforts of the

police, the vehicle could not be traced. Hence, after 90 days, the police gave a non-traceable certificate/report to S. S, thereafter, again pursued the matter of settlement of claim with the insurance company and submitted a copy of the purchase invoice of the vehicle along with copies of the relevant documents. The insurance company did not respond positively and kept delaying the matter on one pretext or the other.

S was aggrieved by this inaction on the part of the insurer, filed a complaint with the District Forum. During the pendency of the complaint, the insurance company repudiated the claim on the ground that the vehicle was being used as a Taxi. The District Forum, after hearing both sides, directed the insurance company to pay S, the insured declared value of the vehicle, i.e., ₹21,24,000 along with interest @ 6% p.a. from four months after the date of lodging of claim till realisation. The District Forum also awarded ₹15,000 as costs. The insurance company filed an appeal before the State Commission. The plea highlighted the fact that the insurer was not liable to reimburse the loss of stolen vehicle as the same was being used as a taxi. This plea was rejected by the State Commission by observing that theft of the vehicle had nothing to do with the use of the vehicle. The appeal, therefore, was dismissed and the awarded amount was ordered to be released by the insurer.

The insurance company further filed a revision petition before the National Forum. During arguments, both sides vehemently advocated their views. Finally, it was pointed out by the counsel of the insured that in the decided case of 'National Insurance Company Ltd. Vs. Nitin Khandelwal', the Supreme Court had held that, "in a case where the vehicle had been snatched or stolen, the breach of condition is not germane and the insurance company is liable to indemnify the owner of the vehicle where the insured owner has obtained a comprehensive policy for the vehicle in question".' In view of the aforesaid judgment of the apex court in the earlier order of the State Commission in the 'Nitin Khandelwal case of 2008', the counsel for the insurance company did not press the point that insurer was not liable to reimburse for the stolen vehicle because it was being used as a taxi. Hence, the claim was finalised at 75% on 'non-standard basis' as upheld earlier by the Supreme Court in 2008 plus cost.

In light of the above, answer the following :

Question

(i) Was the stand taken by the Insurance company to settle the claim on "Non-standard basis" justified ? Give reason. Explain the concept of standard claim and non-standard claim. (12 marks)

Answer 6(i)

The stand taken at first instance by the Insurance Company to repudiate liability on the ground that the vehicle was used as a Taxi by 'S' is totally baseless and is not based on facts which have emerged in the present case. The liability under the policy therefore, was clear and the Insurance Company should have honoured its liability rather that going to the various forums initially and thereafter in a review petition before the National Forum.

(i) Though the Supreme Court in 2008 in *"Nitin Khandelwal Case"* had already laid down that "In a case, where the vehicle had been snatched or stolen, the

breach of condition is germane and the Insurance Company is liable to indemnify the owner of the vehicle where the insured owner had taken a comprehensive policy for the vehicle in question".

(ii) The Court had taken a view that the breach of the policy condition regarding the hire of the vehicle for a commercial purpose has no bearing on its theft and, hence, would be irrelevant. The Supreme Court in "Nitin Khandelwal Case" left the question "whether the State Commission was justified in allowing the claim of the respondent on the non- standard basis" open as the claimant had not filed arty appeal against the said order.

(iii) The insurance company would be bound to pay the insured declared value of the vehicle and not 75 % on non- standard basis.

(iv) Further, the National Consumer Disputes Redressal Commission in case of *"Rekha Sardana* vs. *Oriental Insurance Co. Ltd. & Ors*" held the same as mentioned above.

Thus, keeping in mind the above, the stand taken ultimately by the insurance company to settle the claim on non-standard basis was not justified. Therefore, the non-standard been for the settlement of the clause is not justified.

The Supreme Court has held in "*Nitin Khandelwal Case*" in 2008 that "where the vehicle is snatched or stolen, the breach of condition of policy is not germane, that the insurance company is liable to indemnify the owner of the vehicle when the insurer has obtained comprehensive policy for the loss caused to the insurer". If the Supreme Court's decision is viewed in totally, it becomes clear that in case of theft of a vehicle the nature of use of the vehicle cannot be looked into and the breach of such a condition is not germane and hence the Insurance Company is liable to indemnify the owner for the loss suffered by him.

However, in the present case, since there is no evidence of breach of usage condition, the claim will have to be paid. Further, as per rules, even if is presumed that there is a breach of any condition, a claim cannot be rejected for breach of a policy condition unless such breach is the cause of the loss. When there is no nexus between the breach and the loss, the claim has to be settled on a non-standard basis. Therefore, in the present case, as there is no evidence of misuse of vehicle as taxi, the claimant is liable for total loss payment and not only the total loss suffered by him as a result of theft and not merely settlement on 75% "Non-Standard basis", as the present facts of the case do not qualify under the guidelines for non-standard claims as mentioned below:

- Where a breach of warranty or policy condition arises and where such breach is of a technical nature or is evidently beyond the control or knowledge of the insured or is considered after rectifying the policy and collecting additional premium where due.
- In settling the claim, a deduction may be made from the assessed claim amount equivalent to the extra premium due for three years or three times the additional premium due for voyage which would have been charged had correct information been available originally.

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INTELLECTUAL PROPERTY RIGHTS – LAWS AND PRACTICES
(Elective Paper 9.3)

Time allowed : 3 hours *Maximum marks : 100*

NOTE: *Answer **ALL** Questions.*

Question 1

Read the following case study and answer the questions given at the end :

The Ethiopian economy is heavily dependent on the trade of its primary products. Among the country's limited tradable goods, coffee alone generates about 60 percent of Ethiopia's total export earnings. Indeed, coffee is closely tied to the culture and society of Ethiopia and an estimated 15 million people are, directly or indirectly, involved / engaged in the Ethiopian coffee industry.

Some of the world's finest coffees, such as Harrar®, Sidamo® and Yirgacheffee®, originate in Ethiopia. These coffees have a unique flavor and aroma that distinguish them from coffees of other countries or even from other coffees of Ethiopia. This African nation enjoys a strong reputation for its heritage coffees which command a very high retail price in the international market. However, only 5 to 10 percent of the retail price actually goes back to Ethipopia; most of the profit is shared by distributors and middlemen in the marketing sector. In wealthy countries, a cup of cappuccino may be sold at US$ 4, but many coffee growers in Ethiopia and other developing countries earn less than a dollar a day. There are instances where farmers were forced to abandon coffee production due to low returns and resort to growing more profitable narcotic plants.

Seeking to narrow down this gap between the retail price and the recturn to the producers, the Ethiopian government is trying to use a range of intellectual property rights (IPRs) to differentiate their coffee in the market place and achieve higher returns. In 2004, the government launched the Ethiopian Coffee Trademarking and Licensing Initiative (The Initiative) to provide a practical solution to overcome the longstanding divide between what coffee farmers receive for a sack of their beans and what retailers charge for that coffee when they sell it in retail outlets in different countries.

The Initiative is organized and run by the Ethicpian Fine Coffee Stakeholders Committee (the Stakeholders Committee) — a consortium comprising cooperatives, private exporters and the Ethiopian Intellectual Property Office (EIPO) as well as other concerned government bodies.

The EIPO took the leadership of The Initiative and began working on identifying a mechanism which would lead to a greater share for the country's coffee growers. The Initiative also intended to generate high retail prices for Harrar, Sidamo and Yirgacheffe – the three most famous coffee brands of Ethiopia. "The theory is : make the pie bigger. Let the market pay," explained Mr. Getachew Mengistie, former

Director General of the EIPO. "Rather than focusing on short term gain, this way we can enlist the big companies to do what we don't have the skills or financial means for – that is, building recognition of our brands in international markets and so increasing long term demand for them.

The key strategy, the Stakeholders, Committee agreed, was to achieve wider recognition of the distinctive qualities of Ethiopian coffees as brands and position them strategically in the expanding specialty coffee market; while at the same time to protect Ethiopia's ownership of the names so as to prevent their, misappropriation. This would lead to a greater share of the high, retail price Ethiopian coffees demand going straight to rural producers

The Ethiopian Government had to make a decision on how to best use IPRs to obtain exclusive ownership of Ethiopian coffee names, achieve wider international recognition and maximize returns. At first glance, registration of each Ethiopian coffee as a geographical indication (GI) seemed to be the best course of action. After all, the coffees are made in Ethiopia and named after the regions that made them famous. However, there are many unique circumstances summoning specialty coffee production in Ethiopia that actually make GI registrations less suitable than other forms of intellectual property (IP) protection. As Mr. Mengistie explained, "setting up a certification system would have been impracticable and too expensive."

Used to indicate the regional origin of a particular product, a GI registration must demonstrate a link between a characteristic of the product and the region where it is produced. If each Ethiopian specialty coffee were registered as a GI, it would have to be produced in a specific area of the country under specific circumstances. For example, a GI for Sidamo coffee would require every bag of Sidamo to be produced, processed or prepared in the Sidamo region and have a special quality that is directly dependent on the unique properties of the region. A GI also requires that the government oversee producers and distributors to guarantee that the coffees sold belong to a particular style or region, such as Sidamo.

However this is not a practical solution for Ethiopia. Specialty coffee in Ethiopia is grown on over four million small plots of land by an estimated 600,000 independent farmers spread throughout the country in remote areas. Although Ethiopian coffees such as Sidamo and Harrar are named after specific regions, all of it is not produced in the same region under the same circumstances. Distribution is also a problem, as it is predominately done informally by hauling bags of coffee on foot for many kilometers. Government oversight of coffee producers is therefore nearly impossible. Farmers would be required to pay a surcharge for government oversight, and this would only be an additional burden on them, many of who are already living below the subbistence level. Therefore the very nature of coffee production in Ethiopia makes GI certification difficult and impractical.

The Government of Ethiopia decided that instead of trying to protect Ethiopian coffee's geographical origin, it would be better to protect its commercial origin, which it would do through registering trademarks. This was seen as a more direct route of protection because it would grant the government of Ethiopia the legal right to exploit, license and use the trademarked names in relation to coffee goods to the exclusion of all other traders. Unlike a GI, a trademark registration does not require a specific coffee

to be produced in a specific region or have a particular quality in connection with that region. Using trademark registrations, the government of Ethiopia could then produce greater quantities of specialty coffees from all over the country. Rural producers outside the Sidamo region could grow Sidamo coffee, as it would not need to have a characteristic that is unique to the Sidamo region. The Stakeholders Committee therefore opted for a trademark-based solution, with the Ethiopian Government as the owner of these marks. This strategy gave the Government greater and more effective control over the distribution or its product, which ultimately increases revenue by exporting more goods, enabling a rise in prices and benefits to farmers.

The EIPO began filing applications to register the names Harrar/Harar, Sidamo and Yirgacheffe as trademarks in key markets. In the United States, Yirgacheffe was the first to obtain registration Sidamo and Harrar/Harar were granted registration at a later time. Trademarks for Ethiopian coffees were also registered in the European Union and Canada. In Japan, registration certificates were secured for two of the coffees (Yirgacheffe and Sidamo). The EIPO filed applications for trademark registrations of these three coffees in a number of other countries including Australia, Brazil, China, Saudi Arabia and South Africa.

The trademark strategy for Ethiopian coffee faced a major difficulty in 2006. The United States Patent and Trademark Office (USPTO) had approved the application to register Yirgacheffe. But the National Coffee Association (NCA), representing coffee roasters of the United States, objected to the EIPO's applications to trademark first Harrar, then Sidamo.

The American coffee chain Starbucks Coffee Corporation, was reported to be a driving force behind the NCA objection. It, however, publicly offered to assist the EIPO in setting up a national system of certification marks to enable the farmers to protect and market their coffee as "robust" geographical indications. The EIPO and its advisors disagreed. The designations, they argued, referred not to geographical locations but to distinctive coffee types. Moreover, appropriate intellectual property (IP) tools had to be chosen to meet specific needs and situations. It said that its coffee is grown on four million very small plots of land. Setting up a certification system would have been impracticable and too expensive. Trademarking was more appropriate to our needs. It was a more direct route offering more control.

The EIPO filed rebuttals against the USPTO decisions with supporting evidence to demonstrate that the terms Harrar and Sidamo had acquired distinctiveness. Meanwhile, both Starbucks and the Ethiopian government were keen to resolve their differences quickly and find a flexible way forward. Their joint efforts led to an announcement in 2006 that they had reached a mutually satisfactory agreement regarding the distribution, marketing and licensing of Ethiopia's specialty coffee designations, which provided a framework for cooperation to promote recognition of Harrar, Sidamo and Yirgacheffe.

Starbucks agreed to sign voluntary trademark licensing agreements which immediately acknowledge Ethiopia's ownership of the Harrar, Sidamo and Yirgacheffe names, regardless of whether or not a trademark registration has been granted. Legal commentators have honed in on the use of the term "designation" in the

agreement as a means of circumventing the obstacle caused by the status of the Harrar and Sidamo applications. EIPO felt that designation is used here as a broader term than trademark, to encompass some of the trademarks that are still pending registration. It is not related to certification.

In August 2006, the USPTO informed the EIPO that their rebuttal in the case of Harar had been successful. A trademark for Sidamo was also granted in February 2008.

The Initiative secured financial support from the Department for International Development (DFID) of the United Kingdom, technical advice from a Washington-based Non-governmental Organization (NGO), Light Years IP, and legal assistance from an American law firm, Amold and Porter.

The high cost of legal services for foreign trademark registration created some initial difficulties. Ethiopia, moreover, is not a member of the Madrid system for the international registration of marks. This was overcome by support from law firms which agreed to provide their services pro bono.

After acquiring the trademarks, Ethiopia initiated a royalty-free licensing scheme. The purpose of licensing was to secure recognition from the coffee distribution industry that Ethiopia owns and controls the use of trademarks, thereby building the reputation and good will of its specialty coffees around the trademarks. The government of Ethiopia wanted its coffee to have more market visibility so that the export premium for Ethiopian specialty coffee could be raised. The adopted strategy offered royalty-free license agreements and required the licensee to sell the specialty coffees using the registered trademarks (free of charge) on any product that consists wholly of Ethiopian specialty coffees and to promote Ethiopian fine coffee by educating their customers. The licensing strategy is expected to boost consumer recognition of Ethiopian coffee trademarks and facilitate the growth of the demand for Ethiopian fine coffees. This strategy will ensure that Ethiopian farmers and small businessmen secure a reasonable return from the sale of their coffees.

By mid-2009, almost one hundred license agreements had been concluded with coffee importing, roasting and distributing companies in North America, Europe, Japan and South Africa. Within the country, some forty seven private coffee exporters and three coffee producer cooperative unions in Ethiopia had also signed the agreement.

The high profile dispute with Starbucks increased the popularity of Ethiopian coffee. It was learnt from the coffee farmers' cooperatives and exporters just three months ago that the price of Yirgacheffe had already increased by $ 0.60 cents to $ 2 a pound."

Immediately after the resolution of the dispute, the stakeholders of Ethiopian coffee focused their attention on the need for a marketing strategy. They opted for a well-organized branding instrument. A United Kingdom-based company was given the responsibility of the brand promotion of Ethiopian coffee. The company worked together with the stakeholders and developed the brands and brand guidelines. Under this approach, a total of four brands were created : an umbrella brand with the name "Ethiopian Fine Coffee" and three individual brands entitled "Harar Ethiopian Fine Coffee," "Yirgacheffe Ethiopian Fine Coffee" and "Sidamo Ethiopian Fine Coffee".

The Initiative helped Ethiopia to differentiate Ethiopian coffees from coffees of other countries, which strengthened the confidence and bargaining position of the coffee growers and exporters of the country. The novelty of the Initiative was that it enabled the growers and producers to become Part of price setters instead of being price takers.

Questions:

(a) *Analyse the reasons why the Government of Ethiopia did not favour CI registration of their speciality coffee and instead favoured to protect its commercial origin. (10 marks)*

(b) *Discuss the initiative of Ethiopian Intellectual Property Office in obtaining trademark registration for Ethiopian coffee brands highlighting the steps taken by it to overcome the difficulties. (5+5=10 marks)*

(c) *How did Starbucks and Ethiopian Government resolve their differences and arrive at a flexible way forward ? Did the move pave the way for growing popularity of its coffee ? (5+5=10 marks)*

(d) *Why did Ethiopian Government initiate a royalty-free licensing scheme ? Did the licensing agreement strategy prove successful ? (5+5=10 marks)*

Answer 1(a)

Specialty coffee in Ethiopia is grown on over four million small plots of land by an estimated 600,000 independent farmers spread throughout the country in remote areas. Although Ethiopian coffees such as Sidamo and Harrar are named after specific regions, all of it is not produced in the same region under the same circumstances. Distribution is also a problem, as it is predominately done informally by hauling bags of coffee on foot for many kilometers. Government oversight of coffee producers is therefore nearly impossible. Farmers would be required to pay a surcharge for government oversight, and this would only be an additional burden on them, many of who are already living below the subsistence level. Therefore the very nature of coffee production in Ethiopia makes GI certification difficult and impractical.

Even, trademark registration doesn't require a specific coffee to be produced in a specific region or have a particular quality in connection with that region. Through this registration, government of Ethiopia could produce huge quantity of different kind of coffees across the country. This kind of mechanism can give government better control and supervisory role on production, distribution of their products in their financial interest by raising revenues and exportation.

Therefore, Government of Ethiopia decided that instead of trying to protect Ethiopian coffee's geographical origin, it would be better to protect its commercial origin, which it would do through registering trademarks.

Answer 1(b)

The EIPO began filing applications to register the names Harrar/Harar, Sidamo and Yirgacheffe as trademarks in key markets. In the United States, Yirgacheffe was the first to obtain registration Sidamo and Harrar/ Harar were granted registration at a later time. Trademarks for Ethiopian coffees are also registered in the European Union and

Canada. In Japan, registration certificates have been secured for two of the coffees (Yirgacheffe and Sidamo). The EIPO has filed applications for trademark registrations of these three coffees in a number of other countries including Australia, Brazil, China, Saudi Arabia and South Africa. There are different actions where EIPO has taken in the form of putting rebuttals against different USPTO decisions with corroborative evidence. In certain cases, Ethiopian government and EIPO plays a constructive role in reaching amicable settlement with regard to distribution, licensing of Ethiopia's coffee designations.

The trademark strategy for Ethiopian coffee faced a major difficulty in 2006. The United States Patent and Trademark Office (USPTO) had approved the application to register Yirgacheffe. But the National Coffee Association (NCA), representing coffee roasters of the United States, objected to the EIPO's applications to trademark first Harrar then Sidamo. The grounds for opposition in both cases were that the names had become too generic a description of coffee, and as such were not eligible for registration under United States trademark law. The USPTO turned down the application for Harrar in 2005 and for Sidamo in 2006.

The EIPO filed rebuttals against the USPTO decisions with supporting evidence to demonstrate that the terms Harrar and Sidamo had acquired distinctiveness.

Answer 1(c)

The Ethiopian Intellectual Property Office (EIPO) filed rebuttals against the USPTO decisions with supporting evidence to demonstrate that the terms Harrar and Sidamo had acquired distinctiveness. Their joint efforts led to an announcement in 2006 that they had reached a mutually satisfactory agreement regarding the distribution, marketing and licensing of Ethiopia's specialty coffee designations, which provided a framework for cooperation to promote recognition of Harrar, Sidamo and Yirgacheffe.

Starbucks agreed to sign voluntary trademark licensing agreements which immediately acknowledge Ethiopia's ownership of the Harrar, Sidamo and Yirgacheffe names, regardless of whether or not a trademark registration has been granted. Legal commentators have honed in on the use of the term "designation" in the agreement as a means of circumventing the obstacle caused by the status of the Harrar and Sidamo applications. The famous dispute between Ethiopian government and Starbucks resulted into increase in the popularity of Ethiopian coffee. With expansion of exportation and financial interest of farmer's cooperative, the prf Yirgacheffe. Furthermore, all stakeholders of Ethiopian coffee starting working aggressively for promotion and brand marketing with the help of UK based company as a result which different brands were identified.

"Yes, in view of the above, it can be said that the move paved the way for growing popularity of its coffee.

Answer 1(d)

The purpose of licensing is "to secure recognition from the coffee distribution industry that Ethiopia owns and controls the use of trademarks, thereby building the reputation and good will of its specialty coffees around the trademarks." The government of Ethiopia wanted its coffee to have more market visibility so that the export premium for Ethiopian specialty coffee could be raised. The adopted strategy offered royalty-free license

agreements and required the licensee to sell the specialty coffees using the registered trademarks (free of charge) on any product that consists wholly of Ethiopian specialty coffees and to promote Ethiopian fine coffee by educating their customers. The licensing strategy is expected to boost consumer recognition of Ethiopian coffee trademarks and facilitate the growth of the demand for Ethiopian fine coffees. This strategy will ensure that Ethiopian farmers and small businessmen secure a reasonable return from the sale of their coffees. Information on the Initiative as well as licensing is made publicly available through a dedicated website.

By mid-2009, almost one hundred license agreements have been concluded with coffee importing, roasting and distributing companies in North America, Europe, Japan and South Africa. Within the country, some forty seven private coffee exporters and three coffee producer cooperative unions in Ethiopia have also signed the agreement. Information on the initiative as well as licensing is publicly available through dedicated website. With the passage of time, more than 100 license agreements were determined with diverse entities having experience in coffee importation, distribution across many countries. With different promotional strategy and brand advertisement have raised the bar and confidence of domestic coffee growers and exporters for better bargaining in the sales.

Yes, in view of this, it can be said that the licensing agreement strategy proved successful.

Question 2

(a) ABC Communications, a telecommunications company, is in the design phase of a new device that incorporates a cellphone, PDA, MP3 player, GPS chip and Internet capabilities. There is a concern that the new device may have nearly the same design as their competitor's product, for which an application for registration of industrial design has already been submitted. A former intern, who is now employed by the competitor, is believed to have leaked information. Can ABC Communication apply for registration of the design of the new device under the Designs Act, 2000 ? Give reasons in support of your answer.

(6 marks)

(b) Radha, a researcher in a pharmaceutical company has discovered a molecule that may have a significant effect in the treatment of melanoma, a type of skin cancer. Research was done in patent databases to verify if any patents have been issued for the chemical compound. The researcher found that in 1993, a patent was sealed in the name of another company for a compound that had the same chemical structure, but it had since expired due to non-payment of renewal fees. She has little experience in dealing with intellectual property rights.

Can Radha make an application for the sealing of the patent in her name under the Patents Act, 1970 ? Give reasons in support of your answer. (6 marks)

Answer 2(a)

A design is capable of being registered only if it is new or original.

Novelty : A design shall be considered to be new when it has not been disclosed to the public, anywhere in India or in any other Country, by publication or by use or in any other way, prior to the filing date or priority date.

A design shall be considered new if it is significantly distinguishable from known designs or combination of known designs. (Section 4 of the Design Act, 2000.)

Originality: Original in relation to a design, means

(i) originating from the author of design,

(ii) includes the cases, which though old in themselves yet are new in their application. (Section2(g))

Section 5 of the Act provides that the Controller may, on the application of any person claiming to be the proprietor of any new or original design not previously published in any country and which is not contrary to public order or morality register the design under the Act. Every application for registration is required to be in the prescribed manner and accompanied by the prescribed fee. A design when registered shall be registered as of the date of the application for registration.

As per Section 7 of the Act, the Controller shall, as soon as may be after the registration of a design, cause publication of the prescribed particulars of the design to be published in the prescribed manner and the design be open to public inspection. Under Section 9 of the Design Act, the Controller grants a certificate of registration to the proprietor of the design when it is registered.

The important purpose of design Registration is to see that the artisan, creator, originator of a design having aesthetic look is not deprived of his bona fide reward by others applying it to their goods.

The company who is not actual creator of design cannot apply for registration of design.

Therefore, going through above provisions of Design Act, ABC Communication can apply for registration of design of new device under the Designs Act, 2002 as competitor has just applied for registration of duplicated design which has not been registered. During examination, when ABC Communication will be asked to clarify status of its design with reference to application filed by competitor, it can submit proof of it's own design be original and new and the competitor has stolen it's design while in stage of development.

Answer 2(b)

The Patent will be in force only so long as the renewal fees prescribed are paid from time to time within the prescribed period or within such extended period as may be prescribed. No renewal fee is payable for a patent of addition while the main Patent is in force. Where a Patent has lapsed due to non-payment of renewal fee, the Patentee may have the Patent restored on following the procedure laid down wider Sections 60 and 61 and Rules 84 to 86. There are certain limitations imposed on a Patent restored.

After the grant of patent, every patentee has to maintain the patent by paying renewal fee every year as prescribed in the schedule I.

For first two years, there is no renewal fee. The renewal fee is payable from 3rd year onwards. In case the renewal fee is not paid the patent will be ceased. To keep a patent in force, renewal fees is payable at the expiration of second year from the date of the

patent or of any succeeding year. In other words renewal fee has to be every year up to the completion of 20 years. Renewal fees can be paid beyond the due date within a period of 6 prescribed fees. If a patent is granted later than two years from the date of filing of the application, the fees which have become due in the meantime may be made within a period of 3 months from the date of recording the patent in the register. This time is also extendable by 6 months as described earlier.

The patentee has choice to pay the renewal fees every year or he can pay in lump sum as well. Further, a request for restoration of patent can be filed within 18 months from the date of cessation of patent along with the prescribed fee. After receipt of the request the matter is notified in the official journal for further processing of the request.

In the given case, Radhika can make application for the sealing of patent in her name under the Patents Act, 1970 as in view of above provisions:

(i) The patent of 1993 has expired due to non-renewal of fees.

(ii) The application for restoration of that patent can not be made as period of 18 months for restoration from the date of cessation has also expired.

Question 3

(a) A British manufacturer of biscuits has been selling cookies in India for more than 20 years, and had a registered trademark 'ChipsMore' for these products during all that time. Two years ago, an Indian company started manufacturing and selling cookies under the brand 'ChipsPlus'.

Can the British manufacturer institute a suit seeking relief for infringement/ passing off under the Trade Marks Act, 1999 ? Give reasons and refer to case law in support of your answer.

(b) ABC Ltd. specializing in the production and distribution of professional sealants for commercial and home use, had registered ownership of its trademark and packaging design for its growing sales of sealants in India. After several years of sales in India, it was alerted by its local distributor about the existence of competing products bearing similar packaging design, but with a different logo, being sold by resellers of hardware products in Chennai and Bengaluru. Advise the company regarding the course of action it should take. Give reasons and refer to case law in support of your answer. (6 marks each)

Answer 3(a)

The given case is similar to *Hindustan Unilever Limited* v. *Ashique Chemicals & Ors [BOM] Notice of Motion No. 926 of 2010 in Suit No. 862 of 2010* S.J. Vazifdar, J. [Decided on 08/08/2011]

Brief facts : The plaintiff seeks a perpetual injunction, restraining the defendants from using, in relation to soaps or detergents, the impugned mark "SunPlus" or the word "Sun" with any prefix or suffix or any other deceptively similar mark or the impugned labels containing the words "Sunplus" or any other deceptively similar labels so as to infringe the plaintiff's registered trademarks or so as to pass off the defendants' goods as and those of the goods of the plaintiff. The plaintiff is the registered proprietor of the words marks "Sun", "Sunlight" and "Sunsilk" under class 3. The marks "Sunlight" and "Sunsilk" are associated with the mark "Sun". The plaintiff is also the registered proprietor

of the label marks, which include prominently the word "Sunlight". The plaintiff has admittedly not used the mark "Sun" in India, but the other marks are associated with the word mark "Sun".

Decision : Suit dismissed.

Reason : The defendant has been using the mark since the year 1997. The defendant has developed a reputation in the market on its own in the State of Kerala. There is nothing to suggest that in the State of Kerala, the mark "Sunlight" had acquired such a reputation that the plaintiff derived advantage merely by trading on the same. The mark "Sun" has not been used for over 60 years. There is a possibility that if the plaintiff's mark had acquired reputation in Kerala, it would have come across the plaintiff's mark which has been widely advertised in a variety of ways, including on television channels, hoardings and in magazines. In that event, the plaintiff would have noticed the defendant mark and adopted proceedings earlier. As it is, the defendants have used the mark for almost fifteen years now. In the result, the plaintiff's action for infringement of the registered mark "Sun" cannot succeed. Nor can the action for passing off in respect of the mark "Sun" succeeds as admittedly it has never been used. The next question is whether this action can succeed in respect of the mark "Sunlight". I do not consider the defendant's mark "Sunplus" to be deceptively similar to the plaintiff's mark "Sunlight". The mere fact that the marks are prefixed by the letters "Sun" would not indicate deceptive similarity. The marks "Sunlight" and "Sunplus" are phonetically and visually distinct. Moreover, the word SunPlus is written in the stylized manner, I have described earlier, reducing the possibility of confusion. Further, in both the marks the suffix is pronounced and distinct from the prefix. Thus, on the one hand, the word "Sun" has not been used for over 60 years and on the other, there is no deceptive similarity between the words "Sunplus" and "Sunlight". Thus, even if inspection had been taken by the defendants of the records of the Registrar of Trade Marks, it would have made no difference.

In the light of the decision of above case, suit filed by British manufacturer seeking relief for infringement/passing off under the Trade Marks Act, 1999 will not succeed as the word Chips is a general word and have no specific relation with British manufacturer.

Answer 3(b)

Infringement, very broadly means taking unfair advantage or being detrimental to the distinctive character or reputation of a trade mark.

Under the Trade Marks Act, 1999 the meaning of infringement has been enlarged as more actions shall be taken as constituting infringement which are listed in Section 29.

Section 29 of the Act dealing with infringement of trade marks explicitly enumerates the grounds which constitute infringement of a registered trade mark. This section lays down that when a registered trade mark is used by a person who is not entitled to use such a trade mark under the law, it constitutes infringement. This section clearly states that a registered trade mark is infringed, if the mark is identical and is used in respect of similar goods or services; or the mark is deceptively similar to the registered trade mark and there is an identity or similarity of the goods or services covered by the trade mark; or the trade mark is identical and is used in relation to identical goods or services; and that such use is likely to cause confusion on the part of the public or is likely to be taken to have an association with the registered trade mark.

In the case of *Brooke Bond India* vs. *C. Patel & Co., 1993 IPLR 220 (Cal.)*, the Court held that application by the defendants of the trade mark Taj Tea in India on the packets of tea is an infringement of the registered trade mark of the plaintiff. Interim injunction was issued even though the defendant was willing to alter the colour scheme and get up of his packets bearing trade mark Taj Tea. In Cox Distillery v. McDowell & Co., 1999 PTC 507, the Court said that there is deceptive similarity between the label used by the plaintiff as his trade mark and the one introduced by the defendant. It amounts to infringement of the plaintiff's trade mark within the meaning of Section 29(1). The defendant was restrained from using COX DIPLOMAT premium Whisky as the defendant used the logo and print of similar size and word DIPLOMAT on label with the printed figure of human being which made his label similar to the registered trade mark of the plaintiff.

Therefore, in the present case considering the facts stated in the question and above mentioned position of law w.r.t. infringement or passing off under the Trade Marks Act,1999, ABC Limited Company can take action under Section 29 of the Act alleging infringement/passing off its registered trademark.

Question 4

(a) Describe the mechanism for registering an industrial design in several countries by means of a single application, filed in one language, with one set of fees. *(6 marks)*

(b) Intellectual property rights are often under-valued, under-managed or under-expoited. Comment. What are the major concepts for the valuation of intangible assets ? *(3+3=6 marks)*

Answer 4(a)

The Hague Agreement regarding the International Deposit of Industrial Designs, also known as the Hague system provides a mechanism for registering an industrial design in several countries by means of a single application, filed in one language, with one set of fees. The system is administered by World Intellectual Property Organisation (WIPO).

The Hague Agreement consists of several separate treaties, the most important of which are: the Hague Agreement of 1925, the London Act of 2 June 1934, the Hague Act of 28 November 1960 (amended by the Stockholm Act), and the Geneva Act of 2 July 1999.

The original version of the Agreement (the 1925 Hague version) is no longer applied, since all states parties signed up to subsequent instruments. The 1934 London Act formally applied between a London act states that did not sign up to Hague and/or Geneva Act in relation with other London act states until October 2016. Since 1st January 2010, however, the application of this Act had already been frozen. The system allows owners of an industrial design to obtain protection in several countries by simply filing one application with the International Bureau of WIPO, in one language, with one set of fees in one currency (Swiss Francs). An international registration produces the same effects in each of the designated countries, as if the design had been registered directly with each national office, unless protection is refused by the national office of that country.

Countries can become a party to the 1960 (Hague) Act, the 1999 (Geneva) Act, or both. If a country signs up to only one Act, then applicants from that country can only use the Hague system to obtain protection for their designs in other countries which are signed up to the same Act. For instance, because the Japan has only signed up to the 1999 (Geneva) Act, applicants which qualify to use the Hague system because their domicile is in the European Union can only get protection in countries which have also signed up to the 1999 Act or to both the 1999 and 1960 Acts.

Answer 4(b)

Intellectual capital is recognized as the most important asset of many of the world's largest and most powerful companies; it is the foundation for the market dominance and continuing profitability of leading corporations. It is often the key objective in mergers and acquisitions and knowledgeable companies are increasingly using licensing routes to transfer these assets to low tax jurisdictions. Nevertheless, the role of intellectual property rights (IPRs) and intangible assets in business is insufficiently understood. Accounting standards are generally not helpful in representing the worth of IPRs in company accounts and IPRs are often under-valued, under-managed or under-exploited. Despite the importance and complexity of IPRs, there is generally little co-ordination between the different professionals dealing with an organization's IPR. For a better understanding of the IPRs of a company, some of the questions to be answered should often be:

- What are the IPRs used in the business?
- What is their value (and hence level of risk)?
- Who owns it (could I sue or could someone sue me)?
- How may it be better exploited (e.g. licensing in or out of technology)?
- At what level do I need to insure the IPR risk?

Valuation is, essentially, a bringing together of the economic concept of value and the legal concept of property. The presence of an asset is a function of its ability to generate a return and the discount rate applied to that return. The cardinal rule of commercial valuation is: the value of something cannot be stated in the abstract; all that can be stated is the value of a thing in a particular place, at a particular time, in particular circumstances

There are four main value concepts, namely, owner value, market value, fair value and tax value.

Major Value Concepts are:

– **Owner Value**

  Owner value often determines the price in negotiated deals and is often led by a proprietor's view of value if he were deprived of the property.

– **Market Value**

  The basis of market value is the assumption that if comparable property has fetched a certain price, then the subject property will realize a price something near to it.

– **Fair value**

Is the desire to be equitable to both parties? It recognizes that the transaction is not in the open market and that vendor and purchaser have been brought together in a legally binding manner

– **Tax value**

There are quasi-concepts of value which impinge upon each of these main areas, namely, investment value, liquidation value, and going concern value.

Further, other concepts includes:

– Cost based valuation

– Market price comparability

– Economic based valuation

Question 5

(a) One of the prime factors contributing to the survival and growth of every business in today's competitive world is the development of intellectual property as an instrument of economic development. Discuss.

What are the major areas in which companies in India can take the lead in the global phenomenon of intellectual property rights ? (3+3=6 marks)

(b) Define the terms 'farmer' and 'farmers variety' under the Protection of Plant Varieties and Farmers' Rights Act, 2001. Explain the rights of the farmers envisaged under the Act briefly referring to relevant provisions. (1+1+4=6 marks)

Answer 5(a)

Though the importance of the subject of Intellectual Property Rights has increased with time, it is still not a global phenomenon. The significance and importance accorded to it differs from one country to the other. Chief factors responsible for this difference are: (a) The amount of resources that different countries allocate and spend towards creation of intellectual assets; and (b) The amount of protected knowledge and information that is used in the process of production. A useful indicator to measure the magnitude of resources devoted towards creation of new knowledge and information is the country's expenditure on research and development activities.

Statistics make it clear that Developing countries tend to spent much less on R&D activities as compared to the Developed countries. In general, one of the major factors responsible for increase in R & D funding is the growing importance and participation of the private sector which has also resulted in an increased reliance on IPR protection by the private players seeking state protection from any encroachment on their intellectual property rights. This is not only beneficial for such private entities but also the State since it helps in creation and dissemination of further knowledge and information in the society. However, it has been observed that such R & D funding by the private players is predominant in developed countries only. The other way in which IPRs influence economic activity in a country is through the use of proprietary knowledge and information — owned by both domestic as well as foreign residents — in both production and

consumption. Data reveals that in countries with relatively low-income generation, the share of agricultural output is comparatively higher than the share of income earned through services. This also suggests that the IPRs, relating to agricultural processes and products, are more important in developing countries than in developed countries.

The major areas in which companies in India can take the lead in the global phenomenon of intellectual property rights are:

Agriculture

Traditionally, the relevance of Intellectual Property Rights in the agricultural research has been very minimal. This is on account of the fact that Intellectual Property Rights were mostly concentrated towards protection of the outcome of industries as against the agriculture per se. Furthermore, most of the Research & Development(R & D) carried out in the agricultural sector was by the public sector institutions in both developed as well as developing countries. For instance, the development and dissemination of the technology which led to the Green Revolution in India did not pose any substantial conflicts around the subject of IPR. Moreover, there is still reluctance in the developing nations to accept grant of Patent in the agriculture sector. In India, since the early 1980s, there has been a significant shift in the national policy towards agricultural research. After having tried and made continuous efforts towards public funding for R&D activities in agriculture, the budgets allocation has been rationalized. At the same time, the participation of the private sector in agricultural R&D has grown by metes and bounds. In the developed nations, about one-half of the agricultural R&D is funded by the private sector.

Copyright protection with regard to the digital content on a worldwide basis

In the 1990s, Copyright protection had gained importance for its role in protecting digital information on the Internet. The protection of digital content is still not a moot point or an issue in the developing countries, where computer and network penetration is much lower as compared to the industrial developed countries. In the early 1998, there were, for example, only 0.2 Internet host per 1000 inhabitants in developing countries compared to 31 in developed countries.

Notwithstanding all this, with a consistent trend towards liberalization of telecommunications services and the plummeting costs of computing and telecommunications technologies, there is an expectation for a sustained growth of the Internet in developing countries as well and thus increased relevance of Copyright protection with regard to the digital content on a worldwide basis.

Answer 5(b)

Section 2(k) of the Protection of Plant Varieties and Farmers' Rights Act, 2001 defines the term "Farmer" as, "farmer" means any person who-

(i) cultivates crops by cultivating the land himself;or

(ii) cultivates crops by directly supervising the cultivation of land through any other person; or

(iii) conserves and preserves, severally or jointly, with any other person any wild species or traditional varieties or adds value to such wild species or traditional varieties through selection and identification of their useful properties.

Section 2 (l) of the Protection of Plant Varieties and Farmers' Rights Act, 2001 defines "Farmers Variety" as, "Farmers Variety" means a variety which-

(i) has been traditionally cultivated and evolved by the farmers in their fields, or

(ii) is a wild relative or land race of a variety about which the farmers possess the common knowledge.

Farmers' Rights

Chapter VI (Section 39 to 46) of the Protection of Plant Varieties and Farmers' Rights Act, 2001 deals with the rights of the farmers. They are as under:

Section 39 - Farmers rights

(i) A farmer who has bred or developed a new variety shall be entitled for registration and other protection in like manner as a breeder of a variety under this Act;

(ii) The farmers' variety shall be entitled for registration if the application contains declaration as specified in clause (A) of sub-section (1) of section18;

(iii) A farmer who is engaged in the conservation of genetic resources of land races and wild relatives of economic plants and their improvement through selection and preservation shall be entitled in the prescribed manner for recognition and reward from the Gene Fund: Provided that material so selected and preserved has been used as donors of genes in varieties registrable under this Act;

(iv) A farmer shall be deemed to be entitled to save, use, sow, re-sow, exchange, share or sell his farm produce including seed of a variety protected under this Act in the same manner as he was entitled before the coming into force of this Act: Provided that the farmer shall not be entitled to sell branded seed of a variety protected under this Act.

Section 40 - Certain information to be given in application for registration

A breeder or other person making application for registration of any variety under Chapter III shall disclose in the application the information regarding the use of genetic material conserved by any tribal or rural families in the breeding or development of such variety

Section 41 - Rights of communities

Any person or group of persons (whether actively engaged in farming or not) or any governmental or non-governmental organisation may, on behalf of any village or local community in India, file in any center notified, with the previous approval of the Central Government, by the Authority, in the Official Gazette, any claim attributable to the contribution of the people of that village or local community, as the case may be, in the evolution of any variety for the purpose of staking a claim on behalf of such village or local community.

Section 42 - Protection of innocent infringement

A right established under this Act shall not be deemed to be infringed by a farmer who at the time of such infringement was not aware of the existence of such right; and

A relief which a court may grant in any suit for infringement referred to in section 65 shall not be granted by such court, nor any cognizance of any offence under this Act shall be taken, for such infringement by any court against a fanner who proves, before such court, that at the time of the infringement he was not aware of the existence of the right so infringed.

Section 43 - Authorisation of farmers' variety

Where an essentially derived variety is derived from a farmers' variety, the authorisation under sub-section (2) of section 28 shall not be given by the breeder of such farmers' variety except with the consent of the farmers or group of farmers or community of farmers who have made contribution in the preservation or development of such variety.

Section 44 - Exemption from fees

A farmer or group of farmers or village community shall not be liable to pay any fees in any proceeding before the Authority or Registrar or the Tribunal or the High Court under this Act or the rules made thereunder.

Section 45 - Gene Fund

The Central Government shall constitute a Fund to be called the National Gene Fund for welfare of famers.

Section 46 - Framing of schemes, etc.

The Central Government shall, for the purposes of section 41 and clause (d) of sub-section (2) of section 45, frame, by notification in the Official Gazette, one or more schemes.

Question 6

(a) The protection of trade secrets and undisclosed information is attracting a lot of attention throughout the world for obvious reasons. As the situation stands, trade secrets are not registerd like other intellectual property rights and are also not creatures of statutes. The judicial system of each country determines the requirements for ensuring trade secrets protection.

A survey conducted by the American Society for Industrial Security (ASIS) on intellectual property loss by Fortune 1000 compaies and the 300 fastest growing companies in the US reveals that $44 billion were lost due to known and suspected intellectual property losses during a 17-month period in 1996-1997. And the sum of $44 billion was calculated on the basis of the response of only 12% of the survey participants. At the interational level, Trade Related Aspects of Intellectual Property Systems (TRIPS) Agreement protects trade secrets in the from of undisclosed information.

In the right of the above, highlight :

(i) The role of international institutions for the international protection of trade secrets.

(ii) The status of protection of trade secrets in India. (3+3 marks)

(b) One Unnithan conceived an idea of a reality TV Show SWAYAMWAR concerning match making. He shared the concept note with a film maker Ramesh Chandra.

To his surprise and shock, he came across a newspaper report about Ramesh Chandra planning to come out with a big basket match-making show using his concept.

Has there been a violation of an intellectual property right ? Can Unnithan institute a suit seeking injunction ?

Give reasons and refer to case law, if any. *(6 marks)*

Answer 6(a)

(i) Trade Secrets have been provided protection by a large number of agreements and countries throughout the world as well as various International Institutions. For e.g.: -

NAFTA

Member countries must protect trade secrets from unauthorized acquisition, disclosure or use. Remedies must include injunctive relief and damages. In response to NAFTA, Mexico has amended its 1991 trade secrets law to permit private litigants to obtain injunctive relief.

GATT

On April 15, 1994, the major industrialized nations of the world, including the United States, concluded the Final Act resulting from the Uruguay Round of GATT (General Agreement on Tariffs and Trade). GATT established the World Trade Organization (WTO) and promulgated various trade-related agreements including TRIPS or the Trade-Related Aspects of Intellectual Property Rights. Under GATT, "undisclosed information" must be protected against use by others without the consent of the owner if the use is contrary to honest commercial practices. Also, there is third-party liability for misappropriation if third parties knew or were grossly negligent in not knowing that such information had been obtained dishonestly.

TRIPS

The TRIPS makes it obligatory on member states to ensure Protection of Undisclosed Information under Article 39 of the Agreement.

The TRIPS Agreement under Article 39 protects trade secrets in the form of "undisclosed information", and provides a uniform mechanism for the international protection of trade secrets. Such information must be a secret, i.e. not generally known or readily accessible to person within the circles that normally deal with all kinds of information in question. Also, the information must have commercial value because it is secret and the information must be subject to reasonable steps by its owners to keep it secret.

The TRIPS Agreement also requires member countries to provide effective remedies for trade secret misappropriation including (a) injunctive relief (b) damages and (c) provisional relief to prevent infringement and to preserve evidence.

(ii) Trade Secrets seems to be a neglected field in India, as there is no enactment or policy framework for the protection of trade secrets. This form of intellectual property is a new entrant in India, but is nevertheless a very important field of

IP. Protection of trade secrets is a very important and one of the most challenging tasks for the Indian government as this will enhance the foreign investment in India giving a boost to the Indian economy. So a proper policy for the protection of trade secrets in India is the need of the hour in order to provide a sense of security among the foreign investors and the local businessmen regarding their trade secrets which will further boost the Indian economy.

As mentioned above, in India, no substantive authoritative separate statute to deal with trade secrets. Even very few case laws are available to determine the nature or ambit of trade secrets.

The legislations which are having a connection with the trade secrets can be summed up as:

1. Copyright Act, 1957[Section 51, 55 and 63]
2. The Designs Act, 2000
3. The Information Technology Act, 2000[Section 65, 72]
4. Indian Penal Code [Section 408, 415]
5. The Indian Contract Act [Section 27]
6. The Competition Act, 2002 [Section 3]
7. Civil Procedure Code
8. Criminal Procedure Code

Since India is a signatory to the Paris Convention, it is relevant to mention that Article 1(2) of the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs) states that intellectual property shall include protection of undisclosed information. Further, Article 39 of TRIPs states concerns ensuring effective protection against unfair competition as provided in Article 10bis of the Paris Convention, with respect to trade secrets.

On May 12 2016 India approved the National IP Rights Policy, which has seven objectives. One of these objectives is to ensure an effective legal and legislative framework for the protection of IP rights. The steps to be taken towards achieving this objective include the identification of important areas of study and research for future policy development; one such area identified was the protection of trade secrets.

Answer 6(b)

The facts given in the question are similar to the case *G. Anand* vs. *Delux Films and Ors. AIR 1978 SC 1613* in which the Appellant R. G. Anand wrote and produced a play called 'Hum Hindustani' in 1953 which received huge success and was re-staged numerous times. Appellant narrated the entire play 'Hum Hindustani' to the Respondents. Appellant had elaborate discussions regarding filming the play in January, 1955. However, no further communication was made to the Appellant post the discussion. However the respondents proceeded to make the film and appellant filed a suit claiming copyright infringement. The Hon'ble Supreme Court held that there exists no copyright in relation

to an idea, subject matter, themes, plots or historical or legendary facts. Infringement is restricted only to the form, manner, arrangement and expression of the idea by the author of the copyright work. The Court should settle on whether the similarities are substantial or fundamental in nature or not with respect to the mode of expression adopted in the work. If substantial or fundamental portion has been copied, then it would amount as infringement. The other reliable test to ascertain whether there is an infringement or not is to analyse the impression created on the spectator or reader subsequent to reading or watching the works (Lay Observer Test)

Unlike the case with patents, copyright protects the expressions and not the ideas. There is no copyright in an idea. In *M/s Mishra Bandhu Karyalaya & Others* v. S*hivaratanlal Koshal AIR 1970 MP 261*, it has been held that the laws of copyright do not protect ideas, but they deal with the particular expression of ideas. It is always possible to arrive at the same result from independent sources. The rule appears to be settled that the compiler of a work in which absolute originality is of necessary excluded is entitled, without exposing himself to a charge of piracy, to make use of preceding works upon the subject, where he bestows such mental labour upon what he has taken, and subjects it to such revision and correction as to produce an original result.

Mr. Anil Gupta and Anr. v. *Mr. Kunal Dasgupta and Ors 13 [97(2002) DLT 257]*, the Delhi High Court was encountered with a case related to "concept note". The allegation of the Plaintiff was that he had narrated a concept of "Swyaamwar" for a reality show in while a bride will choose her groom in traditional manner in form of a Swyaamwar. The idea was narrated to the Defendant. The Defendant after a few months launched his own TV reality show, "Shubh Vivah" based on the concept of the Plaintiff, shared to him in confidence. Justice Vijender Jain of Hon'ble Delhi High Court relied on the judgement of Terrapin v Builders Supply Co (Hayes) to evoke the doctrine of confidentiality and found force in the argument and thereby restrained the Defendants and granted injunction in favour of the Plaintiff.

Therefore, in the given case, as it is simply an idea, which is not protected by law of copyrights. Simple idea is not an intellectual property right as stated in above case laws. Therefore, there is no violation of intellectual property right and Unnithan institute cannot file a suit seeking injunction.

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FORENSIC AUDIT
(Elective Paper 9.4)

Time allowed : 3 hours *Maximum marks : 100*

NOTE : *1. Answer ALL Questions.*

2. Suitable assumptions, if considered necessary, may be made while answering a question. However, such assumptions must be stated clearly.

Question 1

Case Study :

Loan against gold jewellery is considered safe and secure. Many banks have started financing against the gold jewellery to their customers. They have also empanelled some jewellers of repute to assess the purity and weight of the gold ornaments so as to judge the quantum of advances to be made to the borrowers. Based on the experiences of other banks, the Prime Mercantile Bank Ltd., also started financing against the gold jewellery. It's Board framed a policy for financing against the gold jewellery which inter-alia contains the eligibility criteria of empanelment of goldsmiths to assess the weight and purity of the gold content in the jewellery, identification of the borrower, maximum amount that can be given to a borrower and repayment period, measures of recovery in case of default of the borrower and other related issues.

At one of the small town branch in Rajasthan, a Branch Manager (BM) named A, was posted and he is known in his fraternity bankers, as aggressive marketer and booster of branch business. After A's joining at Rajathan branch the advances portfolio witnessed rapid rise from ₹50 lakh as of 31st March, 2018 to Rs 125 lakh as at 31st December, 2018. The incremental advances figure consists of 90% of loan against jewellery. This success story of A was shared by his Regional Manager among other Branch Managers.

After the close of the financial year of 31st March 2019, the inspection department of the bank carried out the branch inspection and noted many irregularities, specifically in the portfolio of loan against jewellery, which includes the mounting NPA, major exposure in jewellery loan in the name of a particular borrower, non-verification/non-existence of the KYC documents of the borrowers, impurity in the gold held as collateral, poor analysis report of the gold by the empanelled Goldsmith, etc.

Later it also came into the light that the Branch Manager had a close proximity with the empanelled Goldsmith. This Goldsmith tried to escape as and when approached by the inspecting team to ask some queries. The inspecting team was surprised, how in a small town, the loan against jewellery portfolio increased tremendously in a very short period of time. In the close vicinity of the branch, the crime relating to gold snatching, theft and burglary of the jewellery items increased tremendously as per news published in the local newspapers and crime reporting data of the police to the collector.

The Vigilance team of the central office of the bank was also smelling something wrong and was anxious to unearth fraud, if any, and approached you to carry out forensic audit/ investigation.

Based on the above facts, answer the following :

(a) As a Forensic Auditor, what strategy you will adopt to carry out the audit and investigation ?

(b) During the course of the forensic audit, you came to know that there was nexus between the empanelled Goldsmith and the Branch Manager. Further the burglary in that small area was on also on rise. How you will see these facts while carrying out the forensic audit and inspection.

(c) Disucss the provisions of Indian Penal Code, 1860 and evaluate if the Branch Manager and Goldsmith be treated guilty under such act.

(d) What can be the modus-operandi of the Branch Manager in the instant case ?

(10 marks each)

Answer 1(a)

The following strategy shall be followed by the Forensic Auditor to carry out the audit and investigation:

Policy : Obtain the Policy of Loan against Gold Ornaments framed by the Bank and study the same in order to find out the identification of borrower, quantum of the loan to be given, follow-up of the loan, tenure of the loan, recovery measures to be taken in case of non-liquidation of the loan account.

Empanelment of the Goldsmith

Find out the process of empanelment of the goldsmiths (to access the weight and purity of the gold content of the jewellery etc.) by the bank branch.

- Whether it was duly approved by the Corporate Office of the Bank?
- Whether the due diligence process was done?
- Whether KYC documents of the empanelled goldsmiths was obtained?
- Whether previous back ground of the goldsmiths was assessed?
- The business turnover and network of the goldsmiths, whether assessed by the branch manager, before forwarding the papers for approval to the Corporate Office.
- Whether they empanelled with any other Banks, if yes, feedback from those banks.

Identification and follow-up from the Borrower:

- Whether loan was given to the existing customer of the bank?
- Whether KYC documents have been obtained?
- Whether the quantum of the loan given per borrower was followed?

Examination of the loan Documents:

- Whether the documents executed by the borrower were proper?
- Whether the sanction and disbursement of the loan was within the delegation authority of the sanctioning authority and has been duly signed by the concerned official?
- Whether the loan amount was directly credited in the savings account of the borrower?
- Whether the loan was given to non-existing customer and cash disbursement was made?

Pre and post disbursal visit of the Borrower's address : Check whether the branch manager/officials have followed the Bank's Policy to have pre and post disbursal visit of the borrower's address and due diligence approach has been made?

Legal action in case of non-payment of the loan : Check whether the branch manager has initiated legal action in non-performing accounts?

Public News/ Police Report : Check whether the gold ornaments pledged with the bank branch belongs to borrower ensuring the proof of the ownership of such ornaments by receipts etc. Whether the branch manager has ensured that the gold ornaments pledged with the bank branch is not of stolen ornaments by a police verification / FIR?

Answer 1(b)

The forensic auditor should adhere the following points while carrying out the forensic audit and investigation in cases wherein the forensic auditor came to know about the nexus between the empanelled goldsmiths and the branch manager and in cases wherein observed about the rise in burglary cases in small area:

- Check the names and address of the borrowers, with KYC documents.
- Whether KYC documents are in order and are not fabricated?
- Whether the KYC documents bear the stamp and signature of 'Original seen and verified' and bears the signature of the authorized concerned official?
- Whether In-person verification has been carried out by Banker (In-person verification is a mandatory requirement stipulated by RBI/SEBI.
- Check whether the loan amount is within the limit of per borrower.
- Check whether the customers are suo-motto approaching the branch or they are being referred by the empanelled gold smith.
- Check the savings/ current account of the gold smith in order to verify the deposits made and withdrawn by the gold smith.
- Gather information from the informal sources, branch officials, general public/ villagers, about the integrity of the branch manager and the gold smith.
- Check whether there is any possibility of availing loan by the unscrupulous persons on the stolen ornaments and check the KYC documents.
- There may be the possibility that the KYC documents of genuine persons might

have been submitted and loan has been availed, while the beneficiary may be other culprit / persons.

- There may be a possibility that the gold smith may be engaged in purchasing the stolen ornaments and may be taking loan in the name of genuine persons, but the beneficiaries may be the thieves / culprits.
- Send letter to each of the borrower at their given addresses as a thank you note for availing finance from the bank branch. If any of the borrowers has actually not availed the loan, he may raise his objections.
- Also scrutinise the savings account the branch manager to identify the credit entries in cash, if any, other than from authentic sources, whether it is the bribe / commission deposited in the account.
- Obtain the name list of the family members of the branch manager and to check their account. There may be the possibility that the bribe money earned by the branch manager might have been deposited by him in such accounts.
- Verify the reports of theft (burglary), snatching, criminal breach of trust or criminal misappropriation of property cases registered in the local police station.

Answer 1(c)

Indian Penal Code, 1860 'IPC'

Section 168 of the IPC - Public servant unlawfully engaging in trade: "Whoever, being a public servant, and being legally bound as such public servant not to engage in trade, engages in trade, shall be punished with simple imprisonment for a term which may extend to one year, or with fine, or with both."

Section 171 B - Bribery, read with Section 7 of the IPC Act "Whoever commits the offence of bribery shall be punished with imprisonment of either description for a term which may extend to one year, or with fine, or with both. Provided that bribery by treating shall be punished with fine only" as per Section 171E.

Section 403 - Dishonest Misappropriation of property.

Section 405 - Criminal Breach of Trust: "Whoever commits criminal breach of trust shall be punished with imprisonment of either description for a term which may extend to three years, or with fine, or with both" according to Section 406.

Section 409 - Criminal breach of trust by public servant, or by banker or merchant or agent

Section 413 - Habitually dealing with stolen property

Section 415 read with Section 417 – Cheating

Section 463 read with section 465 - Forgery "Whoever commits forgery shall be punished with imprisonment of either description for a term which may extend to two years, or with fine or with both" Penalties under Prevention of Money Laundering Act, 2002.

Section 477A - Falsification of Accounts

Penalties under Prevention of Money Laundering Act, 2002

Section 3 - Offence of money-Laundering - Whosoever directly or indirectly attempts to indulge or knowingly assists or knowingly is a party or is actually involved in any process or activity connected proceeds of crime including its concealment, possession, acquisition or use and projecting or claiming it as untainted property shall be guilty of offence of money-laundering.

Section 4 - Punishment for money-laundering. - Whoever commits the offence of money-laundering shall be punishable with rigorous imprisonment for a term which shall not be less than three years but which may extend to seven years and shall also be liable to fine which may extend to five lakh rupees.

Based on above provisions both the Branch Manager and Goldsmith be charged guilty under Indian Penal code, 1860 and Money Laundering Act, 2002.

Answer 1(d)

The modus-operandi of the branch manager, in the instant case, may be as under:

- Establish a rapport with the goldsmiths to procure more customers into the branch eventually resulting in more business for the branch and appreciation for branch manager.
- Offer of commission (apart from the bank's commission) to the goldsmiths by the branch manager.
- Indulge in the unethically solicitation of the business by hiding the purity and quality of the gold and obtaining of the incorrect report from the goldsmiths.
- Asking goldsmith to obtain KYC documents from the customers who purchases gold from his shop, so that the same KYC documents may be used to raise loan in the name of authentic borrowers, but beneficiary may be unscrupulous persons.
- There may be the possibility that the prospective gold loan borrowers may come in branch carrying with sub-standard quality of the gold ornament and the report may be fabricated by the goldsmiths to hide the actual purity report on the basis of some exchange of the commission.

Question 2

(a) Sarla Textiles Ltd. (ST) was enjoying a cash credit (CC) limit of ₹20 lakh with XYZ bank. Initially this CC limit was of ₹1 lakh only during the financial year 2014-15. However, on account of the continuous sale rise and integrity of the proprietor the limit was gradually increased on an annual basis. Meanwhile Branch Managers were also changed and the incoming Branch Manager, never visited the business premises of ST.

Proprietor of ST actually diverted his business from cloth to construction, and shop activity was closed. However, the owner of ST fabricated the figures and was regularly submitting the stock statement and the annual accounts to the bank, reflecting the increased turnover and profit figures and was regular to deposit the interest amount in the account.

In June 2019, a new manager was appointed at the branch. The CC limit of the ST was also due for its renewal, however, the Branch Manager was reluctant to renew the papers only on the basis of the financial papers and insisted for the spot verification and on the basis of the address recorded in the books of the branch, visited the addresss. Branch Manager did not found shop at the aforementioned address. Branch Manager also enquired about the whereabouts of the ST from neighbourhood, but he was informed that they have not seen the owner and that such shop was shut several years ago.

The Branch Manager lodged FIR against the proprietor about the absconding of the borrower and sought further instructions form the Regional Officer of the Bank.

(i) Based on the above facts, explain what went wrong in this case ? (4 marks)

(ii) Whether the action of the new Branch Manager in renewing the limits only after making the field visit, was justified ? (2 marks)

(b) Regional office for ABC Bank have been receiving several complaints against a branch in Delhi and has reasons to believe that balance sheet of such branch was manipulated by window dressing including inflated branch expenses and that manager's integrity is doubtful. Also several cases of mis-selling of insurance policies were reported from the branch customers. You have been appointed as Forensic auditor by the regional office, explain what procedures would you consider while conducting a forensic audit of such bank branch. (6 marks)

Answer 2(a)(i)

Based on Investigation performed by the Forensic auditor, the below facts came into light and possibly went wrong from bank's perspective:

- The bank officials failed to perform field visit which was essential at the time of sanction and disbursal of the loan.
- At the time of every renewal and during the intervening intervals, the bank officials failed to invariably visit the business place of the borrower.
- KYC documents were not obtained from borrower and were not placed on records.
- The limit is renewed, based on the sales projections and financial figures and security, including the Prime and Collaterals. In this case, the branch accepts the hypothecation of the goods did not insisted to submit the collateral viz: personal guarantee of other persons.
- The stock statements, which were periodically submitted by the Sarla Textiles Limited (ST), were not scrutinised thoroughly.
- Similarly, the financial records were not thoroughly scrutinised and the branch officials failed to obtain a copy of GST and Income Tax Return to justify the sales and profits as supplementary evidences.

Answer 2(a)(ii)

It seems that, the previous managers have not assessed the limit requirements, nor done the field visits and insisted the collaterals. The actions performed by present branch manager are justified and he has followed the right set of protocols by not renewing

the limits before satisfying himself of borrower records and by performing the field visit, he has been able to unearth the fraud perpetrated by the borrower in connivance of the earlier branch officials.

Answer 2(b)

The below procedures shall be considered while conducting the forensic audit work and reporting to regional office:

Window Dressing Aspect:

- Take in to account the figures of the deposits and advances, just one month before the closing date and perform due-diligence to ensure these are not fake receipts.
- Check whether on or near the closing date, the cash credit limit holders account has been fully utilised to increase the advances portfolio. Whether the amount has been transferred to the respective savings / current account holders to increase the liability side of the balance sheet of the branch. This is called the window dressing.
- Also check whether after the date of closing the amount so debited in the CC accounts has again been credited. This is called the reversal of the window dressing done on the date of closing.
- Use data-analytics techniques to identify unique patterns or if there is any unusual activity in deposits or borrowing that may indicate fraud.
- Also check on possible nexus between the fraudster and the previous Branch Managers. Disk imaging of previous managers to identify suspected mail exchanges.

Branch Expenses :

- Compare the branch expenses figures (other than the operational expenses of interest payment) from YoY / Quarter to Quarter.
- The expenses may be relating to the branch maintenance, repairs and renewals, entertainment expenses, customer meeting expenses, stationery expenses etc. Whether these expenses have been done under the branch manager's delegated authority or the prior-approval has been obtained for it?
- Whether the expenses have been judiciously expended, even though they are within the delegated authority and as per bank's policy?
- Large value expenses shall be evaluated for possible fraud.
- Use of data-analytics shall be made to identify if there are exceptional expenses which shall be reported in the audit along with the supporting evidence.

Insurance Business:

- Examine the KYC records for customers who have purchased the insurance policy from the branch.
- Whether they have been made aware about the terms and conditions of the insurance policy and that premium calculation is correct?

- Collect the data from the branch, the name of the official, who has sold the policy. Also, ensure that policy documents are sent to customers on a timely basis.
- Whether the policy holder is paying the policy premium on a timely basis?
- Perform random checks to ensure that the existing policy holders are satisfied with the policy and branch officials.

Manager's Integrity:

- Ascertain from the past records for the Branch manager and assess whether any disciplinary action is pending.
- Evaluate the living standard of the branch manager and check whether the same in sync with the income, extra sources of income like rent, farm production etc.
- Perform enquiries from other employees in the branch and ascertain if there is any unusual behaviour identified by the branch manager.
- Check the personal accounts of the branch manager and family members of the branch manager to ascertain the un-due credit in excess of his income level.

Question 3

(a) During the course of the assessment of M/s Chandni Enterprises (a Proprietorship firm), the Income tax officer, observed that the assessee has shown some credit entries (aggregating to ₹40 lakh) in his books of accounts. Explanations were called from the assessee, he informed that this amount has been borrowed from some his customers, but their address are not available. The parties who have given such advances to the firm occasionally visits the shop and demand for the interest amount only keeping the principal amount intact. The proprietor has shown such entries in the books of accounts relating to the interest payment (by way of cash payments below ₹10,000). On being interrogated by the assessing officer to submit the proof of deposit, addresses of the depositors and other details, the proprietor could not justify.

The assessing officer, thereafter, treating all the credit as income of the previous year and issued demand notice mentioning there in the amount of income tax, delayed interest, penalty for hiding of income.

Based on the above facts, evaluate and explain whether the action of the assessing officer is justfied ? (6 marks)

(b) BGI Ltd. came out with an Initial Public Offering (IPO) during the period of 11th July, 2019 to 14th July, 2019.

In the prospectus the company had disclosed nine objects of the IPO on which total expenses were estimated at ₹55.53 crore. After the collection of the IPO money and allotment of shares, the company informed the Stock Exchange on 14th November, 2019 that the IPO proceedings had been utilized as per the object of the issue. The SEBI, however found that the said funds were not utilized as mentioned in the prospectus and carried out the detailed investigations. The SEBI investigating official submitted the report of details of the amount raised and utilised which as as under :

(₹ in Crore)

Category	*To be utilised as per the prospectus*	*Utilized as per the company*	*Utilized as per the investigating official of the SEBI*
1. Setting up its owned corporate office at Noida	*3.960*	*0.410*	*0.410*
2. Relocation of branch office at Mumbai	*5.936*	*4.024*	*1.524*
3. Up-gradation of Digital post production studio	*13.655*	*9.389*	*0.000*
4. Investment in IT division	*8.392*	*3.910*	*0.4000*
5. Expansion of R & D Technology	*6.567*	*4.321*	*0.035*
6. Repayment of bank borrowing	*2.697*	*2.931*	*2.931*
7. Working capital requirement	*5.050*	*4.9106*	*2.396*
8. General Corporate expenditure	*6.500*	*2.115*	*0.855*
9. Meeting the issue expenditure	*2.774*	*2.690*	*2.690*
Total	*55.53*	*34.70*	*11.241*

The investigating official further observed various irregularities as detailed below:

(i) Wrong disclosure regarding the vendor's details and non-disclosures of new vendors and payment.

(ii) Non-disclosure of purchase of office space at Kolkata and respective payments made to the sellers in this regard.

(iii) Wrong disclosure regarding purchase order placed for the equipment.

(iv) Investments in contradiction with prospectus.

(v) Diversion of funds to promoters and promoter related entities.

(vi) Diversion of IPO proceeds to traders. It was alleged that an amount of

₹10.53 crore of the IPO proceeds had reached two groups immediately after the receipt of the same by company either directly or indirectly which was used by these two groups in trading of the script of the company on the listing day itself.

(vii) Failure by Audit Committee – The Audit Committee of the company failed to notice this fund diversion. It did not record anything in its minutes of the meeting and did not make any recommendations to the company.

Based on the above facts, assess whether mentioning of wrong information/ hiding of material information in the prospectus is an offence under the Companies Act, 2013 and what are the penal consequences of such act ?

(6 marks)

Answer 3(a)

Cash Credits [Section 68] : As per the provision of Section 68 of the Income-tax Act, 1961, any sum found credited in the books of account of an assessee maintained for any previous year, and the assessee offers no explanation about the nature and source thereof or the explanation offered by him is not, in the opinion of the Assessing Officer, satisfactory, the sum so credited may be charged to Income-tax as the income of the assessee of that previous year.

Unexplained Money [Section 69A] : Moreover as per the provision of Section 69A of the Income-tax Act, 1961, where, in any financial year, the assessee is found to be the owner of any money, bullion, jewellery or other valuable article and such money, bullion, jewellery or the valuable article is not recorded in the books of account, if any, maintained by him for any source of income, and the assessee offers no explanation about the nature and source of acquisition of the money, bullion, jewellery or other valuable article, or the explanation offered by him is not, in the opinion of the Assessing Officer, satisfactory, the money and the value of the bullion, jewellery or other valuable article may be deemed to be the income of the assessee for that financial year.

Amount of Investments, etc., not fully disclosed in Books of Account [Section 69]:

As per the provision of Section 69 of the Income-tax Act,1961, where, in any financial year, the assessee has made investments or is found to be the owner of any bullion, jewellery or other valuable article, and the Assessing Officer finds that the amount expended on making such investments or in acquiring such bullion, jewellery or other valuable article exceeds the amount recorded in this behalf in the books of account maintained by the assessee for any source of income, and the assessee offers no explanation about such excess amount, or the explanation offered by him is not, in the opinion of the Assessing Officer, satisfactory, the excess amount may be deemed to be the income of the assessee for that financial year.

Based on the above points, the action of the assessing officer of treating the credit as deemed Income of the assessee and issue of demand notice seems justified as the assessee could not submit the proof of deposit, addresses of the depositors and other details or could not justify.

Answer 3(b)

Criminal Liability

Section 34 of the Companies Act, 2013 states that where a prospectus, issued, circulated or distributed under this Chapter, includes any statement which is untrue or misleading in form or context in which it is included or where any inclusion or omission of any matter is likely to mislead, every person who authorizes the issue of such prospectus shall be liable under section 447.

Provided that nothing in this section shall apply to a person if he proves that such statement or omission was immaterial or that he had reasonable grounds to believe, and did up to the time of issue of the prospectus believe, that the statement was true or the inclusion or omission was necessary.

Civil Liability

Section 35 of the Companies Act, 2013 states that:

Where a person has subscribed for securities of a company acting on any statement included, or the inclusion or omission of any matter, in the prospectus which is misleading and has sustained any loss or damage as a consequence thereof, the company and every person who-

(a) is a director of the company at the time of the issue of the prospectus; has authorised himself to be named and is named in the prospectus as a director of the company, or has agreed to become such director, either immediately or after an interval of time;

(b) is a promoter of the company; has authorised the issue of the prospectus; and is an expert referred to in sub-section (5) of section 26,

shall, without prejudice to any punishment to which any person may be liable under section 36, be liable to pay compensation to every person who has sustained such loss or damage.

Punishment for Fraud

Section 447 of the Companies Act, 2013 states that "Without prejudice to any liability including repayment of any debt under this Act or any other law for the time being in force, any person who is found to be guilty of fraud involving an amount of at least Rs. 10 lakh or one percent of the turnover of the company, whichever is lower] shall be punishable with imprisonment for a term which shall not be less than six months but which may extend to ten years and shall also be liable to fine which shall not be less than the amount involved in the fraud, but which may extend to three times the amount involved in the fraud:

Provided that where the fraud in question involves public interest, the term of imprisonment shall not be less than three years."

Provided further that where the fraud involves an amount less than [10 lakh or 1% of the turnover of the company, whichever is lower, and does not involve public interest, any person guilty of such fraud shall be punishable with imprisonment for a term which may extend to 5 years or with fine which may extend to Rs.50 lakh or with both.

Question 4

(a) You received an email from the Income Tax Dept., mentioning the following :

> *Dear Taxpayer,*
>
> *You have filed your income tax return for the Assessment Year 2019- 20 and a refund of ₹14,600 is payable to you. However, the account mentioned by you is incorrect and requires validation. Please visit the following link in order to validate your account. http:/jncometaxindiafiling.jov.com*
>
> *Note : Failure to validate your account number will lead to rejection of refund.*
>
> *Regards*
>
> *Team : Income Tax Department*
>
> *Pay tax honestly and contribute in Nation's Development.*

What you will do such a situation and what it is called in Cyber terminology ?

(b) What do you understand by data extraction ? List out few advantages of data extraction tools. (6 marks each)

Answer 4(a)

This is a fake e-mail and the link shall not be clicked and website shall not be opened. The actual URL of the Income tax is as under:

https://www.incometaxindiaefiling.gov.in, while the URL as mentioned in the questions is http:/jncometaxindiafiling.jov.com.

So, if the e-mail is carefully read the following would be observed:

Actual URL	*Fake URL*
https://www.incometaxindiaefiling.gov.in	http:/jncometaxindiafiling.jov.com.
The spelling of the Income tax start with "i"	The spelling of the Income tax start with "j"
The government website always mentioned "gov.in" and not "jov.in"	
The word "e" is missing before the word 'filing'	

It is called as Phishing.

Phishing is just one of the many frauds on the Internet, Phishing trying to fool people into parting with their money. Phishing refers to the receipt of unsolicited e-mails by customers of financial institutions, requesting them to enter their username, password or other personal information to access their account for some reason. Customers are directed to a fraudulent replica of the original institution's website when they click on the links on the e-mail to enter their information, and so they remain unaware that the fraud has occurred. The hacker then has access to the customer's online bank account and to the funds contained in that account.

The incident shall be informed to the police to register a case under the relevant provisions of IT Act, 2000.

Answer 4(b)

Data extraction is the act or process of retrieving data out of (usually unstructured or poorly structured) data sources for further data processing or data storage (data migration). The import into the intermediate extracting system is thus usually followed by data transformation and possibly the addition of metadata prior to export to another stage in the data workflow.

Advantages of using data extraction tool are as under:

- Use of data extraction tools reduces manual process and repeated tasks requirements and helps in improving the accuracy of the extracted data.
- Data extraction tools quickly extract large data sets within short time, thereby help in saving time and allow focusing on other core tasks.
- With appropriate tools in place employees now spend more time on tasks that add value to business and hence their overall productivity is drastically improved.
- Data extraction tools provide full visibility of all the records and makes management of stored data easy.
- By automating time consuming tasks companies now do not need to hire extra staff and hence save on overhead costs considerably.

Question 5

(a) ICSI Anti-Bribery Code is a voluntary code. What are the various clauses of this code ? (6 marks)

(b) Under what circumstances, investigation into the affairs of a company is assigned to SFIO "Serious Fund Investigation Office" by the Government ? (4 marks)

Who shall be comprised in the SFIO committee and to whom shall SFIO report be submitted ? (2 marks)

Answer 5(a)

ICSI had recommended the 'Corporate Anti-Bribery Code to be adopted voluntarily by the private sector, tacking the supply side of bribery in this sector. The Code is a document with 9 clauses for implementation and guideline instructions including model policies on Gift, Hospitality and Expenses, Purchase Procurement Policy and Guidelines for whistle-blower mechanism.

The Code, once adopted by the Company, shall be applicable to the company and its:

- Board of Directors,
- Employees (full time or part-time or employed through any third party contract)
- Agents, Associates, Consultants, Advisors, Representatives and Intermediaries, and
- Contractors, Sub-contractors and Suppliers of goods and/or services.

The Code outlines a systematic approach for the corporate entity to prevent bribery and counter 'Facilitation Payments', including third party gratification.

Clause 1 - Adherence to Anti-Corruption Laws: The Company shall follow all anti-corruption laws applicable in India.

Clause 2 - Bribery in Private Sector: The Company or its employees, directors, agents, associates, consultants, advisors, representatives or intermediaries shall not involve in bribery.

Clause 3 - Facilitation Payments: No facilitation payment shall be made by the company either directly or through its employees, directors, agents, associates, consultants, advisors, representatives or intermediaries.

Clause 4 - Bribery to Foreign Public Officials: The Company, either directly or through its employees, directors, agency, associates, consultants, advisors, representatives or intermediaries in the conduct of international business shall not offer, promise or give any undue pecuniary or other advantage, to a foreign public official, for that official or for a third party, in order that the officials acts or refrains from acting in relation to the performance of officials duties, in order to obtain or retain business or other improper advantage.

Clause 5 - Policy for Gifts, Hospitality & Expenses: The Company shall follow a Policy for gifts, hospitality and expenses as approved by its Board.

Clause 6 - Whistle Blower Mechanism: The Company shall set up a Whistle Blower Mechanism as approved by its Board to enable its employees or others to raise concerns and report violation(s) of the Code.

Clause 7 - Anti-Bribery Training and Awareness Programmes: The company shall put in place an annual Corporate Anti-Bribery awareness-cum-training program as approved by its Board for all its employees, agents, associates, advisors, representatives, intermediaries, consultants, contractors, sub-contractors and suppliers.

Clause 8 - Monitoring Mechanism for Anti-Bribery Code: The Company shall set up a mechanism as approved by its Board for regular monitoring of its Anti-Bribery Code.

Clause 9 - Sanctions for Non-compliance: Any non-compliance of the Code is subject to disciplinary mechanism. The company shall set-up disciplinary mechanism as approved by its Board, for non-compliance of any part of the Corporate Anti-Bribery Code. The disciplinary mechanism shall include:

- Nature of offence
- Penalty of the offence
- Competent Authority

Answer 5(b)

As per Section 211 of the Companies Act, 2013, the Central Government may establish the Serious Fraud Investigation Office and as per section 212 the central government may assign the investigation of the affairs of a company to the Serious Fraud Investigation Office (SFIO) in the following circumstances:

(a) on receipt of report of the Registrar or Inspector under section 208;

(b) on intimation of a special resolution passed by a company requesting an investigation into its affairs;

(c) in public Interest;

(d) on the request of any Department of Central Government or State Government.

The SFIO committee shall consist of experts from the fields of accountancy, forensic auditing, law, law, information technology, investigation, company law, capital market and taxation etc. and will submit its report to the central government.

Question 6

(a) Fraud has always a motive behind it. If an opportunity to commit the fraud exist, the fraudster justifies the crime in such a way that is acceptable to his internal moral compass. Elucidate this statement. (6 marks)

(b) A public limited company had done the following transactions :

Got a Term Deposit Receipt (TDR) from A Bank or ₹1 crore by debiting its current account. After some time, the company requested its banker to issue duplicate TDR, since the original was misplaced (but actually the original TDR was with the company). The bank after doing necessary formalities, issued the duplicate TDR. After some time, the company raised loan against that duplicate TDR and the bank granted loan of 90% of the value which was ₹90 lakh.

From this ₹90 lakh, the company approached another bank say, B Bank and got TDR for ₹90 lakh. Again, the company pretending that the original has been lost and requested for issue of the duplicate. The Bank issued the duplicate TDR after doing certain formalities. The company then asked for loan against the said duplicate TDR and availed loan of ₹80 lakh from C Bank.

The same story was repeated by the company with total 5 Banks as following :

Bank	*Original TDR Amount (₹ in lakh)*	*Loan amount raised by pledging the duplicate TDR (pretending that original has been lost)(₹ in Lakh)*
A Bank	100	90
B Bank	90	80
C Bank	80	70
D Bank	70	60
E Bank	60	50
Total	400	350

By inflating the sales amount, the company showed wrong figures in the financial statement and the proceeds of the same were shown as placement of deposits with various bank.

The company was having original TDR of all the 5 banks, while on the duplicate TDR the loan amount was raised.

For the satisfaction of the auditor the company showed all the 5 TDR in original and the auditor also didn't get suspicious and relied on the primary evidence showed by the company.

Based on the above facts, narrate the deficiencies you observe on the part of the auditor. *(6 marks)*

Answer 6(a)

The statement is true and is the three stages, categorized by the effect on the individual that can be summarised as pressure, opportunity and rationalization. This is termed as fraud triangle theory and was first coined by American sociologist Donald R. Cressey, who worked extensively in the fields of criminology and white-collar crime. Fraud is often a white-collar crime but not always.

According to this theory, the Fraud triangle is a framework designed to explain the reasoning behind a worker's decision to commit workplace fraud. The three stages, categorised by the effect on the individual, can be summarised as pressure, opportunity and rationalisation. Broken down, they are:

Step 1: The incentive / pressure on the individual is the motivation behind the crime and can be either personal financial pressure such as debt problems, or workplace debt problems, such as a shortfall in revenue. The pressure is seen by the individual as unsolvable by orthodox, legal, sanctioned routes and unshareable with others who may be able to offer assistance. A common example of a perceived unshareable financial problem is a gambling debt. Maintenance of a lifestyle is another common example.

Step 2 : The opportunity to commit fraud is the means by which the individual will defraud the organisation. In this stage the worker sees a clear course of action by which they can abuse their position to solve the perceived unshareable financial problem in a way that - again, perceived by them - is unlikely to be discovered. In many cases the ability to solve the problem in secret is key to the perception of a viable opportunity.

Step 3 : The ability rationalise the crime is the final stage in the fraud triangle. This is a cognitive stage and requires the fraudster to be able to justify the crime in a way that is acceptable to his or her internal moral compass. Most fraudsters are first-time criminals and do not see themselves as criminals, 'but rather a victim of circumstance Rationalisations are often based on external factor, such as a need to take care of a family, or a dishonest employer who is seen to minimise or mitigate the harm done by the crime.

Answer 6(b)

In the instant case, the auditor should have the following strategy:

Primary Evidence : The primary evidence, which the company has shown to its auditor was the entire 5 TDR issued by the 5 different banks. The auditor shall have challenged the management intention for opening TDR's in various accounts and around 10% reduction each time the TDR was made. Additionally, the auditor shall have challenged the source of such collection by tracing the bank statements for receipts from customers.

Secondary Evidence : The auditor failed in its responsibility to discharge the duties in a prudent manner. He should have asked from all the 5 banks independently by confirming through a letter that all 5 TDR have been issued by them and no duplicate TDR against these have been issued and also no loan have been given to the company by keeping the said TDR. The auditor should have also asked for the duplicate TDR which was submitted in place of the original.

If the auditor had demanded for the secondary evidence, the fraud would have been unearthed.

***

DIRECT TAX LAWS & PRACTICE

(Elective Paper 9.5)

Time allowed : 3 hours *Maximum marks : 100*

NOTE : *1. Answer ALL Questions.*

2. All the references to sections in the Question Paper relate to the Income-tax Act, 1961 and relevant to the Assessment Year 2021-22, unless stated otherwise.

3. Working notes should form part of the answer.

Question 1

(A) Rust Ltd. is engaged in the business of manufacturing copper bottles. As a Company Secretary you are the key person and heading the taxation wing of the Company. The CFO of the Company approached you for the tax computation for the AY 2021-22. The following information are shared with you :

Profit and Loss Account shows a net profit of ₹72,00,000 for the year ended 31st March 2021, after debiting/crediting the following items :

(a) One time license fee of ₹12,00,000 paid to a foreign Company for obtaining franchise on 1st July, 2020.

(b) ₹12,000 and ₹18,000 paid in cash on 15th October 2020 by two separate voucher to a contractor who carried out certain repair work in the office premises.

(c) ₹2,50,000 being expenses incurred on the travelling of the wife of Managing Director, who accompanied him on tour to Beijing on invitation of Trade and Commerce Chamber, China.

(d) Dividend of ₹5,50,000/- received from a foreign Company, in which Rust Ltd. hold 28% in nominal value of share capital of the Company. ₹50,000/- spent on earning this income.

(e) Depreciation on tangible fixed assets ₹1,50,000/-

(f) ₹15,00,000 and ₹2,50,000 being amounts waived by a bank out of principal and arrear interest, respectively, in one-time settlement. The loan was obtained for meeting working capital requirements two year back.

(g) Provisions for gratuity based on actuarial valuation is ₹15,00,000. Actual gratuity paid ₹5,00,000/- was debited to provision for gratuity account.

(h) The opening and closing stock of the year were ₹18,00,000 and ₹18,72,000 respectively and were undervalued by 10% on cost.

Additional Information:

(i) During the year, the Company purchased 5,000 nos. of shares of RK (Pvt.) Ltd. at ₹20 per share. The Fair Market Value of such shares on the date of transaction was ₹40 per share.

(ii) *A debt of ₹8,00,000 was claimed as bad debts in F.Y. 2019-20, but the Assessing officer allowed only ₹4,00,000 as bad debt. In FY 2020-21, ₹3 Lakh was recovered from that debt, was not given in books of accounts.*

(iii) *Provision for audit fee of ₹1,00,000/- was made in the books for the year ending 31st March 2020 without deducting tax at source. Such fee was paid to the auditors in September, 2020 after deducting tax u/s l94J and the tax so deducted was deposited on 7th October 2020.*

(iv) *Depreciation on tangible fixed assets as per Income Tax Law is : ₹ 1,75,000. You are required to :*

(1) *Calculate the Total Income of the Company and reasons/rational for your treatment of above adjustment in the tax computation. (18 marks)*

(2) *Ascertain the tax payable by Rust Ltd. on the Total income of the Financial year 2020-21. Ignore MAT Provisions & provisions of section 115BAA.*

(6 marks)

(B) *KP (P) Ltd., a domestic Company having two undertakings engaged in manufacture cement and steel, decided to hive off cement division to SA(P) Ltd, a domestic Indian Company by way of demerger. The net book value of assets of KP(P) Ltd. was ₹60 Crore before demerger. The net book value of assets transferred to SA(P) Ltd. was ₹15 Crore. The demerger was made in February 2021. In the scheme of demerger, it was fixed that for each equity shares of ₹10 each (fully paid up) of KP(P) Ltd, two equity shares of ₹10 each (Fully paid) were to be issued.*

Tirlok held 25,000 equity shares in KP(P) Ltd. which were acquired in the Financial Year 2002-03 for ₹6,00,000. Tirlok received 50,000 equity shares from SA(P) Ltd. Consequent to demerger in January 2021, he sold all the shares of SA(P) Ltd. for ₹8,00,000 in March 2021. In this background you are requested to answer the following :

(a) *Does the transaction of demerger attract any Income Tax Liability in the hands of KP(P) Ltd. and SA(P) Ltd. (2 marks)*

(b) *State the conditions in brief, which are to be satisfied under the Act for a demerger. (6 marks)*

(c) *Compute the capital gain that could arise in the hands of Tirlok on receipt of shares of SA(P) Ltd. (1 mark)*

(d) *Compute the Capital gains that could arise in the hands of Tirlok on sale of shares of SA(P) Ltd. (4 marks)*

(e) *Will the sale of shares by Tirlok affect the tax benefit availed by KP(P) Ltd, and/or SA (P) Ltd ? (1 mark)*

(f) *Is Tirlok eligible to avail any tax exemption under any of the provisions of the Income Tax Act, 1961 on the sale of shares of SA(P) Ltd. ? If so, state in brief. (2 marks)*

CII for FY 2002-03: 105

CII for FY 2020-21: 301

Answer 1(A)

(1) Computation of Total Income of Rust Ltd

Assessment Year 2021-22

Particulars	*Amount (Rs.)*	
Profits & Gains from Business and Profession		72,00,000
Net profit as per Profit and Loss Account		
Add : Items / Disallowance considered separately		
(i) License fees for obtaining Franchisee Rs. 12,00,000 less depreciation thereon Rs. 3,00,000 [Note 2]	9,00,000	
(ii) Cash Payment exceeding Rs.10,000 in aggregate in a day to a contractor for repair work [Rs. 12,000+18,000] (Note 3)	30,000	
(iii) Provision for gratuity [Rs. 15,00,000-5,00,000] (Note 7)	10,00,000	
(iv) Difference in stock valuation (Note 8)	8,000	
		19,38,000
Less : Items credited but to be considered separately/ permissible expenditure and allowances		
(i) Dividend received from a foreign company less expenditure incurred to earn dividend [Rs. 5,50,000 – Rs. 50,000] (Note 4)	5,00,000	
(ii) Waiver of interest on Bank Loan (Note 6)	2,50,000	
(iii) Provision for Audit Fees [Note 9]	30,000	
(iv) Bad Debts (Note 10)	1,00,000	
(v) Depreciation on Tangible fixed Assets (Note 5)	25,000	
		9,05,000
Profit and Gains from Business and Profession		82,33,000
Income from Other Sources		
(a) Dividend from Specified Foreign Company (Note 11)	5,50,000	
(b) Shares of Closely held Company purchase for inadequate consideration (Note 12)	1,00,000	
Income from Other Sources		6,50,000
Gross Total Income		**88,83,000**
Deduction under Chapter VI		Nil
Total Income		**88,83,000**

Note:

1. An expense on travelling of wife of Managing Director to Beijing on the invitation of Trade and Commerce Chamber, China is an allowable expense on the ground of Commercial expediency and business consideration. Alternatively may be disallowed u/s 37(1) on the assumption that it is personal nature.
2. Franchise is in the nature of an intangible asset eligible for depreciation @ 25%. Since one time license fee of Rs. 12 Lakh paid to a foreign Company for obtaining franchise has been debited to profit and loss account, the same has to be added back. Depreciation @ 25% has to be provided in respect of the intangible asset, since it has been used for more than 180 days during the year.
3. Disallowance u/s 40A(3) would be attracted in respect of cash payments of Rs. 12,000 and Rs.18,000 paid to a contractor since the aggregate cash payments made to him in a day exceed the limit of Rs.10,000.
4. Dividend of Rs. 5,50,000 received from Foreign Company is to be taxed under the Head "Income from other sources" since the same has been credited to profit and loss account, it has to be deducted while computing business income. Consequently, expenditure of Rs. 50,000 relating to the same which has been debited to profit and loss account has to be added back. In effect, the net amount of Rs. 5,00,000 has to be deducted.
5. Depreciation of Rs.1, 50,000 on Tangible Fixed Assets charged in the Books of accounts has to be added back. Depreciation of Rs. 1,75,000 computed as per Income Tax Rules, 1962 is allowable. Therefore, the net amount of Rs. 25,000 has to be deducted while computing business income.
6. Waiver of principal amount of loan for trading activity is a benefit in respect of a trading liability by way of remission or cessation thereof and is hence, taxable u/s 41(1). Since the loan is for meeting working capital requirement, means it is taken for trading activity. Since the loan waiver has already been credited to profit and loss account, no adjustment is required. However, as per section 43B, since interest is allowable only on actual payment basis, deduction in respect of interest due on loan would not have been allowed as deduction in any previous year. Therefore, such interest cannot be brought to tax now by invoking section 41(1). Since such interest has now been credited to profit and loss account, the same is to be deducted while computing business income.
7. As per Section 40A(7), any provisions made for payment of gratuity of employees on their retirement or on termination of employment for any reason is disallowed. However, any provision made for the purpose of payment of a sum by way of any contribution to an approved gratuity fund or for the purpose of payment of gratuity which has become payable during the previous year shall be allowed as deduction. The question does not mention that the provision of Rs. 15,00,000 is for the purpose of contribution to an approved gratuity fund. Therefore only gratuity of Rs. 5,00,000 paid to the retired employees is allowable as deduction. Hence, the balance provision of Rs. 10,00,000 (i.e.,15,00,000 -5,00,000) is to be added back. If gratuity fund is approved, no adjustment is required.
8. Difference on account of under valuation of opening stock and closing stock by 10% cost to be deducted and added respectively. Therefore, the net amount of Rs. 8,000 (72,000 * 10/90) has to be added.

9. Rs. 30,000 being 30% of 100,000 representing provision for audit fees for the year ended 31.03.2020 for which tax was not deducted in the F.Y. 2019-20 would have been disallowed while computing deduction for FY 2019-20. Since the tax is deducted and paid in F.Y. 2020-21, Rs. 30,000 would be allowable as deduction in A.Y. 2021-22 as per proviso to Section 40(a)(ia).
10. In a case where the debt ultimately recovered in less than the difference between the amount of debt and bad debt allowed, then the amount to the extent of deficiency in recovery is allowed as deduction in the previous year in which the ultimate recovery is made. Therefore, in this case, since the ultimate recovery of Rs. 3,00,000 is less than Rs. 4,00,000 (being the difference between the debit of Rs.8, 00,000 and the amount of Rs. 4,00,000 allowed as bad debts in the previous year 2019-20. The deficiency of Rs. 1,00,000 will be deductible in FY 2020-21 being the year in which the ultimate recovery of Rs. 3,00,000 is made. It may be noted that in case where the result is a deficiency the amount recovered will not be taxable in the year of recovery. Since Rs. 3,00,000 not credited to Profit and loss account, so no further adjustment is required.
11. Under Section 115BBD, dividend received by an Indian Company from a Foreign Company in which it holds 26% or more in nominal value of the equity share capital of the Company would be subject to a concessional rate of tax 15% as against the tax rate of 30% applicable to other Income of a domestic company. The rate of 15% would be applied on Gross dividend, in the sense, that no expenditure would be allowable in respect of such dividend.
12. Difference between the aggregate FMV of shares of a Company and the consideration paid for purchase of such shares is deemed as income in the hands of purchasing Company u/s 56(2)(x). Since the difference exceeds Rs. 50,000 the entire sum is taxable. Therefore Rs.1,00,000 [5000 x (40-20)] is taxable.

(2) Computation of Tax Liability

Particulars	*Amount Rs.*	*Amount Rs.*
Tax 15% on dividend of Rs. 5,50,000 from specified Foreign Company	82,500	
Tax @ 30% on the balance total income of Rs. 83,33,000	24,99,900	25,82,400
Add : Surcharge (As total income is less than 1 Crore)		NIL
Add : Health & Education Cess (4% on 25,82,400)		1,03,296
Total Tax Liability (Round Off)		26,85,700

Answer 1(B)

(a) No, the transaction of demerger would not attract any income tax liability in the hands of KP(P) Ltd or SA(P) Ltd.

As per section 47(vi)(b) of the Income-tax Act, 1961, any transfer in a demerger

of a capital asset, by the demerged company to the resulting company would not be regarded as Transfer for levy of Capital Gains tax liability if the resulting company is an Indian Company. Hence, Capital Gains tax liability would not be attracted in the hands of KP(P) Ltd. The demerged Company in this case, since SA(P) ltd, is an Indian Company.

(b) The conditions which are to be satisfied under the Income-tax Act, 1961 for a demerger are as under:

- All the property of the undertaking, being transferred by the demerged Company, immediately before the demerger, becomes the property of the resulting company by virtue of the demerger.
- All the liabilities relating the undertaking, being transferred by the demerged company, immediately before the demerger, becomes the liabilities of the resulting company by virtue of the de-merger.
- The property and the liabilities of the undertaking or undertakings being transferred by the demerged Company are transferred at the values appearing in its books of account immediately before demerger. (Revaluation is to be ignored)
- The resulting company issues, in consideration of the demerger, its shares to the shareholders of the demerged Company on a proportionate basis. This condition is not applicable where resulting Company itself is holding the shares in demerged Company.
- The shareholders holding not less than 75% in value of the shares in the demerged Company becomes the shareholders of resulting Company or companies by virtue of de merger.
- The transfer of undertaking is on a going concern basis.

(c) There would be no capital gains liability in the hands of Tirlok on receipt of shares of SA(P) Ltd. Since as per Section 47(vi)(d), any issue of shares by the resulting demerger to the shareholders of the Company being demerged will not be regards as transfer for levy of capital gains tax, if the issue is made in consideration of demerger of the undertaking.

(d) Yes, the Capital Gains would arise in the hands of Trilok on sale of Shares of SA(P) Ltd.

Particulars	*Amount (Rs.)*
Sale Consideration	8,00,000
Less: Indexed cost of acquisition	
Cost of acquisition of shares of SA(P) Ltd. as per section 49(2C)	
Cost of acquisition of shares in KP(P)Ltd. * Net book value of assets transferred in a demerger / Net book value of the demerged company immediately before de-merger (600000*15 crore /60 crore) = Rs. 1,50,000	

Indexed cost of acquisition of shares of SA (P) Ltd.	
Rs. 1,50,000*301/105	4,30,000
Long term capital gains (since period of holding in the demerged Co. is also to be considered)	3,70,000

(e) No, sale of shares by Tirlok would not affect the tax benefits availed by KP (P) Ltd. or SA (P) Ltd. One of the conditions to be satisfied is that the shareholders holding not less than three fourths in the value of the shares in the demerged Company become shareholders of the resulting Company by virtue of the demerger. It is presumed that the condition is satisfied in this case. There is no stipulation that they continue to remain shareholders for any period of time thereafter.

(f) Since the resultant capital gain on sale of shares of SA (P) Ltd. is a long term capital gain (on account of the period of holding of shares in demerged Company being considered by virtue of section 2(42). Tirlok can avail exemption:

i. under section 54EE, by investing the long-term capital gain in units of specified fund, within a period of 6 months from the date of transfer.

ii. under Section 54F of Income Tax Act by investing the entire net consideration in purchase (within one year before and two years after the date of transfer) or construction (within three years after the date of transfer) of one residential house in India. If part of the net consideration is invested, only proportionate exemption would be available.

Question 2

(a) Atul, aged 32 years, a resident of India employed with FRT Pvt Ltd, received the following sums during the previous year 2020-21 :

Basic Salary	*₹70,000 p.m.*
DA	*12% of basic salary*
Servant Allowance	*₹6,000 p.m.*
Tiffin/Lunch/Dinner	*₹5,000 p.m.*

He has paid ₹2,25,000 by account payee cheque for Mediclaim premium to insure the health of his mother, aged 62 year, who is not dependent on him as a lumpsum payment for 5 year including the current previous year.

Apart from this, he also provided guest lecture to a university in foreign Country during the year. He received ₹15,79,200 from such university after deduction of tax of ₹3,94,800 in that Country. India does not have any double taxation avoidance agreement under section 90 of the Income Tax Act, 1961, with the said foreign Country. Compute the tax liability of Atul for the A.Y. 2021-22. Assume assessee has not opted section 115BAC. (8 marks)

(b) Aadarsh, a resident and ordinarily resident in India, has derived the following income from various operations (relating to plantations and estates owned by him) during the year ended 31st March 2021 :

Particulars	*₹*
Income from sale of coffee grown, cured, roasted and grounded in Colombo (Sri Lanka). Sale consideration was received at Chennai.	*4,00,000*
Income from sale of coffee grown and cured in Tamil Nadu	*2,00,000*
Income from sale of tea grown and manufactured in Darjeeling	*60,000*

Calculate his business and agriculture income for financial year 2020-21. *(4 marks)*

Answer 2(a)

Computation of total income of Mr. Atul for A.Y. 2021-22

Particulars	*Amount (Rs.)*	*Amount (Rs.)*
Income under the head Salary		
Basic Salary (70,000*12)	8,40,000	
Dearness Allowance (12% of Basic Salary of Rs. 8,40,000)	1,00,800	
Servant Allowance (Rs. 6,000*12) fully taxable	72,000	
Tiffin/Lunch/Dinner Allowance (Rs. 5,000*12) fully taxable	60,000	
Gross Salary	10,72,800	
Less : Standard Deduction u/s 16	(50,000)	
Net salary		10,22,800
Income under the head Other Sources		
Income from lecture in foreign university [Rs.15,79,200 plus TDS Rs. 3,94,800]		19,74,000
Gross Total Income		29,96,800
Less : Deduction under chapter VI-A		
Section 80D – Medical insurance premium of his mother being a resident senior citizen for the year 2020-21 Rs. 45,000 [being 1/5 of the lump sum premium of Rs. 2,25,000 paid for 5 year – fully allowable even though she is not dependent on him, since the same does not exceed Rs. 50,000		(45,000)
Total Income		29,51,800

Computation of Tax Liability of Mr. Atul

Particulars	*Amount (Rs.)*	*Amount (Rs.)*
Tax on Total Income [Rs. 5,85,540 i.e. 30% of Rs. 19,51,800 plus 1,12,500		6,98,040
Add : Surcharge		Nil
Add : Health and Education Cess @ 4%		27,922
Tax Liability		7,25,962
Average rate of tax in India i.e. Rs. 7,25,962/Rs. 29,51,800 * 100	24.59%	
Average rate of tax in Foreign Country i.e. Rs. 3,94,800 / Rs. 19,74,000 * 100	20%	
Relief u/s 91on Rs. 19,74,000 being the doubly taxed income @ 20% [being lower of Indian rate of tax @ 24.59% and foreign tax rate @ 20%		(3,94,800)
Tax Payable (Round Off)		3,31,160

Answer 2(b)

Sr. No.	*Source of Income*	*Gross*	*Business Income*		*Agriculture Income*
1.	Sale of Coffee grown, cured, roasted and grounded outside India.	4,00,000	100%	4,00,000	-
2.	Sale of Coffee grown and cured in India	2,00,000	25%	50,000	1,50,000
3.	Sale of tea grown and manufactured in India	60,000	40%	24,000	36,000
4.	Total			4,74,000	1,86,000

Question 3

(a) Radhika aged 63 years, has gross total income of ₹7,75,000 comprising of income from house property and other sources. She has made the following payments and investments :

(a) Premium paid ₹20,000 to insure the life of her major daughter (policy taken on 1.4.2014) (Insured value ₹1,80,000).

(b) Medical Insurance premium for self - ₹12,000; Spouse - ₹14,000.

(c) Donation to a public charitable institution registered under Section 80G ₹ 1,50,000 by way of cheque.

(d) LIC Pension Fund - ₹60,000.

(e) Donation to National Children's Fund - ₹25,000 by way of cheque.

(f) Donation to Jawaharlal Nehru Memorial Fund - ₹25,000 by way of cheque.

(g) Donation to approved institution for promotion of family planning - ₹40,000 by way of cheque. Compute the total income of Radhika for A.Y. 2021-22. (6 marks)

(b) Discuss the following statements :

(i) Examine the circumstances where the appellant shall be entitled to produce additional evidence, oral or documentary, before the Commissioner of Income Tax (Appeals) other than the evidence produced during the proceedings before the Assessing Officer. (2 marks)

(ii) Company A and Company B who has entered into Advance Pricing Agreement (APA) and eligible for rollback provisions merged to form Company AB. Is the Company AB eligible for rollback provisions as it was formed on the merger of Company A and Company B ? (2 marks)

(iii) The gross total income of Yuvraj Co. Ltd., Indore was ₹70 Lakh which is wholly attributable to a unit located in SEZ since April, 2012. Adjustments to total income made by the Assessing Officer by applying the transfer pricing provisions enhanced their total income by ₹50 Lakh. What is the total income of the year chargeable to tax and explain why ? (2 marks)

Answer 3(a)

Computation of Total Income of Radhika for AY 2021-22

Particulars	*Amount (Rs.)*	*Amount (Rs.)*
Gross Total Income		7,75,000
Less : Deduction u/s 80C		
Life insurance premium paid for insurance of major daughter (Maximum 10% of the assured value of Rs. 1,80,000 as the policy is taken after 31.03.2012)	18,000	
Deduction u/s 80CCC in respect of LIC pension fund	60,000	(78,000)
Less : Deduction u/s 80D – Medical insurance premium in respect of self and spouse		(26,000)
Less : Deduction u/s 80G (working note)		(91,050)
Total Income		5,79,950

Working Note: Calculation of Deduction u/s 80G

Particulars	*Donation (Rs.)*	*% of Deduction*	*Deduction u/s 80G (Rs.)*
National Children's Fund	25,000	100%	25,000
Jawaharlal Nehru Memorial Fund	25,000	50%	12,500
Approved institution for promotion and family planning [Approved Institution is assumed as Govt. / Local authority]	40,000	100% subject to 10% of qualifying limit	40,000
Public charitable trust	1,50,000	50% subject to 10% of qualifying limit	13,550
			91,050

Adjusted total income = Gross Total Income - Amount of deduction under section 80C to 80U except section 80G i.e., Rs. 6,71,000. In this case Rs. 67,100 being 10% of adjusted total income is the qualifying limit, in this case.

(a) Firstly, donation of Rs. 40,000 to approved institution for family planning qualifying for 100% deduction subject to qualifying limit, has to be adjusted against this amount.

(b) Therefore, donation to public charitable trust qualifying for 50% deduction, subject to qualifying limit is adjusted. Hence, the contribution Rs.1,50,000 to public charitable trust is restricted to Rs. 27,100 (being Rs. 67,100 - 40,000) 50% of which would be the deduction under section 80G. Therefore, the deduction under section 80G in respect of donation to public charitable trust would be Rs. 13,550 which is 50% of Rs. 27,100.

Answer 3(b)

(i) As per Rule 46A(1) of the Income-tax Rules 1962, an appellant shall be entitled to produce before the Commissioner (Appeals), evidence, either oral or documentary, other than the evidence produced by him during the course of proceedings before the Assessing Officer, only in the following circumstances:

- Where the Assessing Officer has refused to admit evidence which ought to have been admitted; or
- Where the appellant was prevented by sufficient cause from producing the evidence which he was called upon to produce by the Assessing Officer, or
- Where the appellant was prevented by sufficient cause from producing before the Assessing Officer any evidence which is relevant to any ground of appeal or
- Where the Assessing Officer has made the order appealed against without

giving sufficient opportunity to the appellant to adduce evidence relevant to any ground of appeal.

Further, no evidence shall be admitted unless the Commissioner (Appeals) records in writing the reason for its admission.

(ii) The agreement of APA is between the Board and a taxpayer person. The principle to be followed is that the person who makes the APA application alone would be entitled to enter into the agreement and be entitled for the rollback provisions in respect of international transactions undertaken by it in rollback year.

Since Company A and B were the APA Applicants and not the new Company AB formed as a result of merger, Company AB would not be eligible for the rollback provisions.

(iii) As per the proviso to Section 92C(4) of the Income tax Act, 1961, where the arm's length price is determined by the Assessing Officer by applying transfer pricing provisions, no deduction, inter alia, under section 10AA shall be allowed from the income so enhanced by the Assessing officer. Assuming that the entire turnover represents the export turnover, and consequently, the entire profit of Rs. 70 Lakh is eligible for deduction under Section 10AA, the total income would be computed as follows:

Income of the unit in SEZ (computed)		70 Lakh
Less : Deduction u/s 10AA	=	50% of Rs. 70 lakh, being the 8th year of operation = 35 Lakh
Add : Enhancement in total income by the assessing officer, applying transfer pricing provisions		50 lakh
Total Income		85 lakh

(No deduction u/s 10AA is allowable in respect of income so enhanced.)

Question 4

(a) FRX Ltd. gives a multilevel parking building in front of a shopping mall in Delhi to ABC Ltd. on a lease of 80 year. ABC Ltd. is liable to pay ₹3 Crore as one-time lease premium in addition to an annual lease rent of ₹26 Lakh. What will be the TDS/TCS liability in the hands of FRX Ltd. as well as in the hand of ABC Ltd. What will be your answer if ABC Ltd. does not have PAN ? (3 marks)

(b) Explain the treatment as to their taxability and/or allowability, under the provisions of Income Tax Act, 1961 for the AY 2021-22, in the following case : Saloni Ltd. paid Singapore dollar equivalent to ₹1 crore as sales commission for the year ended 31st March 2021, without deduction tax at sources, to Robin, a citizen of Singapore and non-resident who acted as agent for booking orders, from various customers who are outside India. (3 marks)

(c) "Stylish Trends" filed its return of income as partnership firm for the relevant assessment year admitting a total income of ₹160 Lakh. The firm consisted of

fifteen individuals and two firms. The return of income was selected for scrutiny which led to disallowance of ceftain deductions to the tune of ₹80 Lakh. The assessee preferred an appeal. The CIT (Appeals) invoked section 251 and issued a show cause notice proposing to change the assessee's status to AOP on the reasoning that a partnership cannot be a partner in another firm. Discuss the correctness of the contention of the CIT (Appeals). Also, examine whether the CIT (Appeals) has the power to change the status of the assessee. (6 marks)

Answer 4(a)

FRX Ltd., the Company granting lease of parking lot, is required to collect tax at source @ 2% (1.5% from 14.05.2020 to 31.03.2021) under section 206C from the one-time lease premium of Rs. 3 Crore and annual lease rent of Rs. 26 Lakh, i.e. on 3.26 Crore at the time of debiting the amount payable by ABC Ltd.(assume to be resident in India) or at the time of receipt of such amount, whichever is earlier.

In case ABC Ltd. does not have PAN, tax has to be collected by FRX Ltd. at the rate of 5% being the higher of-

- 5% and
- 4% i.e. twice the TCS rate of 2%

In the hands of ABC Ltd., TDS provisions u/s 194I would not be attracted on the one-time lease premium of Rs. 3 Crore paid for acquisition of long-term leasehold rights over land or building, which are not adjustable against periodic payments. [CBDT Circular No.35/2016 dated 13.10.2016]. But TDS provisions will apply on annual lease rent u/s 194I @ 10%.

Answer 4(b)

A foreign agent of an Indian exporter operates in his own country and not having permanent establishment in India, no part of his income accrues or arises in India. His commission is usually remitted directly to him and is therefore, not received by him or on his behalf in India.

The commission paid to the non-resident agent for services rendered outside India is, thus not chargeable to tax in India. Since commission is not subject to tax in India, disallowances under section 40(a) (i) of Income Tax Act is not attracted even though tax has not been deducted at sources. It shall be allowed as expenses.

Answer 4(c)

The issues under consideration are as under:

1. Whether a firm can be a partner of another firm?
2. Whether the CIT (Appeals) has the power to change the status of assessee. These issues came up before the Madras High Court in *Mega Trends Inc.* v. *CIT (2016).* The Court observed that since a partnership firm is a relationship between persons who have agreed to share the profits of the business carried on by all are any of them acting for all, and the term "persons" can connote only natural person. Since some of the partners are other firms, the assessment

cannot be carried out as a firm, as per the Supreme Court ruling in *Dhulichand Laxminarayan* v. *Cff (1956)*.

The contention of the Commissioner (Appeals) that a firm cannot be a partner of another firm is, therefore, correct.

In Mega Trends Inc's case, the Madras High Court further observed that, under section 251(1), the powers of the first appellate authority are co-terminous with those of the Assessing Officer and the appellate authority can do what the Assessing Officer ought to have done and also direct him to do what he had failed to do. If the Assessing Officer had erred in concluding the status as a firm, it could not be said that the Commissioner (Appeals) had no jurisdiction to go into the issue. The appeal was in continuation of the original proceedings and unless fetters were placed upon the powers of the appellate authority by express words, the appellate authority could exercise all the powers of the original authority. The High Court held that the power to change the status of the assessee is available to the assessing authority and when it is not used by him, the appellate authority is empowered to use such power and change the status. The Court relied on a full bench decision of the Madras High Court in *State of Tamil Nadu* v. *Arulmurugan and Co.* reported in [1982] to come to much conclusion accordingly, applying the rationale of the Madras High Court ruling to the case on hand; the CIT (Appeals) has the power to change the status of the assessee.

Question 5

(a) The books of accounts maintained by Janta Vikash Party registered with Election Commission for the year ended 31st March 2021 disclosed the following receipts:

(a) Rent of Property let out to a Departmental Store at Bhopal – ₹5,32,000.

(b) Interest on deposits other than Banks – ₹14,50,000.

(c) Cash contributions from 1500 persons (who have secreted their name) of ₹10,000 each – ₹1,50,00,000.

(d) Contribution of ₹11 each from 1,00,000 members by cheque (Recorded in books of accounts) – ₹11,00,000.

(e) Net Profit of Cafeteria run in the premises at Delhi – ₹50,00,000.

Compute the total income of the Political Party for the A.Y. 2021-22.

(b) PWSI Ltd. engaged in the business of TMT manufacturing also effected the sales and purchase of shares of other Companies. It suffered loss from such transactions :

(a) Whether such Company can set off its losses from share trading from the profit of TMT business ?

(b) If principal business of such Company is sale and purchase of shares of other Companies, what would be your answer ?

(c) Under the provisions of a tax treaty between India and Dubai, any capital gains arising from the sale of shares of Sun India Ltd, an Indian Company would be taxable only in Dubai if the transferor is a resident of Dubai except where the transferor holds more than 10% interest in the capital stock of Sun India Ltd. A company, Gama Inc, being resident in Dubai, makes an investment in Sun

India Ltd. through two wholly owned subsidiaries (Fama Inc. and Gama Inc.) located in Dubai. Each subsidiary holds 9.95% shareholding in the Indian Company, the total adding to 19.9% of equity of Sun India Ltd. The subsidiaries sell the shares of Sun India Ltd. and claim exemption as each is holding less than 10% equity shares in the Indian Company. Can GAAR be invoked to deny treaty benefit ? *(4 marks each)*

Answer 5(a)

Computation of Total Income of Janta Vikash Party for AY 2021-22

Particulars	*Amount (Rs.)*
(a) Rent of the property of Rs. 5,32,000 located at Bhopal [Exempt u/s 13A]	Nil
(b) Interest received on deposits of Rs. 14,50,000 [Exempt u/s 13A]	Nil
(c) Cash Contribution given by 1500 person of Rs.10,000 each by secreting their identities (Not allowed as exempt u/s 13A, since cash contribution in excess of Rs. 2,000 not permissible)	1,50,00,000
(d) Contribution of Rs. 11 each given by its members being recorded in the books [Exempt u/s 13A]	Nil
Net Profit of cafeteria at Delhi [Cafeteria run by political party will be treated as Commercial activity and hence Income will not be exempt u/s 13A]	50,00,000
Total Income	2,00,00,000

Note : It is presumed that the conditions regarding maintenance of books of account, audit, submission of report under section 29C of the Representation of the People Act, 1951 and filing of return of income under section 139(4B) are fulfilled by the political party, and hence it is eligible for exemption of income under section 13A.

Answer 5(b)

As per Section 73(1) of the Income tax Act, 1961, loss in speculation business can be set-off only against the profit of any other speculation business and not against any other business or professional Income. Explanation to section 73(1) clarifies that where any part of the business of a company consists in the purchase and sale of the shares of other companies, such a company shall be deemed to be carrying on speculation business to the extent to which the business consists of the purchase and sale of such shares.

However, this deemed provision does not apply, inter alia, to a company, the principal business of which is the business of trading of shares.

i. Since of the business of PWSI Ltd. consists of sale and purchase of shares of other companies, the company would be deemed to be carrying on speculation

business to the extent of purchase and sale such shares. Thus the loss from speculative business, i.e., loss from share trading cannot be setoff against profit of TMT business of PWSI Ltd.

ii. If the principal business of PWSI Ltd. is to sell and purchase of shares of other companies, PWSI Ltd would not be deemed to be carrying on speculation business. In such case, the loss arising from the sale and purchase of shares of other company can be set-off against any other business income. PWSI Ltd. can, accordingly, set-off such losses against its profit from TMT Business.

Answer 5(c)

The above arrangement of splitting the investment through two subsidiaries appears to be with the intention of obtaining tax benefit under the treaty. Further, there appears to be no commercial substance in creating two subsidiaries as they do not change the economic condition of investor Gama Inc. in any manner (i.e. on business risks or cash flow), and reveals a tainted element of abuse of tax laws. Hence, the arrangement would be treated as an impermissible avoidance arrangement by invoking General Anti Avoidance Rules 'GAAR'. Consequently, treaty benefit would be denied by ignoring Fama Inc. and Gama Inc. The two subsidiaries, or by treating Fama Inc. and Gama Inc. as one and the same company for tax computation purposes, profits from sale of shares shall be taxable in India.

Question 6

The following are the details of income provided by Manish, the assessee for the financial year ended 31st March, 2021 :

(i) Rental income from property at Bangalore - ₹5,00,000, Standard Rent - ₹4,50,000, Fair Rent - ₹4,80,000.

(ii) Municipal and water tax paid during the year 2020 - 21 : Current year ₹35,000, Arrears - ₹1,50,000.

(iii) Interest on loan borrowed towards major repairs to the property : ₹1,50,000.

(iv) Arrears of rent of ₹30,000 received during the year, which was not charged to tax in earlier year.

Further, the assessee furnished the following additional information regarding sale of property at Chennai :

(a) Manish's fathers acquired a residential house in April 2005 for ₹1,25,000 and thereafter gifted this property to the assessee, Manish on 1st March 2006.

(b) The property, so gifted, was sold by Manish on 10th June 2020. The consideration received was ₹25,00,000.

(c) Stamp duty charges paid by the purchaser at the time of registration @ 14% (as per statutory guidelines) were ₹3,38,000.

(d) Out of the sale consideration received :

- *On 2nd January, 2021 the assessee had purchased two adjacent flats, in*

the same buildings, and made suitable modification to make it as one unit. The investment was made by separate sale deeds, amount being ₹8,00,000 and ₹7,00,000 respectively.

- *On 10th October, 2020 ₹ 10 Lakh were invested in bonds issued by National Highways Authority of India, but the allotment of the bonds was made of 1 st February, 2021.*

Compute Manish's taxable income for the assessment year 2021-22.

Cost inflation index : FY 2005-06 : 117, FY 2020-21 : 301. *(12 marks)*

Answer 6

Computation of Total Income and Tax Payable by Mr. Manish

Particulars	*Amount (Rs.)*	*Amount (Rs.)*
Income from house property		
Gross Annual Value [Higher of expected Rent & Actual Rent]		5,00,000
Expected Rent (lower of Fair Rent and Standard Rent)	4,50,000	
Actual Rent	5,00,000	
Less : Municipal taxes paid during the year (including arrears) [Rs. 35,000+1,50,000]		(1,85,000)
Net Annual value (NAV)		3,15,000
Less : Deduction u/s 24		
a) 30% of NAV	94,500	
b) Interest on loan borrowed for major repair	1,50,000	(2,44,500)
Add : Arrears of rent taxable u/s 25A	30,000	
Less : Deduction @ 30%	(9000)	21,000
Income under the head House Property		**91500**
Capital Gains		
Full value of consideration as per section 50C, the full value of consideratio n would be the higher of	25,00,000	
Actual consideration or	25,00,000	
Stamp Duty Value [3,38,000/14%]	24,14,286	
Less : Indexed Cost of Acquisition [Rs. 1,25,000*301/117] As per section 49(1), cost		

of acquisition of the residential house gifted by Manish's Father to Manish would be a cost for which Manish's father acquired the asset.	(3,21,581)
Less : Exemption under section 54 (8,00,000+7,00,000) Purchase of residential house within the stipulated time (within one year before or two years after the date sale had effected the necessary modification to make it as one house, the assessee would be entitled to exemption under Section 54 in respect of investment in both the flats, despite the fact that they were purchased by separate sale deeds [*CIT* v. *Ananda Basappa (2009) (Kar.)*]	(15,00,000)
Exemption u/s 54 EC [Investments in bonds of NHAI within six months from the date of transfer. Where the payment for bonds has been made within the 6 month period, exemption under section 54EC would be available even if the allotment of bonds was made after the expiry of the six months [*Hindustan Unilever Ltd. (2010) (Born.)]*	(6,78,419)
Long Term Capital Gains	Nil
Total Income	**91,500**

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LABOUR LAWS & PRACTICE

(Elective Paper 9.6)

Time allowed : 3 hours *Maximum marks : 100*

NOTE: *Answer **ALL** Questions.*

Question 1

Case Study :

The case is relating to Compensation under Section 3 of Employees' Compensation Act. In the matter the appeal was filed by the employer against the judgement of the Workmen Compensation Commissioner. The material facts which have given rise to this appeal is briefly stated as mentioned below.

The deceased was employed as a driver on a truck of the appellant which used to carry petrol tank. The deceased reported to the appellant that the tank was leaking upon which the appellant got the tank partly filled with water at night and ordered the deceased to check it on the next morning. On the next morning i.e., on 10th January, 2016, the deceased entered the tank to see from where it leaked and lighted a match stick as a result of which it caught fire and the deceased received burns due to which he succumbed subsequently.

The evidence produced on behalf of respondent was that the match box supplied to the deceased by the appellant. But this fact was denied by the appellant in his deposition and in the opinion of the learned Commissioner it was doubtful that the appellant had given the match box to the deceased though no reasons are given for the aforesaid conclusion. Learned Counsel for the appellant contends :

(i) That in the present case the accident did not arise out of and in the course of the deceased's employment and it occurred due to the 'added peril' that is the lighting of match stick within the petrol tank by him.

(ii) That the Commissioner out to have held the Insurance Company i.e., respondent insurance is also liable for compensation.

(iii) That after remarriage respondent widow was not entitled to claim compensation because she no longer remained a dependent.

In order to appreciate the argument, it would be useful to reproduce the relevant parts of Section 3 of the Employees' Compensation Act, 1923. If personal injury is caused to an employee by accident arising out of and in the course of his employment, his employer shall be liable to pay compensation.

Provided that the employer shall not be so liable :

(a) In respect of any injury which does not result in the total or partial disablement of the employee for a period exceeding three days;

(b) In respect of any injury not resulting in death, caused by an accident which is directly attributable to :

(i) The employee having been at the time thereof under the influence of drink or drugs or

(ii) The willful disobedience of the employee to an order expressly given or to rule expressly framed, for the purpose of securing the safety of employee, or

(iii) The willful removal or disregard by the employee of any safety guard or other device which he knew to have been provided for the purpose of securing the safety of employee.

On the basis of the above facts, answer the following :

(A) Whether the accident of employee is in course of employment ? (8 marks)

(B) Whether the employer can take plea of 'added peril' in his defense ? (8 marks)

(C) Is the employer liable to pay compensation ? (8 marks)

(D) Whether dependents will succeed in recovering compensotion from the employer? (8 marks)

(E) Whether a widow become debarred from claiming compensation ? On account of her remarriage ? (8 marks)

Answer 1(A)

As per Section 3 of the Employee's Compensation Act, if personal injury is caused to a workman by accident arising out of and in the course of his employment, his employer shall be liable to pay compensation in accordance with the Act.

Provided that the employer shall not be so liable-

a) in respect of any injury which does not result in the total or partial disablement of the employee for a period exceeding three days;

b) in respect of any injury not resulting in death, caused by an accident which is directly attributable to :

(i) the employee having been at the time thereof under the influence of drink or drugs, or

(ii) the wilful disobedience of the employee to an order expressly given or to rule expressly framed, for the purpose of securing the safety of workman, or

(iii) the wilful removal or disregard by the employee of any safety guard or other device which he knew to have been provided for the purpose of securing the safety of employee.

The facts of present case resembles with *R.B. Moondra And Co.* vs. *Mst. Bhanwari & Anr AIR 1970 Raj 111*. In the present case it is clear that the deceased was employed as a driver on the appellant's truck used for the purpose of carrying petrol in a tank. On the previous day he had reported to the appellant that the tank was leaking and so water was filled in it for detecting the place from where it leaked. The deceased was asked by the appellant to enter the tank to see from where it leaked. Accordingly, the deceased entered the tank which had no petrol in it, but had been partly filled with water and for the purpose of detecting the place from where it leaked, he lighted a match stick. The deceased was at the place of his work and did something in furtherance of the employer's work when the accident occurred.

So, it is clear that the accident of employee is in the course of employment.

Answer 1(B)

The principle of 'added peril' contemplates that if a workman while doing his master's work undertakes to do something which he is not ordinarily called upon to do and which involves extra danger he cannot hold his Master liable for the risks arising therefrom. This doctrine, therefore, comes into play only when the workman is at the time of meeting the accident performing his duty. When the employee done an act which is not obliged by him to do and puts himself in dangers, the employer cannot be liable to pay compensation for the injuries caused. Therefore, the injury not caused out of employment, the employer is not entitled to compensate or benefit the employee. However, on the facts of the case the defense of 'added peril' has no foundation.

It is established in the given problem that the deceased workman had at that time done something which was a part of his job and through a route not forbidden. The meaning of the phrase 'added peril' and its application to cases arising under the Employee's Compensation Act and lays down that if the act which the workman was doing was within the scope of his employment, the question of negligence greater or small in doing that act is irrelevant. This case, therefore, establishes that no matter how negligent or rash the workman's action, it arises out of the employment if it is within the scope of his duty as an employee.

So, the employer cannot take the plea of 'added peril' in his defense because extra hazard is not only an 'added peril' but a needless peril.

Answer 1(C)

According to Section 3 of the Employee's Compensation Act, 1923, the employer shall not be liable in respect of any injury not resulting in death, caused by an accident which is directly attributable to:

(i) The willful disobedience of the workman to an order expressly given or to rule expressly framed, for the purpose of securing the safety of workman, or

(ii) The willful removal or disregard by the workman of any safety guard or other device which he knew to have been provided for the purpose of securing the safety of workmen.

It would appear from the above provision that if personal injury is caused to a workman by accident arising out of and in the course of his employment, the employer shall be liable to pay compensation except where injury results in death.

Hence, the employer is not liable to pay the compensation.

Answer 1(D)

In order to claim compensation, the employee has to show not only that at the time of the accident he was in fact employed on duties of his employment, but further that the immediate act which led to the accident was within the sphere of his duties and not foreign to them. In case of death of an employee due to accident if it has arisen out of and in the course of his employment it is no defense to plead that there was willful disobedience of any order or rule expressly given or framed for the purpose of securing the safety of the workman. If a workman is doing an act which is *within the*

scope of his employment in a way which is negligent in any degree and is injured by a risk incurred only by that way of doing it he is entitled to compensation.

Looking into the facts of cases there is no doubt that the accident arose out of the deceased's employment and the act of lighting the match stick even if it be held as a rash or negligent act, will not debar his dependent from claiming compensation. So certainly in this matter the dependents will succeed in recovering compensation from the employer.

Answer 1(E)

The widow became debarred from claiming compensation on account of her remarriage has no force because in the Act there is no such provision that after remarriage widow of the deceased would not be regarded as a dependent.

Under Section 21 of the Hindu Adoptions and Maintenance Act, 1956, a widow remains a dependent, within the meaning of that section so long as she is not remarried. But, the definition of 'dependent' under the Act is not so restricted and the fact that she has remarried will not disentitle her to claim Compensation under the Act.

Question 2

(a) The employees employed in an Airline Industry gave notice of strike stating that they would go on strike dated 1st December, 2018. In fact, they struck the work before the said date. Is the strike illegal ? Discuss.

(b) Discuss the Judicial activism in reference to The Contract Labour (Regulation and Abolition) Act, 1970. Also explain the jurisdiction of Industrial Tribunals to abolish Contract Labour. (6 marks each)

Answer 2(a)

Yes, the strike is illegal. As per Section 22 of Industrial Dispute Act 1947, no person employed in a public utility service shall go on strike in breach of contract -

a) without giving to the employer notice of strike, as herein- after provided, within six weeks before striking; or

b) within fourteen days of giving such notice; or

c) before the expiry of the date of strike specified in any such notice as aforesaid; or

d) during the pendency of any conciliation proceedings before a conciliation officer and seven days after the conclusion of such proceedings.

Section 24 of the Industrial Disputes Act, 1947, lays down that, a strike shall be illegal if, it is commenced or declared in contravention of Section 22 or Section 23.

The strike shall be illegal if, it is commenced or continued in public utility service like the Airlines, within fourteen days of giving such notice of strike.

In this case, the workmen struck before the expiry of the date of strike specified in the notice which is in contravention of sub-section (c) of Section 22 of the Industrial Disputes Act, 1947.

Therefore, the strike is illegal.

Answer 2(b)

The Courts took very active role in interpreting and favouring of the abolition of the Contract Labour and regulating the rights of the Contract Labour.

The first of it is the landmark judgment in *Standard Vacuum Refining Company* vs. *Its Workmen* (1960) in which the Supreme Court had affirmed the direction of the Industrial Tribunal for the abolition of the Contract system of labour. Further, the judgment of the Supreme Court in this historic case said that the Contract labour should not be employed where-

(i) The work is perennial and goes on from day to day.

(ii) The work is necessary for the factory.

(iii) The work is sufficient to employ a considerable number of whole time workmen and

(iv) The work is being done in most concerns through regular workmen.

Further in *Catering Cleaners of Southern Railway* vs. *Union of India & Ors.*, AIR 1987 SC 777 the Supreme Court expressed in dismay with reference to contract labour engagement as follows:

"Of late there has been a noticeable tendency on the part of big companies including public sector companies to get the work done through contractors rather than through their own departments".

"It is a matter of surprise that employment of contract labour is steadily on the increase in many organized sectors including the public sector which one expects to function as model employer".

From the above, it can be inferred that the Courts are also of the view that the contract labour engagement shall be abolished over a period of time as it leads to the abuse of labour rights for the economic benefit of the employers and is used mainly to depart from the responsibilities being an employer towards the employees.

Jurisdiction of Industrial Tribunals to abolish Contract Labour:

It has been held by the Supreme Court in *Vegolis Private Ltd.* vs. *The Workmen (1971)* that after enforcement of the Contract Labour (Regulation and Abolition) Act, 1970, the sole jurisdiction for abolition of Contract labour in any particular operation vested with the appropriate Government and thereafter the Tribunals have no jurisdiction to abolish contract labour. Supreme Court cannot under Article 32 of the Constitution order for abolition of Contract Labour System in any establishment (1985).

Question 3

(a) What Penalties are imposed for appointment of Child & Adolescent Labour in The Child & Adolescent Labour (Prohibition & Regulation) Act, 1986.

(b) An employee who is 'laid-off by his employer at Dadar, Mumbai refuses to accept an alternative employment, offered in another establishment situated of Sion in Mumbai, belonging to the some employer. Is the employee entitled to claim 'Lay-off' Compensation? (6 marks each)

Answer 3(a)

Whoever employs any Child or permits any child to work in contravention of the provisions of Section 3 of the Child & Adolescent Labour (Prohibition and Regulation) Act, 1986 shall be punishable with imprisonment for a term which shall not be less than six months but which may extend to two years,or with fine which shall not be less than twenty thousand rupees but which may extend to fifty thousand rupees, or with both.

However, the parents or guardians of such children shall not be punished unless they permit such child for Commercial purposes in contravention of the provisions of Section 3.

Whoever employs any adolescent or permits any adolescent to work in contravention of the provisions of Section 3A shall be punishable with imprisonment for a term which shall not be less than six months but which may extend to two years or with fine which shall not be less than twenty thousand rupees but which may extend to fifty thousand rupees, or with both. However, the parents or guardians of such adolescent shall not be punished unless they permit such adolescent to work in contravention of the provisions of Section 3A.

The parents or guardians of any child or adolescent shall not be liable for punishment, in case of the first offence. Whoever, having been convicted of an offence under Section 3 or Section 3A of the Act commits a like offence afterwards; he shall be punishable with imprisonment for a term which shall not be less than one year but which may extend to three years.

The parents or guardians having been convicted of an offence under Section 3 or Section 3A, commits a like offence afterwards, he shall be punishable with a fine which may extend to ten thousand rupees.

Contravention of the provisions of Section 3A of the Act shall be punishable with imprisonment for a term which shall not be less than six months but which may extend to two years or with fine which shall not be less than twenty thousand rupees but which may extend to fifty thousand rupees, or with both.

Answer 3(b)

The workman is not entitled to claim “Lay-off" Compensation. Section 25E of the Industrial Disputes Act,1947, lays down that, no compensation shall be paid to a workman who has been laid-off, if he refuses to accept any alternative employment in any other establishment belonging to the same employer situate in the same city, town or situate within a radius of 5 miles from his previous employment, provided that such alternative employment does not call for any special skill or previous experience and can be done by the workman and the wages are protected,i.e., the same wages would be paid to workman in such alternative employment also.

In this case, it is not clear whether same wages are offered to the workman or not. Assuming that the wages would be protected, the alternative employment belongs to the same employer and it is within the same city of Mumbai. On these grounds, the workman is not entitled to claim compensation for lay-off.

Question 4

(a) "Audit under labour laws is new concept, which is necessitated, in direct consequence of its non-compliance in large scale". Explain this statement and list out the areas to be checked/verified the Auditor under Factories Act, 1948 of an Industrial Organization.

(b) "Under the Maternity Benefit Act, 1961, women employees are entitled to maternity benefit at the rate of average daily wage for the period of their actual absence up to 26 weeks due to the delivery". In this connection, is it necessary for a working woman to give notice to its employer for maternity benefit ? (6 marks each)

Answer 4(a)

Audit under Labour Legislations is an effective tool for compliance management of labour legislations.It helps to detect non-compliance of various labour laws applicable to an organization and to take corrective measures. The objective of labour audit is to protect the interests of all the stakeholders. This leads to better Governance and value creation for the organization and avoids any unwarranted legal actions against the organization and its management.

Labour Audit is a process of fact finding. It is a continuous process. Labour Audit will ensure a win-win situation for all interested parties. Initially the employers may frown at the idea of such Audits, but with passage of time, the compulsion of labour audit will infuse self-regulation amongst the employers.

The illustrative areas to be checked /verified by Auditor under Factories Act, 1948 compliance are:

- Whether the factory is registered or not? If so, registration number of the factory be given.
- Item of manufacture.
- Whether hazardous industry or not if so steps suggested by appropriate government for safety have been complied with in toto.
- Whether Chapter IV on Safety has been complied with or not.
- Whether Chapter V on Welfare has been taken care of.
- Whether working hours are in accordance with the provisions of the Act.
- Maintenance of proper records of Attendance and Leaves.
- Provisions relating to employment of women, young person's etc. are duly complied with.

Answer 4(b)

Section 6 of the Maternity Benefit Act, 1961 deals with notice of claim for maternity benefit and payment thereof. Any woman employed in an establishment and entitled to maternity benefit under the provisions of this Act may give notice in writing in prescribed form, to her employer, stating that her maternity benefit and any other amount to which she may be entitled under this Act may be paid to her or to such person

as she may nominate in the notice and that she will not work in any *establishment during the period for which she receives maternity benefit.*

In the case of women who is pregnant, such notice shall state the date from which she will be absent from work, not being a date earlier than six weeks from the date of her expected delivery. Any woman who has not given the notice when she was pregnant may give such notice as soon as possible after the delivery.

On receipt of the notice, the employer shall permit such woman to absent herself from the establishment during the period for which she receives the maternity benefit. The amount of maternity benefit for the period preceding the date of her expected delivery shall be paid in advance by the employer to the woman on production of such proof, that the woman is pregnant and the amount due for the subsequent period shall be paid by the employer to the woman within forty-eight hours of production of such proof as may be prescribed that the woman has delivered a child.

Question 5

(a) The concept of Social Justice is so innate and demonstrated in the Industrial Laws of our country". Explain the statement.

(b) "The Primary Objective of International Labour Organization (ILO) is to deal with issues related to Labour, namely, maintaining International Labour Standards, ensuring social protection and providing work opportunities to all".

Based on the above statement, explain the important tasks of the "International Parliament of Labour".

(c) "One of the important measures to be taken by Factories for Health, Safety and Welfare of the workers is 'Ventilation and Temperature' in the work environment". Explain the statutory provisions in this regard under Factories Act, 1948.

(d) "Building and Other Construction Workers (Regulation of Employment and Conditions of Service) Act, 1996 (BOCW) was enacted to regulate the employment and conditions of service and to provide for safety, health and welfare measures for crores of building and other construction workers in the country". One of the welfare measure to the workers by the builders is "Accommodation". Explain the statutory provisions in this regard as per the Act.

(3 marks each)

Answer 5(a)

The concept of social justice is so innate and demonstrated in the industrial laws of our country. As proclaimed in the Preamble of the Constitution and the Directive Principles of State Policy, the industrial jurisprudence of the country is founded on the basic idea of socio-economic equality and its aim is to assist the removal of socio-economic disparities and inequalities. The laws particularly the Industrial Laws of the country revolve on this basic philosophy of the Constitution.

The concept of social justice is though not limited to any particular branch of legislation although it is more prominent and conspicuous in industrial laws and relations. Its scope is comprehensive and is founded to the basic ideals of social economic equality and it aims at assisting the removal of social economic disparities and inequalities of

birth and the competing claims especially between the employers and workers by finding a just fair and equitable solution to their human relation problem, so that peace, harmony and collection of the highest order prevails among them which may further the growth and progress of nations. (Mahesh Chandra, 'Industrial Jurisprudence' (1976. P.47).

Answer 5(b)

The International Labour Conference often called as International Parliament of Labour performs the following important tasks:

- The crafting and adoption of international labour standards in the form of Conventions and Recommendations.
- The Conference supervises the application of Conventions and Recommendations at the national level.
- The Conference also examines the Global Report prepared by the office as a procedural act required by the declaration.
- The Conference acts as a stage for the discussion of questions relating to social and labour issues. The central theme of discussion each year is the report presented by ILO's director general.
- It passes resolutions for setting up guidelines for ILO's future deliberations and activities.

Answer 5(c)

Ventilation and temperature

Section 13 of the Factories Act, 1948 provides that every factory should make suitable and effective provisions for securing and maintaining :

(1) adequate ventilation by the circulation of fresh air; and

(2) such a temperature as will secure to the workers reasonable conditions of comfort and prevent injury to health. What is reasonable temperature depends upon the circumstances of each case.

The State Government has been empowered to lay down the standard of adequate ventilation and reasonable temperature for any factory or class or description of factories or parts thereof. It may direct that proper measuring instruments at such places and in such position as may be specified shall be provided and prescribed records shall be maintained.

Measures to reduce excessively high temperature:

To prevent excessive heating of any workroom following measures shall be adopted:

(i) walls and roofs shall be of such material and so designed that such temperature shall not be exceeded but kept as low as practicable;

(ii) where the nature of the work carried on in the factory involves, or is likely to involve, the production of excessively high temperatures,such adequate measures as are practicable shall be taken to protect the workers there from, by separating

the process which produces such temperatures from the workroom, by insulating the hot parts or by other effective means.

The Chief Inspector is empowered to direct any factory to adopt such methods which will reduce the excessively high temperature. In this regard, he can specify the measures which in his opinion should be adopted.

Answer 5(d)

Accommodation

According to Section 34 of the Building and Other Construction Workers (Regulation of Employment and Conditions of Service) Act, 1996, it shall be duty of the employer to provide, free of charges and within the work site or as near to it as may be possible, temporary living accommodation to all building workers employed by him for such period as the building or other construction work is in progress.

Such temporary accommodation shall have separate cooking place, bathing, washing and lavatory facilities.

As soon as may be, after the building or other construction work is over, the employer shall, at his own cost, cause removal or demolition of temporary structures so erected by him and restore the ground in good level and clean condition.

In case an employer is given any land by a Municipal Board or any other local authority for the purposes of providing temporary accommodation for the building workers under this section, he shall, as soon as may be after the construction work is over, return the possession of such land in the same condition in which he received the same.

Question 6

The Code on Wages, 2019 amalgamate, simplify and rationalize the relevant provisions of the following four Central Labour enactments relating to wages, namely :

(i) The Payment Wages Act, 1936

(ii) The Minimum Wages Act, 1948

(iii) The Payment of Bonus Act, 1965; and

(iv) The Equal Remuneration Act, 1976.

Based on the above enactment of the Code, answer the following questions :

(a) How is the wages fixed for an employee working overtime ?

(b) What are the conditions for fixing the minimum wages ?

(c) When deduction can be made from wages ?

(d) What is not included in wages ? *(3 marks each)*

Answer 6(a)

Under Section 14 of the Code on Wages, 2019, where an employee whose minimum rate of wages has been fixed under the Code by the hour, by the day or by such a longer

wage-period as may be prescribed, works on any day in excess of the number of hours constituting a normal working day, the employer shall pay him for every hour or for part of an hour so worked in excess, at the overtime rate which shall not be less than twice the normal rate of wages.

Answer 6(b)

Under Section 6 of the Code on Wages, 2019, the appropriate government (Central or State) shall fix a minimum rate of wages based on time work or piece work. While fixing the minimum wages, the government may take into account factors such as, skill of workers, and difficulty of work.

Also, by Section 8 of the Code, the minimum wages shall be revised and reviewed by Central or State Government at intervals of not more than Five Years.

Answer 6(c)

According to Section 18 of the Code on Wages, 2019, there shall be no deductions from the Wages of the employee's. But in the following cases deduction can be made which is explained in Section 18(2) of the Code they are:

(i) Fines imposed on him; or

(ii) Absence from duty; or

(iii) Damage to or loss of goods which was entrusted to him for custody; or

(iv) House accommodation provided by the employer; or

(v) For amenities and services provided for the employee.

These deductions should not exceed 50 percent of the employee's total wage.

Answer 6(d)

The definition of Wages excludes bonus payable to employees, value of house accommodation and utilities, any travelling allowance, employer contribution to pension and provident fund, any special expenses, award or settlement, overtime allowance, commission payable to employee,and gratuity payable on termination of the employment. The specified exclusion however may not exceed 50 percent of all remuneration and if exceeding, that amount shall be deemed as remuneration and will be considered as Wages.

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VALUATIONS & BUSINESS MODELLING

(Elective Paper 9.7)

Time allowed : 3 hours *Maximum marks : 100*

***NOTE** : 1. Answer ALL Questions.*

2. Working notes should form part of answer.

PART A

Question 1

LHC is a major hotel chain. The company operates 35 hotels of which 14 are owned by it and the rest are owned by others but managed by LHC.

LHC's operating revenues and expenses for the just concluded year (year 0) were as follows :

Particulars	*₹ in Million*
Operating Revenues	
Room rent	*1043*
Food and beverages	*678*
Management fee for managed properties	*73*
Operating Expenses	
Materials	*258*
Personnel	*258*
Upkeep and services	*350*
Sales and general administration	*350*
Assets	
Net fixed assets (Gross Block 2110, Dep 600)	*1510*
Net current assets	*516*
Liabilities	
Net worth	*1126*
Debt	*900*

LHC has no non-operating assets.

At the beginning of year 0, LHC owned 2190 rooms. It has planned the following additions for next 7 years. Most of the land needed by the company for these additions has been already acquired.

Year	*Rooms (in numbers)*	*Investment in ₹ Millions*
1	*90*	*200*
2	*130*	*300*
3	*80*	*240*
4	*130*	*500*
5	*186*	*800*
6	*355*	*1400*
7	*150*	*1300*

A good portion of investment in year 7 would be towards purchase of land. It is assumed that the addition will take place at the beginning of the year. For developing the financial projections of LHC, the following assumptions may be made:

(i) the occupancy rate will be 60% for year one and thereafter it will increase by 1% per year for next 6 years.

(ii) the average room rent per day will be ₹2500 for year one and it is expected to increase at the rate of 15% per year till year 7.

(iii) food and beverage revenue is expected to be 65% of the room rent.

(iv) material expenses, personal expenses, upkeep & service expenses, and sales & general administration expenses will be respectively 15, 15, 18 and 18 percent of the revenues excluding the management fee.

(v) working capital investment is expected to be 30% of the revenue from owned properties.

(vi) the management fee for the managed properties will be 7% of room rent. Room rent from managed properties will be equal to the room rent from owned properties.

(vii) depreciation is expected to be 7% of net fixed assets.

(viii) effective tax rate 20%.

The market value of equity at the end of year zero is ₹3050 million. The imputed market value of debt is ₹900 million.

Stock has a beta 0.921.

Risk free rate of return is 12% and the market risk premium is 8%.

Post tax cost of debt is 9%.

FCF is expected to grow at a rate of 10% per annum after 7 years.

(a) Build projections for next 7 years. *(10 marks)*

(b) Calculate cost of equity and weighted average cost of capital (WACC). *(7 marks)*

(c) What is the terminal value at the end of explicit forecast period ? (5 marks)

(d) Calculate enterprise value by using DCF method. (12 marks)

(e) Calculate equity value. (6 marks)

Answer 1

(a) Build projections for next 7 years

Rs. in Million

Particulars		*1*	*2*	*3*	*4*	*5*	*6*	*7*
A.	Rooms (in numbers)	2280	2410	2490	2620	2806	3161	3311
B.	Occupancy rate	60%	61%	62%	63%	64%	65%	66%
C.	Average room rent	2500	2875	3306	3802	4373	5028	5783
D.	Room rent from owned properties	1248	1543	1863	2291	2867	3771	4613
E.	Food and beverage revenues	811	1003	1211	1489	1864	2451	2998
F.	Revenue from owned properties (D+E)	2059	2546	3074	3780	4731	6222	7611
G.	Management fee from management properties	87	108	130	160	200	264	323
H.	Total Revenue (F+G)	2146	2654	3204	3940	4931	6486	7934
I.	Material expenses	309	382	461	567	710	933	1142
J.	Personnel expenses	309	382	461	567	710	933	1142
K.	Upkeep and service expenses	371	458	553	680	852	1120	1370
L.	Sales and general admin expenses	371	458	553	680	852	1120	1370
M.	Total operating expenses	1360	1680	2028	2494	3124	4106	5024
N.	EBIDT (H – M)	786	974	1176	1446	1807	2380	2910
O.	Depreciation	120	132	140	166	210	293	329
P.	EBIT	666	842	1036	1280	1597	2087	2581
Q.	Net operating profit after taxes	533	674	829	1024	1278	1670	2065
R.	Gross cash flow (Q + O)	653	806	969	1190	1488	1963	2394
S.	Gross investment (Fixed Assets + Current Assets)	302	446	398	712	1085	1848	1716
T.	Free cash flow from operations (R-S)	351	360	571	478	403	115	678
U.	Net current assets	618	764	924	1134	1419	1867	2283
V.	Net current assets addition	102	146	158	212	285	448	416
W.	Gross block	2310	2610	2850	3350	4150	5550	6850
X.	Capital expenditure	200	300	240	500	800	1400	1300
Y.	Accumulated depreciation	720	852	984	1150	1360	1653	1982
Z.	Net block	1890	1998	2366	3000	4190	4697	4868
AA.	Depreciation	120	132	140	166	210	293	329

(b) Cost of Equity = 12 + 0.921 (8) = 19.37%

Cost of Debt is 9%

WACC based on Market Values

(3050 / 3950) * 19.37 + (900 / 3950) * 9%

= 17%

(c) Terminal Value

$$= \frac{678\,(1.10)}{0.17 - 0.10}$$

= Rs. 10654 million

(d) Enterprise Value

FCF on DCF Method

$$\frac{351}{(1.17)} + \frac{360}{(1.17)^2} + \frac{571}{(1.17)^3} + \frac{478}{(1.17)^4} + \frac{403}{(1.17)^5} + \frac{115}{(1.17)^6} + \frac{678}{(1.17)^7} + \frac{10654}{(1.17)^7}$$

= Rs. 5179 Million

(e) Calculate equity value

Enterprise value – market value of debt + cash & cash equivalents

= 5179 – 900

= **Rs. 4279 Million**

Question 2

(a) The equity stock of Lex Ltd. is currently selling for INR 30 per share. The dividend expected next year is INR 2 per share. The required rate of return by investors on this stock is 15%. If the constant growth model is applied to Lex Ltd., what is the expected growth rate ? *(5 marks)*

(b) The balance sheet of W Ltd. at the end of year zero is as follows :

₹ in crore

Liabilities		*Assets*	
Shareholders funds		*Net fixed assets*	*550*
Equity capital (20,00,00,000 shares of ₹10 each)	*200*	*Networking capital*	*200*
Reserves and surplus	*300*		
Loan funds (rate 10%)	*250*		
Total	*750*	*Total*	*750*

The return on assets (Net Operating Profit After Taxes (NOPAT)) is expected to be 18% on the asset value at the beginning of each year. The growth rate in assets and revenues will be 30% for the first 3 years, 18% for the next 2 years and 10% thereafter. The effective tax rate of the firm is 34%. The pre tax cost of debt is 10%. The cost of equity is 24%. The debt equity ratio of the firm will be maintained at 1 : 2.

(i) Calculate FCF.

(ii) Calculate weighted average cost of capital. *(5 marks)*

Answer 2(a)

According to the constant growth model

$$P_0 = \frac{D_1}{r - g}$$

Where,

P_0 = Current stock price

g = Constant growth rate expected for dividends, in perpetuity

r = Constant cost of equity capital for the company (or rate of return)

D_1 = Value of next year's dividends.

This means:

$$g = r - \frac{D_1}{P_0}$$

$$= 0.15 - \frac{2}{30}$$

= 8.3 percent

Answer 2(b)

(i) Calculate FCF

(Rs. in crore)

Year	*1*	*2*	*3*	*4*	*5*	*6*
1. Asset value (beginning)	750	975	1267.50	1647.75	1944.35	2294.33
2. NOPAT	135	175.50	228.15	296.60	349.98	412.98
3. Net investment (% on opening Fixed Assets)	225	292.50	380.25	296.60	349.98	229.43
FCF (2-3)	(90)	(117)	(152.1)	-	-	183.55
Growth rate (%)	30%	30%	30%	18%	18%	10%

(ii) Calculate weighted average cost of capital

WACC = (2/3) X 24 + (1/3) X (10 (1 – 0.34) = 18.2

Question 3

(a) State whether the under given statements are true or false assuming that all variables are constant except for the variable discussed below :

(i) As the discount rate increases, the value of an asset increases.

(ii) As the perpetuity growth rate increases, the value of an asset increases.

(iii) As the life of an asset is lengthened, the value of that asset increases.

(iv) As the uncertainty about the expected cash flow increases, the value of an asset increases.

(v) Asset with an infinite life will have an infinite value.

(b) Write down the three approaches to valuation. Is it mandatory for the valuer to consider all three approaches ? Which approach a valuer should choose ?

(5 marks each)

Answer 3(a)

(i) False

(ii) True

(iii) True

(iv) False

(v) False

Answer 3(b)

There are three approaches to valuation, i.e., asset approach, market approach and income approach. It is mandatory for the valuer to consider all three approaches. However, it is not mandatory for the valuer to apply all three approaches.

The choice of approach or weightage to results arrived at by each of the approach is subject to valuer's judgment. The valuer must apply judgment in a rationale manner and disclose his rationale in the valuation report.

Question 4

(a) The risk free return is 6% and the expected return on market portfolio is 15%. If the required return on stock is 18%, what is beta?

(b) Arihant EdTech has started a web portal for online education and is at an early stage of business. It desires to value its business. List down the methods it can adopt for valuation along with a short write up on each. *(5 marks each)*

Answer 4(a)

$R_A = R_F + \text{beta } (R_M - R_F)$

Where,

R_F = Risk Free Return

R_m = Expected Return on Market Portfolio

R_A = Required Rate of Return

0.18 = 0.06 + beta (0.15 – 0.06)

$$\text{Beta} = \frac{0.18 - 0.06}{0.15 - 0.06}$$

$$= \frac{0.12}{0.09}$$

= 1.33

Answer 4(b)

Arihant EdTech is a start-up. There are several methods available to it so as to value its business. A list of the methods along with brief description is as under:

1. **Income approach** : It is a valuation approach that converts maintainable or future amounts to a single current amount. The value measurement is determined on the basis of the value indicated by current market expectations about those future amounts.

2. **Cost approach** : It is a validation approach that reflects the amount that would be required currently to replace the service capacity of an asset. A valuer applies cost approach in case income approach cannot be used.

3. **Venture Capital method** : Venture capital method is one of the globally acceptable methodology in estimating the value of a start-up. In this method the value of start-up is done from the venture capital point of view. It indicates the value of pre-money ventures by following the process that VCs go through where, they exit an investment within 3 to 7 years.

4. **First Chicago method** : The first Chicago method is one of the context specific valuation methodologies which consider pay outs to the investors during the holding period. This method takes into consideration three scenarios: success, failures and survival case and associate probability to each case to find weighted average price of start-up business.

5. **Adjusted Discounted Cash Flow method** : This method is a scientific tool used to judge the value of start-up on the basis of its potential which is converted in the form of cash flow and adjusted with differential discount rates based upon the risk perception of a start-up entity.

6. **Rule of Thumb** : Rule of thumb or benchmark indicator is used as a reasonable check against the values determined by the use of other valuation approaches in a valuation engagement. It is technically not a valuation method but still used as a rationality check against the values determined by use of other valuation approaches.

7. **Berkus method** : According to super Angel investor Dave Berkus, the Berkus

method "assigns a number, a financial valuation, to each major elements of risk faced by all young companies after crediting the entrepreneur the basic value for the quality and potential of the idea itself". The Berkus method uses both qualitative and quantitative factors for valuation.

8. **Scorecard Validation method** : It is also known as Bill Payne Valuation method and is one of the most preferred methodologies used by the Angel investors. This method compares the start-up to other funded start-ups modifying the average valuation based on factors such as region, market and stage.

PART B

Question 5

(a) As a business modelling consultant you are required to suggest suitable business model to your client. In this scenario what are the key components you're going to explain to them before finalising the business model?

(b) List down the business models for a start-up business. Write a short note on "On demand model".

(c) Explain the business model followed by Netflix. *(5 marks each)*

Answer 5(a)

The key components of a business model are as under:

1. **High Level Vision** : A basic description of any business model, i.e., couple of sentences which describe the big picture and overall intent of the promoters.
2. **Key Objectives** : The top goals and plan to measure them.
3. **Customer targets and challenges** : The types of customers who will purchase the solution, along with their exact pain points.
4. **Pricing** : How will you package your solution and what it will cost.
5. **Messaging** : A clear and compelling message that explains your solution is worth buying.
6. **Go to market** : The channels that you will use to market and sell to your customers.
7. **Investment** : The costs required to be incurred to make the solution a success.
8. **Growth opportunity** : The ways that you will grow the business, including key partnerships if you need them.

Answer 5(b)

There are nine business models for a start-up business. They are as under:

i) Become the middleman

ii) Become a marketplace.

iii) The subscription model

iv) Customize everything.

v) On-Demand model.

vi) The modernized direct sales model.

vii) Freemium model.

viii) Reverse auction

ix) Virtual Good model.

As the world speeds up, consumers have adopted preference for instant gratification. The on demand economy has a growing appetite for greater convenience, speed and simplicity. Smartphones have driven transformational shifts in how we consume goods and services and many consumers have become acclimated to purchasing at the press of a button. On demand start-ups like UBER are shaking up their industries and also provide stead contracted work for consumers who want to become solo-preneurs.

Start-up HANDY has also seen explosive growth by providing handymen at a moment's notice servicing need for consumers that was not previously available for solutions where a consumer cannot wait a few days to fix problem in their home.

Answer 5(c)

Netflix follows the business model of "the subscription model". Mobile payments continue to rise in popularity and consumers are trending towards a more simple hassle free kind of shopping experience. These trends are leading towards explosive growth in subscription based services that customers can easily set up and then not worry about knowing they will receive their product or services every month.

The other example for this model user is "dollar shave club" that is one of those simple subscription services that made it much easier for men to not worry about running out of razors and save money. Add in some crazy well message commercials with hilarious spokesperson and you have a brand who continues to double and even triple revenues annually.

The business model provides an optimal balance of value to both the start-up and the customer. It is simple and convenient for customers and take a lot of thinking out of the purchasing process. Customers know they will receive their product every month around the same time and don't have to worry about pre orders and know they will get a set, flat rate that will stay within a budget.

On the start-up end the value lies in being able to predict revenues through recurring sales which is incredibly advantageous for a company's valuation. This enhances the saleability of the company, increasing the attractiveness to potential VCs (venture capitalists) and buyers and often leads to valuations up to 8 times that of a similar business with little recurring revenues.

Question 6

(a) Prepare cash flow statement from the table and information given below:

₹

Liabilities	*31st March, 2000*	*31st March, 2001*	*Assets*	*31st March, 2000*	*31st March, 2001*
Share Capital	*4,50,000*	*4,50,000*	*Fixed assets*	*4,00,000*	*3,20,000*
General Reserve	*3,00,000*	*3,10,000*	*Investments*	*50,000*	*60,000*
Profit & Loss	*56,000*	*68,000*	*Stock*	*2,40,000*	*2,10,000*
Creditors	*1,68,000*	*1,34,000*	*Debtors*	*2,10,000*	*4,55,000*
Provision for Tax	*75,000*	*10,000*	*Bank Balances*	*1,49,000*	*1,97,000*
Mortgage	*—*	*2,70,000*			
	10,49,000	*12,42,000*		*10,49,000*	*12,42,000*

Additional Information:

(i) Investments costing ₹8,000 were sold during the year 2000-2001 for ₹ 8,500.

(ii) Provision for tax made during the year was ₹9,000.

(iii) During the year, part of the fixed assets costing ₹10,000 was sold for ₹12,000, profit was included in the profit and loss account.

(iv) Dividends paid during the year amounted to ₹40,000. (7 marks)

(b) Explain the concepts of percentage of sales method and regression analysis method in estimating working capital with the help of suitable examples. (4 marks)

(c) A banker is reviewing your proposal for grant of long term loan and working capital facilities. What are the key ratios he is likely to review to assess serviceability of the credit facilities? Also provide formulas for at least three key ratios. (4 marks)

Answer 6(a)

Cash flow statement for the year ended March 31st, 2001

Particulars	*Amount (Rs.)*	*Amount (Rs.)*
(A) Cash flow from operating activities		
Profit made	12,000	
Add : Non cash or non-operating items		
Interim dividend	40,000	
Provision for tax	9,000	
Transfer to reserve	10,000	
Net profit before tax and extraordinary items		71,000

Add : Depreciation	70,000	
Less : Profit on sale of investments	(500)	
Less : Profit on sale of fixed assets	(2,000)	
Operating profit before working capital changes		1,38,500
Add : Decrease in current assets and increase in current liabilities		
Decrease in stock	30,000	
Less : Increase in current assets and decrease in current liabilities		
Increase in debtor	(2,45,000)	
Decrease in creditor	(34,000)	(2,49,000)
Cash generated from operations		(1,10,500)
Less : Income tax paid		(74,000)
Net cash used in operating activities		**(1,84,500)**
(B) Cash flow from investing activities		
Purchase of investments	(18,000)	
Sale of fixed assets	12,000	
Sale of investments	8,500	
Net cash flow from investing activities		**2,500**
(C) Cash flow from financing activities		
Mortgages loan	2,70,000	
Dividend paid	(40,000)	
Net cash flow from financing activities		**2,30,000**
Increase in cash and cash equivalents (A+B+C)		48,000
Cash and cash equivalents at the beginning of the year		1,49,000
Cash and cash equivalents at the end of the year		1,97,000

Working Notes

Investment Account

Particulars	*Amount (Rs.)*	*Particulars*	*Amount (Rs.)*
To Balance b/d	50,000	By Bank	8,500
To Profit	500		
To Bank (Purchase)	18,000	By Balance c/d	60,000
	68,500		68,500

Fixed Assets Account

Particulars	*Amount (Rs.)*	*Particulars*	*Amount (Rs.)*
To Balance b/d	4,00,000	By Bank	12,000
To Profit	2,000	By Depreciation (Balance)	70,000
		By Balance c/d	3,20,000
	4,02,000		4,02,000

Provision for Taxation A/c

Particulars	*Amount (Rs.)*	*Particulars*	*Amount (Rs.)*
To Cash (Tax Paid)	74,000	By Balance b/d	75,000
To Balance c/d	10,000	By P& L	9,000
	84,000		84,000

Answer 6(b)

1. **Percentage of sales method** : This method of estimating working capital requirements is based on the assumption that the level of working capital for any firm is directly related to its sales value. If past experience indicates stable relationship between the amount of sales and working capital then this basis may be used to determine the requirements of working capital for future. For example, if sales for the year 2020 amounted to Rs. 30,00,000 and working capital required was Rs. 6,00,000, the requirement of working capital for the year 2021 on an estimated sales of Rs. 40,00,000 will be Rs. 8,00,000 that is 20% of Rs. 40,00,000.

   The individual items of current assets and current liabilities can also be estimated on the basis of past experience as a percentage of sales. This method is simple to understand and easy to operate but it cannot be applied in all cases because the direct relationship between sales and working capital may not be established.

2. **Regression analysis method** : This method of forecasting working capital requirements is based upon the statistical technique of estimating or predicting the unknown value of a dependent variable from the known value of an independent variable. It is the measure of the average relationship between two or more variables that is sales and working capital in terms of the original units of the data.

   The relationship between sales and working capital are presented by the equation:

   $Y = a + bx$

   Where y = working capital

   a = intercept of the least square

   b = slope of the regression line

   x = sales

Answe 6(c)

A banker is likely to review the following ratios:

(i) Current Ratio = Current Assets / Current Liabilities.

(ii) Quick Ratio = (Current Assets – Inventory) / Current Liabilities.

(iii) Debt Equity Ratio = Debt : Equity, i.e., Total liabilities / Total shareholders' equity.

(iv) Interest Service Coverage Ratio = Earnings before interest and depreciation / Interest.

(v) Debt Service Coverage Ratio =

Earnings before interest and depreciation / Interest + Current portion of long-term debt.

OR

Debt Service Coverage Ratio =

Net Operating Income / Total Debt Service

where:

Net Operating Income=Revenue-COE

COE=Certain operating expenses

Total Debt Service=Current debt obligations

***

INSOLVENCY -LAW & PRACTICE

(Elective Paper 9.8)

Time allowed : 3 hours *Maximum marks : 100*

NOTE: *Answer **ALL** Questions.*

Question 1

Read the following carefully and answer the questions given at the end :

Pine Food Industries Limited ("PFIL") is one of the top FMCG player and listed entity in India. It is a leading manufacturer and marketer of various edible oils, food products and eatables. Its Authorized Capital is Rs. 252.00 crore and Paid-up Capital is Rs. 65.00 crore. PFIL has borrowed from various Banks and Financial institutions in India and its borrowings were around Rs. 12,000 Crore.

Due to unprecedented crash in global prices of the oil seeds coupled with falling revenues in the oil business gave a crippling blow to PFIL.

AB Bank and BC Bank filed an application under section 7 of the Insolvency and Bankruptcy Code, 2016 ("Code") for initiating the insolvency resolution process against PFIL (hereinafter called as the Corporate Debtor ("CD")). After hearing both the parties, National Company Law Tribunal ("NCLT") admitted the petition filed. The Financial Creditor proposed the name of Kapoor to act as Interim Resolution Professional ("IRP").

An application was filed before NCLT by one of the creditors who made a claim before the Resolution Professional ("RP") stating that the CD owed to pay USD 10.00 crore, based on the Bills of Exchanges, ordering the CD to pay this creditor for the goods supplied by another party. On making of such claim before the RP, it has been rejected by him saying that it is not a Financial Debt as it is an Operational Debt therefore, it could not be considered as Financial Debt as claimed by applicant therein.

Vijay Kumar Jain, suspended Director of the CD, filed an application before the NCLT under section 60(5) of the Code seeking an order for setting aside the decision taken by the Committee of Creditors ("CoC") disallowing the erstwhile representatives of the Corporate Debtor including Vijay to participate in the CoC meetings; declare that the CoC meeting is non est; direct the RP to ensure active participation of the applicant in the meetings of CoC; provide all the documents and information to the applicant.

RP filed application in NCLT under section 43(1) of the Code for seeking reversal of the amounts that were debited from the current accounts of the CD maintained with XYZ Bank which had been debited by the XYZ Bank before the insolvency commencement date and were utilized against the payment of the dues owed by the CD to a Bank in relation to the Letter of Credit issued by them.

The RP submits that the payment of the impugned amount lead to preferential treatment towards XYZ Bank by the CD as such payment has the effect of putting

Respondents (i.e. XYZ Bank) in a beneficial position than it would have been in liquidation of the CD in accordance with Section 53 of the Code. It is further stated by the RP that the payments of the impugned amount by the Corporate Debtor were not in the "ordinary course of business" of the CD.

NCLT, vide its order, held that the respondent Bank, which had debited an amount aggregating to Rs. 65.98 crores from the current accounts of the Corporate Debtor is directed to reverse the said amount within 30 days from the date of the said order. Since the resolution plan is already submitted and under examination of the CoC without consideration of this amount, therefore the appropriation of this amount will be decided by the CoC. XYZ Bank filed appeal in NCLAT against the order of NCLT.

The main plea taken by the Appellant Bank is that the RP before filing an application under Section 43(1) of the Code formed no independent opinion nor afforded an opportunity to the Appellant to explain about the transactions in question.

The RP called for Expression of Interest ("EOI"). 28 prospective resolution applicants showed their interest out of which two prospective resolution applicants were rejected as one was disqualified under Section 29 A of the Code (being related party) and the other was a financial investor who did not meet the criteria in the EOI evaluation parameters.

The applicant reviewed the four Resolution Plans submitted by the Resolution Applicants and found that only the plans submitted by 2 Resolution Applicants (RA1 and RA2) provided for the corporate insolvency resolution of the Corporate Debtor as a whole and on a going concern basis.

The RP filed application under section 30(6) of the Code, seeking order for approval of the resolution plan for the Corporate Debtor submitted by the consortium led by PAL (RA2) as approved by the members of Committee of Creditors (CoC). The said resolution plan was approved by a vote share of 96.85%. RP filed application in NCLT for approval of Resolution Plan.

While the said application was pending for consideration before the NCLT, Hon'ble Supreme Court, in Vijay Kumar Jain Vs. Standard Chartered Bank & Ors pronounced the judgment. Under the Judgment of Hon'ble Supreme Court, the approval of the NCLT to the resolution plan of RA2 was interdicted. In compliance of the above-mentioned Hon'ble Supreme Court order, NCLT by its order directed as follows :

"Resolution Professional is directed to comply with the directions of the Hon'ble Supreme Court and submit the report within the stipulated time as provided by the Hon'ble Supreme Court."

Thereafter, NCLT approved the Resolution Plan submitted by RA2 and passed orders and directions on the reliefs and concession sought.

Since in Para 38, NCLT in their order rejected some of the relief sought, RA2 moved to NCLT for modification of order of NCLT.

In the application filed, RA2 had sought substitution of Para 38 of the order of NCLT approving the Resolution Plan of RA2 as under :

Existing Para

"38. Any relief sought for in the Resolution Plan, where the contract/agreement/ understanding/ proceedings/actions/notice etc is not specifically identified or is for future and contingent liability, is at this moment rejected."

Proposed Para

"All claims that were either not filed or not admitted during CIRP in terms of the provisions of the Insolvency and Bankruptcy Code, 2016 shall stand extinguished. Further, claims admitted/ verified by the Resolution Professional shall stand settled and extinguished as per the Resolution Plan."

Resolution Plan approved by NCLT of RA2 leads to a 60% haircut for the lenders. RA2 completed its acquisition of PFIL.

Referring decided case and relevant provisions of the Insolvency and Bankruptcy Code (IBC), 2016 and Rules and Regulations made thereunder, answer the following questions :

(a) Whether formation of Joint Lender Forum will have any bearing over filing of this case or not ? Brief, referring the provisions of IBC, 2016, who can initiate the case under the Code.

(b) In the instant case explain whether Vijay Kumar Jain succeeded in his contention. Referring Supreme Court's decision, discuss the role and position of suspended Board of Directors in the Committee of Creditors.

(c) Explain the decision of NCLAT in the aforesaid case filed by XYZ Bank for Section 43 transactions. Referring relevant provisions, brief against whom the application under Section 43 of the IB Code can be filed and what orders can be passed thereunder.

(d) Whether Resolution Applicant has powers to request for modification of NCLT's Order on Resolution Plan. Discuss whether NCLT has powers to modify or revise its own order made under the IB Code. (10 marks each)

Answer 1(a)

It has already been held by the Hon'ble NCLAT in the case of *Innoventive Industries Ltd.* vs. *ICICI Bank Ltd.* that Joint Lender Forum proceedings pending against the corporates debtor will not have any bearing on the cases initiated under Insolvency and Bankruptcy Code (IBC), therefore, this plea is hereby dismissed without having any further consideration on this point.

The corporate debtor counsel relied upon *IDFC Bank Ltd.* vs. *Ruchi Soya Industries (Born HC Com. Petition 570/2016*, *Central Bank of India* vs. *Ravindra (2002*) *1 sec 367, Essar Steel India Ltd.* vs. *RBI (SCA 12434 of 2017 dated 31.07.2017*) to say that when a scheme is proposed for settlement of the creditors dues, the creditors will have to wait for settlement of their dues, it is not correct proposition of law as against IBC proceedings for two reasons, one - a mechanism recommended by RBI Circular will not have any bearing on IBC proceedings owing to non-obstante clause present in Insolvency and Bankruptcy Code, it has been settled by Hon'ble NCLAT as well as Hon'ble Supreme Court in *Innoventive Industries Ltd.* vs. *ICICI Bank Ltd. (SC dated 31.08.2017) and this Bench in between Indian Bank vs. Varun Resources Ltd. (NCLT Mumbai dated 14.06.2017)* that RBI Circulars will not have any binding nature on the proceedings under IBC.

Based on the above, Joint application made by the Financial Creditors are allowed. Section 7(1) of the IBC also allows filing of joint application by the Financial Creditors.

The Following persons can initiate the case under IBC, in case of default:

Financial Creditors:

Financial creditors may either be secured creditors or unsecured creditors. The main difference between secured and unsecured financial creditors is that in the event of liquidation and asset distribution proceedings, secured creditors are given a higher priority than unsecured creditors.

When compared to operational creditors, the procedure for financial creditors to initiate insolvency proceedings is a lot easier.

The IBC allows financial creditors to make an application to the NCLT directly and such financial creditors will only need to show that there is a default.

It is also important to note that only financial creditors constitute the committee of creditors, and no operational creditor can be part of this committee.

Operational Creditor:

The term operational creditor has been defined under Section 5(20) of the IBC as any person to whom operational debt is owed or to whom such debt has been assigned.

Operational debt has been defined in the IBC as a claim in respect of the provision of goods or services, including employment or dues payable to any governmental authority.

An operational creditor, while filing an application for corporate insolvency resolution before the NCLT against an operational debtor, in addition to the requirements of proving default, will also have to prove that there is no dispute which exists between the operational creditor and the debtor with respect to the amounts due.

Corporate Debtor:

Under Section 6 of the IBC, the Company itself (being a corporate debtor) can initiate the Corporate Insolvency Resolution Process.

Answer 1(b)

In the case of *Vijay Kumar Jain* vs. *Standard Chartered Bank and others 2019 SCC online SC103*, The Hon'ble NCLT held that the directors have the right to attend the Committee of Creditor (COC) meetings as per Section 24 of the Insolvency and Bankruptcy Code (IBC).

However, the directors could not receive information that is considered confidential by the resolution professional or the COC, including the resolution plans.

In the first appeal, the decision of the NCLT was upheld by the Appellate Tribunal. The Director then moved the Supreme Court, challenging the decision of the Appellate Tribunal.

The Hon'ble Supreme Court held that the scheme of the Code makes it clear that the directors, though not members of the COC, have a right to participate in every meeting of the COC. In addition, for effective participation as vitally interested parties in discussion on resolution plans, they have the right to receive copies of the resolution plans presented to the COC.

The Hon'ble Supreme Court also clarified that under Regulation 21 (3)(iii) of the CIRP Regulations, the notice of the CoC meeting, which is required to be given to the directors as well must contain copies of all the documents relevant for matters to be discussed, including the resolution plans.

The Hon'ble Supreme Court considered the directors to be vitally interested on two counts:

1. Such directors are often guarantors and bound by the approved plan, which may scale down their own debts.

2. The directors, being well versed in the affairs of the company, may be able to assist the CoC on determining whether the resolution plan addresses the cause of default by the company (a mandatory requirement for resolution plans).

The Hon'ble Supreme Court also clarified that any concerns over breach of confidentiality may be alleviated by the resolution professional obtaining a confidentiality undertaking from the directors, which may also contain an indemnity to the resolution professional against any breach.

Of course, this judgement operates along with the judgments of the *Hon'ble Supreme Court in Swiss Ribbons Pvt. Ltd. & Anr.* vs. *Union of India and K. Sashidhar* vs. *Indian Overseas Bank & Ors.*, that have established the finality and non-justifiability of the decisions of the CoC as regards commercial feasibility and viability of a resolution plan. On a positive note, this will enhance transparency and openness in COCs. For now, the suspended directors, though they have no vote, have a seat on the table.

Answer 1(c)

In the case of Shailendra Ajmera, R.P. of *Ruchi Soya Industries Ltd.* vs. *ICICI Bank & Others*, Resolution Professional filed an application in NCLT, Mumbai Bench under section 43(1) of the Code for seeking reversal of the amounts that were debited from the current accounts of the Corporate Debtor (CD) maintained with ICICI Bank which had been debited by the ICICI Bank before the insolvency commencement date and were utilized against the payment of the dues owed by the CD to the ICICI in relation to the Letter of Credit issued by ICICI.

The Applicant submitted that the payment of the impugned amounts lead to preferential treatment towards it by the Corporate Debtor as such payment has the effect of putting Respondents in a beneficial position than it would have been in liquidation of the Corporate Debtor in accordance with Section 53 of the Insolvency and Bankruptcy Code (IBC). It was further stated by the Resolution Professional that the payments of the impugned amount by the Corporate Debtor were not in the "ordinary course of business" of the Corporate Debtor.

The Respondent submitted that the said three transactions, like all other LC transactions involving the Corporate Debtor, were carried out by the Respondent, as per the aforesaid ordinary course of conduct. It was hence submitted by the Respondent that the LC transactions are excluded from the provisions of Section 43 since they were in the "ordinary course of business."

NCLT vide its order directed the respondent ICICI which had debited Rs. 27.35

crore, Rs.10.63 crore and Rs. 28 crore aggregating to Rs. 65.98 crores from the current accounts of the Corporate Debtors to reverse the said amount within 30 days from the date of order. Since the resolution plan is already submitted and under examination of the CoC without consideration of this amount, therefore the appropriation of this amount will be decided by the CoC.

The appellant Bank filed appeal in NCLAT against the order. The proceedings were related to transactions were the transactions undertaken by the Appellant pursuant to the 'Working Capital Consortium Agreement' entered into between the Appellant and the 'Corporate Debtor' and the 'Renewal Credit Arrangement' executed between the Appellant and the 'Corporate Debtor' providing overall limit of 'Letter of Credit' facility for the period ending 15th December 2017.

The main plea taken by the Appellant Bank is that the 'Resolution Professional' before filing an application under Section 43(1) of the Insolvency and Bankruptcy Code (IBC) formed no opinion independently nor afforded an opportunity to the Appellant to explain about the transactions in question.

NCLAT after hearing both the parties held that the NCLT failed to notice the fact that all the transactions were not made on or after the date of commencement of the 'Corporate insolvency resolution process' and in ordinary course of business and in View of such position set aside the impugned order and allowed the appeal.

Answer 1(d)

In the case of *M/s Ruchi Soya Industries Limited* vs. *Patanjali Ayurveda Ltd, NCLT* clarified that no party had any right to dictate the terms of order. There was no need to substitute Para 38 with the proposed para as mentioned in the application.

Anyone who had not filed its claim then he would not have any right to agitate the same after the approval of the resolution plan. Resolution Applicants accepted the terms of the modified resolution plan as had been approved by this Bench by submitting an affidavit in compliance of the order.

The NCLT has got powers to review its own orders as given below:

Section 420(2) of the Companies Act, 2013

The Tribunal may, at any time within two years from the date of the order, with a view to rectifying any mistake apparent from the record, amend any order passed by it, and shall make such amendment, if the mistake is brought to its notice by the parties:

Provided that no such amendment shall be made in respect of any order against which an appeal has been preferred under this Act.

Rule 11 of the NCLT Rules, 2016

Nothing in these rules shall be deemed to limit or otherwise affect the inherent powers of the Tribunal to make such orders as may be necessary for meeting the ends of justice or to prevent abuse of the process of the Tribunal.

Rule 155 of the NCLT Rules, 2016

The Tribunal may, within a period of thirty days from the date of completion of pleadings, and on such terms as to costs or otherwise, as it may think fit, amend any

defect or error in any proceeding before it; and all necessary amendments shall be made for the purpose of determining the real question or issue raised by or depending on such proceeding.

Question 2

(a) *ABC Housing Ltd had initiated Corporate Insolvency Resolution Process against XYZ Infrastructure Ltd. (Corporate Debtor) under Section 7 of the Insolvency and Bankruptcy Code, 2016. The National Company Law Tribunal has dismissed the application as not maintainable in view of the fact that the winding-up proceeding against the Corporate Debtor had already been initiated by the High Court. Referring relevant case explain whether an application under Section 7 of the Code is maintainable when windingup proceeding against the Corporate Debtor has already been initiated ?*

(b) *A Suspended Director of a Corporate Debtor, on whom Corporate Insolvency Resolution Process (CIRP) is ordered by National Company Law Tribunal (NCLT) made a police complaint against a Resolution Professional to stop his actions. Resolution Professional contended that all allegations made by suspended Director is frivolous and are made only to hinder him from doing the duty as Resolution Professional. The Resolution Professional filed an application with NCLT praying protection.*

Referring relevant provisions and decided case clarify whether suspended Director of a Corporate Debtor can file a police complaint against Resolution Professional, if not who can initiate action against the Resolution Professional for alleged wrong doings. *(6 marks each)*

Answer 2(a)

In the matter of *Indiabulls Housing Finance Ltd.* vs. *Shree Ram Urban Infrastructure Ltd.*, the Indiabulls Housing Finance Ltd. Appellant had initiated Corporate Insolvency Resolution Process against Shree Ram Urban Infrastructure Ltd (Corporate Debtor) under Section 7 of the Insolvency and Bankruptcy Code, 2016.

The National Company Law Tribunal, Mumbai Bench by impugned order dated 18th May, 2018 dismissed the application as not maintainable in view of the fact that the winding-up proceeding against the Corporate Debtor had already been initiated by the High Court of Bombay.

Thus, the issue that fell for consideration before the National Company Law Appellate Tribunal was whether an application under Section 7 of the Code is maintainable when winding-up proceeding against the Corporate Debtor has already been initiated?

In the said appeal, the NCLAT examined judgments governing the issue to hold that the High Court of Bombay has already ordered for winding-up of Corporate Debtor, which is the second stage of the proceeding, thus question of initiation of 'Corporate Insolvency Resolution Process' which is the first stage of resolution process against the same Corporate Debtor does not arise.

While arriving at its judgment, the NCLAT relied on the case of *Forech India Pvt. Ltd.* vs. *Edelweiss Assets Reconstruction Company Ltd. & Anr.*, wherein the NCLAT observed

that if a Corporate Insolvency Resolution has started or on failure, if liquidation proceeding has been initiated against the Corporate Debtor, the question of entertaining another application under Section 7 or Section 9 of the Insolvency and Bankruptcy Code (IBC) against the same very Corporate Debtor does not arise, as it is open to the 'Financial Creditor' and the 'Operational Creditor' to make claim before the Insolvency Resolution Professional / Official Liquidator.

The NCLAT further opined that once second stage i.e. liquidation (winding-up) proceedings has already been initiated, the question of reverting back to the first stage of Corporate Insolvency Resolution Process or preparation of Resolution Plan does not arise.

In view of the facts of the present case, the NCLAT concluded that as the High Court of Bombay had already ordered winding-up of Corporate Debtor and the same has been initiated, therefore, initiation of Corporate Insolvency Resolution Process against the Corporate Debtor did not arise.

Answer 2(b)

In the matter of *Alchemist Asset Reconstruction Co. Ltd.* vs. *Hotel Gaudavan Pvt. Ltd.*, the IRP prayed for protection for all acts done by him in good faith and to save him from the frivolous allegations made against him in a FIR filed by a former director of corporate debtor.

The NCLT observed that If, there is any complaint against the Insolvency Professional then the IBBI is competent to constitute a disciplinary committee and have the same investigated from an Investigating Authority as per the provision of Section 220 of the Code. If, after investigation IBBI finds that a criminal case has been made out against the Insolvency Resolution Professional then the IBBI has to file a complaint in respect of the offences committed by him. It is with the aforesaid object that protection to action taken by the IRP in good faith has been accorded by section 233 of the Insolvency and Bankruptcy Code (IBC). There is also complete bar of trial of offences in the absence of filing of a complaint by the IBBI as is evident from a perusal of section 236(1) & (2) of the Insolvency and Bankruptcy Code (IBC).

Therefore, a complaint by a former director with the SHO, Police Station would not be maintainable and competent as the complaint is not lodged by the IBBI. The jurisdiction would vest with Investigation Officer only when a complaint is filed by 'IBBI'.

Question 3

(a) *'Corporate Restructuring is an inorganic business strategy where one or more aspects of a business are redesigned to improve commercial efficiency, manage competition effectively, drive faster pace of growth, ensure effective utilization of resources, and fulfilment of stakeholders' expectations. It serves different purposes for different companies at different points of time and may take up various forms.' – Brief on External and Internal Restructuring through Resolution Plans.*

(b) *Whether the promoters can claim that 'they should have been given an opportunity to settle the dues, if Committee of Creditors did not find any resolution plan as viable and feasible.' Citing relevant decision whether the claim of the promoters is tenable and within the objects of the IBC, 2016.* *(6 marks each)*

Answer 3(a)

External Restructuring

It consists of merger and amalgamation of one company with another or demerger of one or more undertakings of a company into another company, acquisition of controlling stake in a company through purchase of majority stake in it, conversion of debt into equity, etc. The same are briefly explained hereunder.

(i) *Restructuring through mergers, amalgamation and demerger* : A company is merged, amalgamated or demerged to achieve improvement in efficiency in operational and financial performance of the company. In the insolvency proceedings of a corporate debtor, the resolution plan may provide for merger, forward or reverse of the corporate debtor with the resolution applicant (company) or any of its group companies to maximize the utilization of the assets of the corporate debtor. Similarly, the resolution applicant may provide to demerge one or more units of the corporate debtor to gain operational and financial efficiency.

(ii) *Restructuring through acquisition of controlling stake/ purchase of Shares* : The resolution applicant may, through a resolution plan, acquire the controlling stake in the corporate debtor by either reducing or cancelling its existing paid-up share capital and recapitalizing it by infusing further equity capital. Alternatively, the resolution applicant may acquire the existing equity share capital of the company partly or fully by making payment of some nominal consideration to the shareholders of the Corporate Debtor and for meeting the requirement of funds of the Corporate Debtor, the Resolution Applicant may infuse the funds partly in equity or partly in the form of debt or fully in the form of debt only. The management of the Corporate Debtor including its Board is also changed by the Resolution Applicant by appointing his nominee directors on the Board and by appointing other key managerial personnel.

(iii) Restructuring through conversion of debt for issuance of securities: It can be understood that the insolvency of a Corporate Debtor is mainly due to default in its debt, whether financial debt or operational debt, where it could not fulfil its repayment obligation. The Resolution Applicant on the basis of the assessment of the Corporate Debtor, may propose the conversion of debt of the Corporate Debtor into securities of the Corporate Debtor issued in favor of the creditors, thereby, changing the nature and terms of the debt. The said securities may be in the form of equity share, preference share or debentures /bonds. As a result of the said restructuring, the existing debt of the Corporate Debtor is reduced to a sustainable level by conversion of the same into equity and by waiving substantial part of the unsustainable debt.

Internal Restructuring

The internal restructuring includes operational and financial restructuring. These are discussed in detail as follows:

(i) *Operational Restructuring*

Operational Restructuring involves improving the operational efficiency of the corporate debtor so as to increase its business receipts and profitability. It may

consist of creation of new departments to serve growing markets or downsizing or eliminating departments to conserve overheads. A company may undertake restructuring to focus on a particular market segment leveraging its core competencies or may undertake restructuring to make the organization lean and efficient. This type of restructuring affects employees and involves layoffs or collaboration with third parties to upgrade skills and technical knowhow.

(ii) *Financial Restructuring*

Financial restructuring is the process of reorganizing the financial structure, which primarily comprises of equity capital and debt capital. There may be several reasons (financial and non-financial) that trigger the need for financial restructuring. Financial restructuring is undertaken either because of compulsion (to recover from financial distress) or as part of company's financial strategy to achieve better financial performance. Financial restructuring is done for various business reasons such as to overcome poor financial performance, to gain market share, or to seize emerging market opportunities.

Answer 3(b)

In the matter of *Y. Shivram Prasad & Ors.* vs. *S. Dhanapal & Ors*, the NCLAT passed the impugned order of liquidation as Committee of Creditors did not find any resolution plan viable and feasible. The promoters submitted that they should have been given an opportunity to settle the dues.

While rejecting the said submission, the NCLAT clarified that settlement can be made only at three stages, i.e., before admission, before constitution of CoC and in terms of section 12A of the Insolvency and Bankruptcy Code (IBC) and such stages were over in this instant matter.

It, however, observed that during the liquidation process, it is necessary to take steps for revival and continuance of the Corporate Debtor by protecting it from its management and from a death by liquidation.

Wherein this Appellate Tribunal having noticed the decision of the Hon'ble Supreme Court in "*Swiss Ribbon Pvt. Ltd. & Anr.* vs. *Union of India & Ors* where Hon'ble Supreme Court observed that "What is interesting to note is that the Preamble does not, in any manner, refer to liquidation, which is only availed of as a last resort if there is either no resolution plan or the resolution plans submitted are not up to the mark. Even in liquidation, the liquidator can sell the business of the corporate debtor as a going concern" and NCLAT in its matter further held that "in view of the provision of Section 230 and the decision of the Hon'ble Supreme Court in 'Swiss Ribbons Pvt. Ltd.', we direct the 'Liquidator' to proceed in accordance with law."

He will verify claims of all the creditors; take into custody and control of all the assets, property, effects and actionable claims of the 'corporate debtor', carry on the business of the 'corporate debtor' for its beneficial liquidation, etc. as prescribed under Section 35 of the Code.

If the members or the 'Corporate Debtor' or the 'creditors' or a class of creditors like 'Financial Creditor' or 'Operational Creditor' approach the company through the liquidator for compromise or arrangement by making proposal of payment to all the creditor(s), the

Liquidator on behalf of the company will move an application under Section 230 of the Companies Act, 2013 before the Adjudicating Authority i.e. National Company Law Tribunal, in terms of the observations as made in above. On failure, as observed above, steps should be taken for outright sale of the 'Corporate Debtor' so as to enable the employees to continue."

Question 4

(a) *A German Company (Operational Creditor) filed application under Section 9 of the Insolvency and Bankruptcy Code, 2016 against PQR Private Limited (Corporate Debtor) alleging that the 'Corporate Debtor' committed default in making the payment of certain operational dues. The Adjudicating Authority (National Company Law Tribunal), admitted the application. Before, National Company Law Appellate Tribunal (NCLAT), the Corporate Debtor has raised the question of jurisdiction of the National Company Law Tribunal in entertaining the application Under Section 9 of the IBC, 2016. The Corporate Debtor referred to the Agreement reached between the parties and submitted that as per the Agreement and as the Office of the Respondent is in Germany, any suit or case is maintainable only in the Courts at Germany. No case can be filed in any Court in India. Discuss with reasoning whether the contention of the Corporate Debtor is correct.*

(b) *A Financial Creditor filed an Application for a declaration that the Resolution Applicant, ABC Ltd and its promoters have knowingly contravened the terms of the resolution plan, having failed to implement the same and for the reinstatement of the Committee of Creditors (CoC) to run the Corporate Debtor, as a going concern. Referring relevant case explain whether the Financial Creditor will succeed.* *(6 marks each)*

Answer 4(a)

The present facts of the case is similar to the case of *Excel Metal Processors Ltd* vs. *Benteler Trading International Gmbh & ANR. [NCLAT]*. The Appellant (Corporate Debtor - Excel Metal) referred to the Agreement reached between the parties and submitted that as per the Agreement and as the Office of the Respondent is in Germany, any suit or case is maintainable only in the Court at Germany.

No case can be filed in any Court in India. Therefore, the Appellant has raised the question of jurisdiction of the National Company Law Tribunal, Mumbai Bench in entertaining the application under Section 9 of the Insolvency and Bankruptcy Code (IBC).

However, the NCLAT, New Delhi Bench was not inclined to accept the aforesaid statement as it is now settled and decided by the *Appellate Tribunal in Binani Industries Ltd.* vs. *Bank of Baroda & Anr.* - Company Appeal (AT) (Insolvency) No.82 of 2018 etc. Decided on 14th November, 2018 wherein it was held that 'Corporate Insolvency Resolution Process'/ insolvency proceedings is not a 'suit' or a 'litigation' or a 'money claim' for any litigation; No one is selling or buying the 'Corporate Debtor' a 'Resolution Plan'; It is not an auction; it is not a recovery, which is an individual effort by the creditor to recover the dues through a process that had debtor and creditor on opposite sides; and it is not liquidation. The object is mere to get resolution brought about, so that the Company do not default on dues.

Pursuant to Section 408 of the Companies Act, 2013, the National Company Law Tribunal has been constituted in different States. In terms of the said provision, the Central Government has notified and vested the power on respective National Company Law Tribunals to deal with the matter within its territory, where the registered Offices of the Companies are situated.

As per Section 60(1) of the Insolvency and Bankruptcy Code (IBC), the Adjudicating Authority, in relation to insolvency resolution and liquidation for corporate persons including corporate debtors and personal guarantors thereof shall be the National Company Law Tribunal having territorial jurisdiction over the place where the registered office of the corporate person is located. As admittedly, the Registered Office of the 'Corporate Debtor' is situated in Mumbai, we hold that the National Company Law Tribunal, Mumbai Bench has the jurisdiction to entertain an application under Section 9 of the I & B Code and the Appellant cannot derive advantage of the terms of the Agreement reached between the parties.

For the reasons aforesaid, and in absence of any merit, the Appeal was dismissed.

Answer 4(b)

In the case of *Corporation Bank* vs. *Amtek Auto Ltd. & Ors.* the Financial Creditors filed an Application for a declaration that the Resolution Applicant, Liberty House Group PTE Ltd. and its promoters have knowingly contravened the terms of the resolution plan, having failed to implement the same and for the reinstatement of the Committee of Creditors (CoC) to run the Corporate Debtor, as a going concern.

The NCLT held that the Resolution Applicant is not capable of implementation of resolution plan. It allowed the application and excluded the time from the date when Decan Valuers Investors LP, the only other Resolution Applicant, submitted its plan upto the date of the receipt of this order from the CIRP period. It observed: "No matter if the corporate debtor ultimately has to face liquidation, but the permission to restart the process, make advertisement and invite fresh plans etc., would defeat the very mandate of Section 12 of the Code."

The Committee of Creditors can only discuss the Resolution Plan which was submitted by DVI (Decan Valuers Investors LP) only by exclusion of certain period of time while calculating 270 days. "It, however, granted liberty to any member of the CoC or the Resolution Professional to file a complaint before the IBBI or the Central Government with a request to file a criminal complaint."

Question 5

(a) MNO Private Limited has stopped its business operations and management has no further intention to continue its business operations. The Company has Assets in excess of Liabilities and hence, proposed Voluntary Liquidation of the Company as per the Provisions of IBC, 2016. You are proposed to be appointed as Liquidator for the Voluntary Liquidation. The Directors have approached you to know the prescribed timelines for completion of Voluntary Liquidation Process. The Extra-ordinary General Meeting to approve the Voluntary Liquidation is proposed on 1st July 2021. Prepare a timeline mentioning the probable date for the following activities as per the IBC, 2016 and Regulations made thereunder :

(i) Voluntary Liquidation Commencement date

(ii) Date of Public Announcement

(iii) Intimation of Special Resolution for Voluntary Liquidation to IBBI and RoC

(iv) Receipt of claims and preparing list of stakeholders

(v) Submission of Preliminary Report

(vi) Distribution of Assets. *(6 marks)*

(b) National Company Law Tribunal (NCLT) has initiated CIRP on application of one of Operational Creditors of DOP Ltd. A Resolution Professional was appointed after all processes as per the Law. Two viable Resolutions Plans (Plan A and Plan B) were received. Committee of Creditors comprises of Three Financial Creditors. As per Regulations of Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016, what is the approval status of Resolution Plans (Plan A and Plan B) for various instances of Voting outcome as mentioned below ?

Voting Outcome in different scenarios	*% of votes in favour of*		*% of votes against*	
	Plan A	*Plan B*	*Plan A*	*Plan B*
1	*52*	*64*	*48*	*36*
2	*64*	*78*	*36*	*22*
3	*78*	*78*	*22*	*22*

Also clarify the requisite voting percentage and tie-breaker formula as per the aforesaid Regulations. *(6 marks)*

Answer 5(a)

Date of EGM 1st July 2021

(i) Voluntary Liquidation Commencement date - Date of EGM will be treated as Liquidation Commencement date - 1st July 2021

(ii) Date of Public Announcement - Within 5 days from the date of Commencement- 6th July, 2021

(iii) Intimation of Resolution to IBBI and RoC - Within 7 days from the date of Commencement- 8th July 2021

(iv) Receipt of claims and preparing list of Stakeholders - 30 days from the date of Commencement - 31st July 2021

(v) Submission of Preliminary Report - Within 45 days from Commencement date- 15th August, 2021

(vi) Distribution of Assets - Within six months from the receipt of amount to stakeholders.

Answer 5(b)

Status of Voting outcome:

Voting outcome 1

No Plan is approved, as neither of the Plans received requisite votes. The committee shall vote again on Plan B, which received the higher votes, subject to the timelines under the Code.

Voting outcome 2

Plan B is approved, as it received higher votes, which is not less than requisite votes.

Voting outcome 3

The committee shall approve either Plan A or Plan B, as per the tie-breaker formula announced before voting.

As per the amended Provision of Regulation 39 of IBBI (CIRP) Regulations the requisite vote for approving the Resolution plan is 66% (Reduced from 75%).

Tie-breaker formula is a method to break the equality in votes. This has to be decided prior to the meeting and should be communicated to all CoC Members.

Question 6

A Resolution Professional appointed under Insolvency & Bankruptcy Code, 2016 (IBC, 2016), placed before the Committee of Creditors (CoC), a Consortium of Banks, a Resolution Plan submitted to him. The CoC approved the Resolution Plan and National Company Law Tribunal (NCLT), sanctioned it. As the Liquidation Value is not sufficient and there is a hair-cut involved in the dues payable to the secured financial creditors, nothing is provided for the Operational Creditors under the Resolution Plan. The Operational Creditor aggrieved by the decision of the NCLT filed Appeal before National Company Law Appellate Tribunal (NCLAT). The contention of the Operational Creditor is that the Resolution Plan approved is not in compliance with the provisions of the Insolvency and Bankruptcy Code, 2016 and the Regulations made thereunder :

(a) Referring suitable case law answer whether the contention of Operational Creditor is Correct.

(b) Will your answer be different if it is a Liquidation case, listing out the order of priority in case of corporate persons, explain the position of the unsecured Financial creditor and unsecured Operational creditor of a Corporate Debtor under Liquidation ? (6 marks each)

Answer 6(a)

In case of *Hammond Power Solutions Pvt. Ltd.* vs. *Sanjit Kumar & ORS*, the Hon'ble NCLAT has set aside the Resolution plan and Matter remitted back to NCLT and observed that:

If the above minutes are perused, it can be hardly said that there are any reasons given by the Committee to demonstrate that it has taken care of interest of all

stakeholders. Para - 46 of the Judgement in the matter of "Committee of Creditors of *Essar Steel India Limited* vs. *Satish Kumar Gupta & Ors.*" (Civil Appeal No.8766-67 of 2019) in the Judgement dated 15th November, 2019 ["Essar Steel"] requires to see "the reasons given by the Committee of Creditors while approving a resolution plan" from point of view stated in the paragraph.

The reasons for giving NIL to Operational Creditors is not reflected from record. We have already reproduced portion from Part B - Financial Proposal with regard to what the approved Resolution Plan states regarding dues to the Operational Creditors. The proposal is based on the assessment that there is no liquidation value due to Operational Creditors. Although it is not stated but there is reason to doubt that the Resolution Applicants were aware of the liquidation value. There is no dispute that so many of the Operational Creditors have been left high and dry giving them nil amount which Hon'ble Supreme Court has observed that giving NIL to Operational Creditors "would certainly not balance the interest of all stakeholders or maximise the value of assets of the Corporate Debtor if it becomes impossible to continue running its business as a going concern."

For these reasons, we find that the Impugned Order accepting the Resolution Plan cannot be upheld. The Resolution Plan does not appear to have taken care of interest of all stakeholders including Operational Creditors and the decision of the COC also does not reflect that it has taken into account the fact that the Corporate Debtor needs to be kept as a going concern and that there is need to maximise the value of the assets and that the interest of all the stakeholders including Operational Creditor has to be taken care of.

For the above reasons, we set aside the Impugned Order and remit the matter back to the Adjudicating Authority with a direction to send back the Resolution Plan to the Committee of Creditors to resubmit the Plan after satisfying the parameters as laid down by the Hon'ble Supreme Court in the Judgement in the matter of "Essar Steel", portions of which have been reproduced above, and IBC.

The Adjudicating Authority may give specific time period to the Resolution Professional to place matter before Committee of Creditors for resubmitting the Resolution Plan after satisfying the parameters laid down by the Hon'ble Supreme Court and IBC. Further incidental Orders may also be passed. On resubmission of the Resolution Plan, the Adjudicating Authority will deal with the same in accordance with law.

Answer 6(b)

In case of Liquidation the order of Priority as set out in Section 53 of the Insolvency and Bankruptcy Code (IBC) have to be followed. In case no amount is left with after satisfaction of Secured Creditors, operational creditors cannot claim any amount.

Order of priority - Sub-section (1) of section 53 provides that notwithstanding anything to the contrary contained in any law enacted by the Parliament or any State Legislature for the time being in force, the proceeds from the sale of the liquidation assets shall be distributed in the following order of priority and within such period as may be specified, namely: -

(a) the insolvency resolution process costs and the liquidation costs paid in full;

(b) the following debts which shall rank equally between and among the following:

  (i) workmen's dues for the period of twenty-four months preceding the liquidation commencement date; and

(ii) debts owed to a secured creditor in the event such secured creditor has relinquished security in the manner set out in section 52;

(c) wages and any unpaid dues owed to employees other than workmen for the period of twelve months preceding the liquidation commencement date;

(d) financial debts owed to unsecured creditors;

(e) the following dues shall rank equally between and among the following: -

(i) any amount due to the Central Government and the State Government including the amount to be received on account of the Consolidated Fund of India and the Consolidated Fund of a State, if any, in respect of the whole or any part of the period of two years preceding the liquidation commencement date;

(ii) debts owed to a secured creditor for any amount unpaid following the enforcement of security interest;

(f) any remaining debts and dues;

(g) preference shareholders, if any; and

(h) equity shareholders or partners, as the case may be.

As per the order of priority as mentioned above, unsecured Financial Creditors ranks above the Operational Creditors.

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