

Penalties and Remedies

Under Corporate Laws

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Prosecutions on the rise

- As on 31st Dec 2009, total number of 57512 prosecutions were pending
- The rate of disposal is quite small
 - ▣ Only 6973 prosecutions were disposed off
- This is despite several settlement schemes brought by the Ministry from time to time

Statistics of Ministry on Applications/Petitions received

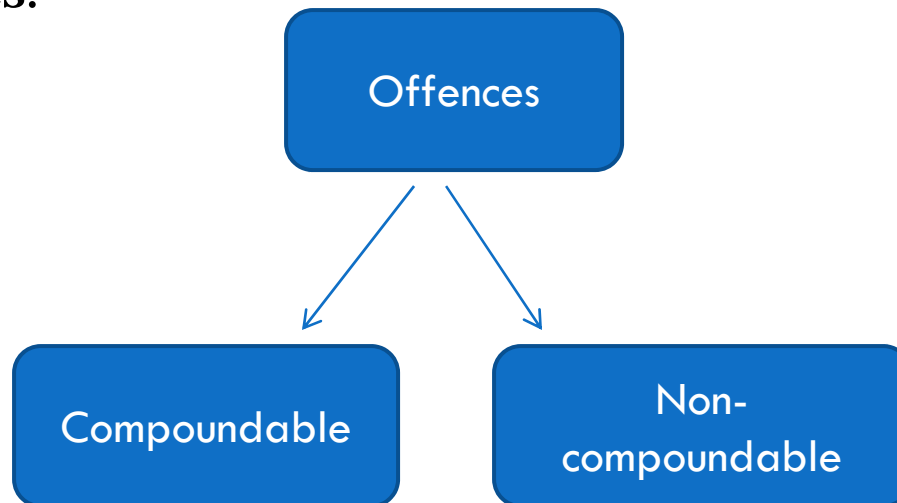
Details for the period from 01-04-2009 to 31-12-2009

Section (1)	Opening Balance (2)	Receipts(3)	Total 4(2&3)	Disposed off (5)	Pending (4-5)
141	82	5038	5120	4929	191
621A	505	1943	2448	1733	715
58A	869	1359	2228	510	1718
58AA	13	0	13	0	13

**Source : MCA Annual Report 2009-10

Types of Offences

- Offences- Compoundable and Non- Compoundable
 - ▣ Compoundable offence- Any offence punishable with fine or imprisonment or fine and imprisonment are compoundable offences.
 - ▣ Non compoundable – Any offence punishable with imprisonment or imprisonment and fine are non-compoundable offences.



Officers in default

- For the purpose of any provisions in the Act officers in default shall be liable to any punishment or penalty. Officers in default means –
 - the managing director(s)
 - the whole-time director(s)
 - the manager
 - the secretary
 - any person in accordance with whose directions or instructions the Board is accustomed to act
 - any person charged by the Board with responsibility of complying with that provision, subject to his consent
 - where company does not have a managing director, whole time director, manager,
 - any director(s) who may be specified by the Board in this behalf
 - or all directors where no one is specified. (Sec 5)
- It is very important for directors to make use of sec. 5 (1) (g) – so independent directors may be saved from embarrassment

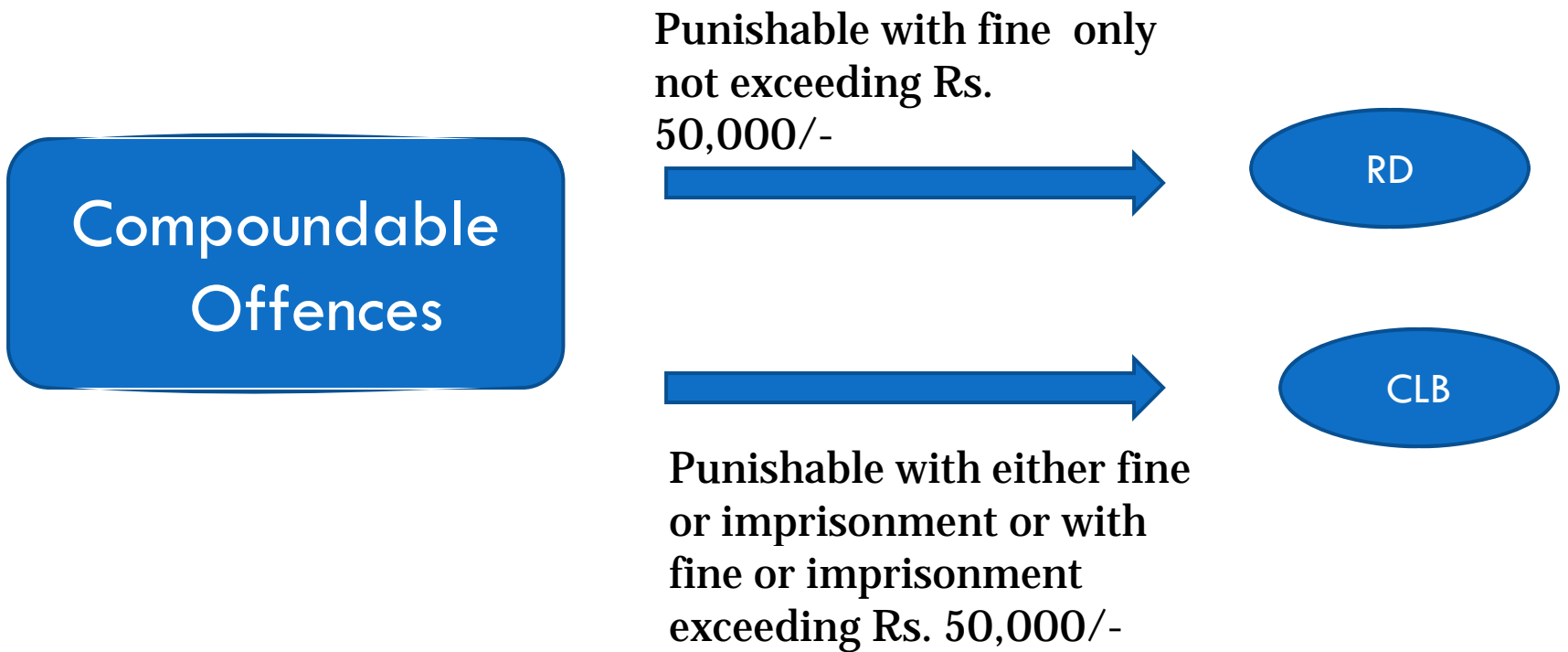
Options where offences have been committed

- Defend the notice at the time of issue of show cause notice
- Once offence is affirmed has having been committed
 - Compounding under sec 621A
 - Relief under sec. 633

Process of prosecutions under Companies Act

- By Central government
 - Usually follows
 - Inspection under sec 209
 - Perusal of documents or information gathered by the Registrar under sec. 234
 - Investigation under sec 235
- By shareholder
- By SEBI
 - All offences pertaining to issue and transfer of securities or non payment of dividends

Authorities to apply for compounding



Compounding procedure

Preparation of applications in the format specified in Form No. 1 of Annexure II of Company Law Board Regulations, 1991



Filing of E-form 61 for each applicant



Submission of applications in duplicate to ROC [section 621A(4)(a)]



Forwarding a copy by ROC to the concerned authority (RD/CLB)



Hearing by the concerned authority and imposition of an amount in composition of the offence



After payment of the amount (either online or DDs), issue of order

Points to be considered while opting for compounding

- ❑ Can be done suo-motu by the Company, before issue of the show cause notice by the Department
- ❑ Once compounded, complainant can not seek remedy through court i.e. prosecution cannot be launched in the court for the same offence
- ❑ Once compounded, further application for compounding cannot be made for the same offence within 3 years from the year for which compounding was done earlier
- ❑ Applicants are to pay the compounding amount from their own resources
- ❑ If, for any section, penalty is not mentioned, then penalty as provided under section 629A shall apply

Some of the common Compoundable offences

Common sections under which Companies commit offences	General observations by the Department	Likely defensive answers
211(1) & (2)	Detailed segregation as per Schedule VI not provided, thereby accounts not revealing true and fair view	Depends case to case basis. Some may be contended on the ground of typo error.
211(1)	Non disclosure of amounts due to Micro, Small and Medium enterprises	Company has not received intimation from the suppliers about their status under Micro, Small and Medium Enterprise Development Act, 2006 hence disclosures not made
211 (1) (2)	Non disclosure with regard to bifurcation of investments into long term and short term investments/ quoted, un-quoted	No short term investments made by the Company so no disclosure/ segregation made Case specific – depending upon the Balance Sheet of the Company
211 (1)	Cash in hand was clubbed with cheques in hand	Cheques in hand cannot be categorised as bank balances and are equivalent to cash in hand, hence clubbed with cash in hand

Some of the common Compoundable offences (cont...)

Common sections under which Companies commit offences	General observations by the Department	Likely defensive answers
211(2)	No bifurcation in Profit & Loss account of the value of imports in respect of raw materials, components and spare parts and capital goods as required in Clause 4(D)(a) of Part II of Schedule VI to the Act	Import value being insignificant, so no bifurcation made
211 (2)	Appropriate head as mentioned in Clause 4(B) not used for remuneration paid to Auditors for various services rendered	Difference in representation, does not infringe upon true and fair view requirement of the Act
211 (2)	Other income by way of interest disclosed but the nature of income not disclosed as required under Clause 3(xi)(b) of Part II of Schedule VI to the Act	Amount small and insignificant and not infringing on the true and fair view requirement of the Act. Also the Clause says the representation of income and expenditure to be made in " <i>most Convenient Heads</i> "

Some of the common Compoundable offences (cont...)

Common sections under which Companies commit offences	General observations by the Department	Likely defensive answers
217(1)(e)	Details not provided for Foreign Exchange Earnings	Details provided in the annexure to the directors report which should be read along with the report to ascertain the true meaning of the report.
211(3A) & 3(B)	Inventories/Raw materials valued either at cost or at market price only and has not taken lower of the two	As per AS 2, valuation should be done at cost or market price – whichever is lower. Valuing at cost is not a due compliance
Schedule VI	Details of raw materials not given – even if the raw materials are less than 10% in value	Please note requirements Schedule VI on this

Some of the common Compoundable offences

Contd...

Common sections under which Companies commit offences	General observations by the Department	Likely defensive answers
383A	Vacancy in the office of Company Secretary for some part of the year	The company had taken all reasonable efforts to employ a CS but failed due to reasons beyond its control
292(1)(c)	Money borrowed without specific approval from the Board	Though no specific approval of the Board was obtained nonetheless the Board was aware of such loans made and have given their tacit consent while approving the Annual Accounts
292(1)(d)	Investment of company's fund without specific approval from the Board	Though no specific approval of the Board was obtained nonetheless the Board was aware of such
		investments made and have given their tacit consent while approving the Annual Accounts

Some of the common Compoundable offences Contd...

Common sections under which Companies commit offences	General observations by the Department	Likely defensive answers
300	The recording in minutes is not specific in terms of requirement of Section 300(1) of the Act, as to whether presence of interested directors was counted for the purpose of forming quorum	The section prohibits voting and participating of interested directors in any matter but does not specify the procedure in which this needs to be recorded or worded in the minutes of the Company. the difference in opinion is only a matter of interpretation of the provisions of the Act and the language of the person taking matters on record
224(8)	Neither shareholders nor Board resolution for fixation of remuneration of auditors on appointment or reappointment of the same	The manner of determining the audit fee is not provided by the Act. The fee can be fixed by the BOD from time to time by passing resolutions and the total remuneration paid to the Auditors can be incorporated in the Annual Accounts of the Company.
295(1)	Loans/guarantee provided to related entities without previous approval of CG	Can be contended on case to case basis.

Some of the common Compoundable offences Contd...

Common sections under which Companies commit offences	General observations by the Department	Likely defensive answers
209 (1)	Books of accounts not maintained at the Registered office or requisite forms not filed with ROC for maintaining records at any other place.	Books were maintained but had gone for binding
220 (1) & (2)	Copy of Balance sheet & profit and loss account not signed as required; all annexures not annexed; reasons not stated in case AGM not held for any year.	Directors affirm having signed the annual report
176 (2)	Omitting to state with reasonable prominence that the members entitled to attend and vote are entitled to appoint proxies	Bold print is not necessarily the only way of gaining prominence
372A	Loan/guarantee provided without approval; Register not maintained or improper records	Can be defended on case by case basis

Non-compoundable offences

Sections	General errors & Omissions	Likely defense
58 A(5)	Omission to make repayment of deposit or acceptance of deposit in contravention of rules	Can be defended on case to case basis
58A(6)(a)(i)	Acceptance of deposit in excess of prescribed limits or in contravention of manner of condition prescribed under sub-section (1) or in contravention of sub-section (2)	Can be defended on case to case basis
209A(8)	Failure to comply with section 209A	Can be defended on case to case basis
207	Not distributing dividend within 30 days	Can be defended on case to case basis

Condonation under section 141

Preparation of petition in the format specified in Form No. 1 of Annexure II of Company Law Board Regulations, 1991



Furnishing of all details along with the clarification for which the delay occurred



Submission of one set to ROC and other set along with the ROC receiving copy to CLB



Hearing by the CLB and issue of order imposing penalty



After payment of penalty online, file E-form 21 for filing of order with ROC

Likely offences under CARO, 2003

- ❑ Improper valuation and disclosures related to fixed assets
- ❑ Failure to check whether adequate internal control system has been adopted by the company
- ❑ Failure to give adverse remark or qualified report on the areas of non compliance by the company

Relief under sec 633

- There are 2 provisions for relief by the court
 - ▣ 633 (1) by the court conducting prosecution
 - ▣ 633 (2) by the High court
- 633 (1) Instead of compounding u/s 621A, anyone facing prosecution may also approach court under sec 633
- 633 (2) – apprehended prosecution may be relieved by High court
- Main differences between sec 621A and sec 633:
 - ▣ There is a proceeding before a court already regarding negligence, misfeasance, default, breach of duty, breach of trust
 - ▣ Several rulings exist to hold that the scope is not limited to Companies Act – several rulings of courts have granted relief even under PF Act
 - ▣ It is not necessary for the accused to admit an offence

Basic principles in a prosecution

- Mens rea is not required for prosecution under Companies Act
- Pleading, not involved in the offence as competent person was charged with observation of the compliance
- Amount of penalty has to be commensurate with the gravity of the offence, several SC rulings on the issue
 - **Zunjarrao Bhikaji Nagarkar vs UOI 1999 7 SCC 409**

Penalties under SEBI Act, 1992

Section	Type of errors or omissions	Penalty
15A	Failure to furnish any document, return or report to the Board or failure to file return or furnish any information.	Rs. 1 lac for each day during which the failure continues or Rs. 1 Cr, whichever is less
15C - For Listed Companies	Failure to redress the investors' grievances after receiving a written notice from the Board, within the specified time.	Rs. 1 lac for each day during which the failure continues or Rs. 1 Cr, whichever is less
15E - For Asset Management Company	Failure to comply with regulations providing for restrictive activities.	Rs. 1 lac for each day during which the failure continues or Rs. 1 Cr, whichever is less
15F – For Stock Brokers	Failure to issue contract notes, delivery of security; charging excess amount of brokerage.	Rs. 1 lac for each day during which the failure continues or Rs. 1 Cr, whichever is less

Penalties under SEBI Act, 1992, Contd...

Section	Type of errors or omissions	Penalty
15G	Practice of Insider Trading by communicating any price sensitive information or dealing, counseling or procuring himself or for anyone else the securities of any body corporate on the basis of such price sensitive information	Rs. 25 Cr or 3 times the amount of profit made from such transaction, whichever is higher
15H	Failure to disclose the shareholding in a body corporate or make a public announcement, to acquire shares.	Rs. 25 Cr or 3 times the amount of profit made from such failure, whichever is higher
15HA	Dealing in any fraudulent and unfair trade practices relating to securities.	Rs. 25 Cr or 3 times the amount of profit made from such practices, whichever is higher

Remedy and Relief

- Offences except punishable with imprisonment or with penalty and imprisonment can be compounded (Section 24A)
 - ▣ Such offences can be heard by SAT or court before which the proceedings are pending
- Immunity from prosecution or imposition of penalty can be granted by CG on recommendation of the Board if full and true disclosures are made in respect of alleged violation (Section 24B)
- Courts shall not take any cognizance of any offence punishable under the SEBI Act, Rules or Regulations (Section 26)

Appeal to SAT

- Can be made within 45 days of passing of order by SEBI or Adjudicating Officer
 - Time of 45 days can be extended on sufficient cause for non filing within time
- After giving opportunity of being heard to the parties, SAT will pass order
- Order copy to be served by SAT on the parties, SEBI and concerned Adjudicating Officer
- Appeal to Supreme Court if aggrieved by the order of SAT within 60 days only on question of law

Rulings on compounding under SEBI laws

- Ketan Parekh – Alleged violation of SEBI Takeover Code Regulations 7 and 10-Regulation 10 dropped and Regulation 7 upheld- **Penalty-1.5 Lac**
- Kosha Investments Ltd. vs. SEBI –Failure to make public announcement under Regulation 11at a minimum price - penalty of Rs. 48 lacs levied- Appeal against penalty to SAT-Penalty confirmed by SAT
- BD Trivedi-conniving with market operators and foul play relating to IPOs-penalty imposed 2 Crs-Appeal to SAT-Penalty reduced to 2 Crs.
- Sometimes, SEBI imposes stringent penalties even for trivial offences
 - In case of Padmini Technologies, a penalty of Rs 1 crores was imposed not appearing in response to summon
 - SAT reduced it to Rs 10000/-