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EDITOR'S DESK

Dear Colleagues,

I am happy to announce and release the first issue of Prachodan: an International Journal of Business and Corporate Law published from Symbiosis Law School, Hyderabad. This Journal is intended to disseminate knowledge to ensure good practice of business with a focus on research and reflections relevant to the academicians and practitioners. We want to make this journal as an essential resource for the students, practitioners, and professors in the field of business and corporate law.

The editors of our journal have long-standing and distinguished careers in their respective fields. The editorial board participants and outside reviewers of our magazine are dedicated in imparting unbiased, speedy critiques of the submitted manuscripts to shorten the period of review follow by final publication. Consequently, the authors shall simply have a pleasant and intellectual experience working with our editors and reviewers.

We would really like to thank all of the personnel and college students of Symbiosis Law School Hyderabad, all participants of the editorial board, reviewers, all authors, and the technical team for their assist towards this magazine. The help provided by the academic staff of Symbiosis Law School and Center for Specialization in Business Innovation for accomplishing this is well appreciated.

We are sure that our journal will provide top-quality original papers and articles, case reports that will continue to help everyone interested in Business and Corporate Law. We, hope that the journal will continue to be an important conduit for information at international level.

Chief Editor
Prof. (Dr.) Sarfaraz Ahmed Khan

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Sarbanes Oxley Act and Corporate Governance

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Abstract

The purpose of this paper is to investigate the impact of government regulation with respect to the Sarbanes-Oxley Act on the existing corporate governance. Specifically, our research question is: Does the various measures of governance and firm-specific characteristics change after the enactment of Sarbanes-Oxley? Empirical results show that prior to the Sarbanes-Oxley Act, shareholders' rights, board size, and the proportion of outside directors are statistically significant factors in explaining a firm's dividend policy and that there has been an immense change in the corporate governance of the corporate of firms across the world. Following Sarbanes-Oxley, however, regulatory changes have structurally altered the impact that governance measures.

Keywords: Corporate governance; Sarbanes Oxley Act; Section 404; Indian perspective of SOX.

Introduction

A compelling and precise definition of Corporate Governance cannot be adequately formulated due to the very nature of the concept. However, there cannot be any two opinions that the very essence of corporate governance is the effective accountability to all the shareholders.

As per The Hindu, the Corporate Governance can be defined as "Corporate governance is not just corporate management; it is something much broader to include a fair, efficient and transparent administration to meet certain well-defined objectives. It is a system of structuring, operating and controlling a company with a view to achieve long term strategic goals to satisfy shareholders, creditors, employees, customers and suppliers, and complying with the legal and regulatory requirements, apart from meeting environmental and local community needs. When it is practiced under a well-laid out system, it leads to the building of a legal, commercial and institutional framework and demarcates the boundaries within which these functions are performed."[1]

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[1] Corporate governance: TIME FOR A METAMORPHOSIS' The Hindu July 9, 1997.

Thus, corporate governance can be defined as the set of processes, principles and systems governs and provides the guidelines as per the way in which the company can be controlled or directed in a manner that it can efficiently fulfill the objectives and goals of the company in such a way that it adds to the value of the company and also provides benefits for all the stakeholders in the long run. Therefore, the role of a trustee for all the others is presumed by the company's management.

Upon the wake of liberalization after the policy of 1991 and the deregulation of business and industries, the question of corporate governance has become more frequent as a result of the rising demand for a new effective and efficient corporate ethos and stricter compliance with the laws that prevail in India. In the context of the unique situation in India where the financial institutions hold substantial stakes in companies, the accountability of the directors, including nonexecutive directors and nominees, has come into sharp focus."[2]

Furthermore, in foreign countries like the UK and USA, there is a diffusion of ownership and shareholding to define and characterize the corporate system and structure, since public holds a large percentage of the subscribed shares. These countries possess a well developed capital market which in engulfed in an active participation of the shareholders. Moreover, the firms have strict norms for disclosure and the protection of the investors. The code of best practice is given the emphasis for the implementation of good governance. Fortunately, even in India, a raucous demand for the evolvement of a code of good practice by the corporate themselves is transpiring. However, in a wider context i.e. the global perspective, this may be taken as to constitute a necessary criteria to penetrate through the labyrinth of prevalent practices that are questionable, improbable management attitudes towards their stakeholders and penetrable non- disclosures.

Corporate governance is related to the maintenance of the balance between the social and economic goals as well as the individual and communal goals. Thus, it spurs the efficient usage of the resources along with the requirement of the accountability for the stewardship of the said resources to align the various interests of all the individuals, corporation as well as the society.

Furthermore, it is based on the principles of conducting the business with all integrity, fairness, and not being opaque with all the transactions, by giving out the necessary disclosures regarding the decisions, along with maintaining the compliance with the laws prevailing in the country,

[2] Corporate Governance: THE NEW PARADIGM CHARTED SECRETARY, October 1997.

accountability and responsibility towards the stakeholders and a efficient commitment to conduct the business in an ethical and unbiased manner which is not arbitrary.

Scandals

Regrettably, the prevalence of numerous scandals related to the corporate in the United States and other countries have led to a wide ranging re-examination of the standards that govern the corporate governance with repercussions that extends even to the financial regulations as well. Some instances of such scandals are the Enron debacle and the dot.com bubble and collapse which brought about a massive change in the corporate governance as in both the cases the investors became enamored of an unsustainable model and that too aggressively.

The scandals related to the frauds in the corporate occurred in relation to the revenues and markers of growth and evidently, not necessarily profits. The firms used the capacity swap to demand higher revenues but their profits weren't enormous, and indeed, reduced the margins of the operating expense and gains, which too was most of the time in negative. Enron was dependent on a series of irregular off- balance sheet transactions to dazzle the stakeholders. The frequent use of this technique became a significant medium to hide the losses and generate profits despite of the underlying results as per the conventions on appropriate accounting reportable.

A rampant increase in the frauds and bankruptcies was thus seen in the last few decades, mainly in the USA. Regardless of the reason behind the substantial bankruptcies, and more importantly due to the collapse of the Enron in the early 2000s, a powerful consensus emerged amongst the policymakers and industry observers regarding the existing practices of management that the oversights of the government on these matters were not sufficient to promote a well functioning and sound security market.

Furthermore it is commonly understood that the separation of ownership and control leads to potential agency-related problems.[3] Thus these costs have persistently caused a challenging situation to the market participants and regulators to efficiently engineer the governance controls and thus mitigate any situations that potentially allows the managers to expropriate wealth from the stakeholders.

[3] Bader, Hans, and John Berlau. "THE PUBLIC COMPANY ACCOUNTING OVERSIGHT BOARD: AN UNCONSTITUTIONAL ASSAULT ON GOVERNMENT ACCOUNTABILITY." *Competitive Enterprise Institute*, 2005. http://www.cei.org/gencon/ 025,04873.cfm

Thus, there was an urgent need for a mechanism that will control the issues that pertain to the rise of such scandals as it was proving to be very difficult for the investors as well as the stakeholder as they were the main targets of such scandal and were suffering immensely. To reduce such scandals, the legislature came up with an Act that would curtail the scandals and mitigate the protection of the investors. In the spate of corporate, accounting and governance scandals, the Sarbanes –Oxley Act was thus legislated in 2002 which intends to protect the interests of the investors. This is done by improvising the accuracy, accountability and reliability of corporate disclosures made pursuant to prevailing laws, including other purposes.

The Act provides the Securities and Exchange Commission of the USA with great powers to enforce its discretion over the public companies by requiring heightened corporate responsibilities and enhanced financial disclosures.

It also imposes draconian corporate and criminal fraud accountability standards and formidable white-collar crime penalties than ever before. Along with the other requirements, the Sarbanes-Oxley Act demands the firms to have compulsorily committees to audit which should comprise of independent directors by forcing the officers to certify the existence of accuracy in the financial statements of the firms. Moreover, the Sarbanes-Oxley Act created the Public Company Accounting Oversight Board to oversee, regulate, inspect, and discipline accounting firms in their roles as auditors.

Thus, this paper deals with the concept of corporate governance in relation to the Sarbanes-Oxley act, 2002 which came into force after a rampant increase in the corporate scandals, specifically the Enron Scandal. Before the impact of the Act is discussed in details, it is more appropriate to have a profound look into the reason to legislate such Act. Thus a detailed discussion on the Enron Scandal is provided in the paper.

Enron Scandal

The collapse of Enron Corp. was unanticipated and sudden and was first in the series of the major corporate scandals that had shaken the core and confidence in the stock market and the corporate governance. The firm was immensely regarded as one of the most innovative, rapidly growing, and efficiently managed businesses in the United States. This was only months before the December 2001 filing of the Enron's bankruptcy.

The aftermath of the collapse was such that the shareholders including thousands of Enron workers holding company stock, lost tens of billions of dollars. It is clear now that the company was in horrendous financial shape as early as 2000. It was oppressed with debts and money-losing businesses, but presented the accounting statements in such a manner that it was manipulated to hide those problems

Enron was basically formed as a result of a merger between Houston Natural Gas and Internorth and became the first nationwide natural gas pipeline network. However, with the passage of time, the focus of the business shifted from the regulated transportation of natural gas to unregulated energy trading markets. This shift was regarded as an outstanding success by observers including the Wall Street professionals and was placed fifth on the Fortune 500.

The root of Enron's problem was not because of its core energy operations but was in its other ventures, specifically, "dot com" investments in the high-tech communications businesses and internet. In addition to it, it also recorded numerous significant losses in certain foreign operations including investments in public utilities of newly-deregulated markets in India, South America, and the U.K.

The reason due to which the Enron's scandal turned into a major financial scandal was the way the company responded to the problems being faced. Rather than disclosing the true conditions to the public investors which was to be presented as per the law required, the company misrepresented and falsified its accounts.

The losses and obsolete assets were assigned to the unconsolidated partnerships and the so called 'special purpose entities,' i.e. the company's public accounting statements was presented in a way that reflected the losses were, instead of occurring to Enron, were occurring to the Raptor entities. These entities were ostensibly independent firms that had agreed to take cognizance of the losses incurred by the company. But the reality was that the losses were in fact accounting contrivances that were created and were entirely controlled by the company's management. Enron also undertook many methods to conceal the extent of its indebtedness.

The main issue rose after the Enron scandal is of transparency which includes improvisation of the quality of the information available about the public corporations. With the increase of transparency in the firms, the ability of the corporate insiders to pursue fraudulent activities at the stake of employees and shareholders decreases.

Some of the crucial aspects of the issue are briefly provided below:

Auditing and Accounting Issues[4]

The statements of accounts of public corporations are to be certified by an independent auditor, as per the requirement of the Federal Securities law. In addition to turning a blind eye to improper accounting practices, the auditor of Enron was even actively participating in devising complex and misrepresented financial structures to deceit the stakeholders. The financial statements were not prepared as per the generally accepted accounting principles. The main question that was raised was that the accounting standards permit corporations to manipulate the numbers, and whether the investors face excessive risk if the financial statements lack consistency, reliability and clarity.

Pension Issues[5]

Enron sponsored a retirement plan called "401(k)" which was for their employees to which they contributed a portion of their pay on a tax-deferred basis. Around 62% of the assets that were held in the corporation's retirement plan were constituted by the Enron stock. Many employees of the company held even larger stock in their retirement plan. After the collapse of the company, the shares which were traded for even more than $80 per share became of worth even less than 70 cents after the fall of Enron. Furthermore, the retirement accounts of many employees were totally wiped out. The question that arises out of this is regarding the laws and regulations that govern these plans.

Corporate Governance Issues

The executives and board of directors were subjected to critical scrutiny after the Enron scandal. The top level management sold shares and stocks worth billions of dollars while the severe financial problems were being window dressed from the public. Thus several provisions were included in the SOX Act to provide a framework and guidelines to the CEOs to remind them of their duties to the firms and shareholders and should personally certify the accuracy of financial statements of the company.

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[4] See also: CRS Report RL31554 , CORPORATE ACCOUNTABILITY: SARBANES-OXLEY ACT OF 2002: (P.L. 107-204), by Michael Seitzinger. CRS Report RS21120, AUDITING AND ITS REGULATORS: PROPOSALS FOR REFORM AFTER ENRON, by Bob Lyke.

[5] See also: CRS Report RL31507, EMPLOYER STOCK IN RETIREMENT PLANS: INVESTMENT RISK AND RETIREMENT SECURITY, by Patrick Purcell (7-7571). CRS Report RL31551, EMPLOYER STOCK IN PENSION PLANS: ECONOMIC AND TAX ISSUES, by Jane Gravelle.

Moreover, any services other than that of audit provided by the firm's auditor were to be compulsorily approved by the board. After the Act, the audit committee must be inclusive of at least one financially expert director who is able to evaluate the accounting issues.

Banking Issues[6]

One of the reasons of Enron's demise was its relationship with the banks. Prominent banking companies which were involved in securities and commercial businesses with the company suffered immense losses after the collapse of the company. The question rose was the reason behind the encouragement of conflicts of interest and unsafe banking lending in relation to the investment banking business with Enron.

Energy Derivatives Issues[7]

Core energy business of Enron involved dealing in derivative contracts which was bases on the prices of oil, gas, electricity and other variables. As of now, no such evidence has emerged that points out that the speculative loss regarding the trade in derivatives, which is in reality an extremely high risk activity, were in fact a factor in Enron's collapse. After the collapse of Enron, innumerable dealers dealing in energy derivatives have admitted that they were involved in the creation of "wash trades". These kinds of trades does not have much economic substance but still gives out an impression of a greater market value than the reality, in addition to facilitating deceptive accounting.

Two of the shortcomings of the failure of Enron were the issues of supervision of the non-regulated market of the derivatives and the derivative trading. Although the bankruptcy did not had much impact on the supplies of energy along with its prices, a similar dealer in the future might damage the partners and lenders of the dealer and could cause widespread disruptions in the financial, real or both commodity markets.

Even if derivative trading was not a major cause, Enron's failure raises the issue of supervision of unregulated derivatives markets. Although Enron's bankruptcy appears to have had little impact on energy supplies and prices, a similar dealer failure in the future might damage the dealer's trading partners and its lenders, and could conceivably set off widespread disruptions in financial and/or real commodity markets.

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[6] See also: CRS Report RS21188, by William D. Jackson.

[7] See also: CRS Report RS21401, REGULATION OF ENERGY DERIVATIVES, by Mark Jickling. CRS Report RS20560, DERIVATIVES REGULATION: LEGISLATION IN THE 106TH CONGRESS, by Mark Jickling.

Sarbanes- Oxley Act, 2002

On December 2, 2001, the Enron Corporation pled the largest bankruptcy petition in U.S. history.[8]

The true attribution of the outrage of the American people was to the fact that in addition to the corporate entities were misleading their investors; the corporate were also doing it right under the purview of the accounting firms that were given the job of regulating practices. Due to the rise such activities, an immense pressure was put upon the Congress to respond to this situation and thus the Sarbanes Oxley Act was created in 2002. On the 30th of July, 2002 the Act was signed by the then President George W. Bush into law stating that "The Act adopts tough, new provisions to deter and punish corporate and accounting fraud and corruption, ensure justice for wrongdoers, and protect the interests of workers and shareholders".[9]

In the wake of scandals like Enron and WorldCom collapses in the starting of the 2000s, there was an immense consensus which emerged amongst the policymakers and industry observers regarding the existing management practices and that the government's oversight were not sufficient in order to promote a well-functioning and sound market.

Thus, the Sarbanes-Oxley Act demands the firms to constitute audit committees which should comprise of independent directors and financial officers that could certify that there exists accuracy in the firm's financial statements.[10] In addition to this, the Act created the Public Company Accounting Oversight Board in order to regulate, inspect, and oversee as well as discipline the auditors to carry their roles in the accounting firms with efficiency.

As of the 3st of December, 2011 over two thousand audit firms from over eighty countries were registered with the PCAOB. In 2011, it conducted inspections of 213 registered audit firms, and initiated an interim inspection program for broker-dealers.[11] It basically identifies the areas that are to be potentially addressed as a way of standing setting, inclusive of the review and analysis

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[8] Explaining the Enron Bankruptcy, http://www.cnn.com/2002/US/01/12/enron.qanda.focus.

[9] Bush, George W., STATEMENT ON SIGNING THE SARBANES-OXLEY ACT OF 2002. Online by Gerhard Peters and John T. Woolley, The American Presidency Project, 2002. Retrieved from http://www.presidency.ucsb.edu/ws/?pid=64514

[10] Romano, R., "THE SARBANES-OXLEY ACT AND THE MAKING OF QUACK CORPORATE CONTROL;' *The Yale Law Journal*, 114, 1532, 2005.

[11] Langevoort, donald c.. INTERNAL CON- TROLS AFTER SARBANES-OXLEY: REVISITING CORPORATE LAW'S DUTY OF CARE AS RESPONSIBILITY FOR SYSTEMS. Journal of corporation law, 31(3): 893-9, 2006

of the information which was obtained from the inspections and the inputs received from its Standing Advisory Group, which includes representatives from investor groups, the audit profession and public company board members.[12] Formally, PCAOB is a nonprofit corporation given a legal mandate to oversee public company auditors to protect investors and the "public interest in the preparation of informative, fair, and independent audit reports."[13]

In addition, the New York Stock Exchange and National Association of Securities Dealers Automated Quotations (NASDAQ) obtruded governance changes on the listed firms. Some of the stock exchange actions might have happened independently of SOX, but it is plausible that others were enacted in anticipation of and in response to SOX.[14]

The primary goal of the SOX legislation was the improvement of the quality of audit and the reduction of fraud on a cost effective basis. The Act has imposed the task on PCAOB to register and set standards for the inspection, investigation and disciplining the audit firms for the public companies. Two members of its five-member board must be auditors; a rule intended to assure that PCAOB has the necessary expertise. The second core component of Sarbanes-Oxley is designed to fight theft by enlisting auditors to enforce new disclosure rules that strengthen the incentives for firms to increase spending on financial control.[15]

Prior to Sarbanes-Oxley, auditors were governed by a system of self-regulation which had apparently not preserved their ability to act as gatekeepers.[16] All the public accountants were given license from the states, in return the state devoted only fews resources to the supervising auditors. A Public Oversight Board for auditors were created in 1978, but it was dominated by accountants, who were given funds by the audit industry, and had no whole directors, no authority for inspection, and no rule-making authority.

A variety of theories have been put forth as per why the auditors failed in their gatekeeper function. Firstly, auditing had for a long period been suffering from a "de-professionalization"-a loss in the capacity of auditors to detect fraud because of an increase in the competition,

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[12] Kraakman, Reiner h,. GATEKEEPERS: THE ANATOMY OF A THIRD-PARTY ENFORCEMENT STRATEGY. *Journal of law, economics, and organization*, 2(1): 53-104, 1986.

[13] PUBLIC COMPANY ACCOUNTING OVERSIGHT BOARD. 2004a. Annual report.

[14] Coates, j. THE GOALS AND PROMISE OF THE SARBANES-OXLEY ACT. *Journal of economic perspectives* 91–116, 2007.

[15] John C. Coates IV, THE GOALS AND PROMISE OF THE SARBANES-OXLEY ACT, T*he Journal of Economic Perspectives*, 21(1) pp. 97. 2007.

[16] Ibid.

decreasing audit fees and persistent liability risks, which reduced long-term rewards for auditing and increased incentives for rule-based accounting requiring little discretion or professional expertise[17]. Secondly, an increase in sales of consulting services by auditors to audit clients, which increased incentives to ignore fraud.[18] Thirdly, legal changes that diminished liability risk for auditors who ignored fraud and to the fact that auditors were appointed and paid by the managers, the very corporate agents those auditors were supposed to keep a check on. Except for legal liability standards for auditors, which remain largely the same as they were in 2001, elements of Sarbanes-Oxley respond to all of these theories.[19]

Not only did Sarbanes-Oxley introduce new criterions for corporate responsibility, but it also established explicit sanctions for breaching those standards.[20] Some specific responsibilities that came with Sarbanes-Oxley were that the (CFO) i.e. chief financial officer and chief executive officer (CEO) were now required to give a letter stating the financial data they provided auditors was indeed accurate.

What does Section 404 entail?

Section 404 (Management Assessment of Internal Controls) requires the SEC to provide rules requiring each annual report required under the 1934 Act to have an internal control report giving management's responsibility for internal controls and assessing the efficiency of internal controls. This section also requires the auditors for the issuer to attest to and report on management's assessment according to the standards to be adopted by the Board. Section 404 has generated immense interest and debate for accountants and is by far the most important one from the Financial Reporting perspective.

As enshrined by Section 404 of the Sarbanes Oxley Act of 2002, the Securities and Exchange Commission (SEC) adopted rules regarding internal controls at public companies in May 2003. Section 404 also requires that a company's independent auditors attest to and report on

[17] Healy, Paul, and Krishna G. Palepu. HOW THE QUEST FOR EFFICIENCY UNDERMINED THE MARKET. *Harvard Business Review*, July 1, 2003.

[18] Levitt, Arthur, Jr.,. ACCOUNTING AND IN- VESTOR PROTECTION ISSUES RAISED BY ENRON AND OTHER PUBLIC COMPANIES.Presented at U.S. Senate, Committee on Banking, Housing and Urban Affairs Hearing, 2002. http:// www.iasplus.com/resource/levittpdf

[19] Coffee, John C., Jr.. GATEKEEPERS: THE PROFESSIONS AND CORPORATE GOVERNANCE. *Oxford: Oxford University Press.* 2006

[20] Sarbanes-Oxley Essential Information. (G. Thomas, Editor) Retrieved June 25th, 2017, from SOX-online:The Vendor-Neutral Sarbanes- Oxley Site: http://www.sox-online.com/basics.html

management's controls assessments, following standards established by the PCAOB. Under the SEC rules, management's annual internal-control report must contain:

- A statement of management's responsibility to establish and maintain sufficient internal control over financial reporting for the company.
- A statement to identify management's framework in order to evaluate the effectiveness and efficiency of internal controls.
- Management's assessment of the effectiveness and efficiency of internal controls as of the ending of the company's most recent fiscal year.
- A statement that the company's auditor has provided an attestation report on management's assessment.

Furthermore, as per the new rule, internal control includes assurances of accurate maintenance of the records, as well as financial reports that are in compliance with generally accepted accounting principles. The rule also stipulates that managers and directors provide their signature on receipts and payouts, and that publicly traded companies maintain adequate systems for the prevention and detection of unauthorized material transactions. Management must make disclosure of all material weakness in a company's internal-controls structure. If there is an existence of material weaknesses, senior executives will then be not able to conclude that the company's internal control over financial reporting is efficient.

PCAOB Issued Auditing Standard which addresses dually to the work that is necessary to audit internal control over financial reporting and the relation between the audits to the audit of the financial statements. The integrated audit ends up in resulting in two audit opinions: one on the internal controls and the other on the financial statements. The standard also requires the auditor to make communication in writing to the audit committee of the company about all the significant deficiencies and material weaknesses of which the auditor is aware. The auditor is also required to make communication in writing to the management of the company regarding all internal control deficiencies, and to notify the audit committee that auditor has made such communication. Section 404 draws attention to the beneficial processes that comprises of the financial reports of an organization. In order for management to make its annual assertion on the efficiency of its internal control, management will be required to document, analyze and evaluate all controls that seems significant to the financial reporting process.

Implications for Indian Companies Issuing Securities in US Markets

After a drawn out time of corporate embarrassments in the United States from 2000 to 2002, the Sarbanes-Oxley Act (SOX) was ordered in July 2002 to reestablish speculators' trust in the money related markets and close provisos that enabled open organizations to dupe financial specialists. The demonstration profoundly affected corporate administration in the U.S. The Sarbanes-Oxley Act requires open organizations to reinforce review advisory groups, perform inside controls tests, make executives and officers by and by subject for exactness of monetary explanations, and fortify revelation. The Sarbanes-Oxley Act likewise builds up stricter criminal punishments for securities extortion and changes how open bookkeeping firms work.

Any Indian company that has listed their securities on New York Stock Exchange, American Stock Exchange or National Association of Securities Dealers Automated Quotations, need to completely comply with the provisions of the Act. The implications are inclusive of the territory beyond the US, criminal penalties for senior management in breach of certain clauses of the Act; enhancement in the disclosure based on harsh internal controls reporting, certification by senior management and independence necessities for audit committee members.

It has been determined that SEC has been taking a stand on these aspects on a case-to-case basis. One recent example is that the SEC's rule concerning the composition of audit committees of listed issuers. Sarbanes-Oxley needed the SEC to pass a rule mandating that every one member of audit committees be freelance administrators. However the company governance laws and rules in European country as an example, and many different countries with twin board systems, needed company audit committees to incorporate a labor representative. SEC rules don't, however, take into account staff of associate institution "independent" for concern that associate unscrupulous company officer might appoint staff to the board UN agency were duty-bound to the company's management. Following a dialogue with the Union, the SEC was confident that in those jurisdictions with twin boards, the obligatory labor representatives on institution audit committees were firmly freelance of the company's management. The ensuing final rule with reference to audit committees contained associate exception for these jurisdictions that might permit staff UN agency don't seem to be officers of a corporation to take a seat on the audit committee. this permits the affected issuers to fits each sets of law. And it preserves the intent of Sarbanes-Oxley - to make sure that freelance administrators will communicate directly with auditors while not management interference. Another example of the SEC seeking to accommodate the special circumstances of foreign issuers came with the foundations associated with the publication of monetary info given in ways in which not strictly in compliance with U.S.A. typically Accepted Accounting Principles or generally accepted accounting practices. During this space, associate exemption was given for non GAAP communications outside the U.S.A., even wherever those communications reach the U.S.A. a 3rd example of accommodation was once the PCAOB pressed out some problems concerning oversight of foreign audit corporations. Underneath the Sarbanes-Oxley Act, all audit corporations, together with non-US audit corporations, providing important audit services for issuers listed within the us, square measure needed to be registered and inspected by the PCAOB. Attributable to potential conflicts with foreign privacy laws and obstruction statutes, the PCAOB has created some changes within the info requested of foreign corporations throughout the registration method.

Conclusion

It’s been a few years since the Act had been implemented; some of the critics feel that the implementation has gone a bit far. Particularly, the Section 404 that demands and requires the certification of internal control is expensive and a bit unnecessary. This provision has even led some foreign issuers to declare that they may leave the USA’s capital market altogether rather than to have the certification of the internal control done. It seems easy for an individual issuer to look upon the cost of compliance with the federal security of American laws and balk. But there exists a beneficial attachment to the cost of capital as well. The capital markets of the America are profound and liquid. Around half of the entire world’s equity shares are traded in the America by capitalization of the market. Moreover, non American investors have a fortune invested in the country’s stock market. Thus, the requirements of the Act cannot be efficiently evaluated in vacuum. They are crucial as they have produced and will definitely produce certain improvements that will help to restore and reinforce the confidence of the investors in the market and thus lower the cost of capital to the certain issuer.

It is already made clear that the provision of the Act is to help strengthen the business operations being carried out in the US and along with the foreign issuers to seize the opportunity to use the internal control assessments as a opportunity to manage and not only as an exercise to comply.

The SEC still remains committed to a level playing field for all the foreign as well as domestic issuers. But it is recognized that cross-border listings frequently entails the issuers to navigate the duplicative or even contradictory regulations in distinct jurisdictions. While the SEC is unwilling to compromise where investor protections are concerned, some duplicative or contradictory regulations can compromise those protections and place an unnecessary burden on issuers, firms and investors.

Probably the best explanation that can be given for the implementation of the Act was the pressure on the politicians to act from the public, interest groups along with the politicians themselves which was so immense that the non implementation of the Act was not an Option. The crisis that was faced by the countries regarding the corporate scandals had triggered the intervention form the government at a scale that is unprecedented in recent times. Furthermore, it is difficult to discern the innumerable principles that were behind the intervention. Thus, the best explanation for the actions of the government was in a way same as that with the Act. Perhaps, the most crucial component of the Act was precisely the delegation of the power to the PCAOB, so that there could be customization of rules and thus the response to the feedbacks could be much more rapid. Professional lobbyists, may seek the outright repealing of the Act as a bargaining technique while planning to settle on regulatory reform as a compromise, but academics, the makers of the policy, and the public would do well to see those techniques for what they are and recognize the Act, like many regulatory institutions, as a work in progress. Rather than pushing for the repletion of the Act, a more cost-effective approach is to push for the SEC and PCAOB for the usage of their authority to curtail the requirements that are not really necessarily cost effective.

The basic idea behind the Act had been developing for years. The creation of auditing oversight body by the federal bills dates back to the 1978 which becam[1]e prominent after the hearings and reports of auditing failures prompted in the market downturn of the early 1970's. Similarly, legislation was debated again in the 1995. The run up to the Act, the congress heard scores of the witnesses the debate and that too in detail about how the auditing should be regulated. In a number of other controversial areas-executive compensation and stock options, audit firm rotation, general design of accounting rules-Congress showed a willingness to choose further study over either regulation or delegation.[21]

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[21] Bratton, William W. "ENRON, SARBANES- OXLEY AND ACCOUNTING: RULES VERSUS PRINCIPLES VERSUS RENTS," *Villanova Law Review* 48, 2003.

An Ingrained Look at Commercial Contracts: Analysis of Energy watchdog vs. Central Electricity Regulatory Authority

- Jai Bajpai[1]

Great sculptors and artists spend countless hours perfecting their talents. They don't pick up a chisel or a brush and palette, expecting immediate perfection. They understand that they will make many errors as they learn, but they start with the basics, the key fundamentals first.

- *Joseph B. Wirthlin*

Abstract

A concomitant of the doctrine of freedom of contract is the binding force of contracts, a force which a classical Roman jurist compared to the binding force of the law itself. However, rather than alluding to the variety of sanctions which are available if a contract is broken, the notion of the binding force of contracts is often used instead to draw attention to the general refusal of the courts to deny them effect on the ground of unfairness or inequality. This refusal is also reflected in the development of the law of frustration. If the view were taken that the rationale for the doctrine of frustration is simple that in the circumstances the law decides that it would be unfair to keep the parties to the term of their agreement, this does not mean that simple unfairness is the test of frustration. In 2013, Central Electricity Regulatory Commission (CERC) allowed Adani and Tata Power to sell at higher price due to increase in coal prices. Later, the same was upheld by Appellate Tribunal of Electricity(APTEL). It was surprising to observe that both CERC and APTEL overlooked simple principles of contract which govern impossibility under Section 56 of Indian Contract Act, 1872. It is pertinent to note that such a compromising agreement continued till the year 2017, during which the honorable Supreme Court took cognizance of the matter and reminded of basic principles of contract which govern impossibility while reversing the order of CERC and APTEL. It has, therefore, become an opportunity to revisit basic principles of law and to remind ourselves and the legal minds of the country to recognize the importance of these principles; if these principles are overlooked they are certain to create havoc such as in this case.

Keywords: Commercial contracts, CERC, APTEL, Indian Contract Act 1872.

Introduction

In the year of 2006, Gujarat Urja Vikas Nigam Limited issued a public notice inviting offers for long term of power supply. Haryana also issued a similar public notice for purchase of 2000 MW on long term basis. Subsequently in 2007, Tata Power won bids of Maharashtra, Gujarat, Punjab and Haryana to sell power at Rs. 2.26 per unit. In 2008, Adani power started its coal based power supply project in Mundra, Gujarat. It agreed to provide electricity at Rs 2.35 per unit. Both of these companies were mainly importing their coal from Indonesia. Thereafter, in 2010, Indonesia made changes in the price of coal in order to match the international standards of pricing. This led to cost escalation for Tata Power and Adani. Both Tata and Adani applied to Central Electricity Regulatory Commission (Hereinafter, referred to as CERC for brevity) in 2012, seeking relief from the increased coal price. They invoked force majeure under Section 56 of the Indian Contract Act, 1872. CERC[1] allowed for compensatory prices to both the companies at 52 paisa per unit to Tata and 41 paisa per unit for Adani respectively. As states were incurring huge losses on this, they applied to Appellate Tribunal of Electricity (Hereinafter, referred to as APTEL for brevity) in year 2014, it upheld the decision of CERC and ordered the same. The Supreme Court was then approached, it ordered the tribunal to reconsider the matter. APTEL then issued orders to CERC for deciding the compensation rates for the companies based on their Power Purchase Agreement (Hereinafter, referred to as PPA for brevity). CERC allows for the same and orders the compensatory charge to be levied on states but asked Supreme Court to take final decision for the matter. Then in April, 2017 the Supreme Court set aside CERC order allowing for compensatory tariff.

Commercial Impossibility: Right to Frustrate AContract?

Section 56 of the Indian Contract Act, 1872 reads as “an agreement to do an act impossible in itself is void." Contract to do act afterwards becoming impossible or unlawful. A contract to do an act which, after the contract is made, becomes impossible, or, by reason of some event which the promisor could not prevent, unlawful, becomes void when the act becomes impossible or unlawful. A contract to do an act which, after the contract is made, becomes impossible, or, by reason of some event which the promisor could not prevent, unlawful, becomes void when the act becomes impossible or unlawful.”[3]

A contract is not frustrated because of its performance has become more onerous or burdensome.[4] Namely because of abnormal rise or fall in prices a sudden depreciation of currency; or an unexpected obstacle to the execution of the contract.[5] The mere price hike in coal faced by Adani and Tata could not be interpreted as something which might frustrate the contract. The Supreme Court was right in recognizing the principle that mere terms of a contract becoming onerous does not amount to the frustration of it. This rule is applicable even in cases where a party has become insolvent or has become unable to get finance, it would still not frustrate the contract, unless of course, the parties have agreed otherwise.[6] The courts have no power of absolving from performance of the contract, merely because it has become onerous on the account of unforeseen circumstances.[7]

Even disappointed expectations of both parties to a contract do not lead to frustrated contract. For example, where a contractor who contracted to build in eight months and could only do so in twenty-two months because of scarcity of labour cannot claim frustration and payment on the basis of *quantum meruit.*
The losses which are being incurred by Adani power and Tata power could not be construed as an impossibility. As a company's agreement to pay bonus to its workmen is not frustrated by its subsequently discovering that its expectations of its state of prosperity envisaged earlier has not been fulfilled.[8] Thus, the profitability of a company is of no concern while deciding for the impossibility of the contract. When a wholly abnormal rise or fall in price, a sudden depreciation in currency, an expected obstacle to execution or the like, do not by themselves affect the contract.[9]

A case on similar facts but on a smaller scale yields the same effect. For example, a contractor having contracted, cannot go back on the agreement simply because it does not suit him to abide by it due to abnormal rise in the market rate of material and labour.[10] In another similar case on a smaller scale, a subsequent order by the government, fixing prospectively a higher price for salt, did not frustrate a previous contract for sale of salt, wherein the price was not dependent upon variations consequent upon government orders.[11] Thus, changes in price due to governmental policies and decisions cannot render the contract void or impossible under section 56 of the Indian Contract Act, 1872.

Even a high rise in the price of coal could not have frustrated the contract, as a contract, to supply freight cannot be said to become impossible, merely because the freight could not be procured except at an exorbitant price.[12]

In India, the law dealing with frustration must primarily be looked at as contained in Section 32 and 56 of the Contract Act.[13] The courts can give relief on the ground of subsequent impossibility when it finds that the whole purpose or the basis of the contract has been frustrated by the intrusion or occurrence of an unexpected event or change of circumstances, which was not contemplated by the parties at the date of the contract.[14] The word 'impossible' in relation to a contract between commercial people must be understood in commercial sense;[15] and the test of impossibility is whether it is practically impossible for a party to perform the contract within the specified time.

Tata Power and Adani failed to fulfill any of the conditions for claiming impossibility of contract under Section 56 of the Indian Contract Act, 1956. In the case of *Satyabrata Ghose v Mugneeram Bangur & Co*[16], the courts stipulated for conditions that would make for impossibility in any contract, it held that that a promise is discharged if, for some cause which the promisor could not prevent performance may become impossible by:

i. Change in law rendering a contract unlawful or impossible of performance;
ii. Destruction or non-existence of the specific subject matter assumed by the parties to exist or continue in existence;
iii. The non-existence of state of things assumed as the foundation of the contract;
iv. Such circumstances intervening which render the performance within the time in way contemplated, impossible, although performance of the contract according to its terms may be literally possible.
v. The death or disability of the promisor, where the promise was to perform something in person.

Subsequently, in the case of *Walamji Lalji v Anil Chandra Bangal*[17] and *Re Mahadeo Prasad Shaw v Calcutta Dyeing& Cleaning Co*[18] essential conditions for application of Section 56 were explained as :-

i. A valid and subsisting contract between the parties;
ii. There must be some part of the contract yet to be performed.
iii. The contract after it is entered into becomes impossible of performance.

CERC's order was given for reasons unknown as the companies did not fulfill the conditions for the applicability of Section 56 of Indian Contract Act, 1872.

Analysis of Power Purchase Agreement (PPA)

Moreover, Supreme Court pondered upon the clause 12.3 of the contract that provided a list of events that were to be considered as "Force Majeure Events" and clause 12.4 which contained "force majeure exclusions" signifying events which were not to be considered as "Force Majeure Events".

The Apex Court observed the doctrine of frustration under common law. According to this doctrine a contract would be frustrated only if the fundamental basis of the contract was affected by the change in circumstances[19]. Specifically, clause 12.4 of the PPA specified that changes in cost of the fuel for the project or in the event of contract becoming onerous would not be considered as a force majeure event. The apex court for reasons unknown travelled to the cases which explained 'Doctrine of Frustration' without going to the statutory provisions which specifically, expressly and clearly provided for events which were not be considered as 'force majeure' events.

A much strong argument for denying application of Section 56 of Indian Contract Act, 1872 would be that the parties assumed the risk of change in prices. Where the parties expressly assume the risk to a certain event happening, they cannot avoid the contract then on the grounds of impossibility[20]. A contract is not frustrated merely because the circumstances in which the contract was made are altered. The Indian Contract Act does not enable a party to a contract to ignore the express covenants thereof, and to claim payment of consideration for performance of the contract at rates, different from the stipulated rates, on some vague plea of equity. The parties to an executor contract are often faced, in the course of carrying it out, with a turn of events which they did not at all anticipate- a wholly abnormal rise or fall in prices, a sudden depreciation of the currency, an unexpected obstacle to execution, or the like. Yet this does not affect the bargain they have made.[21]

It is one thing to say that the profit or remuneration has diminished and another thing to say that the performance has been rendered impossible. The decrees in amount of remuneration has the effect of rendering the contract more burdensome. But to attract the doctrine of frustration, burdensomeness is not necessary consideration; the impossibility of performance of the contract is the true criterion[22]. There is no frustration where performance of the contract remains physically and legally possible though commercially unprofitable. Thus, the law cannot be applied to cases of commercial impossibility. Mere commercial impossibility will not excuse a party from performing the contract. Mere increased cost of performance of losing in a transaction does not make the contract impossible.[23]

The UNIDROIT Principles

The International Institute for the Unification of Private Law (Hereinafter, referred to as UNIDROIT for brevity) is an intergovernmental organization which works on harmonizing private international law. India became a signatory to it in the year 1950 and has accepted to mould its national laws on the models provided by it. It would be pertinent to discuss the principles which were formulated by UNIDROIT in the context of the case. The Principles are based on the principle '*pacta sunt servanda*', and stress that a party for whom its performance becomes more onerous generally, is nevertheless bound to perform,[24] but allow adaptation of the contract in cases of hardship.[25] Hardship occurs where the occurrence of events fundamentally alters the equilibrium of the contract, either because the cost of the disadvantaged party's performance has increased, or because the value of what it has to receive has decreased. The present case falls into the former category. However, provided the events meet the following requirements:

i. The events occur or become known to it after the conclusion of the contract;
ii. The events could not reasonably have been taken into account at the time of the conclusion of the contract;
iii. The events are beyond its contract; and
iv. The risk of the events were not assumed by it.

The fourth essential is not satisfied in the case of Tata and Adani as clause 12.4 of the PPA specified that changes in cost of the fuel for the project or in the event of contract becoming onerous would not be considered as a force majeure event. The courts cannot permit Section 56 of the Indian Contract Act, 1872 to become a device for destroying the sanctity of a contract. The court will also not apply to assist a party which does not want to fulfill its obligations under the contract.[26]

Impossibility and Risk Allocation

The clause 12.4 of the PPA specifying that changes in cost of the fuel would not be considered as a force majeure event must be understood in the light of 'risk allocations' in a contract. The doctrine of frustration is mainly concerned with the incidence of risk, whether anyone or both parties to the contract take the risk of happening of the supervening event. The question ultimately is always one of risk-allocation. The question to be answered therefore is whether one or other party has expressly assumed the risk of the events which have occurred, or, if not, whether the court thinks that one or other party ought reasonably to be treated as having assumed the risk.[27] The parties to the contract are free and can expressly provide that the risk of supervening events shall be borne by one of them or by the other, or that they can apportion it or deal with it various other ways, namely, for suspension of performance, compensation, refund, restitution or discharge. Where the contract makes a provision, this will normally preclude a court from holding that the contract has been discharged by supervening impossibility, because the parties have allocated the risk knowingly.

The present case pertains to a situation where a party to a contract undertakes the risk that performance of their contract may prove more difficult or onerous than expected; or even impossible as a result of normal changes in circumstances; but they may not take the risk of performance proving impossible due to abnormal or extra-ordinary occurrences. However, the apex court was right in observing that escalation in coal prices would not amount to an 'abnormal or extra-ordinary' event, so far as the clauses of the contract are concerned, it was observed that the parties provided for 'risk allocation' as they agreed to perform the contract even if the cost of procuring coal rises or changes substantially. Section 56 cannot be applied where the parities have in terms provided what was to happen in case of impossibility of performance.[28] A party who makes an absolute promise accepts the risk of performance being or becoming impossible. He may not avoid liability, if he fails to perform, even though this is not due to any fault on his part.[29]

Conclusion

The facts of the instant case give rise to suspicion about whether there are certain political factor at play while the judicial bodies of the country decide upon a pertinent matter and its issues. The judicial body such as CERC and APTEL took no heed of the contractual principles and ruled in favor of the companies. However, the apex court reminded the two bodies that contractual principles cannot be overlooked in any case. It serves as an example of how a simple principle, if overlooked, can render a complicated agreement or contract useless. Time and time again, the apex court has been vigilant of such discrepancies. This also serves as an example to the commercial bodies that they cannot overlook basic contractual principles while entering into an agreement. The Supreme Court's overreaching approach include an extended version of an already recognized doctrine of frustration to situations where the parties have decided to forgo the allocation of risk not to the default rule under Section 56, but rather to satisfy their own whims and fancies. Further, this decision did avail the opportunity to strengthen a largely underdeveloped jurisprudence on *force majeure* clauses. The Supreme Court has once again saved the day and reminded each and every body, whether judicial or commercial, the importance of basic principles of contract.

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Corporate Criminal Liability – Issues and Perspectives

- Anupama Agirala

Abstract:

Industrial Revolution, globalisation, liberalisation and privatisation ('etcetra-tions') led the boom of the corporate world thus, making companies an essential and inevitable part of our daily lives. Of course, a company doesn't breathe or function like a living natural human being does, but if any crime is committed by the company, then can it be held liable like any other human being? If yes then, what sort of a punishment would be imposed on it if it is held guilty? Above all the important question that needs to be answered is whether mens rea can be attributed to a company? It is well understood that the fundamental principle of criminal liability is actus non facit reum nisi mens sit reai, which means that an act does not make one guilty unless the mind is also guilty. In other words, actus reus has to be accompanied by mens rea to constitute a criminal offence. So, how does this principle work when the there's a corporate entity invovled? The present paper will try to unravel these issues.

Keywords: Criminal liability, Legal personality, India, Corporate criminal liability

Introduction

A Corporation is a different legitimate element set up through some enactment or enrolment process. They have rights and liabilities isolate from that of their investors. A portion of these companies have resources and offices in different nations separated from their nation of origin also and such organizations are known as multinational enterprises (MNEs). Multinational enterprises have come to assume an enormous part in many parts of human life today. Their forces have developed at a bewildering rate in the course of the most recent few centuries, to such an extent that they are frequently contrasted with whole countries. Hence, forcing a type of methods for responsibility and control over these multinationals and enterprises is of vital significance and ought to be amazingly high on the rundown of needs for each country.

In layman's terms, the convention of corporate criminal risk is basically the teaching of respondent predominant which has been foreign made into criminal law from tort law. This convention expresses that a partnership can be made criminally at risk and sentenced for the unlawful demonstrations of any of its operators, gave those specialists were acting inside the extent of their real or evident expert. Evident expert is that specialist which an operator can be surmised to have by a normal sensible individual, while real expert is expert that a company purposely endows to its specialist or representative. To disentangle matters, if a reasonable relationship can be set up between a worker's criminal direct and his corporate obligations, the organization will be held criminally subject for the representative's lead.

Theories

There are various judicial theories that gave rise to corporate criminal liability. Some of these theories are briefly discussed below:

Theory of Vicarious Liability

From late 1800s and through the early 1900s, this was the theory using which the Courts held the Company liable for the harm caused. The basis of this theory is *Qui facit per alium, facit per se*, which means that he who acts through another acts himself and *respondeat superior* (let the master answer). According to this theory, a company is liable for the harm caused by its employee while acting during the course of employment. In order to apply this theory two steps need to be followed:

i. It should be determined as to what constitutes the *actus reus* of the acts committed by the employee
ii. The determined *actus reus* must be imputed on the Company due to employer-employee relationship.

This theory was used by the Courts in England and Wales for crimes in the nature of strict liability. The point to be noted here is that, in this period the Courts were of the view that corporations were incapable of committing homicide as they lacked requisite intent.

Identification Theory

Identification theory, known as Alter Ego theory, was introduced by the Courts in the case of *H.L. Bolton Co. v. TJ. Graham & Son* in order to expand the scope of corporate criminal liability by holding the company liable for crimes that require intent. In *H.L.Bolton* case, the Court explained that a Company is like a human body with brain, nerves and hands. The managers and directors of the Company represent the directing will of the Company and control the actions of other employees. The employees of the Company represent the hands of the Company. They are just mere servants and agents and do not control the Company. Hence, the state of mind of the managers is the state of mind of the Company.

The landmark case on identification theory is *Tesco Supermarkets Ltd v Nattras* where the Court held that the manager of a separate store was not sufficiently senior to hold the Corporation liable for her acts. The Court explained that a corporation acts through living persons as it does not have mind and hands and other human faculties to carry out functions. But the person through whom the Corporation acts does not speak or act for the Corporation but he acts as the Corporation itself and his mind is the mind of the Corporation. The conduct of the individual and his state of mind can be attributed to the Company only when the person is in control of the Company or a sphere of its activities. Hence, this limits the scope of application of this theory as it is applicable to solely the activities of the senior management, whereas criminal offences are often committed at the lower level. Therefore, it becomes impossible to attribute the liability on bigger corporations.

Identification theory is different from the theory of vicarious liability, in the sense it widens the ambit of criminal prosecution of Companies but holding them liable for offences that require *mens rea*. The Companies can be held vicarious liable for negligent acts or omissions on part of the servants of the Company but not for criminal liability for manslaughter. To hold the Company liable for in such cases it has to be established that the person acted not for but as the Company itself. This difference was clearly explained by the Courts in *R v HM Coroner for East Kent, Exparte Spooner & Others.*

Concept of Reactive Fault

The Concept of reactive fault has been combined with identification theory in the Corporate Manslaughter and Corporate Homicide Act. It is used by Russian law with regard to administrative liability. Reactive fault means that the Company failed to take adequate preventive measures before the criminal act was committed. Here, the *mens rea* is derived from the preceding neglect omission of the Company. But this concept also has a limitation as only senior management can be held liable.

Aggregation theory

This theory in influenced by the theory of vicarious liability and it was introduced by the Courts in United States. The Court in *United States v Bank of New England,* has beautifully explained this theory. The Court stated that as per principle of aggregation all the criminal acts and *mens rea* of various employees of the Company have to be summed up in order to hold the entire company criminally liable. For example, if A, B and C are employees of the Company X. then, the knowledge of A. B and C will be summed and imputed as the knowledge of the Company. This theory is useful in cases where the acts and *mens rea* of one employee is not sufficient to constitute a criminal offence. Therefore, the thoughts of different agents of the Company are linked together in order to create the required mental element. This theory takes into account the practical realities of the corporate decision-making. As there are different directors in a Company each of whom has specialised knowledge and responsibility therefore, when at times it is important to aggregate the knowledge of two or more directors to create the needed mental element for holding the Company criminally liable.

The theory, like the previous theories, has its own limitations in the sense that the *men rea* requires mere knowledge of wrongdoing or negligence. Therefore, it becomes difficult when *mens rea* requires intention or recklessness. In such cases the Company will only be liable when one of the employees satisfies the required *mens rea*.

Position in India

In India essentially there were two obstacles in holding the Company criminally liable:

i. Company not capable to have *mens rea*.
ii. Company cannot be imprisoned and hence, no effective order can be made.

Legal Personality

A company is a legal person which separate from its members or shareholders. It has certain rights and liabilities of its own. A company is not just a legal institution because it is a legal device to meet the social and economic needs and it is publicly and socially responsible. Hence, a company is a political, legal, social and economic institution. In the case of *Solomon v. Solomon & Co*., the court held that a company is a separate person from the people constituting it. It capable of having an independent corporate existence. Similarly, there is Section 11 of the Indian Penal Code which defines' person' to include any company or association of body of persons, whether incorporated or not. Further, Section 3(42) of the General Clauses Ac, 1897 reiterates the same principle. As a company has legal personality therefore it can be subject to certain liabilities in case of violation of any law as any natural person. The only difference between a natural person and a company in this regard is that a company cannot be subject to imprisonment and therefore the penalty is always in the form of fines

Earlier Position

Like the Courts in England and United States or anywhere else in the world, the Indian courts, initially, were also of the view that Company being a legal fiction is not capable of having *mens rea* and hence, it cannot be held criminally liable. Courts were also of the view that as Companies cannot be sentenced to corporal punishment or imprisonment, therefore subjecting them to prosecution would result in nothing as no effective order could be passed in such cases. This attitude of the Courts can be seen in various cases like in *Sunil Chandra Banerjee v. Krishna Chandra Nath,* where the Court held that as a Company is not a natural person therefore, it cannot have requisite *mens rea* for the offence of cheating and it cannot be punished as it is not a physical body.

Similar views were taken in *State of Maharasthra v. Syndicate Transport,* wherein the Court held that a company cannot be prosecuted for offences whose sentence is either corporate punishment or imprisonment like perjury, bigamy or rape. This is because a Company cannot be imprisoned as it is a fictional creation of law. Though it is capable of separate existence from its members even then it is just a fiction and cannot be subjected to such punishments. Barring these exceptions the Company ought to be indictable for criminal acts or omissions of its directors, or authorized agents or servants, whether they involve *mens rea* or not, provided they have acted or have purported to act under authority of the corporate body or in pursuance of the aims or objects of the corporate body.

The Court in *Champa Agency v. R. Chowdhury*, held that a corporate body cannot have the necessary *mens rea* for the offence of criminal breach of trust and hence it cannot be prosecuted.

Similarly in *Kalpanath Rai v. State*, the Court held that the Company is not a natural person and therefore it cannot have *mens rea* and in this case the Court was dealing with TADA where there was no provision to make the Company liable for the acts of its officers. The Court further held that in statutes like Essential Commodities Act, Prevention of Food Adulteration Act, the Companies can be held to be offenders for the acts of the persons responsible for its management.

The High Court of Calcutta in *A.K.Khosla v. T.S.Venkatesan*, held that there are two tests to impute liability on a company namely, the test of *mens rea* and the test of mandatory sentence of imprisonment. Though no opinion was given by the Court in this regard.

Hence, it can be seen that the Courts were hesitant to hold that the Company is capable of having *men rea.*

Present Position

The attitude of the Courts changed with the case of *The Assistant Commissioner, Assessment-II, Bangalore and Ors. v. Velliappa Textiles Ltd. and Ors.*, where the Court held that a Company can be prosecuted for criminal offences and in awarding a sentence there is a lot of discretion given to the Courts but it has to be according to the statutory provisions. The Courts may, if the Company is convicted impose a fine if it is one of the punishments prescribed as a Company cannot be imprisoned. The mere fact that a Company cannot be imprisoned does not mean that it cannot be prosecuted at all. The Court also highlighted the importance of reputation to the Company and that the conviction itself is bound to bring bad name and lower the image of company before the public at large. There it is also some sort of deterrence.

Implication of *Velliappa (AIR2004SC86)* was that a Company cannot be prosecuted in offences that are punishable with imprisonment or imprisonment and fine as in those cases there is no discretion on the Courts. This legal difficulty was solved by the recommendation of the Law Commission of India in its 41st Report which got no response from the Parliament. But again in its 47th Report Law Commission of India made a recommendation (similar to the 41st Report) that offences that are punishable with imprisonment or with imprisonment and fine, in such cases, the Court is competent to impose fine only. Also in offences which are punishable with imprisonment and some other punishment which is not fine, even in those cases the Court is competent to impose fine only and ignore imprisonment.

Finally, *Velliappa* case was overruled in the case of *Standard Chartered Bank and Ors. etc. v. Directorate of Enforcement and Ors. etc,* where the question that came up for consideration before the Court was whether a company or a corporate body could be prosecuted for offences for which the sentence of imprisonment is a mandatory punishment. The Court though remained silent about the issue of *mens rea* of a Company but answered the question regarding the sentence. The Court held that it is well established that a Company can be criminally liable and hence prosecuted except for offences that the Company is incapable of committing by reason of the fact that such offences require personal malicious intent. Indian Penal Code has offences with prescribed punishment of imprisonment or fine or both and other offences with prescribed punishment of imprisonment and fine. So if the point of view is taken that as a Company cannot be imprisoned therefore it cannot be prosecuted for the latter offences, which may be graver than the former, then it will be total injustice and defeat the intent of the Legislature. Therefore, the Courts in such cases have discretion to impose only fine and ignore imprisonment. This discretion is to be exercised only in case the accused is a Company but for natural persons both imprisonment and fine have to be imposed. Then the court would not be passing the sentence in accordance with law. Such a view is important because in the present globalised world Companies undertake vital activities in various sectors that affect the life, liberty and property of the citizens and hence, amenability of the Company to criminal law is essential for a peaceful society with stable economy.

The Supreme Court in *Iridium India Telecom Ltd. v. Motorola Inc and Ors.* has held that it is well established in all jurisdictions of the world that are governed by rule of law that companies and corporate houses are capable of having *mens rea* and therefore they cannot claim immunity from criminal prosecution on the ground of lack of *mens rea.* The Court further held that if a group of persons that guided business of companies had criminal intent that would be imputed to body corporate. The Court relied on *Standard Chartered Bank,* and held that a corporation can be held liable for offences that have imprisonment and fine as the prescribed punishment.

Similarly, in *Aneeta Hada v. Godfather Travels and Tours Pvt. Ltd and Avnish Bajaj v. State and Ebay India Pvt. Ltd. v. State and Anr.,* the Court relying on *Standard Chartered Bank and Iridium India Telecom Ltd.* has held that a company can have criminal liability and further, if a group of persons that guide the business of the companies have the criminal intent, that would be imputed to the body corporate.

Hence, the present position of India is that it uses the theory of identification whereby the *mens rea* of the controlling mind (directors, managers) of the Company is imputed to the Company. But as already mentioned, the problems with identification doctrine is that only senior management should have the requisite criminal intent and also most of the times it is difficult to determine the criminal intent as it might have been a aggregation of intents that results in the requisite criminal intent. Hence, this limits the scope of application of this theory.

Criminal Liability of companies under Legislations

There are many legislations in India under which the companies are held criminally liable. Like under Indian Penal Code a company can be held liable for the offence of cheating and dishonest misappropriation of property. A company may be held liable for corruption offences in India under the Prevention of Corruption Act, 1988, which primarily addresses corruption in the public sector, but also brings within its ambit, private citizens who abet the corrupt actions or omissions of public servants in respect of an official act. While POCA 1988 does not specifically create a corporate offence relating to bribery, a company being a 'person' could be held liable under the provisions of POCA 1988. Running on the same lines section 17 of the Prevention of Food Adulteration Act, 1954 provides that if an offence has been committed by a company then the company and the person in charge of and responsible to the company for the conduct of its business shall be guilty of the offence and be liable to be punish accordingly. Similar principle is reiterated in the Essential Commodities Act, 1955, the Narcotic Drugs and Psychotropic Substances Act, 1985, the Trade Marks Act, 1999 and the Income Tax Act, 1961. The Industrial Disputes Act, 1947 and the Negotiable Instruments Act, 1881, provide that where an offence is committed by a company then the person responsible for the conduct of business of the company will also be liable and hence, punished. Similar provision is also given most environmental laws like the Public Liability Insurance Act, 1991.

Corporate Criminal Liability under Companies Act, 2013

Companies Act, 2013 which has supplanted the Companies Act, 1956 has expanded the corporate risk of the chiefs. The Act has likewise expanded the money related punishments and detainment. Not just corporate criminal obligation under Companies Act, 2013 is perceived however the demonstration additionally perceives common liabilities. The Companies Act, 2013 makes the executive criminally at risk as well as incorporate officers in default under the idea of corporate criminal obligation in India.

The term Officer in a default is a wide term and can incorporate entire time executive, key administrative faculty and such different chiefs without KMP who has been indicated by the Board of Directors and each other chief who knows about the default which is being finished by prudence of accepting of load up procedures or by taking part in same without raising any complaint or where rebelliousness has occurred with his assent or conspiracy.

All these legislations seem good because they enable a company to be criminally prosecuted but the problem is that the penalty in such cases is only fine. For a company earning great profits, paying some fine doesn't affect it in any way. Fine acts as deterrence only for small companies. Hence, even after having such diverse legislations and case laws there are lacunae that have to be filled.

Need for law on corporate manslaughter

India does not have any specific legislation or specific offence regarding corporate manslaughter like that present in United Kingdom or Australia Capital Territory .These countries enacted laws after they experienced incidents/accidents but there is no need for India to wait for an accident to happen to make a law, a stitch in time saves nine. An important fact to be taken into account is that companies are becoming very powerful these days due to globalisation and industrialisation. Most of the business takes place in company form of organisation in the present world and after liberalization the competition between the companies is increasing with each passing second. In such an environment of cut throat competition it becomes essential to make laws to prevent the companies from resorting to unscrupulous practices.

Conclusion

It can be gathered from the above discussion, that most of the jurisdictions in the world started with the attitude that company cannot have *mens rea* and therefore cannot be held criminally liable. Later, plethora of theories were developed which made it possible to attribute *mens rea* to a company. The Courts using these theories shifted to a stage where they recognised a company to be capable to have *mens rea* and therefore can be held criminally liable however there was the problem of sentencing. As a company cannot be imprisoned therefore it could not be held liable for offences that impose imprisonment or imprisonment and fine both. This problem was answered by the courts by giving discretion to Judges to ignore the imprisonment and impose fine only in such cases where the offender is a company. Therefore, the present position in many jurisdictions around the world is that *mens rea* can be attributed to a company.

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Extent of Anti-Trust Interference in IPR

- Swapnil Singh and Sara Jain

Abstract

Since the dawn of science and reason, the human society has been consistently evolving in terms of developing more sophisticated and beneficial technology. Later, it was felt that in order to continuously innovate and progress, efforts of the innovators are duly acknowledged and their novel inventions are effectively protected. In order to achieve the same two laws were enacted; namely, the intellectual property law and the antitrust law. While intellectual property law directly accomplishes this goal by providing exclusionary rights to its holder, antitrust law functions to promote competition i.e. in itself a principal promoter of innovation. However, owing to the intrinsically distinct approach these laws have, it is only reasonable to consider that sometimes, they appear to be antithesis to each other. This is evident as the intellectual property law endangers competition and the antitrust law engenders competition. Thus, there has to be a harmonious interpretation of both the laws so as to protect the interests of all the stakeholders in the market.

The present paper is a study about the extent of interference of anti-trust in Intellectual Property Rights in India. The Patent Act has been subjected to three substantial amendment Acts, in 1999, 2002 and 2005 and these amendments have restricted the rights of patent holders. A significant observation relevant in this regard is that the recommendations of the High Level Committee constituted by the Govt. of India for Competition law were not incorporated in Competition Act, but were added in Section140 of the Patents Act. Although there is a common area where both Intellectual property and competition law intersect with each other yet their objectives are always conflicting with each other but there has to be a harmonious interpretation of both the laws for the benefit of the society.

Key words: Intellectual property rights, Competition law, The Patent Act, Anti-trust

Introduction

Competition law functions towards protection of those practices, which smoothens the functioning of the markets whereas IPRs give exclusive rights over a property to the extent of monopoly.[1] There exists an historical tension[1] and inconsistency[1] between the Patents Act and the Competition Act. This is evident as the former *endangers* competition and the latter *engenders* competition.[1]This is primarily because the intellectual property provides exclusive rights to its holders[1] by rewarding the inventor with a temporary monopoly to encourage innovation.[1] Competition law on the other hand curbs the anti-competitive behavior arising out of such rights.[1]

The Interplay between IPR and Competition

The Patent Act has been subjected to three substantial amendment Acts, in 1999, 2002 and 2005[1] and these amendments have restricted the rights of patent holders[1]. A significant observation relevant in this regard is that the recommendations of the High Level Committee constituted by the Govt. of India for Competition law[1] were not incorporated in Competition Act, but were [1]added in Section140 of the Patents Act.[1] A patent right specifically means a right secured by patent; usually meaning a right to the exclusive manufacture, use and sale of an invention or patented Article.[1]

Thus, by definition, it is an exclusionary right[1] provided in the Patents Act.[1] Furthermore, the philosophy behind giving patent holders a special right[1] is to stimulate innovation by giving increased gains. The U.S Supreme Court in *Mazer v. Stein*[1] stated that the economic philosophy of granting a patent is the conviction that encouragement of individual effort by personal gain advances public welfare. Further this encouragement promotes innovation.[1] The Patents Act and Competition Act must be harmoniously interpreted[1] as competition law and IPR both promote competition in different manners[1]. Also, it is a well-established principle that any repugnancy in statutes cannot be readily inferred[1] and any interpretation in that regard should be avoided.[1] It is based on the belief that while enacting a new law, the legislature has thorough knowledge of the existing legislations[1] and thus, would not deliberately enact a directly contravening law. The Competition Act provides for exemptions to its application in case of IPR[1], but the same is not absolute in nature.[1] It is imperative to note that Section3(5) strikes a balance between protection of patent rights and prevention of anti-competitive behavior arising out of unreasonable restraints imposed by a patentee[1] by excluding only reasonable conditions.[1]

Interface in India

With the advent of excess of cases related to preclusion of the overruling effect of IPR over competition law, it has become imperative to analyze this area in details by looking into judicial precedents and statutory analysis. Disparagingly examining, it can be concluded that not everything under the IPR regime is subject to constitutional law but then it is also not totally immune to it.[1] Talking about the Competition Act of India it specifically provides for the proscription of anticompetitive practices and not particularly monopolies. Competition law mainly functions to control the unfair practices under IPR law regime in accordance with the provisions enumerated

The Legal Analysis

The Competition Act, 2002 is primarily based on the principles of liberalization and economic efficiency. With the initiation of trade barriers and swift influx from international markets, the Indian legislation was had to come up with a robust regulation for the same. Keeping in mind all these new challenges, the formulation of Competition Act took place which sought to fulfill its purposes by way of prohibiting following things[1]

a) Abuse of dominant position by the market players

b) Regulations on Mergers and Acquisitions

c) Anti-competitive practices

Even our constitution has the mention of the competition law and its policy by way of Articles 38 and 39 of the Constitution. The principles of promoting and securing economic, political and social justice are enumerated in it.[1] The obligation is on the State to safeguard the same. Furthermore, the State is loaded with the liability to standardize the ownership of resources and regulate the control so as to fulfill the common good as well as its objectives. This is to guarantee and see that the concentration of power in not only in the hands of few leading to to anti-competitive practices and tying agreements.[1]

The Competition Act, 2002,[1] was legislated with stout provision and insertion of TRIPS guidelines. The interface and interplay between IPR and competition law can be easily traced in the form of incorporation of S. 3(5) of the Act. It is fundamentally an absolute provision which acts as an exception for IPRs. This is done for the sole reason of incentivizing innovations and subsequently promotes technologically advancement.[1]Nevertheless, it also controls proficiently, the unreasonable practices related to IPR.[1] Thus, there exist provisions for safeguarding such agreements under IPR that go primarily against the spirit of the Competition Act, 2002.[1] Provisions have been elucidated to address any anti-competitive practice pertaining to the IPR which has to be proved through the canal of abuse of dominant position as stated under S.4 of the Competition Act, 2002.[1]

Excludability of IPR from Competition Law: The Grey Area

There are certain areas where competition law has to intervene even in the cases where matter is specifically related to IPR because it harms the public at large and then it can come under the ambit of section 27 of the Competition Act which provides for the provision of cease and desist.

Remedies available under the Patent Law and Competition Law are inherently distinct

The Patents Act does not provide an exhaustive account of all remedies available in case of abuse of dominant position by the patentee.[1] While the Patents Act provides for compulsory licensing[1] and insertion of restrictive conditions[1], it excludes the remedies that may result out of refusal to grant license on reasonable terms or violation of FRAND commitments.[1] This aspect is covered under Section4 of the Competition Act and if it is concluded after investigation[1] that an enterprise has abused its dominant position, the remedies under Section27 can be resorted to.[1] The remedies under Section27 are materially and fundamentally different from those available under the Patents Act.[1] Hence, if the remedy for such complaints is not considered by barring the jurisdiction of the Competition Commission, it would be detrimental to the interests of the general public as the orders passed by the CL are in rem, whereas the Patents Act provides for specific remedies only.

Section 3(5) does not exclude the jurisdiction of Competition Commission

In *United States v. Microsoft*[1], it was held that an IPR does not give its holder immunity from the laws of general applicability, including the anti-trust laws.[1]The Competition Act provides for exemptions to its application in case of IPR[1], but the same is not absolute in nature.[1] It is imperative to note that Section3(5) strikes a balance between protection of patent rights and prevention of anti-competitive behavior arising out of unreasonable restraints imposed by a patentee[1] by excluding only reasonable conditions.[1] The Competition Act retains the power to adjudicate on the legality of the patentee's conduct,[1] even though the CLs may provide remedy against anti-competitive practices.[1] Thus, Section3(5) would not exclude the application of the provision as the right put forward i.e. to demand unreasonable royalty cannot be characterized as protecting an intellectual property.[1]

Engendering and Endangering: Judicial Precedents

There have been plethora of cases and various landmark judgments relating to the conflict between competition law and IPR. An abuse of dominant position under Section 4[1] of the Competition Act is not a cause that can be made a subject matter of a suit or proceedings before a civil court.[1] It has been held in *Aamir Khan Productions Pvt. Ltd.* v. *Union of India*[1] wherein the Court while dealing with a matter pertaining to the issue of IPR held that CCI has the jurisdiction to deal with all cases concerning competition law and IPR where there is serious concern regarding an anti-competitive practice regarding competition.[1] It is a blanket provision incorporated in the competition law. However, there is no provision under S. 4 on the ground of IPR abuse or public policy for interference in such cases. It specifically enumerates that action can be taken only in cases where there is abuse of dominant position leading to appreciable adverse effect on the competition. Cartel is yet another issue that is dealt elaborately under the competition law. Formation of cartels is a prevalent practice among industries and firms. Recently the proprietors owning IPRs have indulged in formation of cartels and thereby causing distortion of competition in the market. An evident example of the same can be traced from the film industry as it involves both IPR issues i.e. copyright along with competition law provision affecting the industry. In the case of *FICCI Multiplex Association of India v. United Producers/Distributors Forum (UPDF),*[1] the petitioner (FICCI) filed a complaint against the UPDF alleging the formation of market cartels in the film industry. This was deliberately done by UPDF to boost their revenue, and thus, it had refused to strike deal with the multiplex owners. This has direct and drastic effect on the multiplexes as their business is wholly dependent on the film industry.

Consequently, this resulted in anti-competitive practice of refusal to deal leading to distortion of competition adversely for gaining profits. Further, defendants held 100 per cent share in the industry and thus indulging in limitation of supply of films in the market qualifies as an anti-competitive practice. It qualified as a violation of S. 3(3) the Competition Act too. The parties on delivery of the show cause notice filed a petition in Bombay High Court on the pretext of lack of jurisdiction of CCI to decide a matter pertaining to IPR. The Court citing S. 3(5) of the Competition Act 2002 read with S. 3(1) held that the latter section cannot curtail the right to sue for infringement under IPR, and further CCI has jurisdiction to entertain all matters that can be presented before the Copyright Board. Recently, CCI also held that copyright is not an absolute right but is merely a statutory right under the Copyright Act, 1957.[1]

It can, therefore, be safely concluded that the precedents enumerate greater protection to original artistic works as compared to the furtherance of commercial interest. CCI has come out with a landmark decision as it undoubtedly moved towards checking the abuse of dominance by forming cartels in the market of the film industry. In *Hawkins Cookers Limited v. Murugan Enterprises,*[1] The Delhi High Court held that a well-known mark on the pretext of being prominent and well-known cannot be left unchecked to create a monopoly in the market by indulging in practices of controlling the incidental market. The same would fall under the category of abuse of dominant position in the market and is prohibited.

Undoubtedly, IPR owners can enjoy the fruits of their labour via royalty by issuing licenses but the same is not absolute. The jurisdiction of other countries also highlights the fact that exercise of rights under IP laws is subject to the competition law/anti-trust law. Dealing a case pertaining to refusal of license, a U.S. Court in Kodak II and in In re Independent Service Organizations,[1] held that IPR does not grant an unfettered right to violate the anti-trust law. Further, in United States v. Microsoft,[1] the Court held that the IP laws are not immune from anti-trust laws and all the general laws are equally applicable on IP laws and exclusive right holders.

Excessive pricing and predatory pricing is yet another problem that competition law is grappling with. It is also closely associated to refusal of license. In Union of India v. Cyanamide India Ltd. and another,[1] the Hon'ble Court held that overpricing of lifesaving drugs is also prohibited, and the same does not fall beyond the ambit of price control. Competition law is currently facing a lot of trouble in keeping the branded agencies and patented products under the ambit of price control. In case of lack of substitutes, there is always a potential danger hovering in the form of monopolies. The domain of life saving drugs in relation to high pricing is a major concern in developing nations. Competition law is enacted to promote fair practices prevent abuse of dominant position and completion in the market that is prevalent in the form of tie-in arrangements, excessive pricing, exclusive licensing etc. In the case of tying arrangements, a highly usable product or service is tied with a less marketable product or service and the seller agrees to sell both together irrespective of the choice of the buyer. Practicing illegal, tying arrangements is against the competition law or anti-trust law. In Tele-Direct case,[1] it was observed that the selective refusal to license a trademark constitutes an abuse of the dominant position. Recently, the Microsoft case is yet another example that dealt with the issues of abuse of dominant position and refusal to deal with third parties and inclusion of tying arrangements.

Conclusion

In can now be readily inferred that competition law and IPR have complementary goals. Both work towards attaining the definitive objective of promoting innovation by giving incentives and protecting economic & consumer welfare. IP furthers promotes innovation which subsequently results in advancement of competition in the market. Competition law has to enforce regulation on IPR only to that extent where interference by holder of IPR is in the applicability domain of competition law. The need of present is to strike an optimal balance between the policies of Competition and IPR. Only by such measure the long term relationship between two distinct regimes can be secured. Though, there are certain implications that need to be taken into contemplation while merging the IP law and competition law.

IPR law must be controlled by antitrust laws only when there adverse effect on the competition. IPR regime *endangers* competition Antitrust laws *engenders* competition.[1] This is primarily because the intellectual property provides exclusive rights to its holders[1] by rewarding the inventor with a temporary monopoly to encourage innovation.[1] Competition law on the other hand curbs the anti-competitive behavior arising out of such rights.[1] Despite both laws are very different but their objectives and goals are converging. The bottom line which remains is that, the Anti- trust laws have to intervene in matters related to intellectual property in the cases where there is a adverse effect on competition. Therefore, a true application of laws and rationale behind the precedents would help in ensuring that there exist a smooth functioning of both the domains and there can be a harmonious interpretation of both the laws.

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Sweat Equity Shares: A Legal Perspective

- Ayushi Gupta

Abstract

Earlier Security and Exchange Board of India (SEBI) came up with certain Regulations for the issuance of sweat equity shares. A few measures were also introduced to avoid the misuse of sweat equity shares. However, the entire plan and its limits and conditions are capable of being exploited. In any case, before we go into the regulations, it becomes pertinent to understand the fundamental idea of sweat equity shares as enumerated under Section 79A of the Companies Act, 1956 and Section 54 of the Companies Act, 2013. The objective of this paper is to provide an understanding of sweat equity shares in light of Companies (Share Capital and Debentures) Rules, 2014 with an analysis depicting the abuse of these shares. Lastly, it is shown how the misuse can be prevented.

Keywords: SEBI, Equity shares, Companies Act 2013, Sweat Equity

Introduction

Sweat Equity Shares are provided to company's employees in return for their contribution which they make towards the company.[1] It is one of the methods to allow share based discounts meaning that these shares are offered at discount but not in terms of money. Basically, these shares are issued at a concessional price or for consideration. The rights available to are in the form of Intellectual Property Rights or Value addition. The purpose of these shares is to acknowledge the work made by the employee towards the company by rewarding employee. The question now arises what is the need to incentivize the employee? This is to ensure that employees continue to remain in the company. It also motivates employees to contribute to the company. Thus, it ensures employee's stake and growth in the company.[1] This leads to development of the company and it can draw substantial benefits from it.

Legislative Clause

A. **Sweat Equity Shares**

Sweat Equity Shares is defined as follows:-

"Sweat Equity Shares means such equity shares as are issued by a company to its directors or employees at a discount or for consideration, other than cash, for providing their know-how or making available rights in the nature of intellectual property rights or value additions, by whatever name called."[1]

B. **Employee**

The term 'Employee' has been defined as:-

"a)A permanent employee of the company working in India or out of India; or

b)A director of the company, employed as a whole time director or executive director of a company."[1]

C. **Value Addition**

The term 'Value Addition' has been defined as:-

"Value addition means anticipated economic benefits derived by the enterprise from expert and/or professional for providing know-how or making available rights in the nature of intellectual property rights, by such person to whom sweat equity is issued for which the consideration is not paid or included in –

(a)The normal remuneration payable under the contract of employment, in the case of an employee and/or

(b)Monetary consideration payable under any other contract,in the case of non-employee."[1]

Aspects Relating to Sweat Equity Shares under the Companies (Share Capital and Debentures) Rules, 2014

Employee is defined as:-

(a) Permanent employee of the company who has been working in India or outside India, for at least last one year; or

(b) A director of the company, whether a whole time director or not; or

(c) An employee or a director as defined in sub-clauses (a) or (b) above of a subsidiary, in India or outside India, or of a holding company of the company.[1]

Restrictions on the Issue of Sweat Equity Shares[1]

The following restrictions are imposed to prevent the misuse of Sweat Equity Shares:-

- The special resolution passed by the company is valid till the period of 12 months from the date when the special resolution passed.[1]
- These shares issued will be locked in for the period of three years from the date when these shares were first issued. That is the directors and employees cannot transfer these shares for the period of three years. The share certificate of the company will contain the date of expiry of these shares which can be mentioned in any prominent manner.[1]

Procedure for the Issue of Sweat Equity Shares[1]

- Organize and arrange a meeting to think over the proposition of issue of sweat equity shares and set a date, time, place and plan for general meeting and to pass a special resolution for the same.
- Send notices (writing) that will contain explanation for the same to shareholders for conducting general meeting. This explanation to be added to the notice for the general meeting according to Section 102 of the Act must contain the following details.

Under Section 102 the details of the explanatory statement attached to the notice of the general meeting. The details will contain:-

- The date of the Board meeting at which the proposal for the issue of sweat equity shares was approved.
- The basis for the issuance of such shares.
- Shares issued as sweat equity shares or are intended to be issued as sweat equity shares.
- Directors or employees to whom sweat equity shares were issued.
- The terms and conditions for issue of sweat value shares, as well as the basis or reasons for the same.

- The time period consisting of how long a particular person is associated with the company.
- The names of the all the directors or employees to whom the sweat equity shares will be issued and their association with the promoter or/and key managerial personnel.
- The cost at which the sweat equity shares are to be issued.
- Consideration including non cash consideration as well, if any to be obtained for the sweat equity.
- The limit on managerial remuneration, assuming if infringed by issuance of such sweat equity shares and the procedure as to how it is to be managed.
- A declaration that the company will follow the pertinent accounting standards.
- Diluted Earnings per share after the issue of sweat equity shares calculated as per the applicable accounting standards.[1]
- Hold the General Meeting and pass special resolution as per Section 114(2) of the Act.[1]
- Filing should be done within 30 days of passing the same with MCA in Form No. MGT
- Allotment of sweat equity shares in the board meeting.
- Form No. PAS-3 should be filed within the period of 30 days from the date allotment of sweat equity shares made in the board resolution.
- There will be Register of sweat equity shares in Form No. SH-3 maintained by the company which should contain the details of sweat equity shares issued.

Quantum of Sweat Equity Share

The limit to the issuance of sweat equity shares is fifteen percent of the existing paid up equity share capital or shares worth of 5 crore rupees whichever is higher. However, at any given point of time this limit will not surpass 25 % of the paid up equity capital of the company.[1]

Pricing of Sweat Equity Share

The price of these shares will be decided by the registered valuator as the fair price. Justification is also required for the same. Registered valuator is also responsible for the determining the value of IPR, Know how or value addition for the issuance of sweat equity shares. A report is also to be prepared which should contain the justification for the same and submitted to the Board of directors.

Accounting Treatment of Sweat Equity Share Issued[1]

At a time when sweat equity shares are issued for consideration other than the cash based on the report by the registered valuator this non cash consideration should be dealt in the following manner maintained in the books of the account of the company:-

- When the consideration is in the manner of depreciable or amortizable asset, it should be mentioned on the balance sheet of the company according to the accounting standards.
- If clause (a) is not applicable it will be followed according to the accounting standard.

For the Section 197 and 198 of the Act, the amount of sweat equity shares will be considered part of managerial remuneration under the following circumstances[1]:-

- When sweat equity shares are issued to directors to director or manager of a company.
- When these shares are issued for non- cash consideration which can be maintained in the balance sheet of the company according to the accounting standards.

In regard of sweat equity shares issued amid the accounting period, the estimation value of the sweat equity shares should be considered a type of compensation in the financial statement of a company, when these shares are issued before the acquisition of an asset.[1]

When the shares are issued after the acquirement of an asset, the estimation of the of the value of asset, as decided by the valuation report, should be conveyed in balance sheet according to the accounting standards and if such value of sweat equity shares is in more than the of the cost of the asset acquired, according to the valuation report, then it should be dealt as a type of compensation given to the employee or the director in the financial statements of the company.[1]

Disclosure in the Directors' Report[1]

It is the responsibility of the Board of Directors to disclose, in the Directors Report for the year in which sweat equity shares are issued the following particulars to the issuance of sweat equity shares:-

- Directors or employees to whom sweat value shares were issued.
- Shares issued as sweat equity shares.

- The number of sweat equity shares issued to the directors, key managerial personnel or other employees indicating distinctly the number of such shares issued to them.
- In case of the non-cash consideration issued and the individual names of assignees carrying one or more than one percent issued share capital.
- The basis for the issuance of such shares.
- The terms and conditions for issue of sweat value shares, as well as the pricing formula.
- The aggregate number of offers emerging because of issue of sweat equity shares.
- The percentage of the sweat equity shares of the aggregate post issued and paid up share capital.
- The consideration comprising of non-cash consideration obtained or benefit ensued to the company from the issue of sweat equity share.
- The diluted Earnings Per Share (EPS) after the issuance of sweat equity shares. The company should keep up a Register of sweat equity shares in Form No. SH.3 and as per Section 54 should mention the details of sweat equity shares issued.

Registrar of A Company[1]

The Register of sweat equity shares might be kept up at the registered office of the company or any other place as the board may choose. The Company Secretary of the organization or by some other individual sanctioned by the board will verify the sections in the register.

Provisions under The Companies Act, 2013

According to the Section 53 of the Companies Act, 2013 a company cannot issue share at discount except provided in Section 54 and shares issued at a discounted price will be void.

Conditions to be Fulfilled

Despite anything contained in Section 53, a company can issue sweat equity shares of a class of shares issued already, if the following pre requisites are satisfied[1]:-

(a) The issue is approved by a special resolution passed by the company

(b)The resolution indicates the number of shares, the present market cost, consideration assuming any, and the class directors or employees to whom equity shares are to be issued.

(c) At least one year has passed since the date on which the company had started business and

(d) Where the equity shares of the company are recorded on a distinguished stock exchange, the sweat equity shares are issued as per the directions made by the Securities and Exchange Board and in the event that they are not recorded, the sweat value shares are issued as per the rules mentioned.

(2) The rights, limitations, restrictions and statutory requirements as are for the time being applicable to equity shares should be pertinent to the sweat equity shares issued under this section and the holders of such shares should rank pari passu with other equity shareholders.

Penalty

Under Section 53 violation of these provisions prescribes minimum fine of one lakh rupees and maximum 5 lakh rupees. Default of fine will lead to imprisonment of maximum 6 months or fine which will be minimum 1 lakh rupees and maximum 5 lakh rupees or both.[1]

Provisions under the Companies Act, 1956

A company shall not issue shares at a discount with the exception of Section 79.[1] A company can issue discount shares in the company of a class already issued if the accompanying conditions are satisfied:-

(a) Resolution passed by the company in general meeting should be authorised and approved by the Central Government.

(b) The resolution indicates the maximum rate of discount at which the shares are to be issued. Given that no such resolution will be authorized by the Central Government if the maximum rate of indicated in the resolution which surpasses 10% unless Central Government is of the view that higher percentage of discount can be permitted in the special circumstances.

(c) At least one year since the date on which the company was initiated its business.

(d)The shares to be issued at a discount within two months after the date on which the issue is authorized by the Central Government or within such extended time as the Central Government may permit.

(3) Where a company has passed a resolution approving the issue of shares at a discount it might apply to the Central Government for a request authorizing the issue; as well as any such application, the Central Government if, considering every conditions of the case, it supposes appropriate to do so, may make a request sanctioning the issue on such terms and conditions as it supposes fit.

Penalty

Every officer of the company who is in default shall be punishable with fine which may extend to five hundred rupees.

Comparative Analysis of Companies Act, 1956 And Companies Act, 2013

According to Companies act, 1956 as per Section 79 shares can be issued at discount after complying some conditions On the other hand according to Section 54 of the Companies Act, 2013 only sweat equity shares can be issued at discount. Under the new Companies Act issuance of shares with the permission of central government has been omitted. Also, the penalty has been increased in the new Companies Act. There is also a minimum and maximum limit to it which is not provided under the old Companies Act i.e. Companies Act, 1956. This shows that with the passage of time contravention of this provision is a serious offence and violation of conditions can even lead to imprisonment.

Recent Development

The Ministry of Corporate Affairs bought changes in some provisions of the Companies (Share Capital and Debentures) Rules, 2014 (Rules) through the Companies (Share Capital and Debentures) Third Amendment Rules, 2016 (Amendment). This amendment bought a positive change. This amendment gives an opportunity to the startups to issue their shares. By way of this amendment now any startup can issue sweat equity shares. The limit to which is 50% of their share capital for first five years from the date of its incorporation while other for other companies this limit is 25%.[1]This amendment gives an advantage to the startups over other companies now they can use this benefit to retain the employees. It is a known fact that startups suffer in setting the business initially. This amendment is a much welcome move by the ministry. It provides more flexibility to the startups.

Case Analysis

Brief Facts

Rendezvous Sports World Private Limited allowed giving sweat equity shares worth of 70 crores to Sunanda Pushkar asserting that she has an expert ability in event and brand management. This company has united different shareholder to make a consortium for offering to bid in IPL Kochi Franchise.

ABOUT THE RENDEZVOUS SPORTS WORLD LIMITED

Rendezvous Sports World started in August 2009 and the Kochi franchisee contract was made on March 17, 2010. As indicated by the rules, a company can issue sweat value shares only after one year has elapsed since the initiation of its business. In this way, as one year has not completed, the company isn't allowed to issue sweat equity shares.

Controversy

It has come to spotlight by the media that Rendezvous Sports has misused all the provisions of the Companies Act, 1956 in allowing sweat equity to Sunanda Pushkar. This made her give up her shares contending that she is profoundly hurt. BCCI claims that there is a condition in the bidding document that no details are to be disclosed as a "confidential proviso". The Government (central) has chosen to investigate the issue, Finance Ministry is investigating the issue of sources of funds. Also, Corporate Ministry is looking into non fulfillment of provisions under Companies Act.

Analysis

In the present scenario, Ms. Pushkar needs to provide an explanation for the issuance of the sweat equity shares given to her. Remembering the previously mentioned meaning of sweat equity shares which can be issued only to an employee or director of the company how she can be given sweat equity shares considering her role as sales and marketing consultant with RSW. Indeed, even the board of RSW will be responsible for the issuance of sweat equity shares. As sweat value shares were issued for a non-cash consideration, RSW would have appointed auditors or chartered accountants to complete the valuations of the IP or know-how or other value additions so as to legitimize such issuance of sweat equity shares as per Rule 9 of the

Sweat Equity Rules. This is one angle which should be completely examined, more particularly on meeting such statutory prerequisites. Moreover, Rule 6 prohibits a company from issuing sweat equity shares of over 15% of total paid up equity share capital in a year or shares exceeding the value of Rs. 5 crores, whichever is higher. In the occasion the limit is to be surpassed, consent of government would be required.[1]

In the present case, the estimated issue of sweat equity was for Rs. 70 crores, i.e. far beyond the limit stipulated under the said Sweat Equity Rules and that too without the consent of Central Government. Subsequently, this question needs to be inspected whether such an essential condition for issuing sweat equity under the Companies Act has been breached. The Companies Act additionally prescribes that one year should have been passed when the company has started its business for the issuance of sweat equity shares. In this aspect, RSW apparently commenced its business only in March 2010. This fact should be confirmed by the Registrar of Companies (ROC) and the Ministry of Corporate Affairs as if it is false, it will be infringement of the Companies Act.

What is distinct about the contract between RSW and Ms. Pushkar is that the Sweat Equity Shares had a lock in period of only 2 years, while the rule 10 of the Sweat Equity Rules provides for at least three years lock in period for sweat equity, which implies that these equity shares can't be transferred before the completion of three years from the date of issuance. A probe would only uncover whether such conditions were appropriately fulfilled; if not, the effect and results thereof.[1]

It remains a question what these legislative examinations in the long run yield. This obscured imbroglio, has uncovered India's deep rooted issues of transparency and governance over all spheres of life – be it sports, be it legislative issues, be it corporate morals. This is an illustration of intricacies in prohibitive trade practices issues and corporate dispute. The dispute predominantly rotates around the issues of tender on one side and issue of sweat equity shares contravening the provisions of Companies Act and Sweat Equity Rules, on the opposite side. Examination by Central Government and Competition Commission are necessary in order to bring the complex issues to an end. Many issues identified with the problem are till now unanswerable. Couple among those is confidentiality asserted by BCCI, status of IPL and its constitution, issues of corporate administration have again come forward

Suggestion

The misuse of Section 79A has unfolded on the media in the light of ill affair of Kochi cricket team and will transfer itself to people soon. Bribes can be disguised as shares, favors can be returned through assigning of shares and one's silence can be purchased by assigning of shares. The predictable outcomes are huge as the general population associated with a clandestine deal.

Section 79A hence should be changed with the goal that sweat equity is only for the individuals who sweat it out for the company. All others sweating it out for themselves or generally should pay straightforwardly for the shares.

Conclusion

Sweat equity shares are issued as a consideration to “employees”. This sweat equity shares are issued at discount to the employees. Discount here means not in monetary value but in the form

Know how, to avail Intellectual Property Rights or Value addition. Sweat value means a person commitment to a task or assignment of a company in terms of effort – rather than money related value. The value that is made in a company or some other asset is an immediate consequence of hard work by the owner. For instance, the work one may put into reconstructing the motor 1968 Mustang to enhance its value would be deemed as sweat equity.

Given the mayhem made by this IPL, different provisions of law have emerged, which are being investigated by the Government through its different organizations. In any case, one facet in this whole scenario, which has not been sufficiently analyzed and rather needs a deliberation, is that of "sweat equity shares" and the legitimate consequences thereof. In the light of actualities that have been accounted for in the media. It becomes pertinent to inspect the legal regime relating to "sweat equity shares".

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Flipdeal or Snapkart: An Unfinished Agenda

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Abstract

Flipkart has been constantly trying to take a lead in online shopping business market keeping in mind that it is the biggest player in non- Amazon camp. Snapdeal though the last, is also a competitor of Flipkart due to which the investors of Flipkart (Tiger global in particular) would want it to die and turn into ashes and the best way to do it is to embrace it and kill it. Moreover the other benefits that Flipkart can possibly draw is that after merger it will have a support of deep pocketed investor like Softbank which has a vision of USD 100 Billion fund and an open option of strategic approach to Alibaba, who is also one of the investors in Snapdeal, which will help to takedown Amazon. The other side Snapdeal on the other hand would be a part of this merger due to the decision of its majority shareholders such as Softbank who have invested USD 1 Billion and more in Snapdeal to fetch nothing but loss. Keeping in mind the benefits that both the companies would derive from the merger, they agreed to merge. An attempt has been made in this paper to study the impact of the merger on the both Flipkart and Snapdeal. Though the merger has not happened but we tried to know the probable impact on these two firms.

Keywords: Merger, Telecom sector, Strategic decision, Competitive Practices

Introduction

The Flipdeal or the Snapkart Horizontal Merger was basically an upshot of a strategic decision taken by the majority shareholders of both the companies in order to overpower the market share in online shopping business in India by giving a tough competition to their leading business rival, Amazon.[1]

The basic idea of merging or say acquiring Snapdeal was that Flipkart has been constantly trying to take a lead in online shopping business market keeping in mind that it is the biggest player in non- Amazon camp, so if it could possibly merge with a company which is the oldest player in the market with largest number of distribution centres and a good employee base then it may come at par with the popularity of Amazon.[1] In addition to the point, Snapdeal though the last, is also a competitor of Flipkart due to which the investors of Flipkart (Tiger global in particular) would want it to die and turn into ashes and the best way to do it is to embrace it and kill it. Moreover the other benefits that Flipkart can possibly draw is that after merger it will have a support of deep pocketed investor like Softbank which has a vision of USD 100 Billion fund and an open option of strategic approach to Alibaba, who is also one of the investors in Snapdeal, which will help to takedown Amazon.[1]

Snapdeal on the other hand would be a part of this merger due to the decision of its majority shareholders such as Softbank who have invested USD 1 Billion and more in Snapdeal to fetch nothing but loss.[1] These shareholders see this as a last resort of hope to recover their losses suffered since 2010, where Snapdeal has seen twelve rounds of funding in seven years of its survival.[1] The constant problems of growing losses and diminishing cash reserves for the survival of the company, in a kind of business which majorly depends on discounts and sale, have led the shareholders to favour the possible acquisition of the company by its closest and oldest rivals, Flipkart. Moreover, this merger is also the best possible idea for Snapdeal because Snapdeal being the “Dog Company under BCG Matrix” has limited option to either wind up the company, which is a very cumbersome process or be acquired by a stronger company and have a share in their combined entity stock deal.[1]

Keeping in mind the benefits that both the companies would derive from the merger, they agreed to it but price was still the setback of this venture. Conjecture about the merger surfaced in March 2017, when the investor of Snapdeal, Softbank was seeking out buyers and since then it has been struggling for the valuation of the company. Snapdeal which once in 2016 valued at $6.5 Bn fell down to $1 Bn in April 2017 suffering a loss of $495 Mn in Financial Year 2016. Still the two companies signed a non- binding Letter of Intent in May 2017 which led to further negotiations. In july 2017 Flipkart proposed to buy Snapdeal at a price between $700 Mn to $800 Mn but Snapdeal rejected the offered asking for a price of $900 Mn, to which later Flipkart negotiated and offered a price of $850 Mn. Unfortunately in August 2017 Snapdeal terminated the idea of merger with Flipkart stating that it can do better individually.

Strategic Decision Making

Strategic decision in form of Merger and Acquisition has always been a popular and preferable option for growing companies. The most popular types of M&A are horizontal or vertical market extension, which are not only means of corporate growth but are an alternative to organic growth which may not be a viable option at all times. Companies prefer M&A over other alternatives due to some strategic objectives such as Growth and expansion of the company, reduction of cost through economies of scale, gaining competitive edge in existing market, market or product extension and Risk reduction.

The proposed merger between the two companies driven by SoftBank was in the form of share swap.[1] SoftBank, being a very strategic and repeat buyer has been repeatedly investing in Indian start-ups such as Snapdeal and cab aggregator Ola. In May this year, it had infused over a $1.4 billionin digital payments platform Paytm.[1] The deal involved a changes in the stock-holding structure and not a cash component.[1]

When Snapdeal had initially started business it acted as an offline couponing businesses named moneysaver. The business underwent a quantum growth considering which they decided to take it online. Initially it performed really well but they wanted to do something big in the market. For this it started acquiring certain start-ups. This was a turning point in its business strategy. It started losing its charm when acquires the company which had no relations with the e-commerce. This problem further aggravated when Snapdeal was not able to expand its business in any other product. The brand value in e-commerce segment is majorly based on unique transactions and unique users versus biggies like Amazon and Flipkart. In light of this Snapdeal did not have a lot of options and therefore, ought to look for a support in the form of which is building itself as a marketplace around its wallet offering.[1] Despite the fact Snapdeal has over a million customes visiting its website every day, it has reported losses of Rs 2,960 crore in 2015-16, double that of the previous year. The investment of Ratan Tata also could not help in this respect.Windig up or liquidating was not an option as it is a very cumbersome process in India. Merger seemed to be a very strategic and efficient decision as it would give Snapdeal's investors a share in the combined entity in a stock deal. On the other hand Flipkart has a lot of loyal customer base but that does not necessarily mean that it has not had its share of problems.The markdowns at Flipkart came at a time when there was an exodus of talent form the company, especially at the senior levels.[1] The merger of Snapdeal and Flipkart seemed to be a better choice because Fipkart's investors, particularly Tiger Global, would want Snapdeal to die down and the best way to do that would be to embrace it and kill.[1] However, it is also said that from a business point of view, Snapdeal assets are not valuable to Flipkart, acquiring it makes sense to prevent it from doing further harm in Flipkart's fight against Amazon.[1] There exists a very limited scope for exploiting the synergies with Snapdeal due to an existing overlap between the customers and seller base of the two corporations. The acquisition of Snapdeal would not go a long way to ease the burden of Flipkart in terms of competition faced from Amazon.

According to several experts, there are two perspectives of viewing this deal as a one form a branding point of view and the other from a business point of view.[1] From the former point of view, once the acquisition takes place, if Snapdeal gets destroyed, the sellers would merge with Flipkart, but then the brand values is going to concern the investors ad Flipkart will have to bear an additional burden managing a lot of aspects as the businesses strategies of both the businesses are very different. From the business perspective once SoftBank takes out its investments from Snapdeal it would result in creation of a monopolistic market in the e-commerce industry. Whenever one business captures another it does so as to seamlessly integrate its expertise into both the businesses. But how far would a merger between the two entities playing in the same segment would generate strengths is still an unanswered question.

The proliferation of the business base and capacity of Amazon had become a major threat for both the companies. Its model being based on three universal core principles of online shopping: providing a massive selection for the shoppers, maintaining low prices, and creating a great shopping experience.[1] With this it has created a state of art infrastructure for itself. Amazon had pledged to infuse funds in the e-commerce sector until it captured the entire market. It has had a similar track record in the United States as well. Given the deep pockets they hold and the kind of incentives they provide to their investors, it would take a ton to pitch a fight against the biggie. Looking at how well it has been performing and in order to combat this problem the rivals Flipkart and Snapdeal proposed to unite in order to prevent Amazon from capturing the entire market.

The online Shopping Business market is mainly concerned with the market share of each company and the capacity of industrial growth rate that the companies have, as these two factors define the actual position of online sites in the market. The other factors such as product or technology are not an important factor in this kind of business because sites like Snapdeal, Flipkart or Amazon have similar product range and technology. Thus, to analyse the two factors of Market share and Industrial growth rate in respect of the decision of merger can be done through BCG Matrix which is growth-share matrix.

In BCG Matrix there are four kinds of companies; Star, Question mark, Cash cows and Dogs. Stars are the companies who have both high market share and industrial growth rate hence having the best position like Amazon presently. Question Mark are those companies which have high industrial growth rate but low market share. Cash Cows are companies with high market share but low industrial growth rate and lastly, Dogs are the companies with both low market share and industrial growth rate.

Now, in the present case Flipkart can be termed to be a Cash Cow company because like mentioned above Flipkart being the biggest player in after Amazon has a high Market share but it has no further scope of growth without being investment being flushed in its system. On the other hand, Snapdeal has fell to the category of a Dog company, though not a appropriate term to use but the position of position of Snapdeal is such that neither its has good market share nor it has any scope of growth. All the investors of Snapdeal have suffered only loss and the organic structure of Snapdeal has also shaken as both its employees and managers are not satisfied, thus the option that is left with Snapdeal is to either wind up the company or sell its shares to a strong yet to company who need it so as get an appropriate price.

Therefore, the scenario demanded the merger if seen from a strategic point of view because selling the company is the most convenient option that owners of Snapdeal have to their rescue and Flipkart in turn will get an investor like Softbank who can inject the required investment in the system of Flipkart. If the merger would have been effective then Flipkart had a chance to convert itself into a “Star” company and simultaneously Snapdeal would have received a fair value for their company.

Reasons for Drifting Apart

The fate of the proposed merger, however, proved to very bleak and hence could not see the sunlight of the day due to multiplicity of reasons.[1] The reasons majorly included potential prospective aftermath that it could have resulted into and inflicted upon a variety of stakeholders such as shareholders, employees and the governing board of respective corporations. The operative mechanism of the merger deal suffered a major impediment in the form of differences of proposed clauses of valuation. The prevalence of a complex structure of deal could have resulted in multi fold increase in the amount of tax liability on the part of investors coupled with an inefficient taxation structure arising out of the governing legal provisions. Since the tax incidence was not measured out as a part of valuation on a prior basis, it caused a major drift between the shareholders and Board members. Further, opposition was also faced due to differential payout to some of the investors like Kalaari and Nexus Venture Partners and influential shareholders like Premji Invest and Temasek.[1]

In addition to this, the agreement of merger, if would have come into effect, a five years non-solicit clause would bar all shareholders approaching any employee, buyer or seller working with Flipkart for the next five years. The kind of restrictions imposed on shareholders was manifestly rejected by them as it imposed unworkable restrictions thereof. The online e-commerce business having a feature of common buyers and sellers along with a small pool of skilled workforce and one multiple investors having stake in multiple companies could not support this restriction and potential conflict and chaos was bound to arise.[1]

For the two companies, in light of having a major shift in focus from gross merchandise value (GMV) to cash profits, quantum growth in profitability was a distant dream. Initially, due to discounts, short term prosperity could be achieved but consequently once the discounts go, so would the customers. The cash flow from Venture Capitalists has never been limitless to sustain the losses.

Key Players in the Deal

Founders and investors

The driving force of the deal was Japanese giant SoftBank – the largest stakeholder in Snapdeal with an investment of US$900 million accounting for 33% holding in the company.[1] Some of the other minority stakeholders in the company included early investors Kalaari Capital and Nexus Venture Partners, holding 8 percent and 10 percent of equity, respectively and the founder members Kunal Bahl and Rohit Bansal, who hold about 6.5 percent. The kind of benefits that each of the investors differed invariably which became a major reason for the fallout of the deal.

The two companies had greater expectations in terms of the benefits that the deal would offer them as compared to the investments that they had made in Snapdeal. For supporting the mega funding round of Snapdeal in 2014 Kalari had sold some of its stock for US$100 million. This step was termed as a type of hedge funding by the company in 2011 when the entire e-commerce business was still in a very nascent stage. Similarly, when Nexus joined Snapdeal, it brought with itself huge amount of funds to support Kalari's Funding.

On the other hand SoftBank is considered as a very strategic player in the Indian ecosystem in light of the multiple investments made by it in the Snapdeal and other companies such as Ola coupled with a pledge to invest US$10 billion in India over the next 10 years.

It has been observed that the Snapdeal Founders Kunal Bahl and Rohit Bansal while denying the reports of sale are more amenable it. It is possible that may not be as hard hit as it seems. By selling a large chunk of their shares to Ontario Teachers' Pension Fund at optimum valuation, they have turned themselves into angel investors in a number of start-ups since then. Along with it both the founders have drawing increasing annual compensation.

Initially the two founders had envisaged for an IPO for the purposes of reorganising of the company and tackle problems of cash crunch and inability to raise funds. However, with the insistence of SoftBank, the focus must shift to sale and not funding Snapdeal on hopes of profitability and IPO. It is also said that the major reason why SoftBank wishes push this merger ahead is that it wants to avoid writing off its investment.

Buyers, Sellers related Entities

The benefits of the merger are multifarious in spite of the fact that the Gross Sales or Merchandise Value of Snapdeal has come down by nearly a third, it could bring about several benefits. While all of Snapdeal's business may not come to Flipkart, the e-retailer wouldn't have to invest more on people or infrastructure if the two merge. Also, the deal would give Flipkart additional supply chain infrastructure to take on Amazon, which is aggressively expanding its network across India. With the help of this, operational efficiencies such as fast deliveries, regional fulfilment of orders, lower supply chain costs, additional sellers (Snapdeal has three times the sellers as compared to Flipkart's) and higher customer satisfaction could be achieved (which is questionable because according to certain sources, Snapdeal itself does not enjoy a sound customer base).

However, uniting of the two entities could not prove to be a smooth marriage strictosenso as compared to earlier experiences of Flipkart with Myntra and Jabong. Although both companies are giant e-commerce players, the models followed by each of them are not similar. Flipkart additional supply chain infrastructure to take on Amazon, which is aggressively expanding its network across India. Further, achieving operational efficiencies is not something that can be achieved in a blink of an eye. It demands a plethora of synergies in terms of logistics and business, which till achieved would increase the cash burn of the two entities combined. Issues of business structures, culture and practices, geographic barriers would pose challenge like any other deal.

Competitive Practices

Undoubtedly, the merger between Flipkart and Snapdeal is not just meant for the purposes of achieving operational efficiencies in the e-commerce business. The driving force behind the adoption of this strategy for reconstruction is the *'pitched battle for supremacy'*between US online retail giant Amazon and homegrown market leader Flipkart.[1] As more and more Indians are shopping online, the two players have been locked in the intense battle for leadership and thereby infusing millions of cash to strengthen infrastructure and capture larger market share both in terms of sellers and buyers.[1] The strategies that have been adopted by Amazon of commitment of investment worth US$5 billion have caused an upside down change in the market dynamics. Such action had the rug pulled from the feet of Flipkart and Snapdeal and thereby dwindled their markets.

However, if the proposed merger had the chance of seeing the light of day, the Indian e-commerce market would have witnessed three extremely competitors in the market, i.e. Alibaba, Amazon and the rejuvenated Flipkart with a bigger market share through the acquisition of Snapdeal. Interestingly, SoftBank would be in a more profitable position as it would hold a major stake in two companies i.e. Flipkart and Snapdeal.

Snapdeal while it reduced levying of charges on the seller had acquired lowest marketing fees among competitors in half its product line.[1] Such kind of practices could have deeply rooted in the operational structures of the so formed new entities thereby giving rise to an extremely high competitive or possibly anti-competitive market in India.

Impact Analysis of Merger

Though the biggest acquisition of India did not see the sunlight of the day but what if the deal would have fallen through, what would have been the benefits that acquirer could have derived or the decision of terminating the idea of merger was a thoughtful decision, what could have been the impact on consumers, other stakeholders and market.[1]

To begin with the benefit analysis of acquirer, Flipkart primarily seems to be benefited by the merger for reasons that when Flipkart is in fight with a company like Amazon then having Softbank on its investor roster, the world's largest start-up investor plays the primary attraction of the deal. Specially, when the Softbank need the return on their investment and is ready to invest in Flipkart after the deal is effective, sharing a little burned of Fixel (Investor in Flipkart), who wants to take out some cash from Flipkart.[1] But at the same time taking up Snapdeal may not be such good deal for Flipkart because engrossing Snapdeal will be very challenging for Flipkart and where Flipkart is still processing the acquisition of Ebay, during such time acquiring Snapdeal will be a big distraction for the management of Flipkart.[1] On the operation front as well, Snapdeal is not a great option for Flipkart since the monthly sales of Snapdeal is less than even the average monthly sale of Flipkart owned fashion site Myntra.[1]

The grounds on which the merger can be analysed are the other benefits that a mergers are generally expected to yield, as mentioned above. Among these benefits first is expansion and growth of company which in the present case is to a little extent true as with Snapdeal will come all its distributing units that is infrastructure as well and other the human resources etc. Second is Market extension which may not be a benefit for Flipkart as the functioning area of both the companies is same thus, give no edge to the acquirer. Third the reduction of cost which definitely is not happening as Snapdeal if kept as a separate company will require investment and expansion of business will anyway lead to incurring of more cost initially. Lastly, gaining of competitive edge in the market is the only benefit that might have come to the doorstep of Flipkart through this merger.

The next that we shall analyse is the impact of merger on consumers.[1] Viewing the last few record we can see that due to the competition between the three rival that is Amazon, Flipkart and Snapdeal, it's the consumers who have been at the receiving end of advantages as more and more discounts come their way to lure them but the deal of merger might put an end to this deep discounting era for the consumer. This is being said because the big companies have understood that levying off heavy discount to gain customers is a temporary option where consumers are not committed to one retailer, so the companies need to build trust and relationship with customer in order to hold onto them. Also the companies have understood that other players also have capital to invest so, discounts won't eliminate the players from the market but will only lead to wastage of their own capital. Moreover it has also been observed that often big companies use the tactic of discounts to trouble the small competitions that it has but now when all the major players are merging into one there may be no significant small retailer due to whom this trick might come into play.

But on the other hand the scenario can be exactly opposite, deal of merger like this may actually accelerate the trail of discounts coming to the end of consumers because Amazon has declared that it will invest in India until it wins it, thus if the deal became effective then both the big companies would have flooded the market with more luring offers to consumers in order to get an edge over each other. In addition to this the consumers could have got the best experience possible as Snapdeal has the highest seller base and Flipkart has good customer service, thus when combined together they may have resulted in a best deal possible for consumer. But then at the same time merger or no merger, the consumer is not going to be affected at a large level because all the three companies continue to remain in competition due to which the consumer is always the end beneficiary.

The other impact analysis which needs the attention is on the employees and managers of the companies. Lately the employee and in fact key managerial persons of both the companies have left their position being unhappy from the decision taken by major investors of the company. It has been generally observed that it is the organic structure and players who are mostly impacted by the inorganic decisions. it all depends on the way the Flipkart would handle Snapdeal, if Snapdeal is still treated to be an individual company like Ebay and Myntra then the employees may be benefitted by the merger as the company which was running into losses may revive and they may reap the benefits from the same but if Flipkart decides to take off Snapdeal from the market then employee may suffer termination and salary cuts. Though in the present case if the deal would have been through then Snapdeal promised its employees a Rs. 193 Crore bonanza or half of what the Snapdeal founder would have got from the deal. Thus, the deal was a lucrative option for employee and staff.[1]

To conclude the analysis, it is clear that the Merger was both beneficial and bane for the companies but every deal has its pros and cons, what we need to analyse is the cost benefit analysis i.e pros shall supersede the cons to be beneficial for the dealers and the present analysis depicts that if the merger would have fallen through, it would have actually been a good deal for all the stakeholders involved because it seems that both the companies need each other and the real outcome can only be known after the actual functioning of the deal. But Alas! The deal did not get the opportunity to prove its merits as the companies decided their fate itself.

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Tax Breaks for the Small Scale Industries in India- A Conceptual Analysis

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Abstract

Small Scale Industries play a very vital role in the Economy of any nation. This industry is mainly specialized in the production of customer's commodities. It creates more opportunity for employment with less investment in compares with large and Medium Industries. In a developing country like India, Small Scale Industries play a significant role in economic development of the country. They are a vital segment of the Indian economy in terms of their contribution towards country's industrial production, exports, and creation of an entrepreneurial base. These industries by and large represent a stage in the economic transition from traditional to modern technology. Small industry plays a very important role in widening the base of entrepreneurship. The development of small industries offers an easy and effective means of achieving broad based ownership of industry, the diffusion of enterprise and initiative in the industrial field. The promotional policy of the Government for the SSI's is fiscal incentives as tax concessions and exemptions of direct or indirect taxes leviable on production or profits. This paper discusses the economic stability of Small Scale Industries and the impact of direct and indirect tax on Small Scale Industries.

Keywords: Small scale industries, India, Direct and Indirect taxes, Tax breaks

Introduction

India is the developing nation, small scale industries play a significant role towards employment generation, control poverty, rural development and growth of various development activities, This industry is mainly specialized in the production of consumer commodities and generate huge employment due to the utilization of labour power for the production of goods. In a developing country like India where unemployment is a major issue; these industries pave the way for employment of trained and untrained persons. Particularly, the new industrial policy 1991 has given many incentives, concessions, and relaxation to boost up small-scale enterprises. Among such concessions, one of the significant concessions is that of exemption from Excise Duty.

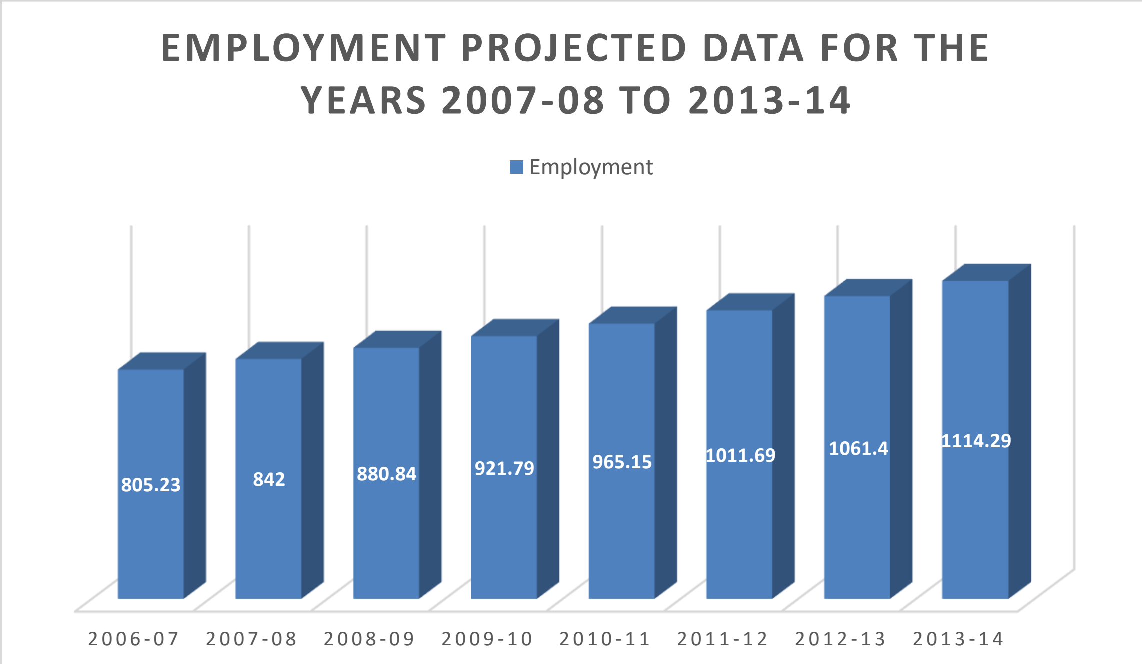
India is contributing almost 50% of the industrial output and 42% of India's total export. For a developing country like India and its demographic diversity, small scale industries have emerged as the leading employment-generating sector and have provided balanced development across sectors. For promotion and development of small scale industries, the central government passed an Act in 2006 to empower the sector and also has formed a Ministry (Ministry of MSMEs). It was the Micro, Small and Medium Enterprises Development Act-2006 that defined the three-tier of micro, small and medium enterprises and set investment limits.

The small-scale sector is normally not required to obtain a license either from the Central and State Government for setting up units in any part of India. Registration of small scale businesses is also not compulsory. But, its registration with the State Directorate or Commissioner of Industries or DIC's makes the unit eligible for availing different types of Government assistance like financial assistance from the Department of Industries, medium and long-term loans from State Financial Corporations and other commercial banks, machinery on hire-purchase basis from the National Small Industries Corporation, etc. Registration is also an essential requirement for getting benefits of special schemes for promotion of SSI viz. Credit Guarantee Scheme, Capital subsidy, reduced customs duty on selected items, ISO-9000 Certification reimbursement & several other benefits provided by the State Government. The researchers are the focus of the promotional policy started by the government for small-scale industries as a financial incentive in the form of tax concessions and exemptions of direct or indirect taxes leviable on production or profits.

Economy Aspects of Small Scale Industries

The small scale industries sector has acquired a significant position in the economic structure of the country. According to the Report of the Development Commissioner, Small Scale Industries (DCSSI), the sector covers about 32 lakh units, during 1998-99 which produce over 7500 different items for domestic and foreign markets as well, contributing to about 40% of the value added to the manufacturing sector and its share in national exports stands at over 34%. This Sector accounts for about 95% of industrial units in India and provides employment to about 175 lakh persons.

Employment in MSME Sector



GST Impact on Small Scale Industries

Goods and Services Tax is refers to bring indirect form of tax under one rooftop, The Goods and Services Tax bill has been passed in the Rajya Sabha and is set to be discussed in the state legislative assemblies in this winter session. With the ball set to roll for a unified country-wide tax reform, the market is filled with new found optimism amongst industry leaders and government officials. This sets the necessary momentum for the passage of the two Bills—Central GST (CGST) and Integrated GST (IGST) Bills. For Small Scale Industries, manufacturers have to take care of different Level taxes and have to run to various departments of tax. Before GST, total tax levied by the central and the state governments add up to 32%, but after the implementation of GST, the business holders have to pay a much lower tax of around 18-22 percent.

Small Scale Industries will be affected the most with the rollout of the GST and the impact will be favourable in ways more than one. Some of the ways GST will benefit Small Scale Industries.

1. **Ease of starting a business**

In old tax regime it is very difficult to starting new business, because new entrepreneurs require obtaining VAT registration for every state individually. Under GST too requires businesses to register in every state, but rules under GST are more uniform and mention clearly on the GST portal. This also makes it easier to set up For Small Scale Industries.

2. **Tax burden on new business**

   In old tax regime, businesses with a turnover of more than 5 Lakh need to pay VAT registration fee. The government mulls the exemption limit under GST to 25 Lakh giving relief to over 60% of small dealers and traders.

3. **Better logistics**

   Goods and Services Tax will result in savings in logistical costs. According to an estimate by CRISIL, the logistics cost for manufacturers of bulk goods will get reduced significantly—by about 20%. This is expected to boost ecommerce across the nation.

4. **Input credit Mechanism**

   Input Credit Mechanism provides facility of input credit facility wherein businesses will be able to avail credit on input expenses such as supplies. For Example, for the business that procures wood as a raw material to manufacture pencil, the owner of the business will need to pay tax on the raw materials procured. He can adjust the tax paid on inputs from the taxes collected on outputs. This means that only the actual “value addition” will be taxed.

5. **Compete with multinationals and multi-state Business**

   Goods manufactured goods by Small Scale Industries will pay the same amount of tax rate as imported goods from multinationals. Furthermore, corporates generally ‘stock transfer’ transfer goods to escape the taxes on inter-state transfers. Small Scale Industries are not able to ‘stock transfer’ goods due to lack of infrastructure; they physically transfer goods and pay inter-state taxes, leading to higher expenses. Under GST, the stock transfers would be taxed. This will help put Small Scale Industries at par with large multinational corporations, allowing them to compete on equal tax footage.

Composition Scheme

Goods and Service Tax is set to bring a new era of business compliance in India. Many small scale industries struggle in order to complete these provisions. To resolve such kind of situations, the government has introduced a Composition Scheme under GST. Under this scheme, small taxpayer will pay as a percentage of business turnovers during the Accounting Year without the Advantage of Input Tax Credit. The flooring rate of tax for CGST and SGST shall not be less than 1%. A taxpayer opting for composition scheme will not collect any tax from the Consumer. This scheme can opt by the manufacturers, Food and Restaurant Services and Traders.

Criteria for Acquiring the Composition Scheme

1. Composition Scheme is not for all taxpayer, this is for that taxpayer who's aggregate turnover do not exceed Rs. 1.5 crore for India except North-Eastern States and Rs. 75 lakhs for Special States.

   **Aggregate Turnover = Value of Outward Supplies + Zero Rated Outward Supplies + Exempt Outward Supplies*

   ** Aggregate Turnover covers all the supplies affected by a person having the same PAN.*
2. Composition Scheme is not for the manufacturer of – ice cream, pan masala or tobacco (and its substitutes)
3. In Composition Scheme taxpayer shall pay tax at normal rates in case he is liable under reverse charge mechanism.
4. All businesses with similar PAN has to be additional up to calculate turnover for the purpose of composition scheme
5. Composition scheme is applicable subject to the condition that the taxable person does not affect interstate supplies.
6. Service Providers are not eligible for Composition Scheme under GST.
7. A Composition Dealer has to issue Bill of Supply. They cannot issue a tax invoice. This is because the tax has to be paid by the dealer out of pocket. A Composition Dealer is not allowed to recover the GST from the customers
8. The taxable person is required to furnish only one return i.e. GSTR-4 on a quarterly basis and an annual return in FORM GSTR-9A

   Also, auto drafted details are not available for a composition dealer for the quarters July – September, and October – December. This means that all sales details have to be manually entered by the Composition Dealer.

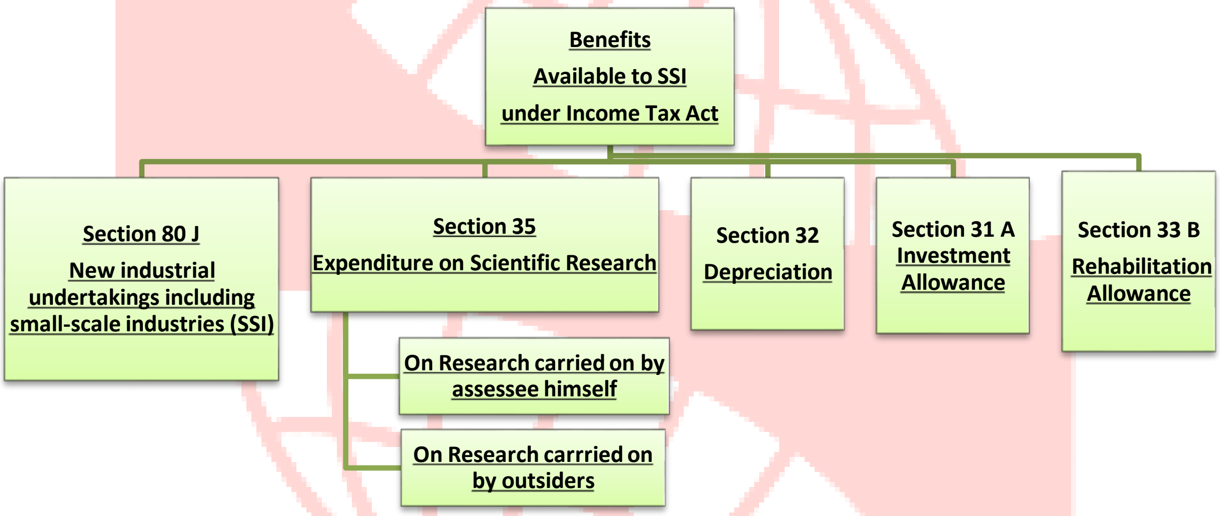
Rates of taxes under the Composition Scheme

Business	CGST	SGST	TOTAL
Manufacturer and Trader(Goods)	0.5%	0.5%	1%
Trader(Goods)	2.5%	2.5%	5%

Therefore, Composition Scheme is very beneficial for Small Scale Industries as they continue to remain outside the ambit of normal levy. This will contribute on a huge scale to the GDP as well as job segment of the country

Direct Tax Benefits for Small Scale Industries

Income tax is only of the direct means of taxation like capital gains tax, securities transaction tax, etc. this form of taxation gives direct impact on small scale industries. Billow mention Provisions of income tax Act 1961 briefly disused about exemption and Allowances provide for small-scale industries



1. **New industrial undertakings including small-scale industries (SSI):** Under section 80 J small-scale industries are exempted from the payment of income-tax on their profits which is subject to a maximum of 6 percent per annum of their capital employed. The exemption in tax payment is allowed for the period of five years from the date of commencement of production. In order to avail this exemption facility, a small-scale industry should follows the following two conditions;

A. The unit should not have been formed by the reconstitution or splitting of an existing unit.

B. The unit should employ ten or more workers in a manufacturing process with power, or at least twenty workers without power.

2. **Rehabilitation Allowance:** According to the section 33 B of Income Tax Act, 1961 the rehabilitation allowance is allowed to small-scale industrial units and the manufacturing small

enterprises. The rehabilitation allowance is given to only those small businesses that had suffered because of the following reasons:

A. Action taken in combating an enemy or action by an enemy.

B. Cyclone, Flood, earthquake or other natural upheavals.

C. Civil disturbance or riot, explosion or accident fire.

The rehabilitation allowance should be utilized within three years of the unit's reestablishment reconstruction of revival for the business purposes only. This allowance is allowed to the industrial undertaking equal to 60 % of the amount of the deduction allowable to the enterprise.

3. **Expenditure on Scientific Research:** Following deductions in respect of expenditure on scientific research are allowed under the section 35 of the Income Tax Act 1961:

A. The capital expenditure (except land) incurred on scientific research must be related to the business of the assessee, but it is subjected to the provision of section 35(2) of the Income Tax Act, 1961

B. The revenue expenditure must be incurred on scientific research related to the business of the assessee in the current previous year.

C. The sum that it pays to a scientific research association or a university, college, institutions or to a public company which must have its objective of scientific research.

4. **Investment Allowance:** The investment allowance was introduced in the year 1976 to replace the initial depreciation allowance. Investment allowance defined under section 31 A of IT Act 1961, this provision is allowed at the rate of 25% of the cost of acquisition of new plant or machinery installed. A special dispensation has been provided for the plant and machinery installed in small-scale industries. In comparison with other industries, small-scale industries are at an benefit in claiming a deduction of investment allowance.

5. **Depreciation:** Under section 32 of IT Act 1961 entitled to a deduction on depreciation account on black of assets at the specified rate. Small enterprise is allowed subject to a maximum of Rs. 20 lakh deduction for depreciation on plant and machinery. A small-scale industry should satisfy the billow mention conditions before it becomes eligible for deduction in depreciation:

A. .The assets must be owned by the assessee.

B. The assets must actually be used for the purpose of the assessee’s business or profession.

C. Depreciations allowance or deduction is allowed only on fixed assets, i.e. building machinery, plant and furniture.

Conclusion

After analysing all the scenarios small scale industries it's been observed that Indian taxation policy had never been any intention of discriminating against small business. Indeed, for many years, it has favoured small-scale sectors by moderately graduating the rates at which corporate income has been taxed. Introducing direct and indirect taxation reform governments are promoting small-scale industries in the national and international platform. After the welcome move of government in indirect tax i.e., GST this will lift the overall productivity of India. Make One India One tax and One India One Market. It may improve the quality of the product for the end user.

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STUDENT RESEARCH PAPER

Methods of Raising Finance for Business – An Overview

- Harshit Dhandhia

Abstract

In this paper we would be first understanding the meaning of business and why it is necessary for any business to procure funds. Then we would understand the various methods of raising finance that are either through investors; from foreign investors; raising in the form of loan; raising finance by listing the company. After understanding and having a basic idea of obtaining finance this paper would deal with the understanding why obtaining funds is difficult from various sources.

Key words: Investments, Strategic Investment, Financial Investment, FDI, Due diligence.

Introduction

What do we mean by business?

Business a word which we all know it very well doesn't needs any explanation it's one of those sectors for a country which contributes maximum for the nations development be it in the form of providing employment, generating income through dealing with other countries or anything . In a layman's language it is one of those sectors which consist of group of people having certain passion, desire and pooling together their best areas of experiences gained over the years in order to generate money. It is an organization that provides goods and service for human needs and which is involved in various activities like accounting marketing research and development, raising of finance, benefits for shareholders, generating maximum profits by sales for which it adopts various advertisement methods. It is not a cakewalk that every person could do it, one needs proper education have a good knowledge of what he is going to be involved in; how he would make that business survive over a period of time; how he would benefit the shareholders or its investors and the most important thing is how one would comply with the rules and regulation which have been framed in each country for the business sector. It isn't an easy job to match with all the laws and come out profitable and still maintain a good reputation in the market. After getting a basic knowledge of what we understand by business this paper would basically deal with how businesses raise finance in various ways in order to expand themselves.

Rising of finance from investors

Raising investment is an essential source for any business or company to function that is to grow and expand, sometimes business start from meager capital and thereby raise funds from internal cash flows and then they move on to raise capital either in the form of equity or debt. The most essential idea that needs to be kept in mind while raising finance is whether the investor which would be investing in the company would make financial or strategic investments. Financial investment are those in which the investor does not like to take the control of the business he would invest his portion of money for certain period of time and would like to generate a greater return form it after keeping that investment for a period of 4 to 5 years. Venture capitalist, private equity investors, angel investors are the financial investors their sole intent in making investments to earn profit in the form of dividend or getting appreciation in the value of amount they have invested over the years. They are the ones who rely on the existing management to work properly and have the power to remove the existing managements and hire professional for the business to grow. They are the ones who invest in the first round of application of shares that is they do not buy shares from the existing shareholders which leads to the fresh amount of money getting invested in the business although they invest in a lot of companies knowing that some of their investment decision won't yield profit and some would generate a huge profit which would in turn cover all those losses. Strategic investments are those investments which are made by big giant cooperation's to smaller ones so that they could get benefit from business synergies. Here the basic idea is not to earn profits form the investee company but to use the investee company in such a way so that it would increase the profits of the investors company or sometimes using the resources of the investor company so that the investee company could gain more profit. The best example of strategic investment is Google buying the Motorola Company. In this the investors are aiming to control the board and the business. Strategic investments generally occur in the form of share acquisition or mergers or joint ventures between the companies.

The process of raising investment basically involves 4 stages which include: finding of the potential investors, in this the organization must enter into a NDA agreement with the investor so that all his business policy and model and ideas do not become public. After signing of NDA the expression of interest of investor is taken into account which includes term sheet that involves all the essential information regarding the business deal and all the closed information even the expenses incurred that is called as fees could also be attached in to it like break fess which involves applying of the charges which were borne by the investor during negotiation. It evenincludes certain clauses like no shop clause which restricts the promoters to reach other investors during that particular duration when they have reached out to one of the investors. It includes the terms and conditions which acts as a basis for preparation of definitive legal agreements like shareholders agreement, share purchase agreement. Afterall these the process of due diligence is conducted which includes having a detailed information about the organization whether any pending charges are there on them which have been hidden from the investors and which would strategically impact them. Due diligence is one of the most important or the essential function of the investors to know the insight of the organization. The final stage involves the execution of all the requisite documents and then finally the funds are transferred.

After raising finance through the investors if the company still requires any additional capital it can go on to raise finance in the form of equity or debt. Equity financing happens by undergoing IPO that is Initial public offer it is one of the best way to raise finance since company doesn't needs to repay the money back to the shareholders they just need them to give a favorable exit amount which would be greater than their investment made in the company at the starting time and receive some additional benefit like getting dividend, right issue, tag along benefits etc. Whereas in the debt financing the company has an obligation to pay back the whole amount coupled with the interest rate which has been fixed by them. They need to pay it off even when the company gets wind up either by selling of the assets or even when the company suffers losses.

Raising of finance from foreign investors

Another method of raising finance which is the dream or one of the most prestigious things to boast of, for any company is getting investment form foreign companies. Most of the Indian companies desire to get investment form reputed foreign companies in order to expand their business. It is even considered that foreigner do tend to invest a greater amount of money than the domestic investors which in turn benefit the promoters to exit with greater profits. Generally receiving investment form foreign companies is called foreign direct investment(FDI). Foreign investors are attracted to India due to their growing customer base and since foreign capital can witness more growth in an emerging economy like India unlike those countries which has already been developed or captured by the various companies. It has been found by one of the statistics that the rate of growth in the world is 3.2% while that of in India is 6-7%. Apart from investing in Indian companies many foreign companies are establishing their subsidiaries in India which would help them generate income and even majority of foreign companies are entering into a joint venture between Indian companies for e.g. Hero Honda is a joint venture between Hero and Honda of Japan; even Maruti Suzuki which is also a joint venture between Maruti and Suzuki of China. Having a detailed information of about FDI policy is one of the most crucial place for the lawyers to generate handsome amount of money since FDI requires a lot of legal service to be answered and various procedure need to be adopted in order to sanction the FDI amount properly. FDI is allowed almost in all the companies except to some sector like industrial sectors which includes arms and ammunition, railways, iron mining and coal mining. Even FDI isn't allowed in some place like LLP that is in the limited liability partnership and among the trusts except the venture capital funds which are registered with SEBI and investment vehicle. Although an investment in LLP is subject to the compliance conditions of LLP Act, 2008. FDI in venture capital fund structured as trust requires permission form Department of Industrial policy and promotion(DIPP). NRI's are subjected to make investment in companies with respect to certain condition that the investment would be made on non-repatriation basis and the firm won't be involved in certain sectors like that of print media, agriculture or real estate business. Nonresident apart from NRI can make investment by receiving prior approval form RBI for investing in the capital of an Indian business. FDI is basically governed by the FDI policy which states that investment can be made in the form of either route, like the automatic route in this no permission is needed from the government and under approval route recommendation of government is needed in order to receive the procured funds. Some of the sectors that works under the approval routes are defenses, air transport service, telecom service, print media, private security agencies, insurance and banking companies. Before 2017, all FDI proposals need to be approved by foreign investment promotion board(FIPB) but after June 2017 it was abolished a single online portal named Foreign investment facilitation portal (FIPP) was created where all FDI application are made. The application will be processed by the competent authority of the sector to whom the application is made. FDI is not necessary to be madein liquid cash it can be in the former of exchange of shares, bringing of technology exchange of shares between two companies. Violation of the FDI policy involves the penalty of up to thrice the amount of money involved

Raising of finance in the form of loans

Apart from these two methods of raising finance companies can also look out for loans from various banks to meet their working capital requirement; purchase of specific business requirements; specific business transactions. Getting loan is not an easy task lender needs to get some assurance in first case to provide the loan then they will assess the requirement of loan critically and then only would provide the amount. Some of the basic things they take into consideration are purpose of loan and then determine the cost that is what kind of interest will be charged be it fixed or floating interest repayment schedule guarantees. Even some institutions go for ECB known as External Commercial Borrowings which involves borrowing form the foreign institutions. These are basically taken form some foreign bank in the form of foreign currency it is one of the most popular source for many businessman to opt for loan because loan is received at a lower rate of interest as compared to other institutions . Not every one is allowed to take loan from foreign institutions only some handful and reputed businessmen are allowed if loan is given to everyone then it would lead to foreign exchange problem and Indian banks would collapse as no one would borrow from them since they charge higher interest as compared to them. There are certain restriction where ECB can be used that is it should be used only for the purpose of making investments in the form of capital goods and for modernization and expansion of various industrial sectors excluding the real estate sector. It should be noted that ECB and FDI are different FDI is concerned with investing in the capital of the business that is convertible instruments are covered under FDI whereas ECB means every kind of funding except the equity one. Another way of obtaining loan when the amount is huge which is generally demanded by organization or government is known as syndicate loan. In this the group of lenders collectively extends loan to a single borrower in which all the terms and conditions of a document are similar in nature and is administered by a common agent this is known as syndicate loan. There is a lot of negotiation involved in this and obtaining of these types of loan is quite complex and involves execution of numerous agreements. Syndicate loan isn't easily procured because the amount demanded is huge and it will be only financed depending upon various factors like the credit rating of the country; credit rating of the borrower; average life span of loan; amount of risk involved etc.

Problem of raising finance in India

The above are the mentioned ways form where one company can raise finance but in India it isn't an easy task to get funds these are due to various reasons like in India there are only handful of investors and satisfying them is a major task. There are certain cases in which most of the companies fail though getting loan and IPO's have helped them to raise finance but still they need some huge amount to back themselves in order to reach the stage of IPO. Even for an IPO the company needs to be a public limited company and should have at least minimum capital of approximately 5 lakh rupees since only large company can afford to go for IPO there has been a special market to raise finance for small and medium enterprises. Due to the problem of procuring finance many startups fail and the reason behind that is that they don't get loans at an easy interest and they sometimes even lack collateral due to which banks refuse to provide them loans. In India since majority of the businesses are micro, small and medium enterprises (SME)their credit scoring is very less and thus banks hesitate to provide loan. The maturity gap for the loans demanded by the SME's are very less this is also one of the reasons why bank hesitate to provide loan since longer term loans are secured with mortgage against property. There are also some cases when some businesses don't get the procured funds form any of the above ways and actually that is the scenario for most of the businesses in India due to which they take loan from some unauthorized persons and in turn they find themselves attached to some serious problem since in the need of funds they even agree to the higher rates of interest which these moneylenders charge.

Thus it could be seen that there are various problems in procuring finance it isn't an easy task to get loan one first needs to understand how he wants the fund and after getting it he must ensure that those funds generate profit otherwise he would be in a deep trouble of paying off the loan since the amount would be huge coupled with the interest rate it would become a serious problem. One should do an extensive research and find the best way of obtaining the finance which would match up with his requirements.

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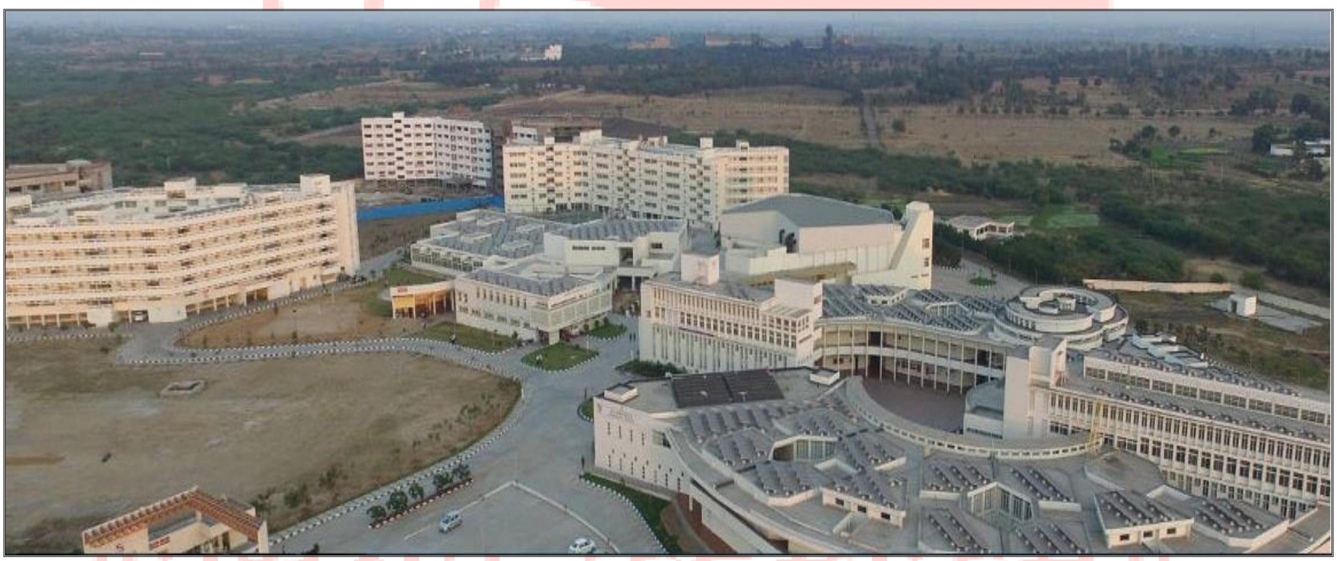

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