

Inquiry, Inspection & Investigation

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Structure of Presentation

- ❖ Why Inquiry , Inspection or Investigation
- ❖ Legal Provisions
- ❖ Detecting non compliances
- ❖ Types of non compliances
- ❖ Fraud and punishment for frauds
- ❖ reports
- ❖ How, why and who commit frauds

Why Inquiry

- ✓ Strengthen Information In registry or to fill the missing gaps/incomplete filings.
- ✓ Financial statements/documents indicate prima-facie non compliances like variances in dates/financial data
- ✓ Audit Qualifications.
- ✓ When there are doubts on existence of the company
- ✓ Redress grievances raised by investors/depositors/other stakeholders .
- ✓ References from other regulators/ departments
- ✓ Verify facts on the basis of investor complaints or otherwise .
- ✓ Financial statements indicate too good or too bad financial position - exceptional/irrational changes in financial results or state of affairs
- ✓ Verify the utilization of IPO/FPO proceeds as per stated objects

Why Inspections.....

- ❖ Refusal /disobedience of the scrutiny /inquiry orders .
- ❖ Inquiry indicates need for deeper examination of the Books of Account like volume of records
- ❖ Need to verify the disclosures in Financial statements with the Books and records.
- ❖ Collection of evidence
- ❖ Recording of statements
- ❖ Physical verification of Registered or other offices of the company .
- ❖ Higher Number or frequency of investor complaints .

Why Investigations

- ❖ Normally the similar reasons but where larger interests of number of investors or stakeholders are affected .
- ❖ Larger Public issues – issues of revenue etc.
- ❖ Inquiry/Inspection indicates elements of fraud.
- ❖ Specific issues are to be examined instead of general examination of books and records –Targeted Surgery

Legal Provisions

- ❖ Chapter XIV of the Companies Act, 2013
- ❖ Sections 206 to 229
- ❖ Section 90
- ❖ Section 457
- ❖ Section 447, 448 and 449
- ❖ All those sections of the Act where punishment for fraud is provided

Section 206 – Inquiry – calling of further information and Inspection- Power Of Registrar..

✓Opinion of the Registrar

- ✓On Scrutiny of any document filed by the Company ;or
- ✓ on any information received by him

✓Registrar can call by written notice:

- ✓To Furnish in writing such information or explanation
- ✓To produce such documents

✓Within the time and to the extent specified in notice

Inquiry

- ❖ Duty of the Company and its officers to furnish information and to produce documents
[Section 206(2)]
- ❖ Past employees are also duty bound if so called by Registrar by notice in writing
- ❖ **Section 206(3)**: If no information is furnished after first notice or on examination ROC forms an opinion that the information furnished is incomplete or an unsatisfactory state of affairs exists. Registrar can :
 - ❖ Call for information: or
 - ❖ to produce record for inspection
- ❖ ROC to record reasons before action under **Section 206(3)**

Section 206(4)-information or representation before the Registrar

- ✓ On the basis of information available with ROC.
- ✓ Representation made to ROC by any person.
- ✓ The business of the Company is carried on for a fraudulent or unlawful purpose.
- ✓ Not in compliance with the provisions of the Act.
- ✓ Grievance of Investors are not addressed.
- ROC to inform the Company of the allegations made against it by written order may Call for information or carry on any inquiry as he deems fit.

Section 206(4)

- ❖ Opportunity of being heard to the Company is mandatory for action under **Section 206(4)**
- ❖ The Central Govt. can also direct the Registrar or an Inspector appointed to carry out inquiry under **Section 206(4)**
- ❖ Punishment for fraud under **Section 447** where the business of the Company has been or is being carried out:
 - ❖ For a fraudulent purpose
 - ❖ Unlawful purpose
 - ❖ Every Officer of the Company who is in default shall be punishable for fraud under Section 447

Power Of The Central Govt. To Order Inspection [Section 206(5) And (6)]

- ✓ In addition to the powers of the Registrar, the Central Govt. may direct inspection of Books and papers of the Company by an Inspector
- ✓ Central Government may, by special or general order, authorize any Statutory Authority to carry out the Inspection of Books of Accounts of a Company or class of Companies
- ✓ Such Authorities may be like RBI, in case of NBFCs, NHB, in case of Housing Finance Company etc.

Penal Provisions [Section 206(7)] Disobedience of Inquiry Orders

- ✓ Company and every officer in default with fine up to Rs. 1 Lac
- ✓ If default continues, additional fine which may extend to Rs. 500/- for every day after the first during which the default continues

Conduct Of Inspection And Inquiry (Section 207)

- Duty of every Director, Officer or other employee to produce all such documents and furnish such statements etc. in such form as required and render assistance
- Registrar/IO empowered to take copies, mark identification
- The Registrar/IO empowered with powers of Civil Court under the Code of Civil Procedure, 1908 in the matters:
 - Discovery and production of Books of Account and records
 - Summoning and enforcing the attendance of persons and examination of oath and inspection of any Books and records at any place

Penal Provisions On Disobedience of Inspection [Section 207(4)]

Every Director or the Officer of the Company punishable with imprisonment which may extent to one year; AND with

- ❖ Fine which shall NOT be less than Rs. 25,000/- but may extent to Rs. 1 Lac
- ❖ Section 207(4)(ii) On conviction such Director or Officer shall be deemed to have vacated his office as such on and from the date of conviction ; AND
- ❖ Disqualified from holding an office in any Company.

Report On Inquiry and Inspection (Section 208)

- ❖ Report is must on Inquiry (Section 206) and Inspection (Section 207);
- ❖ The Registrar/Inspector is duty bound to submit report to Central Govt. along with documents;
- ❖ Empowered to recommend investigation into the affairs of the Company with reasons;
- ❖ Report to be submitted as per proforma prescribed for inspection;

reports

- ❖ Report in the prescribed proforma;
- ❖ Should be covered the basis of inquiry, inspection or investigation;
- ❖ All pages to be serially numbered;
- ❖ All attachments to be serially numbered and indexed;
- ❖ All the relevant attachments to be referred at relevant para;
- ❖ It should be signed;

Search And Seizure (Section 209)

- ❖ In case of belief of possibility of destruction, mutilation, alteration of evidences/ Books/records, Registrar/Inspector empowered to search and seizure after taking approval from Special Court:
 - ❖ Records relating to Company, KMP, Director, Auditor, Company Secretary in practice
 - ❖ Seek search and seizure into any place or places where such Books or papers are kept.
 - ❖ Power to keep such seized records upto 180 days and return but empowered to call for further period of 180 days by an order in writing
 - ❖ Empowered to keep copies before return of records
 - ❖ The provisions of Cr. PC apply to such search and seizure

Investigations [Section 210]

- ❖ Central Govt. on forming opinion **may** order investigation:
 - ❖ On receipt of report of Registrar or Inspector under Section 208
 - ❖ On intimation of special resolution passed by a Company
 - ❖ In Public interest
- ❖ Central Govt. **shall** order investigation:
 - ❖ On order passed by a Court; or
 - ❖ the Tribunal
- ❖ The Central Govt. may appoint one or more Inspector to investigate into the affairs of the Company and report in the manner as directed by Central Govt.

Investigations By SFIO

- SFIO gets a statutory status and organization structure [Section 211]
- Central Govt. empowered to order investigations by SFIO:
 - On receipt of report of the Registrar/Inspector under Section 208
 - On intimation of special resolution passed by a Company
 - In Public interest
 - **On request from any Department of the Central Govt. or State Govt.**

Investigations By SFIO

- ❖ The Director, SFIO to designate Inspectors
- ❖ Once investigation is ordered by CG for SFIO no other agency to investigate matters under this Act and shall transfer the relevant records to SFIO
- ❖ 15 offences made cognizable and no person accused of such offences shall be released on bail or on his own bond unless PP is given an opportunity to oppose the application for such release [Section 212(6)]
- ❖ Powers of arrest with SFIO [Section 212(8)]

Investigations by SFIO

- ✓ Central Government may order investigation to be conducted by SFIO:
 - ✓ on report of Registrar
 - ✓ intimation of SR by a Company
 - ✓ In the public interest; or
 - ✓ On request from any Department of CG or SG
- ✓ SFIO, of its own, cannot take up any investigation
- ✓ Once investigation is ordered by SFIO, no other investigating agency of CG or SG shall proceed with investigation in such case in respect of any offence under this Act.
- ✓ SFIO has powers to arrest (not yet notified) and to make searches
- ✓ SFIO to submit report and also interim report

Investigation In Other Cases: [Section 213]

- ❖ Investigations on orders by Tribunal
- ❖ Tribunal may pass order on applications by specified number of members
- ❖ On allegations of fraudulent activities of the Company or unlawful purposes or other matters specified under Section 213(b)

Investigation of Ownership of Company [Section 216]

- ❖ Central Govt. empowered to appoint Inspectors to investigate and report on matters relating to Company and its membership to determine true persons:
 - ❖ Who are or have been financially interested in the success or failure, real or apparent
 - ❖ Who are or have been able to control or to materially influence the policy of the Company
- ❖ Such investigation may be ordered by Central Govt. on orders by Tribunal
- ❖ CG may define scope of the investigation, define period or limit investigation to matters with particular shares or debentures.

Imposition Of Restrictions Upon Securities [Section 222]

- Tribunal is empowered (for investigations under Section 216 into ownership) to put restrictions upon on securities for period not exceeding three years
- Default attracts major penalties under Section 222(2)

Other Provisions relating to Investigations

- ❖ Procedures/powers of the Inspector is defined under Section 217
- ❖ Protection of employees during investigation is provided under Section 218
- ❖ Inspector is empowered to conduct investigation into affairs of the related Companies with prior approval of Central Govt.
- ❖ Inspector are empowered for seizure of documents during investigations [Section 220]
- ❖ Freezing of assets of the Company in inquiry and investigation by Tribunal, on reference by:
 - ❖ Central Govt. or
 - ❖ in reference to inquiry or investigation or
 - ❖ on any complaint made under Section 244 or
 - ❖ on any complaint from creditor having Rs. 1 Lac amount outstanding or

Other Provisions relating to Investigations

- ✓ Voluntarily winding up not to stop investigation [Section 226]
- ✓ Legal Advisors and Bankers not to disclose certain information [Section 227]:
 - ✓ Legal Advisor are not required to disclose privileged communication made to him in that capacity except as respects the name and address of his client
 - ✓ Bankers are not required to disclose any information as to the affairs of any of their customers other than such Companies, Body Corporate or Person
- ✓ Investigation of Foreign Companies [Section 228] – All provisions of investigations apply *mutatis mutandis* to Foreign Companies

- ✓ Penalty for furnishing false statement, mutilation, destruction of documents [Section 229]:

- ✓ Penalty for fraud as provided under Section 447:
 - ✓ On providing false explanation or information
 - ✓ Making or party in making a false entry in any document concerning the Company/Body Corporate
 - ✓ On destruction, mutilation, falsification, concealing or tampering or unauthorized removing or party thereto of any property, assets or affairs of the Company or Body Corporate

- ✓ Investigation of beneficial ownership of shares in certain cases [Section 90]

Non-disclosure Of Information In Certain Cases [Section 457]

- ❖ Notwithstanding anything contained in any other law, the Registrar or any Officer of the Govt. or any other person shall NOT be compelled to disclose to any Court, Tribunal or other Authority the source from where he got any information which;
 - ❖ has lead the CG to order an investigation under Section 210 or
 - ❖ is or has been material or relevant in connection with such investigations

Nature of Non Compliances

- **Secretarial :**

- Statutory Registers /Books either are not maintained or are in complete .
- Filing of statutory documents with ROC/MCA.
- Secretarial compliances in calling and holding of meetings , notices , certifications , passing of proper resolutions , agreements etc

- **Accounting :**

- Compliance of Format and contents –Accounting Principles and polices
- Accounting Standards
- Audit , Cost Audit Rules

- **Corporate Governance Norms and certifications**

Non Compliances /Violations/Red flags

- ❖ Default/delay in filing of due documents
- ❖ Not maintaining registered office
- ❖ Non maintenance/incomplete secretarial records
- ❖ Non holding/delayed holding of meetings
- ❖ Filing of documents with incomplete information
- ❖ Non compliances of Accounting Standards
- ❖ Financial Statements not prepared on the prescribed format
- ❖ Incomplete/no prescribed disclosures given
- ❖ Shifting of registered office without intimation
- ❖ Abnormal related party transactions

Non compliances vs. Frauds....

- A Non Compliance can be an innocent mistake without any intention to harm the organisation or any of its stakeholders.
- On the Contrary , Fraud encompasses an array of irregularities and illegal acts characterized by **intentional deception**. It can be perpetrated for the benefit of or to the detriment of the organization and by persons outside as well as inside the organization .
- A non compliance can also “ indicate” a potential Fraud if it is corroborated with array of events with “*mens rea*” or guilty mind.

THANKS