

GUIDELINE ANSWERS

PROFESSIONAL PROGRAMME

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MODULE 3



**THE INSTITUTE OF
Company Secretaries of India**

IN PURSUIT OF PROFESSIONAL EXCELLENCE
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These answers have been written by competent persons and the Institute hopes that the **GUIDELINE ANSWERS** will assist the students in preparing for the Institute's examinations. It is, however, to be noted that the answers are to be treated as model answers and not as exhaustive and the Institute is not in any way responsible for the correctness or otherwise of the answers compiled and published herein.

In answers to the questions based on case study, the students may write any other alternative answer with valid reasoning.

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

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(i)

NOTE : Guideline Answers of the last Four Sessions need to be updated in the light of changes and references given below :

PROFESSIONAL PROGRAMME
UPDATING SLIP
ADVANCED TAX LAWS AND PRACTICE

MODULE – 3 – PAPER 1

<i>Examination Session</i>	<i>Question No.</i>	<i>Updation required in the answer</i>
All Previous Sessions	—	<p>The Income Tax, Service Tax, VAT, Sales Tax, Central Excise and Customs Laws are subject to changes by the Annual Finance Acts. In order to update all the answers, the students are advised to refer to the latest law keeping in mind the following amendments for June 2016 examination.</p> <p>(i) Finance Act, 2015 relevant to Assessment year 2016-17 (Previous Year 2015-16) is applicable. Further, all the Circulars, Clarifications, Notifications, issued by CBDT / CBEC/ Central Government etc. which became effective, on or before six months prior to the date of the respective examinations are applicable.</p> <p>(ii) Wealth Tax Act, 1957 has been abolished w.e.f. 1st April, 2016. The questions from the same will not be asked in examination from December 2015 session onwards.</p> <p>The questions based on case laws, in conflict with the latest law be treated as of academic interest only.</p>

(ii)

UPDATING SLIP

DRAFTING, APPEARANCES AND PLEADINGS

MODULE – 3 – PAPER 2

<i>Examination Session</i>	<i>Question No.</i>	<i>Updation required in the answer</i>
All Previous Sessions	—	Notified provisions of Companies Act, 2013 and the provisions of Companies Act, 1956 which is still in force.

(iii)

UPDATING SLIP

BANKING LAW AND PRACTICE

MODULE – 3 – ELECTIVE PAPER 9.1

<i>Examination Session</i>	<i>Question No.</i>	<i>Updation required in the answer</i>
All Previous Sessions	—	All relevant amendment pertaining to Banking Laws and Notification/Circulars issued thereunder upto 6 months prior to the date of examination.

(iv)

UPDATING SLIP

CAPITAL, COMMODITY AND MONEY MARKET

MODULE – 3 – ELECTIVE PAPER 9.2

<i>Examination Session</i>	<i>Question No.</i>	<i>Updation required in the answer</i>
All Previous Sessions	—	Amendments to SEBI Act, Securities Contract Regulations Act, Forwards Contract Regulation Act, Securities Contract Regulations Rules, various Rules/Regulations issued by SEBI from time to time. Master Circulars issued by RBI from time to time.

ADVANCED TAX LAWS AND PRACTICE

Time allowed : 3 hours

Maximum marks : 100

NOTE: 1. Answer ALL Questions.

2. All the references to sections mentioned in Part-A of the Question Paper relate to the Income-tax Act, 1961 and relevant Assessment Year 2015-16, unless stated otherwise.

PART A

Question 1

- (a) Jatin submits the following information relevant for the assessment year 2015-16 :

	₹
Short-term capital gains	1,25,000
Income from owning and maintaining race horses	20,000
Income from units of mutual fund	17,000
Long-term capital gains in respect of buildings	7,000
Business profits	14,000
The following items have been brought forward :	
Long-term capital loss in respect of assessment year 2012-13	30,000
Brought forward business loss from assessment year 2013-14	15,000
Brought forward loss from the activity of owning and maintaining race horses from the assessment year 2011-12	27,000
Speculation losses of the assessment year 2012-13	35,000

Calculate the gross total income of Jatin for assessment year 2015-16.

(5 marks)

- (b) From the following information, advice as to which shall be a better option, i.e., repair or replacement of machine :

- The cost of repair is ₹90,000 and the machine will work for 4 years.
- An expenditure of ₹18,00,000 shall be incurred on the purchase of new machine and the scrap value of machine after 10 years would be, ₹72,000.
- On purchase of new machine the production will increase and the profit of the organisation will increase from ₹9,00,000 to ₹5,00,000 per year.
- Rate of interest is 15% (on purchase).
- The old machine can be sold at present for ₹1,50,000 and after 4 years it would be sold for ₹30,000.
- The rate of income-tax is 30% and no surcharge is payable. Education cess is applicable as per rules.

(5 marks)

(c) Alfa Ltd., a domestic company purchased its own unlisted shares on 4th July, 2014. The consideration for buy-back amounting to ₹10.50 lakh was paid on the same day. The amount received by the company two years back for issue of such shares was ₹6.5 lakh. The Assessing Officer has issued a notice to tax the gains on shares to which company denies. State the correctness of the contention of Assessing Officer and also compute the tax payable, if any. Also, compute the amount of interest, if any, payable by company assuming that the tax due is paid to the credit of the Central Government on 29th September, 2014. (5 marks)

Answer 1(a)**Computation of Gross total income of Mr. Jatin for the Assessment Year 2015-16**

<i>Particulars</i>	<i>Amount (in Rs.)</i>	
A Profits and Gains of Business & Profession		
Business Profits	14,000	
Less : B/F Business Loss from the AY 2013-14	(15,000)	
Loss to be C/F to next Year	(1,000)	-
B Capital Gains		
Short-term Capital gains	1,25,000	
Long-term Capital Gains	7,000	
Less : B/F Long-Term Capital Loss from AY 2012-13	(30,000)	
Loss to be C/F to next Year	(23,000)	1,25,000
C Income From Other Sources		
Income from owning and maintaining Race Horses	20000	
Less : B/F Loss from owning and maintaining Race horses from AY 2011-12	27000	
Balance loss cannot be C/F as the limit of 4 Years expired with this AY	(7000)	
B/F Sepculative losses from the AY 2012-13	(35000)	
Less : Speculative Incomes	-	
Speclative losses carried forward	(35000)	-
D Gross Total Income		125000

Note: Income received from units of a mutual fund registered with the Securities and Exchange Board of India is exempt in the hands of the unit holder.

Answer 1(b)**Comparative Statement Showing After Tax Profit From Different Alternatives**

<i>Particulars</i>	<i>Repair Amount (in Rs.)</i>	<i>Replacement Amount (in Rs.)</i>
Annual Repairing expenses (Note 1)	22,500	–
Depreciation on new machine (Note 2)	-	1,72,800
Interest on Rs. 18,00,000 @ 15% p.a.	-	2,70,000
Depreciation on old machine (Note 3)	30,000	
Total Expenses	52,500	4,42,800
Expected Profit	9,00,000	15,00,000
Less : Total Expenses	(52,500)	(4,42,800)
Net profit before tax	8,47,500	10,57,200
Less: Income Tax @ 30.9%		
(Tax @ 30% + Cess & SHEC @ 2% & 1%)	(2,61,878)	(3,26,675)
Profit After Tax	5,85,622	7,30,525

It is better to replace old machinery with a new one.

Note :

Annual Repairing expenses = Rs. 90,000 / 4 = Rs. 22,500

Depreciation on new machinery = (Cost – scrap value)/ life of asset

= Rs. (18,00,000- 72,000)/10

= Rs. 1,72,800

Depreciation on old machinery = (Present value – sale value)/ balance life

= Rs. (1,50,000 – 30,000)/ 4

= Rs. 30,000

Answer 1(c)

As per section 115QA of the Income Tax Act, 1961, any amount of distributed income by the company on buy-back of shares (not being shares listed on a recognised stock exchange) from a shareholder shall be charged to tax.

Further, such company shall be liable to pay additional income-tax at the rate of 20% on the distributed income.

Thus, the contention of the Assessing Officer relating to taxability of the gains resulting from the buy back of shares is correct.

Computation of Tax Payable by Alfa Ltd.

<i>Particulars</i>	<i>Amount (in Rs.)</i>
Consideration for Buy Back	10,50,000
Consideration received for issue of shares	(6,50,000)
Distributed Income	4,00,000
Additional Tax @ 20%	80,000
Surcharge @ 10%	8,000
Cess & SHEC @ (2% + 1%)	2,640
Total Tax Payable	90,640

* Rate of surcharge applicable 10%

The above tax should be paid on or before 18th July, 2014.

However, it was paid on 29th September, 2014.

Thus, for this delay interest is payable @ 1% per month for each month in whole or part. Therefore, interest is payable for 3 months.

Interest = Rs. (90,640 X 1/100 X 3) = Rs.2,719.20

= Rs.2,719

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

Question 2

(a) Ms. Alicia is a German national working in Sinsang Ltd., in Turkey. Sinsang Ltd., neither has any office in India nor done any business in India. The company deputed Ms. Alicia to India on 31st January, 2015 for conducting market survey. She went back to Turkey on 30th March, 2015. Salary of US \$50,000 for the period of her stay in India was credited in an account maintained by her in India.

Examine the taxability of the salary income received by her in India. Would your answer be different, if Sinsang Ltd. is maintaining its office in Delhi? (5 marks)

(b) Narrate the provisions of the Income-tax Act, 1961, with respect to surcharge on income-tax for various types of assesseees for the assessment year 2015-16.

(5 marks)

(c) State the rate of deduction allowable under the Income-tax Act, 1961 while assessing income from business or profession in the following cases :

(i) For acquisition and installation of new plant or machinery by a manufacturing company.

(ii) For expenditure (revenue or capital) on in-house scientific research by a company engaged in business or manufacture or production of any article other than those specified in the Eleventh Schedule of the Income-tax Act, 1961.

- (iii) Contribution to approved scientific research association including social and statistical research.
- (iv) Capital expenditure (other than on acquisition of land, goodwill or financial instrument) incurred for setting-up and operating cold chain facility.
- (v) Expenditure incurred by companies on notified skill development projects.
(5 marks)

OR (Alternate question to Q.No. 2)

Question 2A

- (i) Nitin, a resident of India has the following incomes during the previous year 2014-15:

	₹
Income from textiles business in India	7,30,000
Income from garment business in Canada (with which India does not have double tax avoidance agreement)	2,40,000
Tax levied in Canada on the above said income	54,000
Purchase of NSC VIII Issue	70,000
Compute the tax liability of Nitin.	(5 marks)

- (ii) What do you mean by 'transfer pricing' ? Explain its importance and benefits.
(5 marks)
- (iii) Under what circumstances an application for advance ruling will not be allowed ? Is advance ruling binding on the income-tax department ? When does an advance ruling become void ?
(5 marks)

Answer 2(a)

Section 10 (6) (vi) of Income Tax Act, 1961 states that remuneration received by a foreign national as an employee of a foreign enterprise for services rendered during his / her stay in India is exempt from tax provided

- Foreign enterprise is not engaged in any business or trade in India;
- Stay of employee does not exceed 90 days in such Previous Year; and
- Such remuneration is not liable to be deducted from the income of employer chargeable under the Income Tax Act.

In the given case,

Ms. Alicia stayed in India for a period of (1+ 28+30) 59 days inclusive of the days of coming to and going from India.

Since, Ms. Alicia satisfies all the above condition, she is not required to pay tax on US \$ 50,000 received by her in India during January to March, 2015.

Yes, if Singsang Ltd. had its office in Delhi, it would have meant that foreign enterprise was engaged in business in India and accordingly exemption under section 10(6)(vi) would not have been available to Ms. Alicia.

Answer 2(b)

Provisions of Income Tax Act, 1961 with respect to Rate of Surcharge are discussed below:

1. For resident individuals (including senior citizens and super senior citizens), Cooperative societies, firms and local authorities whose total income exceeds Rs. 1 crore - 10% on income tax payable.
2. For domestic company having a total income of exceeding Rs. 1 crore but not exceeding Rs. 10 crore - 5% on income tax payable.
3. For domestic company having a total income of exceeding Rs. 10 crore - 10% on income tax payable.
4. For Company other than a domestic company having a total income exceeding Rs. 1 crore but not exceeding Rs. 10 crore - 2% on income tax payable
5. For company other than a domestic company having a total income exceeding Rs. 10 crore - 5% on income tax payable.

Answer 2(c)

- (i) 15% of aggregate amount of actual cost of new assets acquired and installed.
- (ii) 200% of the expenditure
- (iii) Contribution to an approved Scientific research association which has its object undertaking of scientific research qualifies for 175% deduction under section 35(1)(ii). However where the contribution has been made to a research association which has as its object the undertaking of research in social science or statistical research, the deduction is 125% under section 35(1)(iii) of the Income Tax Act, 1961.
- (iv) 150% of the capital expenditure
- (v) 150% of the expenditure

Answer 2A(i)

Computation of tax liability of Mr. Nitin for the Previous year 2014-15

<i>Particulars</i>	<i>Rs.</i>	<i>Rs.</i>
Indian Income		7,30,000
Foreign Income		2,40,000
Gross Total Income		9,70,000
Less: Deduction U/S 80C (Purchase of NSC)		(70,000)
Total Income		9,00,000
Tax on first Rs.2,50,000	Nil	
Tax on next Rs. 2,50,000 @ 10%	25,000	

Tax on next Rs. 4,00,000 @ 20%	80,000	
Tax	1,05,000	
Add :		
Education Cess @ 2%	2,100	
SHEC @ 1%	1,050	1,08,150
Less : Double taxation relief under section 91:		
1) Tax on doubly taxed income=		
1,08,150/9,00,000 X 2,40,000	28,840	
2) Tax levied in Canada	54,000	(28,840)
(Whichever is less)		
<hr/>		
Tax payable		79,310
<hr/>		

**Doubly taxed income is the foreign income earned in Canada where there is no double tax avoidance agreement*

Answer 2A(ii)

Transfer Price means the value or price at which transactions take place amongst related parties. It is the price at which an enterprise transfers physical goods and intangible property and provides services to associated enterprises. It is used in accounting for transfer of goods or services from one responsibility centre to another or from one company to another associated company. It affects the revenue of transferring division and the cost of receiving division. As a result, the profitability, return on investment and managerial performance evaluation of both divisions are also affected.

Transfer pricing mechanism is very important and beneficial due to the following reasons:

1. *Helpful in correct pricing of Products/Services* : An effective transfer pricing mechanism helps an organization in correctly pricing of its products and services. Since, in any organization, transaction between associated parties occurs frequently, it is necessary to value all transactions correctly so that the final product/ service may be priced correctly.
2. *Helpful in Performance Evaluation* : For the performance evaluation of any entity, it is necessary that all economic transactions are accounted. Calculation of correct transfer price is necessary for accounting of inter-related transaction between two associated enterprises.
3. *Helpful in complying Statutory Legislations* : Since related party transaction have a direct bearing on the profitability or cost of a company, the effective transfer pricing mechanism is very necessary. For example, if the related party transactions are measured at less value, one unit may incur loss and other unit may earn undue profit. This will result in income tax imbalances at both parties end.

Transfer pricing is also helpful in checking the practice of tax evasion.

Answer 2A(iii)

Application for advance ruling shall not be allowed when the question raised in the application:

- 1) is already pending in applicant's case before any Income Tax Authority.
- 2) involves determination of fair market value of any property.
- 3) relates to a transaction which is designed for avoidance of income tax.

Advance ruling shall have binding only on the Commissioner and the Income Tax Authorities subordinate to him in respect of the applicant and the transaction.

The advance ruling shall be *void ab-initio*, if it is subsequently found to have been obtained by fraud or misrepresentation of facts.

PART B**Question 3**

- (a) *Cost of production of a product manufactured by ABC Ltd. worked out to ₹350 per piece. Out of the total produced pieces, company sold 120 pieces @ ₹700 per piece to industrial consumers, 70 pieces to a Central Government department @ ₹690 per piece, 210 pieces to wholesaler @ ₹720 per piece and 70 pieces in retail @ ₹800 per piece. 20 pieces were distributed as free samples. Out of the 70 pieces sold to Government department, 20 pieces were rejected by them, which were subsequently sold to other customers @ ₹300 per piece, without bringing them back into the factory. Balance pieces were in stock, out of which 25 pieces got damaged and have become unsaleable.*

All the above prices are exclusive of excise duty and VAT. The rate of excise duty on the product is 12% plus education cess @ 3%.

- (i) *Calculate the amount of excise duty payable.*
 - (ii) *Advise the management about the steps to be taken in respect of 25 pieces which were damaged in storage and became unsaleable. (5 marks)*
- (b) *Shyam Ltd. makes an unauthorised import of 3,000 pieces of a product CIF priced at \$2 per piece by air from USA. The consignment is liable to be confiscated. The import is adjudicated. Assistant Commissioner gives to the company an option to pay a fine in lieu of confiscation. It is proposed to impose fine equal to 50% of margin of profit. The market price is ₹200 per piece. The rates of duty are as under :*

<i>Basic customs duty</i>	<i>20%</i>
<i>Additional customs duty under section 3(1)(vi)</i>	<i>2%</i>
<i>Additional customs duty under section 3(5)</i>	<i>Nil</i>

Exchange rate is ₹50 per U.S. Dollar.

Compute — (i) the amount of fine; and (ii) total amount payable by the company to clear the consignment. (Calculations should be made to the nearest rupee). (5 marks)

(c) Comment on the applicability or otherwise of service tax, in the following cases:

- (i) Service provided by a private transport operator to higher secondary school in relation to transportation of students to and from the school.
- (ii) Vehicle parking service provided to general public in a shopping mall.
- (iii) Transportation of petroleum and petroleum products and household effects by railways.
- (iv) Transportation of postal mails and mail bags by a vessel.
- (v) Transport facility provided by a school (not recognised by government) to its students through a fleet of buses and cabs owned by the school.

(5 marks)

(d) Majboot Constructions undertakes works contracts and maintains sufficient records to quantify the labour and other service charges. From the details given below, calculate the taxable turnover, input tax credit and net VAT payable under the State VAT law (output VAT rate is 12.5%) :

	₹
Total contract price (excluding VAT)	90,00,000
Materials purchased and used for the contract taxable @ 12.5% VAT (inclusive of VAT)	16,87,500
Labour charges paid for execution of the contract	20,00,000
Other service charges paid for the execution of the contract	12,00,000
Cost of consumables used not involving transfer of property in goods	3,00,000

Majboot Constructions also purchased a plant for use in the contract for ₹10,40,000 (inclusive of VAT). In the VAT invoice relating to the plant, VAT was charged at 4% separately. Assume 100% input tax credit is available on capital goods immediately. (5 marks)

(e) Mahesh Engineers Ltd. removed goods from their factory at Kanpur on 20th April, 2015 for sale from their depot at Baroda. On that date, the normal transaction value of goods at Kanpur factory was ₹35,000 while normal transaction value at Baroda depot was ₹33,000. The rate of excise duty was 12% ad valorem. The said goods were sold from Baroda depot on 15th May, 2015. On that date the normal transaction value at Baroda depot was ₹39,000 and rate of duty was 16%.

Mahesh Engineers Ltd. paid the duty on ₹35,000 @ 12%. The Central Excise Department claimed that central excise duty should be levied @ 16% on the value ₹39,000.

Examine the Department's claim and comment.

(5 marks)

Answer 3(a)**Calculation of excise duty payable**

<i>Particulars</i>	<i>No. of pieces</i>	<i>Rate per pc. Rs.</i>	<i>Total Rs.</i>
Industrial Consumers	120	700	84,000
Central Government Department	70	690	48,300
Wholesaler	210	720	1,51,200
Retailers	70	800	56,000
Others (Free sample) (Rule 4)	20	720	14,400
Assessable Value			3,53,900
Basic excise duty @ 12% (3,53,900 X 12%)			42,468
Education Cess @ 2%			849
SAH Cess @ 1%			425
Total Excise Duty			43,742

- As per Rule 4 of Central Excise Valuation (Determination of Price of Excisable Goods) Rules 2000, value of the excisable goods shall be based on the value of such goods sold by the assessee for delivery at any other time nearest to the time of removal of goods under assessment.
- Rule 4 cannot be applied here as the dates/ times of removal are not available in the question. Hence best judgement method under Rule 11 has been applied. Normal transaction value (price of the greatest aggregate quantity) ie. Wholesale price of highest quantity of 210 has been taken.
- The pieces returned by Government department and subsequently sold to others at lesser price will also be charged at the value at which the same were first removed because the same have not entered back in to the factory after its first removal.

Treatment of damaged units : As per Rule 21 of the Central Excise Rules, 2002, Management is advised to obtain the remission certificate from the central excise department for the damaged 25 pieces, if the same is not obtained then, duty shall be charged on such units also. Further, it is advised that such certificate must be obtained before the removal of the damaged goods from the factory.

Answer 3(b)**Computation of Amount Payable to Clear the Consignment**

<i>Particulars</i>	<i>Amount (In Rs.)</i>
CIF of imported goods 3,000 X \$2 X Rs.50 per piece	3,00,000
Add: Landing charges (1% of CIF)	3,000
	<u>3,03,000</u>

<i>Add</i> : Basic Customs Duty @ 20%	60,600
	<u>3,63,600</u>
<i>Add</i> : Additional Custom Duty @ 12% on Rs.3,63,600	43,632
<i>Add</i> : Education Cess 3% on BCD & CVD (3% x (60,600 +43,632))	<u>3,127</u>
Total cost to company	4,10,359
Market price 3,000 pieces x Rs.200	6,00,000
Profit Margin (Market Price - Cost)	1,89,641
Fine equal to 50% of profit margin	94,820
Total amount payable (Duty + Fine) (60,600+43,632+3,127+94,820)	2,02,179

Note:

- As per Section 125 of the Customs Act, redemption fine shall not exceed market value of the goods excluding import duty.
- Amount payable to redeem goods = redemption fine + import duty.

Answer 3(c)

- Exempt*: service provided to educational institutions by way of transportation to students is exempted from service tax vide Notification No. 25/2012 ST dated 20.06.2012.
- Taxable*: services provided by way of vehicle parking to general public are not exempted from service tax.
- Taxable*: transportation of petroleum and petroleum products and household effects by railway is not exempted from service tax.
- Taxable*: transportation of postal mails and mail bags through vessel is not exempted from service tax.
- Exempt*: services provided by an education institution to its student are exempted from service tax even if such institution is not recognized by government. (Notification No. 25/2012 ST dated 20.06.2012 as amended)

Answer 3(d)**Computation of taxable turnover, input tax credit & Net VAT payable**

<i>Particulars</i>	<i>Amount Rs.</i>
Total Contract Price	90,00,000
Less : Deductions admissible :	
Labour charges paid	20,00,000
Service charges paid	12,00,000
Cost of consumables	3,00,000 (35,00,000)

PP–ATLP–December 2015	12	
Taxable Turnover		55,00,000
Output VAT payable @ 12.5%		6,87,500
Less: Input tax credit admissible		
On the material purchased (16,87,500X 12.5/112.5)	1,87,500	
On the plant purchased (10,40,000X4/104)	40,000	(2,27,500)
Net VAT payable		4,60,000

Note:

1. Under works contract, VAT is imposed on the sale price of the goods in which there is a transfer of property. Labour and other service charges incurred for such execution are deductible.
2. Cost of consumables has been treated as service portion as ownership is not transferred in those goods

Answer 3(e)

Rule 7 of the Central Excise (Determination of price of Excisable Goods) Rule, 2000 interalia, provides that where excisable goods are not sold at the factory gate but are transferred to a depot, the assessable value for the goods cleared from factory is the normal transaction value of such goods at the depot or about the same time at which the goods as being valued are removed from the factory or warehouse.

In the given case, Rs.35,000 represents value on 20.04.2015 (time of removal) at Kanpur factory, but it is not the value prevalent at the depot. Similarly, Rs.39,000 represents depot price, but it is not the price prevalent on 20.04.2015 (time of removal).

The correct value to be adopted in this case is the depot price of such goods (normal transaction value) on 20.04.2015. ie. Rs.33,000.

Further, the applicable rate of duty shall be the rate of duty in force on the date when such goods are removed from the factory. Hence, the correct rate of duty will be 12%. Thus, the Department's claim is not correct in the instant case.

Attempt all parts of either Q.No. 4 or Q.No. 4A

Question 4

- (a) *State whether the physician samples of the patentor and proprietary medicines are excisable goods despite being statutorily prohibited from being sold. Discuss briefly in the light of a decided case law. (5 marks)*
- (b) *With reference to section 9AA of the Customs Tariff Act, 1975, state briefly the provisions of refund of anti-dumping duty with reference to relevant case law. (5 marks)*
- (c) *The petitioner, a charitable society is engaged in running internationally renowned schools. It allowed other schools to use its name, logo and motto and as a consideration thereof, received collaboration fees from such schools which*

comprised of a non-refundable amount and an annual fee. The schools were required to observe certain obligations/terms and un-impeachable confidentiality.

Department contended that the petitioner was engaged in providing franchise service and accordingly issued show cause notice proposing to recover service tax along with interest and penalty.

Examine the validity of the Department's action with reference to decided cases, if any. (5 marks)

OR (Alternate question to Q.No. 4)

Question 4A

- (i) *Bhuwan Ltd. was awarded a contract for providing repair and maintenance services in respect of an immovable property for ₹3,50,000. As per the terms of contract, the material required for repair and maintenance was also provided by Bhuwan Ltd. Are said services subject to service tax ? If so, determine the service tax liability of Bhuwan Ltd. (5 marks)*
- (ii) *Is assessee required to reverse the CENVAT credit availed on capital goods destroyed by fire when the insurance company reimburses the value of such capital goods inclusive of excise duty ? State with relevant provisions of law. (5 marks)*
- (iii) *Quoting the relevant provisions of the law, state the relevant dates for determining:*
- (a) *Rate of duty, when warehoused goods are removed for home consumption.*
- (b) *Rate of duty, if the warehoused goods are not removed from the warehouse within the permissible period. (5 marks)*

Answer 4(a)

Facts of the Case : The question for consideration is whether physician samples of patent and proprietary medicines intended for distribution to medical practitioners as free samples, satisfies the test of marketability, when the sale of the physician samples is prohibited under the Drugs and Cosmetics Act, 1940.

In case of *Medley Pharmaceuticals Ltd., Vs. CCE - 2011 (269) E.L. T. A20 (S.C)*, the Supreme Court observed that merely because a product was statutorily prohibited from being sold, would not mean that the product was not capable of being sold. Sale is not a necessary condition for charging duty as excise duty is payable in case of free supply also. Since, physician samples were capable of being sold in open market, the same were marketable and thus, liable to excise duty.

Moreover, the Drugs and Cosmetics Act, 1940 (Drugs Act) and the Central Excise Act, 1944 operated in different fields. The restrictions imposed under Drugs Act could not lead to non-levy of excise duty under the Central Excise Act, thereby causing revenue loss. Prohibition on sale of physician samples under the Drugs Act did not have any bearing or effect on levy of excise duty.

Since, physician sample was capable of being sold in open market, the physician samples were excisable goods and were liable to excise duty.

Answer 4(b)

According to the provisions of Section 9AA of the Customs Tariff Act, 1975, wherein importer proves to the satisfaction of the Central Government that he has paid any anti-dumping duty imposed on any article, in excess of the actual margin on dumping in relation to such article, he shall be entitled to refund of such duty.

However, the importer will not be entitled for refund of provisional anti dumping duty under Section 9AA as the same is refundable under section 9A(2) of the said Act. Refund of excess anti-dumping duty paid is subject to provisions of unjust enrichment. This view was held by Apex Court in the case of - *Automotive Tyre Manufacturers Association Vs. Designated Authority* 2011 (63) ELT 481

Answer 4(c)

The facts of the given case are similar to the case of Mayo College General Council decided by the High Court. In the instant case, the High Court held that when the petitioner permitted other schools to use their name, logo and also motto, it clearly tantamounted to providing "franchise service" to the said schools and if the petitioner realised the "franchise" or collaboration fees from the franchisee schools, the petitioner was duty bound to pay service tax to the Department. Therefore, in view of the above mentioned ruling of High Court, the action of the Department is valid.

Answer 4A(i)

The contract entered into by Bhuwan Ltd., required the provision of both services and materials. Therefore, it falls within the scope of the term "Works Contract" as defined under Section 65 B (54) of the Finance Act, 1994 and thus, is liable to service tax as declared service under Section 66 E (h) of Finance Act, 1994.

In the given case, since the details of material value / service portion are not available, the value of the service portion in the execution of the works contract will be determined as per rule 2A(ii)(B) of the Service Tax (Determination of value) Rules, 2006. It provides that service tax shall be payable on 70% of the total amount charged for the works contract.

Computation of Service Tax Liability

70% of the total amount charged 3,50,000 x 70%	Rs. 2,45,000
Rate of service tax	14%
Amount of service tax payable	Rs. 34,300

Note : Since, the question is silent about the point of taxation and the date of contract applicable, it is assumed that point of taxation is after 31st May, 2015 and hence the rate of service tax has been assumed to be 14%. However, the point of taxation may be assumed to be the date prior to 1st June, 2015 and then the rate of service tax would be 12.36% and accordingly service tax payable would be Rs. 30,282

Answer 4A(ii)

The issue under discussion is similar to that of *CCE Bangalore vs. Tata Advance Material Ltd.* 2011(271)ELT 62 where Karnataka High Court observed that the assessee

had paid the premium and covered the risk of the capital goods and when they were destroyed, the assessee was compensated.

The High Court held that merely because the insurance company paid the assessee the value of goods including excise duty paid would not render the availing of CENVAT Credit wrong and thus Excise Department cannot demand the reversal of credit of the said amount from the company.

Accordingly, the assessee is not required to reverse the CENVAT credit availed on the capital goods destroyed by fire.

Answer 4A(iii)(a)

As per Section 15(l)(b) of the Customs Act, 1962, rate of duty as prevalent on date of presentation of Bill of Entry for clearance for home consumption from warehouse is applicable and not the rate prevalent when goods were removed from customs port.

Answer 4A(iii)(b)

Goods which are not removed within the permissible period are deemed to be improperly removed on the day it should have been removed. Thus, duty applicable on such date i.e., last date on which the goods should have been removed is relevant and not the date on which the goods were actually removed.

Question 5

- (a) *Who are not eligible for composition scheme under the VAT regime ? (3 marks)*
- (b) *With reference to the Central Excise Act, 1944 and the rules thereunder, state with reasons, whether the following persons require registration or not :*
- (i) *Persons manufacturing goods which are chargeable to nil rate of duty.*
- (ii) *Central Government undertakings manufacturing excisable goods.*
- (iii) *100% export oriented undertaking (EOU). (3 marks)*
- (c) *Write a brief note on taxpayer's identification number (TIN) for the purpose of VAT. (3 marks)*
- (d) *XYZ Ltd., an Indian company, provides a taxable service to its other establishment in USA. Can the services provided by an establishment of a person in a taxable territory to another establishment of the same person in a non-taxable territory be considered as export of service ? Give reason in brief. (3 marks)*
- (e) *A show cause notice demanding customs duty was issued in case of clearance made by 100% export oriented undertaking (EOU) to domestic tariff area (DTA). Is the show cause notice defective in law ? Explain in brief. (3 marks)*

Answer 5(a)

The following persons are not eligible for the composition scheme under the VAT regime:

1. Having turnover of previous year above the specified limit, say Rs. 50 lakhs.
2. Making sales or purchases
3. Making import or export sales.

4. Making interstate stock transfer.
5. Making interstate transfer of goods for execution of works contract.

Answer 5(b)

- (i) No, because manufacturers of goods which are chargeable to NIL rate of duty are exempt from registration provided a declaration is filed.
- (ii) Yes, registration is compulsory as the provisions of Section 6 of the Central Excise Act, 1944 read with Rule 9 of Central Excise Rules, 2002 apply in respect of every person who manufactures or produces excisable goods (including Central/State Government Undertakings or Undertakings owned or controlled by autonomous corporations) in India.
- (iii) No, as 100% EOU is deemed to be registered under Rule 9 of the Central Excise Rules, 2002. However, such unit shall be required to get itself registered if it removes excisable goods to Domestic Tariff Areas (DTA) or procures excisable goods from DTA.

Answer 5(c)

Tax Payer's Identification Number (TIN) is the registration number of a dealer. It consists of 11 digit numerals. First two characters represent the State code and the next nine characters are different in different States. TIN facilitates computer applications such as detecting stop files and delinquent accounts. It also helps in cross checking the information on tax payer compliance.

Answer 5(d)

No, even though such persons have been specified as distinct person under explanation 3 to Section 65B (44), yet the transaction between such establishments have not been recognised as export of service in terms of Rule 6A (l)(f) of the Service Tax Rules, 1994. As a consequence, there cannot be any export of service between XYZ Ltd., and its other establishment in USA.

Exports are not eligible for tax benefit where the exporter is entitled to claim rebate of duties and taxes paid on inputs or input services used in exported service. Further, in case of service provided to the overseas establishment of the same person, benefit of CENVAT credit is denied.

Answer 5(e)

Yes, the show cause notice issued is defective in law as in respect of clearance made by a 100% Export Oriented Undertaking to Domestic Tariff Area the duty to be paid by the 100% EOU is the Duty of Excise (equal to custom duty) and not Custom Duty. Therefore, show cause notice using the word Customs Duty instead of Excise Duty is not maintainable.

Question 6

- (a) *Explain the role of Company Secretaries under the VAT regime in India.*
(5 marks)
- (b) (i) *Name the quarterly returns to be filed under Rule 12 of the Central Excise Rules, 2002.*
(3 marks)

(ii) *When is duty drawback prohibited under the Customs Act, 1962 ?*
(2 marks)

(c) *"All purchases of goods meant for re-sale or manufacture of taxable goods are eligible for input tax credit." Comment.*
(5 marks)

Answer 6(a)

The Company Secretaries have to verify all documents to be filed before VAT authorities about the correctness of the documents.

- (1) They have to see that returns are filed in proper forms.
- (2) They have to take care of the procedural aspects.
- (3) They are consultant and advisor to his client.
- (4) They are also the legal advisor of the dealers in VAT.
- (5) They have to ensure that records and documents are maintained in proper form.
- (6) They are authorized to conduct VAT audit in certain states.
- (7) Certain states have recognized Company secretaries to act as authorized representative in the matter of VAT.

Answer 6(b)(i)

Quarterly returns to be filed include :

- (1) ER-3 by SSI units availing exemption
- (2) Form - A by units availing area based exemption
- (3) ER-8 by assesseees availing exemption under Notification No. 1/2011 and 12/2012.

Answer 6(b)(ii)

Duty Drawback is prohibited under the Customs Act when:

- (1) the drawback due on any goods is less than Rs. 50.
- (2) the market price of the goods is less than the amount of duty drawback due thereon.
- (3) the exported goods are likely to be smuggled back to India.

Answer 6(c)

The statement is not correct since no Input Tax Credit is allowed in respect of the following purchases:

- (1) Goods purchased from unregistered dealers
- (2) Goods purchased from registered dealers who opt for composition scheme
- (3) Goods purchased from other States or Countries

- (4) Goods purchased to manufacture exempted goods
- (5) Goods purchased for personal consumption
- (6) Goods purchased and returned within the specified period
- (7) Goods purchased or destroyed by fire or are stolen or lost
- (8) Goods purchased are given away as free samples
- (9) Goods purchased for which purchase invoice is not available with the claimant.

DRAFTING, APPEARANCES AND PLEADINGS

Time allowed : 3 hours

Maximum marks : 100

NOTE : Answer ALL Questions.

Question 1

- (a) Anuradha and Sudha are partners running a fashion designing boutique. They now propose to induct Seema as another partner in their firm w.e.f. 1st September, 2015. Draft a deed of agreement of admission of Seema into the firm. Assume data.
- (b) Surya Power Ltd. proposes to insert an article in its articles of association enabling it to buy-back its shares. It seeks your professional advice on the draft articles. Advise.
- (c) Draft an application for grant of bail.
- (d) Draft an affidavit of a creditor in proof of his debt in proceeding for the liquidation of a company. (5 marks each)

Answer 1(a)

Deed of Agreement of Admission into Firm of a New Partner

THIS DEED OF AGREEMENT is made the day of 2015 BETWEEN Anuradha, Daughter of aged R/o and Sudha, Daughter of aged R/o partners in the firm AnuSudha Co. of the ONE PART, AND Seema, daughter of aged years resident of of the OTHER PART.

WHEREAS the said Anuradha and Sudha are partners in the firm AnuSudha Co. situated in and are bound as such under a deed partnership executed by them on the day of 2015 hereinafter referred to as the "partnership deed".

AND WHEREAS the said Seema is desirous of being admitted as a member in the aforesaid firm of AnuSudha Co. and invest a sum of Rs..... AND the said Anuradha and Sudha are willing to admit him as an additional partner.

NOW THEREFORE THE DEED WITNESSES that in pursuance of the said agreement and in consideration of the said Seema bringing in and contributing the sum of Rupees..... (Rs.....) only as additional capital of the above partnership firm, it is mutually agreed as follows:

1. The parties hereto shall, as from the date hereof be and continue partners for the unexpired residue of the terms mentioned in para..... of the partnership deed subject in all respects to the conditions, stipulations, and provisions of the aforesaid partnership deed, so far as applicable, and except as varied by this deed of agreement.

2. The capital mentioned in the partnership deed shall hereafter be changed to the sum of Rupees..... only and the partners shall hereafter have the undernoted shares in the capital.

Anuradha shall have Rs..... in the said capital;

Sudha shall have Rs..... in the said capital; and

Seema shall have Rs..... in the said capital.

3. The profits and losses of the partnership shall continue to be borne by the partners hereto in proportion to their above named respective shares.

IN WITNESS WHEREOF the said Anuradha, Sudha and Seema have hereto at..... signed the day and the year first above mentioned.

WITNESSES:

- | | |
|----|---------------|
| 1. | Sd/- Anuradha |
| 2. | Sd/- Sudha |
| 3. | Sd/- Seema. |

Answer 1(b)

Model article on Buy-back of shares for Surya Power Limited

"Notwithstanding anything contained in these Articles, the Board of Directors may, when and if thought fit, buy back such of the Company's own shares or securities as it may think necessary, subject to such limits, upon such terms and conditions, and subject to such approvals, as may be permitted by the law"

Answer 1(c)

BEFORE THE DISTRICT AND SESSIONS JUDGE COURT AT _____

IN THE MATTER OF

STATE

vs

Mr. ABC

FIR Number: (Mention the FIR number)

Under Section: (Mention the sections under which the FIR has been filed)

Police Station: (Mention the name of the Police Station)

Accused under custody since (Give the date from when the accused is in custody)

Application u/s 439 Criminal Procedure Code 1973 for grant of bail on behalf of the accused (name of the applicant of the bail)

MOST RESPECTFULLY SUBMITTED AS UNDER:

1. That the present FIR has been registered on false fact. The facts stated in the FIR are fabricated, concocted and without any basis.

2. That the police has falsely implicated the applicant in the present case, and arrested him although the applicant is a respectable citizen of the society and is not involved in any criminal case.
3. That the facts stated in the complainant against the applicant are civil disputes and does not constitute any criminal offence at all.
4. That the applicant is not required in any kind of investigation nor any kind of custodial interrogation is required.
5. That the applicant is having very good antecedents, he belongs to good family and there is no criminal case pending against them.
6. That the applicant is a permanent resident and there are no chances of his absconding from the course of justice.
7. That the applicant undertakes to present himself before the police/court as and when directed.
8. That the applicant undertakes that he will not, directly or indirectly make any inducement, threat or promise to any person acquainted with the facts of the case so as to dissuade him from disclosing such facts to the Court or to any police officer.
9. That the applicant further undertakes not to tamper with the evidence or the witnesses in any manner.
10. That the applicant shall not leave India without the previous permission of the Court.
11. That the applicant is ready and willing to accept any other conditions as may be imposed by the Court or the police in connection with the case.
12. That the Court below has failed to consider all the facts and circumstances of the case and has wrongly dismissed the bail application.

It is therefore prayed that the court may direct the release of the applicant on bail in the interest of justice.

Any other order which the court may deem fit and proper in the facts and circumstances of the case may be also passed in favor of the applicant.

APPLICANT

THROUGH
COUNSEL

Answer 1(d)

Specimen Affidavit of Creditor in proof of his debt in Proceeding for the Liquidation of a Company

IN THE HIGH COURT OF.....

The matter of the Indian Companies Act, 2013

and

The matter of the liquidation of..... Company Limited.

I, A.B., aged..... years, Son of Shri..... Resident of....., do hereby on oath (or on solemn affirmation) state as follows:

1. That the above named company was on the..... day of....., 2015, the date of the order for winding up the same, and still is justly and truly indebted to me in the sum of Rupees..... (Rs.....) only in account of (describe briefly the nature of the debt).
2. That in proof of the aforesaid debt I attach hereto the documents marked A, B and C.
3. That I have not, nor have any person or persons by my order or to my knowledge or belief for my use, received the aforesaid sum of Rupees..... or any part thereof, or any security or satisfaction for the same or any part thereof except the sum or security (state the exact amount of security).
4. That this affidavit is true, that it conceals nothing and no part of it is false.

Sd/- A.B.

Dated.....

Deponent

Verification

I, the above named deponent, verify that the contents of paragraphs 1 to 4 of this affidavit are true to my personal knowledge.

Sd/- A.B.

Dated.....

I,.....,S/o.....
R/o declares, from a perusal of the papers produced by the deponent before me that I am satisfied that he is Shri A.B.

Sd/-.....

Solemnly affirmed before me on this..... day of..... 2013 of..... (time) by the deponent.

Sd/-.....

(Oath Commissioner)

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

Question 2

Comment on the following :

- (a) *Appellate authorities under the Companies Act, 2013 on refusal of transfer/ transmission of shares.*
- (b) *Acts going beyond the memorandum of association are ultra vires.*
- (c) *A letter of authority is nothing but a power of attorney.*
- (d) *Registration of a will is not mandatory.*

(4 marks each)

OR (Alternate question to Q.No. 2)**Question 2A**

Distinguish between the following :

- (i) *'Supplementary deeds' and 'endorsements'.*
- (ii) *'Partnership' and 'limited liability partnership'.*
- (iii) *'Appellant' and 'defendant'.*
- (iv) *'Memorandum of understanding' and 'memorandum of association'.*

(4 marks each)

Answer 2(a)

Section 58 of the Companies Act, 2013 provides that the transferor or transferee, or the person who gave intimation of the transmission by operation of law, as the case may be, may appeal to the Board/Tribunal against any refusal of the company to register the transfer or transmission, or against any failure on its part within the specified period, either to register the transfer or transmission or to send notice of its refusal to register the same.

The appeal under above shall be made within two months of the receipt of the notice of such refusal or, where no notice has been sent by the company, within four months from the date on which the instrument of transfer, or the intimation of transmission, as the case may be, was delivered to the company.

According to Section 423 of the Companies Act, 2013 any person aggrieved by any decision or order of the Appellate Tribunal may file an appeal to the Supreme Court within sixty days from the date of communication of the decision or order of the Appellate Tribunal to him on any question of law arising out of such decision or order. However, the Supreme Court may, if it is satisfied that the appellant was prevented by sufficient cause from filing the appeal within the said period, allow it to be filed within a further period not exceeding sixty days.

Answer 2(b)

The Memorandum of the company should state the objects for which the company is proposed to be incorporated and any matter considered necessary in furtherance thereof;

The objectives of the company may be categorized as

- (i) the main objects to be pursued by the company on its incorporation;
- (ii) subjects incidental and ancillary to the attainment of the main objects; and
- (iii) other objects not included in (i) and (ii) above.

An act beyond the objects mentioned in the memorandum is ultra vires and void and cannot be ratified even by all members of the company. There is no restriction on objects except it should be legal and lawful.

Answer 2(c)

A letter of authority is nothing but a power of attorney. It is executed on plain paper and not on stamp paper. A letter of authority is usually issued for collecting some documents or papers dividend or interest on behalf of another. By and large, the law relating to the power of attorney will apply to letter of authority. A power of attorney includes an instrument empowering a specified person to act for and in the name of the person executing it. It is always kept by the attorney. It may be either general or special, i.e., to do all acts or to do some particular act.

Answer 2(d)

As per Section 18 (c) of the Registration Act, 1908 registration of will is not mandatory. It is optional, however, a registered will has certain advantages. Any testator may either personally or by duly authorized agent deposit with any registrar his will in a sealed cover super subscribed with the name of the testator and that of his agent and with a statement of the nature of the documents as per Section 42 of the Registration Act, 1908.

Answer 2A(i)**Supplementary Deed**

Supplementary deed is a document which is entered into between the parties on the same subject on which there is a prior document existing and operative for adding new facts to the document on which the parties to the document have agreed which otherwise cannot be done by way of endorsement. Thus, supplemental deed is executed to give effect to the new facts in the deed. When a deed or document is required to be supplemented by new facts in pursuance of or in relation to a prior deed this can be affected by either endorsement on the prior deed when short writing would be sufficient, or by executing a separate deed described as supplemental deed.

Endorsement

Endorsement means to write on the back or on the face of a document wherein it is necessary in relation to the contents of that document or instrument. The term “endorsement” is used with reference to negotiable documents like cheques, bill of exchange etc. For example, on the back of the cheque to sign one’s name as Payee to obtain cash is an endorsement on the cheque. Thus, to inscribe one’s signatures on the cheque, bill of exchange or promissory note is endorsement within the meaning of the term with reference to the Negotiable Instrument Act, 1881. Endorsement is used to give legal significance to a particular document with reference to new facts to be added in it.

Answer 2A(ii)**Partnership**

Partnership is an association of two or more like minded persons formed with a common objective to establish a lawful business house of their choice with the idea of earning profits. Therefore, all partners of a firm mutually agree to share all profits and losses of the business amongst them according to their predetermined shares/proportions fixed by them in the partnership agreement. Partnership is defined in Section 4 of the Partnership Act, 1932 as a relation between persons who have agreed to share profits of business carried on by all or any one of them acting for all.

Persons who have entered into partnership with one another are called individually partners and collectively a firm, and the name under which their business is carried on is called the firm name. In a partnership, the property of the firm is the property of the individuals comprising it. Creditors of a partnership firm are creditors of individual partners and a decree against the firm can be executed against the partners jointly and severally. Partners are the agents of the firm. A partner's liability is always unlimited.

Limited Liability Partnership (LLP)

As per section 2(n) of the Limited Liability Partnership Act, 2008 limited liability partnership means a partnership formed and registered under the LLP Act.

LLP is an alternative corporate business form that gives the benefits of limited liability of a company and the flexibility of a partnership. LLP can continue its existence irrespective of changes in partners. It is capable of entering into contracts and holding property in its own name. LLP is a separate legal entity, is liable to the full extent of its assets but liability of the partners is limited to their agreed contribution in the LLP.

Further, no partner is liable on account of the independent or un-authorized actions of other partners, thus individual partners are shielded from joint liability created by another partner's wrongful business decisions or misconduct. Mutual rights and duties of the partners within a LLP are governed by an agreement between the partners or between the partners and the LLP as the case may be.

Answer 2A(iii)

Appellant

Appellant is one who appeals against a decision, or remove a cause from a lower to a higher Tribunal /Court. An appellant, sometimes called the petitioner must demonstrate sufficient grounds for appeal, which are usually specified by statute, in order to challenge the judgement or findings.

Defendant

The party sued in an action. One who is sued or prosecuted. The title defendant is more generally applied to a party in civil than in a criminal suit or proceeding. The word defendant may include a respondent.

According to the Limitation Act, 1963, "defendant" includes- (i) any person from or through whom a defendant derives his liability to be sued; (ii) any person whose estate is represented by the defendant as executor, administrator or other representative.

Answer 2A(iv)

Memorandum of Understanding

A document that expresses mutual accord on an issue between two or more parties.

Memorandum of understanding are generally recognized as binding, even if no legal claim could be based on the rights and obligations laid down in them. To be legally

operative, a memorandum of understanding must (1) identify the contracting parties, (2) spell out the subject matter of the agreement and its objectives, (3) summarize the essential terms of the agreement, and (4) must be signed by the contracting parties.

Memorandum of Association

Memorandum of association of the company is the fundamental formation document. It is the constitution and charter of the company. It contains the basic conditions on the strength of which the company is incorporated. Thus, it defines and confines the area of operation of the company. It lays down the area, beyond which the action of the company cannot go. Section 4 of the Companies Act, 2013 and Table A, B, C, D and E in Schedule-I as may be applicable to such company deal with contents, form and printing and signature of memorandum of association.

Attempt all parts of either Q.No. 3 or Q.No. 3A

Question 3

Examine the following statements :

- (a) *Drafting is the synthesis of law and fact in a language form.*
- (b) *A sub-lease is an absolute assignment.*
- (c) *The right of appeal is not a natural or inherent right.*
- (d) *A legal opinion should be structured.* (4 marks each)

OR (Alternate question to Q.No. 3)

Question 3A

- (i) *Discuss the requisites of a valid complaint, citing relevant case laws.*
- (ii) *Briefly explain compounding of offences under the Securities and Exchange Board of India Act, 1992.*
- (iii) *Explain electronic data interchange (EDI).*
- (iv) *What do you understand by slump sale.* (4 marks each)

Answer 3(a)

It is appropriate to state that drafting is the synthesis of law and fact in a language form. This is the essence of the process of drafting. All three characteristics rank equally in importance. Legal drafting is the crystallization and expression in definitive form of a legal right, privilege, function, duty or status. A power of attorney includes an instrument empowering a specified person to act for and in the name of the person executing it. It is always kept by the attorney. It may be either general or special, i.e., to do all acts or to do some particular act.

The process of drafting operates in two planes, viz conceptual and verbal. Besides seeking the right words draftsman seeks the right concepts, effective drafting in right thinking and right composing.

Answer 3(b)

In India, a sub-lease is not an absolute assignment Privy Council in *Hunsraj vs*

Bejoylal Seal (1930) 57 Cal 1176). Further in *Akshay Kumar vs Akman Molla* (1915) 19 CWN 1197, it was held that there is no privity of estate as between the lessor and the sub-lease, who does not step into the shoes of lessee. A sub-lease is not prejudiced by the surrender of the head lease (Section 115 of Transfer of Property Act) but the position is different in the case of forfeiture which annuls all sub-leases except in case of fraud as between the lessor and lessee. A sub-lessee is entitled to relief against forfeiture under Section 114 of the Transfer of Property Act, 1882, which is applicable only in the case of non-payment of rent. No relief is open to the sub-lease in case of transfer of breach of covenant in restraint of transfer.

Answer 3(c)

A right of appeal is not a natural or inherent right; it is a creation of the statute. It is the statute alone to which the court must look to determine if a right of appeal exists in a particular instance or not. Parties cannot create a right of appeal by agreement or by mutual consent. It is not a matter of procedure but a substantive right and can be taken away only by a subsequent enactment if it says so expressly or by necessary intendment and not otherwise. It is for the appellant to show that the statute gives a right of appeal to him.

Answer 3(d)

Drafting a legal opinion should always split into three processes, the mental attitude, the thinking process and the writing process.

1. *The mental attitude* - It involves four fundamental principles dealing with a legal situation, facts are more fundamental than the law, the law is a means to the end and answer the question.
2. *The thinking process* – read and digest the instructions, answers the primary questions, understand and organize the facts, consult the legal framework, look at the case as a whole and consider the advice.
3. *The writing process* - It needs to be structural, divided into paragraphs and consistent.

Answer 3A(i)

Complaint under Section 2(d) of the Criminal Procedure Code means any allegation made orally or in writing to a magistrate with a view to his taking action under this court, that some person whether known or unknown has committed an offence but it does not include a police report. However, a report made by a police officer in a case which discloses after investigation the commission of a non-cognizable offence shall be deemed to be a complaint. In general, a complaint into an offence can be filed by any person except in case of offences relating to marriage, defamation, mentioned under Sections 195 and 197. A complaint in a criminal case is what a plaint in a civil case. The requisites of a complaint are

1. An oral or written allegation
2. Some person known or unknown has committed the offence
3. It must be made to a magistrate

4. It must be made with the object that action should be taken

There is no specific format for a complaint. A petition addressed to the Magistrate with an allegation that an offence has been committed and ending with a prayer that the complaint be suitably dealt with (*Mohd. Yousuf vs. Jahan* AIR 2006 SC 705). It need not be presented in person.

Answer 3A(ii)

Compounding of offences is a process whereby an accused pays compounding charges in lieu of undergoing consequences of prosecution. Section 24A of the SEBI Act, 1992 permits compounding of offences by the court where prosecution proceedings are pending. Section 24A states that notwithstanding anything contained in the Code of Criminal Procedure, 1973 any offence punishable with imprisonment only or with imprisonment and also with fine may either before or after the institution of any proceeding be compounded by the Securities Appellate Tribunal or a court before such proceedings are pending. Compounding of offences can cover appropriate prosecution cases filed by SEBI before the criminal courts.

Prosecution here means filing of criminal complaints before various criminal courts by SEBI for violation of provisions of securities laws which may lead to imprisonment and/or fine. Compounding of offence can take place at any stage after filing criminal complaint by SEBI. Where a criminal complaint has not yet been filed but is envisaged, the process for consent orders will be followed rather than the one for compounding.

Answer 3A(iii)

Electronic Data Interchange (EDI) is an electronic communication method that provides standards for exchanging data via any electronic means. By adhering to the same standard, two different companies or organizations, even in two different countries, can electronically exchange documents (such as purchase orders, invoices, shipping notices, and many others). EDI implies a sequence of messages between two parties, either of whom may serve as originator or recipient. The formatted data representing the documents may be transmitted from originator to recipient via telecommunications or physically transported on electronic storage media. It distinguishes mere electronic communication or data exchange, specifying that in EDI, the usual processing of received messages is by computer only. Human intervention in the processing of a received message is typically intended only for error conditions, for quality review, and for special situations. EDI can be formally defined as the transfer of structured data, by agreed message standards, from one computer system to another without human intervention.

Answer 3A(iv)

Slump Sale is one of the widely used ways of business acquisitions. A slump sale is the transfer of a whole or a part of a business concern as a going concern; lock, stock and barrel. The concept of 'slump sale' was incorporated in the Income Tax Act, 1961 ("IT Act") by the Finance Act, 1999 with the inclusion of section 2(42C). The term 'slump sale' is defined as transfer of one or more undertakings as a result of the sale for a lump-sum consideration without values being assigned to the individual assets and liabilities in such sales.

Slump sale is carried out through following steps:

- (a) To find Buyer
- (b) To enter into & sign MoU/Term sheet
- (c) To make Valuation of the undertaking
- (d) To negotiate and deal Structuring
- (e) To enter into final Slump sale agreement

Question 4

- (a) *Dinson Inc., a Malaysian food processing company intending to expand its business in India plans to form a joint venture with Himalaya Agro Pvt. Ltd., a company incorporated under the Companies Act, 2013, engaged in the business of processing and marketing of food products. You are required to draft a specimen joint venture agreement for establishing the business with assumed data.*
- (b) *Draft a specimen underwriting agreement as per the requirements of the Companies Act, 2013. (8 marks each)*

Answer 4(a)

THIS AGREEMENT IS MADE on thisday of 2016 BETWEEN DINSON INC., Incorporated under the appropriate laws of the Malaysia having its office at 5 Seventh Street, Malaysia of the ONE PART and HIMALAYAAGRO PVT LTD a Company registered under the Companies Act, 2013 having its office at 99 Chowring Road Calcutta, West Bengal-700071 of the OTHER PART.

WHEREAS DINSON INC., (hereinafter referred to as DINSON) carries on business of food processing and intends to extend its market here in India and elsewhere.

Whereas HIMALAYAAGRO PVT LTD. (hereinafter referred to as HIMALAYA AGRO) carries on business of processing and marketing of food products and intends to extend its market here in India and outside India

Whereas DINSON and HIMALAYA AGRO intend to co-operate in manufacturing/ dealing in and exporting food products in India and abroad for mutual benefit by setting up a new joint venture company.

NOW THESE PRESENTS WITNESSETH and the parties hereby agree as follows:

1. A Joint-stock company would be formed under the name and style of Indo-Malaysian Company Pvt. Ltd. under the Companies Act, 2013 having its Registered Office at 99 Chowring Road, Calcutta - 700071.
2. DINSON and three of its nominees and HIMALAYA AGRO and three of its nominees would be the subscribers to the Memorandum and Articles of Association of the said company to be incorporated.
3. The shareholding in the Share Capital of the said company to be incorporated would be in equal proportions between DINSON and HIMALAYAAGRO.

4. The Memorandum and Articles of Association of the company proposed to be incorporated would be settled in mutual consultation and the same would govern the rights and obligations of DINSON and HIMALAYA AGRO in relation to the said proposed company.
5. DINSON will be allotted shares in the said new company partly in cash and partly towards the cost of plant, machinery and equipment to be supplied by DINSON to the new company and in consideration for assignments by DINSON of its Patent Rights, Trade Marks, Trade Names and Licences in favour of the new company to be incorporated. The consideration for allotment of shares to DINSON would also include the supply and transfer of technical formula, new inventions, secret processes, technical information concerning the production, manufacturing, testing, specifications, instructions and information as to the manufacture of, development, use and servicing, maintenance and improvement of quality of food products.
6. DINSON will furnish necessary technical assistance and expertise to the new company for assembling, installation, start-up and for smooth running of the manufacturing and selling processes as might be required by the new company from time to time.
7. DINSON will furnish to the new company all other technical assistance and advice in relation to the operation of the plant and machinery, repairs thereof, testing facilities, training facilities and Research & Development facilities should be arranged for, provided and continued for successful running of the business of the new company.
8. The shares that would be allotted by the new company should not be transferred by either DINSON or HIMALAYA AGRO within a period of five years from the date of allotment and thereafter if any of the parties intends to transfer any share then the same shall be offered first to the other party at a price to be determined by a Valuer to be appointed by mutual agreement and in absence by application to the Indian Chamber of Commerce.
9. The new company will manufacture food products and the same would be marketed in India and exported to other countries under the Trade name or Brand name made available by DINSON and by any other name and shall obtain new Trademark and obtain Patents for further and better manufacturing, selling and exporting the new company's products.
10. DINSON will buy 75% of the products of new company for exporting; to other countries through its own organisations or outlets at a remunerative price not below the price at which the products are sold in India.
11. Neither party shall carry on their own business in a manner which will directly adversely affect the business and profitability of the new company.
12. The expenses for the setting up and promotion of the new company would be shared equally by DINSON and HIMALAYA AGRO.
13. The consideration for allotment of shares of the new company to DINSON shall be paid in cash and in kind such as by transfer of immovable properties for the

setting up of factory and making arrangement for the office accommodation of the new company. The valuation of such immovable properties including office accommodation would be decided by mutual agreement between DINSON and HIMALAYA AGRO.

- 14. Any disputes or differences arising in relation to this agreement, its construction, validity, performance, breach or any other question shall be referred to the Indian Chamber of Commerce for settlement by Arbitration or Conciliation in Calcutta and the decision of the said Arbitrator shall be final and binding on both the parties.
- 15. This agreement is made subject to obtaining approvals of the Indian Government and other concerned authorities.
- 16. In the event certain additions or alterations are required under this agreement due to imposition of certain terms and conditions by Government of India or appropriate authority granting the approval shall be incorporated in this agreement by way of a supplemental agreement and if required the Memorandum and Articles of Association of the new company would also be in conformity with such directions or approvals of the appropriate authorities.
- 17. IN WITNESS WHERE OF the parties hereto have signed, sealed and delivered these presents on the day, month and year first above-written.

Signed, sealed and delivered by

Mr.....

Pursuant to the Board Resolution

Dated of DINSON INC Signature

in the presence of:

1.....

2.....

Signed, sealed and delivered by

Mr.....

Pursuant to the Board Resolution

Dated of HIMALAYA AGRO PVT LTD.

Signature in the presence of:

1.....

2.....

Answer 4(b)

Name and address of the firm of brokers
who agree to act as underwriters
(Letter form)

Ref. No.....

Date.....

The Board of Directors
(Name and address of the Company
for whose public issue the firm
agrees to act as underwriter)

Dear Sir(s),

Re: Proposed Public Issue of Equity Shares

We, hereby record the terms on which we (hereinafter referred as “underwriters”) have agreed to underwrite..... Equity Shares of the aggregate nominal value of Rs..... out of the total issue of..... Equity Shares to be offered to the public at Rs...../- each for cash at par.

1. The prospectus as approved by the underwriters will be delivered to the Registrar of Companies..... on or before..... for registration in accordance with the provisions of Rule 13 of the Company (Prospectors and Allotment of Secretaries) Rules, 2014. Sufficient number of copies of the prospectus and application forms shall be printed and made available to the underwriters, brokers and members of the public who intend to apply for the Equity Shares as soon as possible thereafter.
2. Underwriters shall be entitled to arrange sub-underwriting with respect to their respective commitments for their own account on terms to be arranged at their discretion with their sub-underwriters.
3. If by the closing date of the subscription list or such earlier date as may be agreed to by the underwriters, the Equity Shares offered to the public are not subscribed in full by the public and the application money payable in respect thereto is not received by you, you will within 14 days or such extended time as may be agreed to by the underwriters, notify the underwriters in writing as to the amount/number of Equity Shares which have not been so subscribed. The underwriters shall within 21 days after the receipt of such intimation apply for and subscribe such unsubscribed amount/number of Equity Shares and pay or procure to be paid the money payable on application in respect of such Equity Shares in proportion that the amount underwritten by each of them bears to the total amount of the issue.
4. In determining the amount/number of Equity Shares to be taken up by the underwriters the following factors shall be taken into consideration:
 - (a) In no circumstances will the underwriters be liable to take up Equity Shares more than the amount underwritten by them.

- (b) All applications made before the closing of the subscription list by the underwriters, or on forms of application bearing the stamp of the underwriters, and not withdrawn in the meantime shall be taken into account in pro tanto reduction of the liability of the underwriters under this underwriting agreement.
 - (c) After scrutiny of the applications received, the total shortfall shall first be allocated among all persons who have underwritten the issue and who have not fulfilled their quota, in proportion to the amount underwritten by each of them.
 - (d) Credit shall be given to each underwriter who has not fulfilled his quota in relation to applications made by members of the public independently proportionately to the amount underwritten by each underwriter, any amount or such credit being in excess of the commitment of any underwriter being similarly shared proportionately by the others.
5. Subject to the terms of the prospectus, you will allot Equity Shares for which applications have been received as soon as possible and despatch Equity Share Certificates within six months of such allotment.
 6. In consideration of the underwriting you will, within 14 days from the date on which we shall have fulfilled our obligation, pay the underwriters a commission at the rate of two and a half per cent on the issue of the amount/ number of Equity Shares underwritten by the underwriters.
 7. Notwithstanding anything stated above the underwriters shall have the option to be exercised by them at any time prior to the date fixed finally for publication of the “Announcement” of terminating underwriting arrangement in the event of a complete breakdown or dislocation of business in the financial markets of the cities of Calcutta, Bombay, Madras and Delhi due to war, insurrection, civil commotion or any other serious or sustained or political or industrial disturbances or if the whole present basis of Stock Exchange prices in any such city should undergo substantial change through the occurrences of such catastrophe or similar event at present not foreseen. In the event of underwriters exercising such option they shall be released from all obligations arising out of the underwriting agreement.
 8. Our offer is valid subject to your subscription list opening on or before.....
Please acknowledge receipt of this letter and intimate to us your acceptance of the terms and conditions mentioned above.

Thanking you,

Yours faithfully,

For.....

Question 5

- (a) *Explain briefly the various types of writs provided under the Constitution of India for the enforcement of fundamental rights.*

- (b) *Business and knowledge process outsourcing has emerged as a key growth driver in the Indian services sector. Discuss the factors to be considered in drafting of an outsourcing agreement.* (8 marks each)

Answer 5(a)

The Constitution of India has provided following types of writs for the enforcement of fundamental rights:-

Habeas Corpus : The writ of habeas corpus is a remedy available to a person who is confined without legal justification. The words “Habeas Corpus” literally mean “to have a body”. This is an order to let the Court know on what ground he has been confined and to set him free if there is no legal justification for his detention. This writ has to be obeyed by the detaining authority by production of the person before the Court. Under Articles 32 and 226 of the Constitution, any person may move the Supreme Court and the High Court of competent jurisdiction respectively, for the issue of this writ.

Mandamus : The expression “Mandamus” means a command. The writ of mandamus is, thus, a command issued to direct any person, corporation, inferior Court or Government authority requiring him to do a particular thing therein specified which pertains to his or their office and is further in the nature of a public duty. This writ is used when the inferior tribunal has declined to exercise jurisdiction. Mandamus can be issued against any public authority. The applicant must have a legal right to the performance of a legal duty by the person against whom the writ is prayed. Mandamus is not issued if the public authority has discretion.

Prohibition : The writ of prohibition is issued by the Supreme Court or any High Court to an inferior Court preventing the latter from usurping jurisdiction which is not legally vested in it. It compels courts to act within their jurisdiction when a tribunal acts without or in excess of jurisdiction or in violation of rules or law. The writ of prohibition is available only against judicial or quasi-judicial authorities and is not available against a public officer who is not vested with judicial functions. If abuse of power is apparent this writ may be prayed for as a matter of right and not a matter of discretion. The Supreme Court may issue this writ only in case of Fundamental Rights being affected by reason of the jurisdictional defect in the proceedings. This writ is available during the pendency of the proceedings and before the order is made.

Certiorari : The writ of certiorari is available to any person whenever any body of persons having legal authority to determine questions affecting the rights of subjects and having the duty to act judicially, acts in excess of its legal authority. The writ removes the proceedings from such body to the High Court in order to quash a decision that goes beyond the jurisdiction of the deciding authority.

Quo warranto : The writ of quo warranto is prayed for an inquiry into the legality of the claim which a person asserts to an office or franchise and to oust him from such position if he is an usurper. The holder of the office has to show to the Court under what authority he holds the office. This writ is issued when:

- (i) the office is of a public and of a substantive nature;
- (ii) the office is created by a Statute or by the Constitution itself; and

- (iii) the respondent must have asserted his claim to the office. It can issue even though he has not assumed charge of the office.

The fundamental basis of the proceedings of quo warranto is that the public has an interest to see that no unauthorised person usurps a public office.

Answer 5(b)

Outsourcing may be understood as the contracting out of a company's non-core or non revenue producing activities to specialist. It is strategic management tool. The conditions or factors to be considered in drafting an outsourcing agreement are as follows:

- Duties and obligations of outsourcer
- Security and confidentiality
- Legal Compliance
- Fees and payment terms
- Proprietary rights
- Auditing rights
- Applicable laws, jurisdiction and arbitration
- Term of the agreement
- Interim measures/provisional remedies
- Privacy and non-compete agreement
- Survival terms
- Default terms

Question 6

- (a) *Excellent Corporation Ltd. incorporated under the Companies Act, 2013 purchased an independent house comprising two floors in Gurgaon in the state of Haryana for a sum of ₹3.5 crore for providing company accommodation to Dinesh, Company Secretary on the first floor and it was decided that the company shall have its guest house at ground floor.*

For facilitating its registration, Mrs. Kiran, the Chairman-cum-Managing Director executed the following special power of attorney :

"By this power of attorney, I, Kiran, Chairman, Excellent Corporation Ltd., do hereby appoint and authorise Dinesh to be my agent and authority for the purposes of executing registration of the property purchased by the company from Antarctic Builders Ltd. on this 15th day of September, 2015.

For and on behalf of Excellent Corporation Ltd.

Sd/- Kiran

Chairman

On presentation of this document, the Registrar refused to complete the registration procedure stating that the power of attorney is void.

In light of the above answer the following :

- (i) *Is the action of the Registrar legally tenable ? State reasons. (2 marks)*

- (ii) *Draft a power of attorney as you would have been the Company Secretary.*
(4 marks)
- (iii) *Property registration charges are 8% for a man and 6% for a woman. Will you advise that the power of attorney be executed in favour of Mrs. Kiran to derive this benefit ?*
(2 marks)
- (b) *Draft a complaint under section 498 of the Indian Penal Code, 1860 for enticing away a married woman.*
(4 marks)
- (c) *Robin has availed a loan of ₹ 50,000 from Mohan against assignment of life insurance policy. Draft a deed of assignment of life insurance policy.* (4 marks)

Answer 6(a)

- (i) The due execution of documents is important to create legal binding documents. This is particularly so for the execution of a deed, which has strict requirements to ensure that it is valid and enforceable. Further when a document is to be registered with the Registrar, the execution must strictly comply with certain requirements otherwise the document will not be accepted.

In the present case a specific power of attorney is to be executed to attain the purpose of a specific Act.

Further as per the provision of Section 22(2) of the Companies Act, 2013 a company may, by writing under its common seal, authorise any person, either generally or in respect of any specified matters, as its attorney to execute other deeds on its behalf in any place either in or outside India.

It may be noted that that in case a company does not have a common seal, the authorisation under this sub-section shall be made by two directors or by a director and the Company Secretary, wherever the company has appointed a Company Secretary.

A deed signed by such an attorney on behalf of the company and under his seal shall bind the company.

Thus the refusal by Registrar is legally tenable as the specific power of attorney is not in the prescribed manner.

- (ii) Specific Power of attorney to be presented to execute registration of property

BY THIS POWER OF ATTORNEY I KIRAN CHAIRMAN of Excellent Corporation Limited do hereby appoint Mr. Dinesh company secretary of the Company, my attorney for me and on my behalf to appear for and represent me before the Registrar of Gurgaon, Haryana of all times as may be necessary and to present before him for Registration the Title Deed datedday ofand to do any Act, deed or thing as may be necessary to complete the registration of the said deed in the manner provided by law and when it has been returned to him after being duly registered, to give proper receipt and discharge for the same.

And I Kiran the Chairman of Excellent Corporation Limited, do hereby agree and declare that all acts, deeds and things done, executed or performed by the said

Mr. Dinesh shall be valid and binding on me to all intents and purposes as if done by me personally which I undertake to ratify and confirm whenever required.

Signed, sealed and delivered Kiran, Chairman of Excellent Corporation Limited

Witness

Dated 15th September, 2015

- (iii) Chairman being a female will not make any difference as the property is to be registered in the name of the Company. If the property would have to be registered in the personal capacity of Mrs. Kiran the benefit could have been in the terms of savings in Stamp Duty.

As far as issue of power of Attorney is concerned there is no distinction between man and woman.

Answer 6(b)

A Complaint u/s 498 Indian Penal Code

In the Court of the Judicial Magistrate of the 1st Class, Hyderabad

Case No.....of 20.....

AB.....Complainant

Vs.

CD.....Accused

Offence u/s 498, IPC

1. The complainant is the mother of A residing along with her grandmother Z, son A, A's wife B, and A's two year old son 'X'.
2. About six months back complainant's son left for Bahrain, a foreign country on business purposes.
3. The accused who was a friend of the complainant's son developed intimacy with B, in the absence of B's husband.
4. On theday of both the accused and B were found missing.
5. Friends and others on inquiry told the complainant that they saw both the accused and B at the Hyderabad Airport waiting to board a foreign bound flight.
6. The complainant, being the lawful guardian of B in the absence of B's husband prays that a search warrant under Section 100 of the Criminal Procedure Code be issued for the production of B, the daughter-in law of the complainant before this court.
7. The complainant also prays that a non-bailable warrant against the accused be issued as he is preparing to leave the country.

8. The police were informed about this offence that has referred the complaint to this Court.

Witnesses:

Sd/-

1.

Complainant

2.

Place :

Date :

Answer 6(c)

The specimen deed of assignment of life insurance policy

THIS ASSIGNMENT made this.....day ofbetween Robin , son of David, resident of..... (hereinafter known as the assignor) of the one part and Mohan son of Ghanshyam resident of..... (hereinafter known as the assignee) of the other part.

WHEREAS a policy of assurance being No..... for Rs. 50,000 (Rupees fifty thousand only) was issued by the Life Insurance Corporation of India on the life of the assignor on the..... day of..... to be paid to the assignor or to his executors, administrators or assigns after his death, subject to the annual premium of Rs.....;

AND WHEREAS the said assignor has agreed to transfer and assign to the said assignee the said policy of assurance of a sum of Rs..... (Rupees.....);

THIS DEED WITNESSES that in consideration of the sum of Rs 50,000 (Rupees fifty thousand only) the receipt whereof the said assignor hereby acknowledges, the said assignor as beneficial owner, hereby transfers and assigns unto and to the use and for the benefit of assignee the hereinbefore recited policy of assurance, and the sum of Rs..... (Rupees.....) hereby assured and all the other moneys, benefits and advantages to be had, recovered or obtained under or by virtue of the said policy:

TO HOLD the same unto and to the use of the said assignee absolutely, subject to the conditions as to payment of future premiums and otherwise to be henceforth observed in receipt of the said policy

AND the said assignor hereby covenants with the said assignee that he, the said assignor, shall not do, or knowingly suffer anything to be done, whereby the said policy may be rendered void or voidable or the said assignee or his heirs, executors, administrators or assigns may be prevented from receiving the said sum of Rs..... (Rupees.....) or any benefit thereunder.

IN WITNESS WHEREOF the assignor and the assignee do hereto affix their respective signatures on the day, month and the year stated above.

Witness:

Assignor

Witness:

Assignee

BANKING LAW AND PRACTICE (Elective Paper 9.1)

Time allowed : 3 hours

Maximum marks : 100

NOTE: Answer **ALL** Questions.

Question 1

Read the following case :

The liberalisation process initiated by the Government of India during the early 1990s witnessed the entry of several private players in the Indian banking sector. ABC Bank (ABCB) was one of the earliest private sector banks incorporated on 30th October, 2004, in Hyderabad promoted by Joy, Jatin and Chandan. Joy, a development banker, was employed with the Asian Development Bank, Manila; Jatin was Chairman of Vysya Bank for 10 years and Chandan was a former bank executive. Apart from these three promoters, the Global Finance Corporation (GFC) and the Global Bank for Development (GBD) were other major shareholders. ABCB offered an array of products and services in retail, wholesale, corporate, treasury and investment banking for non-resident Indians, apart from depository and advisory services. The bank specialised in lending to software, energy, telecom, textiles, pharmaceuticals and jewellery sectors.

Within three years of operations, the total business exceeded ₹43.02 billion, making it one of the fastest growing private sector banks in India. It was also the first among Indian banks to raise Tier-II capital from multilateral institutions. In five years, ABCB's deposits were worth ₹40 billion, out of which 70% were from retail investors. Its presence in the states of Maharashtra, Andhra Pradesh, Karnataka and Tamil Nadu was significant, with more than 70% of branches in seven major cities and four metros. By July, 2014, the bank had grown to 104 branches in 34 cities, 275 ATMs and 1,400 employees. It had more than a million depositors with deposits worth ₹65 billion. The loans disbursed were to the tune of ₹35 billion.

Despite all the sound state of affairs, ABCB collapsed in the year 2014-15 and the collapse resulted on account of many mistakes committed by the bank's management including lack of financial supervision, weak corporate governance coupled with indulgence of promoters and management in financing collusion with the borrowers. RBI's probe into ABCB's accounts revealed a significant erosion of the bank's net worth and huge number of NPAs. Moreover, ABCB's attempts to strengthen its capital base through investments from overseas failed due to regulatory problems, resulting in total collapse of the bank.

The major factors that led to the fall of ABCB included disbursement of loans of ₹1.4 billion to Carl, a leading stockbroker at the Bombay Stock Exchange (BSE). Carl used the money to purchase ABCB's shares from the BSE and the National Stock Exchange (NSE). ABCB's share trading volumes, usually in thousands, shot up during June and July, 2010 to millions. Its share price shot up from ₹65 to ₹114

between October, 2010 and January, 2011. The Securities and Exchange Board of India (SEBI) later confirmed that ABCB's stock price increased because of price manipulation. After the price increase, Carl sold the shares and reaped huge profits. Later, in 2011, investigation reports on the securities scam revealed that Carl had received insider information. In December, 2012, SEBI imposed a ban on the promoters of ABCB, Carl and his associates from dealing in ABCB shares until completion of investigation into the bank's capital market activities.

RBI charged ABCB with several financial irregularities and lack of transparency in its banking operations. It had not followed SEBI guidelines which capped a bank's direct exposure to capital markets at five per cent of total advances of the bank. Since 2009, ABCB had given loans worth ₹17 billion to many stock brokers against shares as security. When the stock market witnessed a major fall in the aftermath of the securities scam in 2011, loans given by ABCB against the security of shares turned into bad debts, taking a toll on the bank's financial position.

In late 2010 and early 2011, ABCB gave loans of over ₹8 billion to corporate and stock market related entities. For the fiscal 2010-11, ABCB had a total of 55 major corporate NPA accounts; highest NPA accounts in trading (15); broking accounts (11); followed by accounts in food processing, textiles and petrochemicals. Other NPA accounts were from distillery, agriculture, gems and jewellery and media companies. In the last quarter of fiscal 2010-11, ABCB reported a fall of 164% in profit after tax (PAT) because of ₹900 million provisioning for NPAs.

ABCB's exposure to the capital market in the fiscal ending 2010-11 was around 24% of total advances; which came down to 14% by March, 2012 and around 5% for the fiscal ending March, 2013. Though the exposure to capital markets had been brought down gradually by ABCB, the damage had already been done as most advances turned into NPAs due to the downtrend of the stock market after the securities scam. ABCB had to write-off ₹2.52 billion towards NPAs for the financial year 2011-12, after securing RBI approval to utilise reserves of ₹2.0195 billion. Still, there was under-provisioning in the books. Much of ABCB's NPAs were due to the loans given to Carl of ₹2.8 billion, a telecom company linked to Carl of ₹2.5 billion and a media company of ₹2.5 billion. As on 31st March, 2013, ABCB reported gross NPAs of ₹9.158 billion while total provisioning for the period was at ₹2.68 billion and the bank's net NPAs for the period stood at 19.7% of its advances.

RBI's annual financial inspection (AFI) showed that the networth had been further eroded and capital adequacy ratio (CAR) had also turned negative. For the financial year 2012-13, ABCB recorded loss of ₹2.720 billion with gross NPAs at ₹9.17 billion, accounting for 28% of the bank's total advances. High NPAs were a primary reason for ABCB's poor performance as it had lent indiscriminately to stockbrokers, diamond traders and exporters, without following RBI norms.

In the wake of these financial irregularities, RBI placed ABCB under monthly monitoring and its operations relating to advances, premature withdrawal of deposits, declaration of dividend and capital market exposure were restricted. The statutory auditors of the bank were also asked to be changed. The central bank further advised ABCB to infuse fresh capital to prevent the networth from remaining negative and restore its CAR to a minimum of nine per cent. The bank was advised to explore all possible options for infusion of capital through domestic sources or through merger with another bank.

All these factors resulted in the imposition of moratorium by RBI and on 24th July, 2014, the Government of India imposed a moratorium on the bank on the grounds of 'wrong financial disclosures'. The moratorium was for three months from close of business on 24th July, 2014 till 23rd October, 2014. RBI said that the moratorium was imposed in public interest and to protect the interests of depositors. All operations of ABCB were frozen and it was ordered not to give loans without RBI permission. It was allowed only to make payments for day-to-day operations or for meeting obligations entered into before the order.

On 26th July, 2014, RBI announced that ABCB would be merged with the Northern Bank of Commerce (NBC). As per the scheme, NBC took over all the assets and liabilities of ABCB on its books. It acquired all 104 branches of ABCB, 275 ATMs, a workforce of 1,400 employees and one million customers at an estimated merger cost of ₹8 billion. NBC's total business volume was expected to reach ₹65 billion and the total branch network to cross 1,100. All corporate accounts including salary accounts were transferred to NBC. The entire amount of paid-up equity capital of ABCB was adjusted towards its liabilities. There was no share swap between ABCB and NBC, which meant that ABCB's shareholders were the ultimate losers, as they did not get any shares of NBC.

Though the interests of ABCB's depositors were protected, its shareholders lost their total investments in the bank overnight.

ABCB's collapse raised doubts on the credibility of private sector banks in India. Before ABCB, two other private sector banks, namely, Bank of XYZ and the EFG Bank had collapsed in 2010 and 2012 respectively. Analysts said that ABCB's customers should have been more aware about protecting their interests as the bank catered primarily to educated, city-based customers who were expected to be more knowledgeable and prudent. When ABCB's weak financial position was made public, they should have understood that their deposits in the bank were unsafe. However, they seemed to have been carried away by the bank's higher rate of interest. The entire issue served as a lesson for small investors to exercise more diligence while choosing a private sector bank.

In the backdrop of this case, answer the following questions :

- (a) Describe the basis on which RBI would have granted licence to ABCB to set-up the bank. How far ABCB has not been able to comply with these requirements?
(10 marks)*
- (b) Analyse the reasons that led to the fall of ABCB, duly supported by facts and specific data.
(10 marks)*
- (c) State the norms for exposure to capital market as enumerated by RBI. How far has ABCB followed such norms ?
(10 marks)*
- (d) Examine the role of RBI and SEBI as regulating authorities in the collapse of ABCB. Also give your suggestions to ensure non-recurrence of such debacle.
(20 marks)*

Answer 1(a)

ABC Bank was incorporated in Hyderabad on 30th October, 2004, of which main promoters worked for several years in the banking industry on very high responsible

positions, with the sound financial stake made by GFC and GBD. The bank after its incorporation carried out a wide range of activities. Apart from depository and advisory services, it was involved in provision of services in retail, wholesale, corporate etc., and treasury and investment banking for non-resident Indians.

A banking company has to comply with various parameters as specified u/s 22 of the RBI Act in order to get the license to set-up and operate a bank in the country. RBI examines the following aspects prior to grant of a license:-

1. Whether the company is or will be able to pay its present and future depositors in full as and when their claims accrue?
2. Whether the affairs of the company are being conducted or likely to be conducted in a manner detrimental to the interests of its present and future depositors?
3. Whether the company has an adequate capital structure and earning prospects?
4. Whether public interest will be served by grant of license to the company?
5. Other issues relating to branch expansion, unbanked area and other aspect.

The promoters of ABC bank fulfilled all these criteria by having adequate capital base participated by the promoters and by GFC and GBD which ensured the protection of interest of the depositors. The bank also raised Tier-II capital from multilateral institutions. ABC Bank complied with the license requirements, RBI has not committed any mistake while granting the license to ABC Bank to operate.

Answer 1(b)

ABC Bank after its incorporation in 2004 was working smoothly and in the correct directions and well planned manner till the advances given by it in collusion with the Promoters or other top Management Persons caused huge NPA and ate away the investment made by the stake holders. The main reason of its collapse was lack of corporate governance and transparency in its affairs. There was lack of corporate governance and involvement of promoters in giving finance to Carl. He was a stock broker who used the money for trading in the shares of the bank by having insider information and making good profits by dealing in bank's shares. The reason for his making huge profit was the insider information available to him. As a result, SEBI imposed a ban on Carl as well as on the promoters of the ABC Bank and their associates to not to deal in shares of the bank till the completion of the investigation of the capital market activities of the bank. Further the bank was charged with several financial irregularities and lack of transparency in its banking operations by the RBI. The ABC bank did not follow SEBI guidelines limiting a bank's direct exposure to capital markets to five per cent. The bank had provided huge advances to many stock brokers against the security of shares and most of these turned out to be NPAs after the market followed a downtrend. Out of total NPAs, much of were owing to the loans given to Carl, these were to the extent of Rs 2.8 bn given to Carl, Rs 2.5 bn each given to a telecom company and a media company having link with Carl. The high level of NPA of the bank (19.7% of the total advances) resulted into the collapse of bank in which share holders lost their entire investment. Due to regulatory problems, ABC Bank also failed in strengthening its capital base through overseas investments.

Answer 1(c)

Limits on Banks' Exposure to Capital Markets as enumerated by RBI:

1. *Statutory limit on shareholding in companies* : No banking company shall hold shares in any company, whether as pledgee, mortgagee or absolute owner, of an amount exceeding 30% of the paid-up share capital of that company or 30% of its own paid-up share capital and reserves, whichever is less, except as provided in sub-section (1) of Section 19 of the Banking Regulation Act, 1949. Shares held in demat form should also be included for the purpose of determining the exposure limit.
2. *Regulatory Limit*
 - (i) A Solo Basis: The aggregate exposure of a bank to the capital markets in all forms (both fund based and non-fund based) should not exceed 40% of its net worth as on March 31 of the previous year.
 - (ii) Consolidated Basis: The aggregate exposure of a consolidated bank to capital markets (both fund based and non-fund based) should not exceed 40% of its consolidated net worth as on March 31 of the previous year.

If the bank does not observe above guidelines and keep giving finances to the particular sectors, indiscriminate of the guidelines such as financing to the capital market, gems and jewellery, petro chemicals and telecom/media companies beyond the limits prescribed may result into over exposure to these sectors. ABC Bank had also made exposure to stock broker Carl, a leading stock broker of the Bombay Stock Exchange, to the extent of Rs 1.4 bn. The advance taken by Carl was used in share trading of the bank's shares and turnover of which was inflated from thousands to millions in a short span and the share prices of the bank almost doubled in a period of 2 months. The entire shares held by Carl and the promoters were off-loaded causing a steep fall in the value of bank's shares causing damage and loss to the shareholders/investors. The fall in the share prices of the bank resulted into loss of advance of Rs 1.4 bn given to Carl as well as of the advances given to his associates and linked persons. The bank besides the advance to Carl had also made exposure to other stock brokers against the shares as security to the extent of Rs 17 bn. Most of these advances turned out to be bad advances because of security scam in 2011 adversely impacting the financial position of the bank. Had the bank not made such heavy and over exposure to the stock brokers in the capital market then it would have not collapsed because such advances turned out as bad advances. Therefore, it can be concluded that the over exposure to the capital market resulted into huge loss to ABC Bank.

Answer 1(d)

Reserve Bank of India formulates, monitors and implements India's monetary policy. Main functions of the RBI in this regard in accordance with the provisions of the RBI Act, 1934 are:

- (i) operating monetary policy with the aim of maintaining economic and financial stability and ensuring adequate financial resources for development purposes;
- (ii) meeting the currency requirement of the public;

- (iii) promotion of an efficient financial system;
- (iv) foreign exchange reserve management;
- (v) conduct of banking and financial operations of the government.

Since the onset of the process of economic reforms, including the on-going liberalization and globalization of the economy, the role of the RBI as the Regulator of the financial sector has grown and diversified. The entire institutional function of providing finance comes under the regulatory oversight of the RBI. In case of ABC Bank, RBI was derelict in its handling given that the RBI had detected that ABC Bank had a negative net worth as long back as March 2012. Instead of taking any serious action, it had simply removed the bank's auditors. The imposition of moratorium on ABC Bank seems to be a belated action on the part of the regulator. The bank's customers, particularly depositors, would have expected Reserve Bank of India to have warned them beforehand that they were banking with a shaky bank. The shareholders, particularly those holding nominal shares, would feel that they had been let down.

The Functions of SEBI are:

- to protect the interests of investors in securities and to promote the development of, and to regulate the securities market;
- regulating the business in stock exchanges and any other securities markets;
- registering and regulating the working of stock brokers, sub-brokers, share transfer agents, bankers to an issue, trustees of trust deeds, registrars to an issue, merchant bankers, underwriters, portfolio managers, investment advisers;
- prohibiting fraudulent and unfair trade practices relating to securities markets;
- prohibiting insider trading in securities;
- regulating substantial acquisition of shares and takeover of companies;

The primary objective of SEBI is to promote healthy and orderly growth of the securities market and secure investor protection. Investors are the backbone of the securities market. As a part of investor's protection, SEBI is to take necessary steps to prohibit insider trading by checking and curbing unhealthy and manipulative practices by persons who have more access than others to the information about the company. In case of ABC Bank SEBI could have taken action against it for price manipulation since Carl received insider information.

However if the situation is analysed objectively, it has to be understood that based on the recent developments in the banking system, particularly the events affecting the functioning of private sector banks, the RBI has placed in the public domain the draft policy framework for ownership and governance in private sector banks in order to strengthen the functioning of private sector banks. The public in general and those closely associated with the financial system and well-wishers of the banking system may want implementation of the guidelines quickly. It may be necessary to tighten the policy guidelines on ownership and governance in private sector banks in course of time to avert recurrence of such incidents as has happened in case of ABC Bank because of lack of governance and delayed actions of RBI. RBI and SEBI should keep vigil mechanism and try to ensure that small investors act carefully while banking with a private sector bank.

Question 2

- (a) *NPA management is the most important responsibility of bankers. Explain how a banker can reduce the probability of an advance turning into NPA.*
(15 marks)
- (b) *Explain how information technology has changed the face of banking in India.*
(15 marks)

Answer 2(a)

The Banker and his ability to assess the customer and the loan requirement go a long way in securing an advance and preventing the same from becoming an NPA. The banker who lends funds should:

1. Do a proper assessment of the customer. The Banker should have the ability to assess whether the customer can be trusted and will repay the amounts borrowed.
2. He should monitor the advance and the business of customer. The major source of information for monitoring would be the operation of the current or cash credit accounts, the stock and book debts statements submitted by the client and the nature of bills submitted for collection or discount and the inspection of stocks and book debts carried out at regular intervals
3. The banker should have the ability to maintain friendly relationship with the customer. The customer should treat the banker as a friend to whom he can confide the ups and downs of business.
4. To check whether the advance requested by the customer is commensurate with his needs.
5. Regular interaction/discussion with the customer is a win-win situation for both. The banker gets an opportunity to learn about the business of the client and the customer gets benefit of the knowledge of the banker.

The above are general principles for assessment. This has to be followed by a full-fledged assessment of the risks of the customer's business and how the said advance can be secured with an adequate mix of marketable and less liquid securities and how the bank can be safeguarded against unforeseen circumstances. For this he has to ensure the following:

1. Marketability of securities
2. Taking adequate margins
3. Documentation
4. The law of limitation
5. The realization of the Advance

Answer 2(b)

The banking system in India has matured in the last decade. Earlier the banking was manual and had the following difficulties/lacunas:

- (i) The banking records were maintained manually.
- (ii) The records of transactions in an account were hand written in ledgers and thus prone to errors.

- (iii) The manual activity demanded building of procedures and rules to detect errors. Thus the bankers were required to maintain and update the general ledgers on daily basis and tally the same i.e. ensure that debits equal credits.
- (iv) The major time of the staff was spent in in-house book keeping. This included general ledger and individual ledger balancing.
- (v) The customer was required to visit the branch for every transaction and had to wait in queues to be serviced.
- (vi) The customer could be serviced at the branch where he maintained the account and could not avail of any facility at other branches.
- (vii) The transactions were done through issuance of cheques and the system used to take 2 to 21 days to clear the cheques as the cheques were required to be sent to the branch of the payee where the account was maintained.

With the advent of IT in the banking system, all the problems mentioned above have vanished. As a result the following benefits have accrued to staff and customers:

- (i) The books are balanced automatically and thus there is very little in-house book keeping to be done. The staff can concentrate on customer service and marketing of banking as well as investment products.
- (ii) The customer is no longer required to visit his home branch only as he can avail of all the services from any branch.
- (iii) The customer can do all his banking from home and office and even on the move through mobile banking.
- (iv) Payments have been automated and now customers can make all payments electronically. The banks now offer the following facilities for payment: Electronic Funds Transfer, Electronic Clearing System (ECS), Real Time Gross Settlement (RTGS), Banks can settle interbank and forex transactions on real time basis, National Electronic Funds Transfer (NEFT).
- (v) Automatic Teller Machines (ATM): In order to automate all small cash transactions banks have setup ATMs in convenient locations for withdrawal and deposit of cash and for performing selected transactions.
- (vi) Internet banking and mobile banking: The customer can do almost all transactions using internet and mobile.
- (vii) Bill pay facility: Under this facility the customer can register the details of all service providers including credit card companies, insurance companies and mutual funds to whom the payments have to be made periodically. The bank would collect the details from the said service providers and remit the amounts to them.
- (viii) Conveyance banking: Under this all accounts of a customer are grouped under one customer id and he can access them through a common login.

Question 3

Banks are required to freeze the accounts of customers on the orders of the government/ enforcement authorities. During the currency of such orders, a term deposit gets matured. What procedure should be followed by the bank in such cases? Explain. (5 marks)

Answer 3

The issue of such frozen accounts was examined in consultation with Indian Banks' Association and banks are advised to follow the procedure detailed below in the case of Term Deposit Accounts frozen by the enforcement authorities:-

- (i) A request letter may be obtained from the customer on maturity. While obtaining the request letter from the depositor for renewal, banks should also advise him to indicate the term for which the deposit is to be renewed. In case the depositor does not exercise his option of choosing the term for renewal, banks may renew the same for a term equal to the original term;
- (ii) No new receipt is required to be issued. However, suitable note may be made regarding renewal in the deposit ledger;
- (iii) Renewal of deposit may be advised by registered letter/speed post/courier service to the concerned Government Department under advice to the depositor. In the advice to the depositor, the rate of interest at which the deposit is renewed should also be mentioned;
- (iv) Where the overdue period does not exceed 14 days on the date of receipt of the request letter, renewal may be done from the date of maturity. If it exceeds 14 days, banks may pay interest for the overdue period as per the policy adopted by them, and keep it in a separate interest free sub-account which should be released when the original fixed deposit is released.

Question 4

What do you understand by Cheque Truncation System (CTS) ? (5 marks)

Answer 4

Cheques are used as a medium for exchange of funds, and play a key role in the funds management of customers and banks. The efficient cheque clearing system helps in settlement of receipts and payments. Cheque Truncation is a new system introduced in Indian Banking Scenario. It is a system of cheque clearance and settlement between banks based on electronic data and/or images without the need for exchange of physical cheques and negotiable instruments like demand drafts, pay orders, dividend warrants, etc. Special features of Cheque Truncation are:-

- Cheque realization is faster
- Quick realization helps the customer in better cash management
- In the long run, it reduces the administrative costs of bank
- Assists banks in reconciliation and reducing clearing frauds.

Question 5

State the role of RBI as a banker to the government. (5 marks)

Answer 5

In terms of Section 20 and 21 of RBI Act, the RBI has the obligation to transact the

banking business of the Central Government. Accordingly, it is required to accept money for account of the Government, to make payments on its behalf up to the amount outstanding in the credit of the Government, and also to carry out the Government's exchange, remittance and other banking operations including the management of the public debt. It acts as an advisor to the Government. RBI performs similar functions on behalf of State Governments by virtue of agreements entered into with them under Section 21 A. RBI has entrusted the work of payment and receipts on behalf of Government to its agents like State Bank of India and its Associate Banks. Some other commercial banks are also doing some Government transactions as an agent of RBI.

Question 6

Explain the following terms with reference to electronic banking and IT activities in the banks :

- (i) SWIFT
- (ii) CHIPS
- (iii) NEFT
- (iv) RTGS
- (v) DWH/EDW

(1 mark each)

Answer 6(i)

The Society for Worldwide Inter-bank Financial Telecommunications (SWIFT) provides the international lines used for such interbank advice.

Answer 6(ii)

Clearing House Inter Bank Payment System (CHIPS) is a clearing system run by New York clearing house. The financial transactions such as – foreign and domestic trade services, international loans, syndicated loans, foreign exchange trade settlements, are carried out through CHIPS.

Answer 6(iii)

National Electronic Funds Transfer (NEFT) is a funds transfer system which enables a customer of a bank to transfer funds to another customer of another bank having account with any participating bank.

Answer 6(iv)

Real Time Gross Settlement (RTGS) is an electronic payment system, where payment instructions are processed on a 'continuous' or 'REAL TIME' basis and settled on a 'GROSS' or 'individual' basis without netting the debits against credits.

Answer 6(v)

A Data Warehouse or Enterprise Data Warehouse (DWH/EDW) is a database used for reporting and data analysis. It is a central repository of data which is created by integrating data from one or more separate sources.

CAPITAL, COMMODITY AND MONEY MARKET
(Elective Paper 9.2)

Time allowed : 3 hours

Maximum marks : 100

NOTE: Answer **ALL** Questions.

Question 1

A Ltd. and B Ltd. operate in the same industry. Following are their financial statements for the financial year ended 31st March, 2015 :

Balance sheets

<i>Particulars</i>	<i>A Ltd. (₹)</i>	<i>B Ltd. (₹)</i>
<i>Total current assets</i>	14,00,000	10,00,000
<i>Total fixed assets (net)</i>	10,00,000	5,00,000
TOTAL ASSETS	24,00,000	15,00,000
<i>Equity capital (₹10 each)</i>	10,00,000	8,00,000
<i>Retained earnings</i>	2,00,000	—
<i>14% Long-term debts</i>	5,00,000	3,00,000
<i>Total current liabilities</i>	7,00,000	4,00,000
TOTAL LIABILITIES	24,00,000	15,00,000

Income statements

<i>Particulars</i>	<i>A Ltd. (₹)</i>	<i>B Ltd. (₹)</i>
<i>Net sales</i>	34,50,000	17,00,000
<i>Less : Cost of goods sold</i>	27,60,000	13,60,000
<i>Gross profit</i>	6,90,000	3,40,000
<i>Less : Operating expenses</i>	2,96,923	1,45,692
<i>Interest</i>	70,000	42,000
<i>Earnings before tax (EBT)</i>	3,23,077	1,52,308
<i>Less : Tax (35%)</i>	1,13,077	53,308
<i>Earnings after tax (EAT)</i>	2,10,000	99,000

Additional information

<i>Particulars</i>	<i>A Ltd.</i>	<i>B Ltd.</i>
<i>Number of equity shares</i>	1,00,000	80,000
<i>Dividend payment (D/P) ratio</i>	0.40	0.60
<i>Market price per share (MPS)</i>	₹40	₹15

Assume that the two companies are in the process of negotiation for merger through exchange of equity shares. You have been asked by management of both the companies to assist in establishing equitable exchange terms. You are required to —

- Decompose the share prices of both the companies into earnings per share (EPS) and price earnings (P/E) components and also segregate their EPS figures into return on equity (ROE) and book value or intrinsic value per share components. (15 marks)
- Estimate the future EPS growth rate for each company. (5 marks)
- Based on expected operating synergies, A Ltd. estimates that the intrinsic value of B Ltd.'s equity share would be ₹20 per share on its acquisition. Develop a range of justifiable equity share exchange ratios that can be offered by A Ltd. to B Ltd.'s shareholders. Based on your analysis in part (a) and (b) above, would you expect the negotiated terms to be closer to the upper or the lower exchange ratio limits? Give reasons. (10 marks)
- Calculate the post-merger EPS based on exchange ratio of 0.4:1 being offered by A Ltd. Indicate the immediate EPS accretion or dilution, if any, that will occur for each group of shareholders. (10 marks)
- Based on a 0.4:1 exchange ratio and assuming that A Ltd.'s pre-merger P/E ratio will continue after the merger, estimate the post-merger market price. Show the resulting accretion or dilution in pre-merger market prices. (10 marks)

Answer 1

(a) Determination of EPS, P/E Ratio, Return of equity (ROE) and Book Value per share BVPS of A Ltd And B Ltd

Particulars		A Ltd.	B Ltd.
Earnings After Tax	(EAT)	2,10,000	99,000
No. of Shares	(N)	1,00,000	80,000
Earnings Per Share (EPS)	(EAT/N)	2.10	1.2375
Market Price per Share (MPS)		40	15
P/E ratio (MPS/EPS)		19.05	12.12
Equity Funds (EF)		12,00,000	8,00,000
BVPS (EF/N)		12	10
ROE(EAT/EF)		0.175 or 17.5%	0.1237 or 12.3%

(b) Growth Rates in EPS

		A Ltd.	B Ltd.
Dividend Payment (D/P) Ratio		0.4	0.6
Retention ratio (1-D/P ratio)		0.6	0.4
Growth rate (ROE x Retention ratio)		0.105 or 10.5 %	0.0495 or 4.95 %

(c) Justifiable equity share exchange ratio

- (i) Market price based= MPSB/MPSA = Rs 15/Rs 40 = 0.375:1 (lower limit)
(ii) Intrinsic value based = Rs 20/40 = 0.5:1 (upper limit)

Since A Ltd has a higher EPS, ROE, P/E ratio, and higher EPS growth expectations, the negotiated terms would be expected to be closer to the lower limit, based on the existing share prices.

(d) Post-Merger EPS

<i>Particulars</i>		<i>A Ltd.</i>	<i>B Ltd.</i>	<i>Combined</i>
EAT	(Rs.)	2,10,000	99,000	3,09,000
Shares outstanding		1,00,000	80,000	1,32,000*
EPS	(Rs.)	2.10	1.24	2.34
EPS accretion or (dilution)	(Rs.)	0.24	(0.30**)	-----

Working Notes:

- * Share Outstanding (Combined) = 1, 00,000 shares + (.40 x 80,000) = 1,32,000 shares
** EPS claim per old share = Rs 2.34 x 0.4 = Rs.0.936
EPS dilution = (Rs 1.24- Rs 0.936) = Rs 0.304

(e) Post-Merger Market Price

<i>Particulars</i>		<i>A Ltd.</i>	<i>B Ltd.</i>	<i>Combined</i>
EAT	(Rs.)	2.10	1.24	2.34
P/E ratio		(*) 19.05	(*) 12.12	(*)19.05
		40	15	44.60
MPS accretion		4.60	2.84***	

*** MPS claim per old share = 44.60*0.4 = Rs 17.84

Less: MPS per old share	15.00
	<u>2.84</u>

Question 2

- (a) The spot price of Rose Ltd. on 4th June is ₹1,701 per share, and June future on this is being traded at a price of ₹1,740 per share. The lot size is 400 shares. Rohan takes long on this future for 6 lots. Subsequently, on 12th June, the spot price moves to ₹1,750 per share and June future is being traded at a price of ₹1,798. He squares-up two lots at this price. On 23rd June, the spot price falls

to ₹1,690 per share and June future is being traded at ₹1,720 per share. He squares-up 3 lots. On the date of valuation, the closing spot price is ₹1,725 per share and his open position is settled through cash differences. Show the outcomes. (10 marks)

- (b) List out the name of some Indian and international credit rating agencies. Describe the main features of the SEBI Regulations relating to credit rating agencies in India. (10 marks)
- (c) Explain the factors affecting the flow of foreign institutional investment (FII) in India in present scenario. (10 marks)

Answer 2(a)

Here Mr. Rohan has created long on June futures on ABC Ltd. at a strike price of Rs 1,740 per share. His open interest on 4th June is equal to six lots, i.e. a total open interest quantity of 2,400 shares (6 x 400) long position. As it is a futures transaction, therefore, he has the right as well as obligation to settle the transaction. Subsequent outcome is as follows:

On 12th June 2011

He has squared up two lots, i.e. sold June futures on ABC Ltd at a strike price of Rs 1,798 resulting into a profit of Rs 58 (1,798- 1,740) per share a total profit of the Rs 46,400 (58 x 2x 400). Now his open interest after this squares up remains only four lots i.e. a quantity of 1,600 shares long on futures.

On 23th June 2011

He has squared up three lots, i.e. sold June futures on ABC Ltd. at a strike price of Rs 1,720 resulting into a loss of Rs. 20 (1,740- 1,720) per share a total loss of the 24,000(20x 3x 400). Now his open interest after this square up remains only one lot i.e. a quantity of 400 shares long on futures.

(In case of square-up the difference between the strike price of the position and the current strike price at which square up is taken, the spot price is of no use.)

On 28th June 2011 (value date)

The open long position equal to one lot, i.e. 400 shares is being settled through cash difference settlement. The difference will be taken between the settlement price of ABC Ltd. (closing spot price on the value date) and the strike price of open position. Here, the settlement price is Rs 1,725 per share and the strike price is Rs 1,740. The difference, Rs 15 (1,740-1,725) per share is the loss for him as he is the buyer of the futures and the spot price has fallen below the strike price. The total cash difference to be paid by him is Rs. 6,000 (15 x 400).

The net outcome is as follows:

<i>Date</i>	<i>Cash flow (Rs)</i>
4th June	Nil
12th June	(+) 46,400
23th June	(-) 24,000
28th June	(-) 6,000
Net Total	16,400

Answer 2(b)**Indian credit rating agencies**

- Credit Analysis & Research Ltd (CARE)
- Credit rating Information services of India Ltd. (CRISIL)
- Investment Information and Credit Rating Agency (ICRA)
- India Ratings and Research Pvt. Ltd.
- Brickwork Ratings India Pvt. Ltd.
- SME Rating Agency of India Limited (SMERA)
- Infomerics Valuation and Rating Pvt. Ltd.

International Credit rating agencies

- Moody's Investors Service
- Standard & Poor's (S&P)
- Shanghai Credit Information Services Co., Ltd.

Main features of SEBI (Credit Rating Agencies) Regulations, 1996

- Every credit rating agency is required to obtain a certificate of registration from SEBI and the period of validity of such certificate of registration is three years.
- A Credit Rating Agency (CRA) cannot rate securities issued by any borrower, subsidiary, an associate promoter of CRA, if there are common Chairman, Directors and Employees between the CRA or its rating committee and these entities.
- Every credit rating agency shall abide by the Code of Conduct contained in the Third Schedule of these regulations.
- Every credit rating agency is required to enter into a written agreement with each client whose securities it proposes to rate.
- Credit rating agency should make public the definitions of the concerned rating, along with the symbol and state that the ratings do not constitute recommendations to buy, hold or sell any securities.
- Every credit rating agency shall, during the lifetime of securities rated by it continuously monitor the rating of such securities.
- Every credit rating agency shall comply with such guidelines, directives, circulars and instructions as may be issued by SEBI from time to time, on the subject of credit rating.
- Every credit rating agency shall appoint a compliance officer who shall be responsible for monitoring the compliance of the Act, rules and regulations, notifications, guidelines, instructions etc. issued by SEBI or the Central Government.

- Every credit rating agency shall keep and maintain, for a minimum period of five years, the books of accounts, records and documents prescribed by SEBI in this regard.
- Every credit rating agency shall treat, as confidential, information supplied to it by the client and no credit rating agency shall disclose the same to any other person, except where such disclosure is required or permitted by under or any law for the time being in force.

Answer 2(c)

FII inflows augment the sources of funds in the Indian capital markets. In general, an increase in the supply of funds reduces the required rate of return for equity and enhances stock prices. Simultaneously, it fosters investment by Indian firms in the country. The factors affecting FIIs flows can be classified in two categories (i) International (ii) Domestic

(i) International Factors

- International market Capitalization
- Exchange Rate Variance
- Foreign Interest Rate
- Foreign Industrial Production
- International Crisis

(ii) Domestic Factors

- Market Return on Investment in Shares
- Variance of Return in Stock Market
- Beta of the Share Market
- Information Asymmetry
- Impact Cost
- Non-promoter Share Holdings
- Domestic Credit Rating
- Domestic Companies P/E Ratio
- Infrastructure Facility
- Macroeconomic Factors

FIIs investments in India are also influenced by factors like rupee movement, policy reforms, investment regulations, interest rates, liquidity and macro economic conditions.

Question 3

"Options writer has limited profit and unlimited loss whereas options buyer has limited loss and unlimited profits." Discuss this statement with examples. (5 marks)

Answer 3

"Option writer has limited profit and unlimited loss whereas option buyer has limited loss and unlimited profits". The statement is correct.

Buyer of an option has limited loss but unlimited Profit with the right but not the obligation to buy or sell the underlying option. Whereas seller of an option has profit limited to premium received, but unlimited loss with obligation to purchase or deliver the underlying assets.

Making it simple, suppose X is willing to buy a mobile which is now available at Rs.45,000 which is in high demand and price may rise up and suppose, X doesn't have enough funds now. So X goes to a seller and deal with him by giving Rs 1000 now that he will buy the same mobile after 1 month at current price and the deal is sealed.

After one month, let's say mobile price is Rs 48,000; X can go to the dealer pay rest Rs. 44,000 and exercise the deal. So in this case, seller of the mobile is in loss because he is selling the mobile $(48000-45000)=Rs\ 3000$ below the market price and his loss will continue till the market keeps on increasing since he is obligated to deliver the mobile. Hence, he has unlimited loss.

The profit will only be Rs 1000 which is received if price goes down and buyer will not exercise the deal.

Exchange derivatives are all cash settled. If you short one lot of option 7500 CE at Rs 50 = you receive Rs 2500 as a premium but If market rises up, the Premium will also go high from 50 to 100-150 which will depend on % increase hence, loss from a writer of the option will be huge.

Hence, margin collected from the seller or writer of the option is huge. It is basically combination of (SPAN + EXPOSURE + PREMIUM RECEIVED).

Question 4

Explain mark-to-market system of futures market alongwith the various types of margins in Indian financial derivatives market. (5 marks)

Answer 4

Mark to Market is a measure of the fair value of accounts that can change over time, such as assets and liabilities. Mark to market aims to provide a realistic appraisal of an institution's or company's current financial situation. It is an accounting act of recording the price or value of a security, portfolio or account to reflect its current market value rather than its book value.

Problems can arise when the market-based measurement does not accurately reflect the underlying asset's true value. This can occur when a company is forced to calculate the selling price of these assets or liabilities during unfavorable or volatile times, such as a financial crisis. For example, if the liquidity is low or investors are fearful, the current selling price of a bank's assets could be much lower than the actual value. The result would be a lowered shareholders' equity.

This is done most often in futures accounts to make sure that margin requirements are being met. If the current market value causes the margin account to fall below its required level, the trader will be faced with a margin call. Mark-to-market margins (MTM or M2M) are payable based on closing prices at the end of each trading day. These margins will be paid by the buyer if the price declines and by the seller if the price rises. This margin is worked out on difference between the closing/clearing rate and the rate of

the contract (if it is entered into on that day) or the previous day's clearing rate. The Exchange collects these margins from buyers if the prices decline and pays to the sellers and vice versa.

Various types of margins in Indian Financial Derivatives market are:

- Initial Margin
- Premium Margin
- Assignment Margin
- Exposure Margin
- Value at risk margin
- Extreme loss margin
- Mark to market Margin

Question 5

Anchor investor plays a vital role in the Indian capital market. Explain. (5 marks)

Answer 5

In July 2009, SEBI introduced an alternative IPO mechanism, referred to as the book building route with “anchor” investor. Anchor investor is the new concept introduced in the capital market. The anchor investor invests in an IPO before the offer opens to the public. The investors are got attracted to public offers before they hit the market to infuse a measure of confidence. The volume and value of the anchor subscriptions may serve as an indicator of the company’s reputation and soundness of the offer. The concept could be explained as under:

- Anchor investors or cornerstone investors (as they are called globally) are marquee institutional investors like sovereign wealth funds, mutual funds and pension funds that are invited to subscribe for shares ahead of the IPO to boost the popularity of the issue and provide confidence to potential IPO investors.
- The benefit for institutional investors applying in anchor quota is that they get guaranteed allotment. Allotment to investors applying in an IPO depends on the number of times the issue gets subscribed. Anchor investors, however, cannot sell their shares for a period of 30 days from the date of allotment as against IPO investors who are allowed to sell on listing day.
- Roping in anchor investors gives a lot of comfort to the issuer and banker, as nearly a third of the IPO gets covered even before the opening day.

Question 6

Explain briefly the capital protection oriented scheme of a mutual fund. (5 marks)

Answer 6

Capital Protection Oriented Scheme is a scheme which protects the capital invested in the mutual fund through suitable orientation of portfolio structure. A capital protection-

oriented scheme is typically a hybrid scheme that invests significantly in fixed-income securities and a part of its corpus in equities. These are closed-end schemes that come in tenures of three and five years. Regulation 38A of the SEBI (Mutual Funds) Regulations, 1996 provides that a capital protection oriented scheme may be launched, subject to the following:

- (a) the units of the scheme are rated by a registered credit rating agency from the viewpoint of the ability of its portfolio structure to attain protection of the capital invested therein;
- (b) the scheme is close ended; and
- (c) there is compliance with such other requirements as may be specified by SEBI in this behalf.

INSURANCE LAW AND PRACTICE (Elective Paper 9.3)

Time allowed : 3 hours

Maximum marks : 100

NOTE: Answer **ALL** Questions.

Question 1

Ramesh, a senior executive working in Delhi, purchased a Tata Sumo vehicle from Prime Motors on 27th September, 2014 for a sum of ₹7,80,000. After getting the vehicle registered, Ramesh on 29th September, 2014 got the vehicle bearing no. DL2C-J-7250 insured comprehensively with Bright Insurance Co. for the period from 29th September, 2014 to 28th September, 2015.

On 8th November, 2014, Ramesh paid a visit to Noida for official work. He parked and locked the car on the side road adjoining the office and went for work at around 10:30 AM. After finishing his work around 3:30 PM, he came out to return to Delhi. To his surprise, he found the vehicle missing.

He searched for the car frantically and on not finding it, lodged an FIR with the Noida police station for the missing car. Next day, he also informed Bright Insurance Co., the insurer in writing about the said theft of the vehicle.

Despite vigorous efforts of the police, the vehicle could not be traced. Hence, after 90 days, the Noida police gave a non-traceable certificate/report to Ramesh, the complainant. Ramesh, thereafter, again pursued the matter of settlement of claim with the insurance company and submitted a copy of the purchase invoice of the vehicle alongwith driving license, proof of road tax payment and other relevant documents including the final report in support. Despite passage of over 21 days, the insurance company did not respond positively and kept delaying the matter on one pretext or the other.

Aggrieved by this inaction on the part of the insurer, Ramesh after five weeks, filed a complaint with the District Forum. During the pendency of the complaint, the insurance company repudiated the claim on the ground that the vehicle was being used as a Taxi by Ramesh.

The District Forum, after hearing both sides on 29th March, 2015 allowed the complainant and directed the insurance company to pay Ramesh, the insured declared value of the vehicle, i.e., ₹7,80,000 alongwith interest @ 6% p.a. from four months after the date of lodging of claim till realisation. The District Forum also awarded ₹7,000 as costs.

The insurance company, being aggrieved with this decision, filed an appeal before the State Commission. The plea highlighted the fact that the insurer was not liable to reimburse the loss of stolen vehicle as the same was being used as a taxi. This plea was rejected by the State Commission by observing that theft of the vehicle had nothing to do with the use of the vehicle. The appeal, therefore, was dismissed

and the awarded amount was ordered to be released by Bright Insurance Co. to Ramesh. The insurance company being still not satisfied filed a revision petition before the National Forum. During arguments, both sides vehemently advocated their views.

Finally, it was pointed out by the counsel of the insured that in the decided case of 'National Insurance Company Ltd. vs. Nitin Khandelwal' in 2008 (CPJ ISC 2008-SEC-259), the Supreme Court had held that, "in a case where the vehicle had been snatched or stolen, the breach of condition is not germane and the insurance company is liable to indemnify the owner of the vehicle where the insured owner has obtained a comprehensive policy for the vehicle in question."

In view of the aforesaid judgment of the apex court in the earlier order of the State Commission in the 'Nitin Khandelwal case of 2008', the counsel for the insurance company did not press the point that insurer was not liable to reimburse for the stolen vehicle because it was being used as a taxi. Hence, the claim of Ramesh was finalised at 75% on 'non-standard basis' as upheld earlier by the Supreme Court in 2008 plus cost.

In light of the above, answer the following questions :

- (a) Do you agree with the stand taken ultimately by the insurance company to settle the claim on 'non-standard basis' ? Give reasons. (10 marks)
- (b) In the case cited above of the apex court in 2008, the claim was finalised at 75% being 'non-standard basis'. On consideration of the totality of the facts and circumstances in such cases, the law seems to be well settled that in case of theft of a vehicle, the nature of use of the vehicle cannot be looked into and the insurance company cannot repudiate the claim on this basis. If that be the case, should such claim be settled only on 'non-standard basis' ? Comment. (10 marks)
- (c) Extending the logic further, could the claim of Ramesh be not settled at 100% had his counsel pressed for the same ? Elaborate with reasoning. (8 marks)
- (d) What do you understand by 'standard claim' and 'non-standard claim' ? (10 marks)
- (e) If you were the adjudicating authority and a case of this nature is brought before you for decision, what would be your stand ? Elaborate with reasons. (6 marks)
- (f) Is it not desirable for insurers to implement the philosophy of 'under promise and over delivery' in settlement of claims ? Comment. (6 marks)

Answer 1(a)

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

- Though the Supreme Court in 2008 in "Nitin Khandelwal Case" had already laid

down that “in a case, where the vehicle had been snatched or stolen, the breach of condition is germane and the Insurance Company is liable to indemnify the owner of the vehicle where the insured owner had taken a comprehensive policy for the vehicle in question”.

- The court had taken a view that the breach of the policy condition regarding the hire of the vehicle for a commercial purpose has no bearing on its theft and, hence, would be irrelevant.
- The Supreme Court in “Nitin Khandelwal Case” left the question “whether the state commission was justified in allowing the claim of the respondent on the non standard basis” open as the claimant had not filed any appeal against the said order. The insurance company would be bound to pay the insured declared value of the vehicle and not 75 % on non standard basis.
- Further, the National Consumer Disputes Redressal Commission in case of “*Rekha Sardana Vs. Oriental Insurance Co. Ltd & Ors*” in 2010 held the same as mentioned above. Thus, keeping in mind the above, I do not agree with the stand taken ultimately by the insurance company to settle the claim on non-standard basis.

Answer 1(b)

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

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

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

Answer 1(c)

Yes, the claim of Ramesh could have settled at 100% of insured declared value and not 75% on non-standard basis as it was held by National Consumer Disputes Redressal Commission in case of "Rekha Sardana Vs. Oriental Insurance Co. Ltd. & Ors" that insurance company would be bound to pay the insured declared value of the vehicle.

Answer 1(d)

The term non –standard claim is not defined anywhere. The term is used in various decided cases by various forums. Based on those, "Non-Standard Claims" are those claims where the breach of warranty is of a technical nature and is not material to the loss.

A Standard Claim is one where there is neither a breach of condition nor of warranty and the claim falls fully under the terms and conditions of an Insurance Contract and is payable in full. The conclusion is that a claim cannot be rejected for breach of a policy condition unless such breach is the cause of the loss. When there is no nexus between the breach and the loss, the claim has to be settled on a non-standard basis.

Answer 1(e)

If I were the Adjudicating Authority and the claim of this nature was brought before me, for decision, I would have settled the claim at 100% being a standard claim as there has been no violation of any warranty or condition of a Motor policy, as there is no evidence or proof to evidence such breach or violation of usage clause. The claim was lodged in time, regular follow-up was done by the insured, the delay and lack of decision making was only on the part of the Insurance Company and therefore they have to face the consequences. Hence, the payment must include the interest component, and the costs.

Answer 1(f)

Insurers the world over, suffer from an "Image" problem. They are prompt in collection of premium, but take their own time in meeting their liability under a claim. There is thus, a need for Insurers to realize that they are "Custodians of Public Fund". The money that they collect from the customer is a "Trust Money" and is to be safely invested to meet future liabilities under the policy contract. Hence they should endeavour to "under promise and over deliver" rather than "Over Promise" and "Under Delivery" which appears to be the present norm in the market.

Question 2

- (a) *You have been appointed as the CEO of a newly started life insurance company. Indicate how you intend to market the products of the company in the Indian market. (Your answer will have to indicate the various sources available to you to market the products and your preference to any one or more of the agencies). (10 marks)*
- (b) *Kapil purchased an automobile service station from Vimal. The purchase price included the costs of building, equipment and other assets. The business was financed by a loan taken by Kapil from a scheduled bank, which also held a*

mortgage of the building. Kapil, after purchase, converted one of the car-repair bays into a quick-service restaurant. Kapil had secured an insurance cover on the property but did not disclose to the insurer about the conversion. Six months after the commencement of the business, a car undergoing servicing at the station caught fire and damaged the roof over a bay in the service station area.

From the above information, answer the following questions with reasons in brief:

- (i) Who had insurable interest in the property at the time of fire ? (2 marks)*
- (ii) Vimal told Kapil that in order to save money, Kapil could takeover Vimal's insurance cover instead of buying a new policy. Would it have been appropriate to do this, without Vimal's insurer being informed ? (2 marks)*
- (iii) Investigation into the fire accident revealed that the car owner knew that the vehicle's gas tank had a leak but this was not disclosed to Kapil when the car was left for service. Will the principle of subrogation apply in this case ? (2 marks)*
- (iv) Did Kapil show utmost good faith when he applied for property insurance ? (2 marks)*
- (v) Could Kapil's insurer deny coverage for fire on the basis of material misstatement of facts ? (2 marks)*
- (c) What do you mean by 'nomination' ? Explain the difference between 'nomination' and 'assignment' of an insurance policy. (10 marks)*

Answer 2(a)

Insurance companies need to market their products because they are in competition with other insurers for the same customers, and in addition to this, the insurance company are also competing with banks and mutual fund companies too. Many times the only thing that distinguishes a company's products is price as well as the advertising message. The marketing of insurance products can be done directly by an insurance company as well as through agents or company representatives. There are various agencies available for intermediation in the marketing and sale of insurance products, agents, brokers, tied agency relationship, corporate agents, bank assurance, tele- marketing, direct sale etc.

Life Insurance policies are canvassed and sold on the basis of personal and consistent efforts on the part of individual agents. It is this category that sustains the business. All over the world, life insurance business is generated and sustained to a large extent by individual agents. The commission paid to such agents has to be market driven. Efforts are being made by the IRDAI to cut down drastically rates of commission payable to individual agents, so that this move can easily be categorized as “non-progressive”. The pace of growth of life policies depends on the efforts of the individual agency force which has to be reasonably compensated.

Corporate agencies or bank assurance schemes are being pushed through vehemently by the IRDAI. The proposal to convert all bank assurance schemes to bank brokerage business does not seem to have a good start. Most of the insurance companies in India have a bank as a partner. But, banks have to attend to their core business of banking and

to concentrate on insurance selling may affect their business. However, the banks have the advantage of huge customer base and they can target these customers easily.

The various other sources as available to the Life Insurance Company to market products are as follows.

1. Direct mail-letters sent to consumers on the basis of addresses available from various sources like telephone directory etc.
2. Telephone contacts, on the basis of subscriber lists
3. Television programmes
4. Advertisements and loose insertions in main line as well as professional and trade journals
5. Displays in conferences, seminars for specialized products
6. Direct contact from the salaried staff
7. Stalls in exhibitions and even solo exhibitions in remote areas with large potential customers
8. Kiosks with touch technology
9. Internet

Out of above sources product selling through insurance agent networks and bancassurance are preferable.

Answer 2(b)(i)

Kapil has insurable interest in the property. Vimal after sale of the business, does not have an insurable interest. The bank as a mortgagee too, has limited insurable interest on the property.

Answer 2(b)(ii)

No, Vimal cannot pass on the rights under the old insurance contract to Kapil without consulting that insurer and obtaining its consents. Insurance policy is a personal contract by nature, hence is non-transferrable. Kapil should apply for a policy and only then can benefit from it, after issuance of the same.

Answer 2(b)(iii)

Yes, the principle of subrogation is applied. According to this principle, when the insured is compensated for the losses due to damage to his insured property, then the recovery rights of such payments, shifts to the insurer. In this case, the insurer of the car, after compensating for the loss of the car to that insured, can recover the loss from the service station owner (Kapil) or from his insurer.

Answer 2(b)(iv)

Mr. Kapil has breached the principle of utmost good faith, by not revealing material fact of converting part of the car bay into a restaurant. In this situation, Mr. Kapil is bound to intimate any alteration to the property to the insurer if he intends to extend the coverage

of the same, which can be done through an endorsement. In the present case, Mr. Kapil has not informed the company about the conversion, which is a material fact as it increases the degree of risk of the insured property.

Answer 2(b)(v)

The insurer has right to cancel the contract (reputation) and can deny the coverage/ claims for the misstatement/concealment of material fact by assuming that the fire was due to restaurant operations, which was not informed to the insurance company.

Answer 2(c)

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

Difference between Nomination and Assignment

<i>Sl. No</i>	<i>Nomination</i>	<i>Assignment</i>
1.	Nomination is appointing some person(s) to receive policy benefits only when the policy has a death claim.	Assignment is transfer of rights, title and interest of the policy to some person(s).
2.	By merely nominating someone, the right, title and interest of the insured over the policy is not transferred straight forwardly to that nominated person and remains with the insured person only.	The insurer is bound to pass over the benefits, claims and / or interests to the assigned person(s). Even during the time the insured is alive (or even prior to the death of the insured person). Since the policy benefits are assigned till the time the assignment is revoked once again.
3.	Nomination is done at the instance of the Insured.	Along with the instance of the insured, consent of insurer is also required.
4.	It can be changed or revoked several times.	Normally assignment is done once or twice during the policy period. Assignment can be normally revoked after obtaining the "no objection certificate" from the concerned Assignees.
5.	No attestation is prescribed in case of nomination.	Attestation is required in case of assignment.

Question 3

*Define the concept and nature of a 'cover note' under a general insurance agreement.
(5 marks)*

Answer 3

Cover note is the document which is issued immediately after insurance premium is received to prove that insurance cover exists. Cover note is valid for 60 days from the date of issue. Cover note is mostly used in motor insurance and transit insurance, particularly for import covers by sea. The cover note in marine insurance would be valid for duration of transit.

The cover note does not amount to a policy or an engagement to issue the policy and can be used only for compelling the delivery of the policy and cannot be used for any other purpose.

If a claim were to arise between the issue of the cover note and the regular policy, authorities have proceeded to decide claims. But often, difficulties arise in the case of special policies. But, the fact remains that a cover note evidences the payment of premium, assumption of the risk from the date mentioned therein and is for all purposes a policy.

Question 4

What is the amount of compensation payable under the Motor Vehicles Act, 1988 in respect of death of any person ? (5 marks)

Answer 4

Section 140 of the Motor Vehicles Act, 1988, provides for liability of the owner of the Motor Vehicles to pay compensation in certain cases, on the principle of no fault. The amount of compensation so payable is Rs.50, 000 for death of any person resulting from an accident arising out of the use of the motor vehicles.

The principle of "no fault" means that the claimant need not prove negligence on the part of the motorist. Liability is automatic in such cases. Further, under Section 141(1) of the said Act, claims for death or permanent disablement can also be pursued under other provisions of the Act on the basis of negligence (fault liability).

Question 5

What are the liabilities that require a compulsory cover under a policy of motor insurance ? Discuss. (5 marks)

Answer 5

Section 146 of the Motor Vehicles Act, 1988 states that no person shall use, other than as a passenger or allow to use a motor vehicle in a public place unless a policy of insurance which covers the liability to third party on account of death or bodily injury to such third party or damage to any property of a third party arising out of the use of the vehicle in a public place. Therefore, it is mandatory for the owner of any motor vehicle to obtain, at the minimum, a policy from any General Insurance Company holding a valid license from IRDAI, which covers the risk of death or bodily injury to a third party arising out of usage of the vehicle in a public place. The liabilities that require a compulsory insurance under a motor policy are:-

- (a) Death or bodily injury of any person including the owner of the goods or his authorized representative carried in the carriage;

- (b) Damage to any property of a third party;
- (c) Death or bodily injury of any passenger of a public service vehicle ;
- (d) Liability under the Workmen's Compensation Act, 1923 in respect of death or bodily injury of the paid driver of the vehicle, conductor, ticket examiners (public service vehicles) and workers carried in a goods vehicle;

Question 6

State the exclusions as regards a fire insurance policy. (5 marks)

Answer 6

A Fire Insurance Policy usually does not cover a certain amount known as "Excess" under the policy. The policy also excludes damage caused by war and war like operations, nuclear perils, pollution or contamination, electrical/mechanical breakdown, burglary and house breaking.

Certain perils like earth quake and spontaneous combustion can be covered on payment of additional premium. Fire Insurance policies are issued for one year except for dwellings, where a policy may be issued for long term (with minimum period of three years), and the premium for the entire duration should be paid in advance subject to the discounts available as per the policy provisions.

INTELLECTUAL PROPERTY RIGHTS – LAW AND PRACTICE **(Elective Paper 9.4)**

Time allowed : 3 hours

Maximum marks : 100

NOTE: Answer **ALL** Questions.

Question 1

Read the case given below and answer the questions given at the end :

This case is between US-based multinational Bristol-Myers Squibb and a mid-sized Mumbai based company BDR Pharma over 'Dasatinib', an anti-cancer drug.

Bristol-Myers is the exclusive owner of Dasatinib and its derivatives by the claims of Patent No. IN203937 in India. The patent is valid and subsisting and has a term of 20 years from 12th April, 2000 in India. It enjoys patent protection in several other countries such as United States, Australia, New Zealand, Japan, etc.

Chronic Myeloid Leukemia (CML), one of the most common forms of leukemia, arises from the excessive production of abnormal stem cells in the bone marrow which eventually suppress the production of normal white blood cells. The development of imatinib mesylate, a small-molecule tyrosine kinase inhibitor (TKI), was the first rationally designed drug for CML.

Bristol-Myers product Dasatinib was approved by the US Food and Drug Administration on 28th June, 2006. It is presently sold in approximately 50 countries throughout the world. A marketing approval for Dasatinib was also granted by the Drug Controller General of India (DCGI) on 30th August, 2006.

Apart from the above patent, Bristol-Myers also made a patent application in India for crystalline monohydrate form of Dasatinib. The said application is numbered 4309/DELNP/2006 dated 4th February, 2005 and is currently pending before the Indian Patent Office. The monohydrate form of Dasatinib has been granted patents in 45 countries and is an improvement patent of the Indian Patent No. IN203937.

Cause of Action and Grounds

In December, 2008, Bristol-Myers received information that Mumbai based company, BDR Pharma had applied to the DCGI for the marketing approval for Dasatinib. It sent a 'cease and desist' letter to BDR Pharma on 12th January, 2009 asking them to restrain from infringing its Patent No. IN203937. In view of the apprehension that the defendant may infringe the plaintiff's exclusive right of the patent, the plaintiff filed a suit in the nature of a quia timet action against the defendant on 3rd December, 2009 for the infringement of IN203937.

The defendant has not launched the product in the market, hence, no loss or irreparable harm will be caused to BDR Pharma if it is restrained from doing activities that they have not yet commenced.

BDR Pharma admitted that the defendant is intending to launch the generic version of Dasatinib only if the DCGI grants licence to the defendant to manufacture under the provisions of Drugs and the Cosmetics Act, 1940.

Patent Licensing

On 5th May, 2013 the Controller of Patents considered the compulsory licence application filed by BDR Pharma and opined that the BDR Pharma had not made out a prima facie case for grant of a licence as the applicant (BDR Pharma) did not make efforts to obtain a licence from the patentee on reasonable terms and conditions and relegated the applicant to approach the plaintiff for voluntary licence.

By letter dated 13th March, 2012, Bristol-Myers, the patentee raised certain queries on BDR Pharma's application for voluntary licence such as 'facts which demonstrate an ability to consistently supply high volume of the API, Dasatinib, to the market', 'facts showing your litigation history or any other factors which may jeopardise Bristol-Myers Squibb's market position', 'quality related facts and in particular compliance with local regulatory standards and basic GMP requirement', 'quality assurance system due diligence', 'commercial supply terms', 'safety and environmental profile' and 'risk of local corruption'.

BDR Pharma argued that the drug in question is important in the treatment of Leukemia and is exorbitantly priced at ₹1,67,000 for a month's course, putting it beyond the reach of majority of Indian population. Therefore, public interest lies in compulsory licences with royalty being given to Bristol-Myers. Blood cancer patients have a right to get the drug at low price.

Ever since the launch of Dasatinib in India, Bristol-Myers has addressed the access and affordability needs of the patients by an aggressive commercial Patient Access Program (PAP) through which prices of the drug are reduced to a fraction of the MRP. This has evolved over time thereby consistently reducing the cost of drug to patients. The program is available through a third party service provider, for the self paying patients prescribed 'Dasatinib', by an Oncologist. The service provider through a centralised call center delivers the drug to the prescribed patients at their doorstep anywhere in India with no additional delivery cost.

BDR Pharma Defense

BDR Pharma claimed that Dasatinib patent is invalid as it doesn't pass the non-obviousness test and that in any event, the public interest lies in granting an alternative remedy such as ongoing royalties instead of an injunction. The arguments for invalidity of the patent were stated under section 3(d). Under section 3(d) of the Patents Act, 1970, BDR Pharma said that Dasatinib is a mere derivative of a previously-known compound and that Bristol-Myers is 'evergreening' the patents by patenting minor modifications to previously patented inventions. The other aspect is that of efficacy. The compound should display enhanced efficacy over the previously known compound.

BDR Pharma further contended that it is a quia timet injunction, i.e., based on an expectation of harm rather than actual harm. A quia timet action is a bill in equity. It is an action preventive in nature and a specie of precautionary justice intended to prevent apprehended wrong or anticipated mischief.

According to section 83 read with section 90(d) of the Patents Act, 1970, the patent has to be worked in India by manufacture and not by import. BDR Pharma submitted that same principles would apply in respect of the Indian law and thus, in the absence of definition of commercial scale, natural and ordinary meaning should be given to the expression.

It said that in terms of the said treaties the general principles set out are that, a patentee must manufacture the product in that country and it should not also be mere improvement.

In light of the above, answer the following questions —

- (a) In this case, BDR Pharma has not actually infringed the Bristol-Myers patent by way of manufacture or trade. The court has, nevertheless, given an injunction against BDR Pharma not to work the patent. Explain the provisions under which the injunction was given. (15 marks)*
- (b) The question of public interest in compulsory licensing on grounds of high price of the drug is relevant. How can BDR Pharma work the Bristol-Myers patent to undercut the high prices of Dasatinib ? Give suggestions. (15 marks)*
- (c) What do you understand by 'evergreening' ? Discuss this in the above case in the context of 'efficacy'. (10 marks)*
- (d) Who grants patent ? What is the role of Drug Controller General of India (DCGI) in the patent process, does it grant patents ? While giving approval for marketing a drug, does it consider patent status ? (10 marks)*

Answer 1(a)

Provisions of Patents Act, 1970 under which injunction was granted are as under:

Section 106 of the Patents Act, 1970 deals with power of court to grant relief in cases of groundless threats of infringement proceedings.

Section 106 states that:

- (1) Where any person (whether entitled to or interested in a patent or an application for a patent or not) threatens any other person by circulars or advertisements or by communications, oral or in writing addressed to that or any other person, with proceedings for infringement of a patent, any person aggrieved thereby may bring a suit against him praying for the following reliefs, that is to say—
 - (a) a declaration to the effect that the threats are unjustifiable;
 - (b) an injunction against the continuance of the threats; and
 - (c) such damages, if any, as he has sustained thereby.
- (2) Unless in such suit the defendant proves that the acts in respect of which the proceedings were threatened constitute or, if done, would constitute, an infringement of a patent or of rights arising from the publication of a complete specification in respect of a claim of the specification not shown by the plaintiff to be invalid, the court may grant to the plaintiff all or any of the reliefs prayed for.

Explanation : A mere notification of the existence of a patent does not constitute a threat of proceeding within the meaning of this section.

Section 108 of the Patents Act, 1970 deals with reliefs in suits for infringement.

Section 108 provides that:

- (1) The reliefs which a court may grant in any suit for infringement include an injunction (subject to such terms, if any, as the court thinks fit) and, at the option of the plaintiff either damages or an account of profits.
- (2) The court may also order that the goods which are found to be infringing and materials and implement, the predominant use of which is in the creation of infringing goods shall be seized, forfeited or destroyed, as the court deems fit under the circumstances of the case without payment of any compensation.

Section 114 of the Patents Act, 1970 deals with relief for infringement of partially valid specification

Section 114 states that:

- (1) If in proceedings for infringement of a patent it is found that any claim of the specification, being a claim in respect of which infringement is alleged, is valid but that any other claim is invalid, the court may grant relief in respect of any valid claim which is infringed:

PROVIDED that the court shall not grant relief except by way of injunction save in the circumstances mentioned in sub-section (2).

- (2) Where the plaintiff proves that the invalid claim was framed in good faith and with reasonable skill and knowledge, the court shall grant relief in respect of any valid claim which is infringed subject to the discretion of the court as to costs and as to the date from which damages or an account of profits should be reckoned, and in exercising such discretion the court may take into consideration the conduct of the parties in inserting such invalid claim in the specification or permitting them to remain there.

Answer 1(b)

The grounds which are available for the person interested while seeking an application for the compulsory licensing or revocation of the patent on the ground of non working of the patent could be argued before the relevant authority as a matter of defence to the suit for infringement as the civil court hearing the suit for infringement cannot transgress within the domain of the authority/ controller/ Central Government which are distinct functionaries having their powers and consideration specially defined under the specific provisions of the Act.

Under the World Trade Organization TRIPs Agreement, Compulsory Licenses are recognized in order to overcome barriers in accessing affordable medicines and on other ground of non-workable of suit patent as per conditions prescribed under Sections 83 and 84 of the Act.

This is a case of *quia timet*. There is a fear that BDR will infringe in future since they have made application for compulsory licence to DGCI.

Quia Timet Action, it is settled law that such action is maintainable. If a party fears or apprehends, who may obtain injunction to prevent some threatened act being done which if done, would cause him substantial damage and which money would not be an adequate or sufficient remedy. In a quia timet action, in the absence of evidence if a strong case is made out against the defendants, after valid justification, the interim order may be passed by the Court.

BDR should apply to a patent authority for compulsory licence in public interest on grounds of high price. The licence will, however, be given to all India parties and not just BDR.

It is an admitted position that BDR have not yet launched the generic version of Dasatinib commercially in the market. This may be another option.

Hence, if the patent is valid and BDR has not been able to establish prima-facie credible defence, the case of infringement is made out. Under the said circumstances, public interest is an exception to the patent; otherwise the rights granted under Section 48 by the Sovereign towards monopoly would be undermined. The plea of public interest may be invoked once the Court would find that prima-facie the case of credible defence is made out.

Answer 1(c)

In the case of *Novartis AG v. Union of India & Ors* (Civil Appeal Nos. 2706-2716 of 2013 Arising out of SLP(C) Nos. 20539-20549 OF 2009, decided by Supreme Court on 1st April, 2013, AIR 2013 SC 1312, 1313), the Supreme Court held that the primary purpose of section 3(d), as is evidenced from the legislative history, is to prevent “evergreening” and yet to encourage incremental inventions.

“Evergreening” is a term used to label practices that have developed in certain jurisdictions wherein a trifling change is made to an existing product, and claimed as a new invention. The coverage/protection afforded by the alleged new invention is then used to extend the patentee’s exclusive rights over the product, preventing competition. By definition, a trifling change, or in the words of the section “a mere discovery of a new form of a known substance”, can never ordinarily meet the threshold of novelty and inventive step under clauses (j) and (ja) of section 2(1). An invention cannot be characterized by the word “mere”. The word “invention” is distinct from the word “discovery”.

As per Section 3(d) of Patents Act, the mere discovery of a new form of a known substance which does not result in the enhancement of the known efficacy of that substance or the mere discovery of any new property or new use for a known substance or of the mere use of a known process, machine or apparatus unless such known process results in a new product or employs at least one new reactant is not an invention.

Section 3(d) provides an explanatory clause to make it more clear which reads as follows:

“*Explanation* : For the purposes of this clause, salts, esters, ethers, polymorphs, metabolites, pure form, particle size, isomers, mixtures of isomers, complexes, combinations and other derivatives of known substance shall be considered to be the same substance, unless they differ significantly in properties with regard to efficacy”.

In a case in relation to a pharmaceutical substance, the Madras High Court held that efficacy means therapeutic efficacy. It was held that:

- going by the meaning for the word “efficacy” and “therapeutic”... what the patent applicant is expected to show is, how effective the new discovery made would be in healing a disease having a good effect on the body? In other words, the patent applicant is definitely aware as to what is the “therapeutic effect” of the drug for which he had already got a patent and what is the difference between the therapeutic effect of the patented drug and the drug in respect of which patent is asked for.”

“Due to the advanced technology in all fields of science, it is possible to show by giving necessary comparative details based on such science that the discovery of a new form of a known substance had resulted in the enhancement of the known efficacy of the original substance and the derivatives so derived will not be the same substance, since the properties of the derivatives differ significantly with regard to efficacy.” (*Novartis AG Vs. Union of India*, W.P. No. 24760/06).

Efficacy means “the ability to produce a desired or intended result”. Hence, the test of efficacy in the context of section 3(d) would be different, depending upon the result the product under consideration is desired or intended to produce. In other words, the test of efficacy would depend upon the function, utility or the purpose of the product under consideration.

Answer 1(d)

Controller of Patents grants patent.

Drug Controller General of India (DCGI) does not grant patent. It lays down the standards and quality of manufacturing, selling, import and distribution of drugs in India as well as acting as appellate authority in case of any dispute regarding the quality of drugs.

There is no linkage between Patents Act and Drugs and Cosmetics Act in India. The objective of the Drugs and Cosmetics Act is to regulate the import, distribution, manufacture and sale of drugs and the Act does not impose any obligation under any provision on the Drug Controller General to deny marketing approval to a person based on existence of Patent rights.

Patents Act and Drugs and Cosmetics Act are two independent statutes and no linkage can be established between them in the absence of an express provision. Indian legislature stayed away from bringing about a Patent linkage with respect to regulatory approval of drugs.

Question 2

Ericsson is a Swedish multinational company and is the registered owner of eight patents pertaining to AMR technology, 3G technology and Edge technology in India. It is amongst the largest patent holders in the mobile phone industry along with Qualcomm, Nokia and Samsung. The patents owned by Ericsson are considered to be standard essential patents. Standard essential patents are those patents which form a part of a technical standard that must exist in a product as a part of the

common design of such products. In the past two years, Ericsson has been suing various mobile handset companies on the ground of patent infringement in India, such as Xiaomi Technology (Xiaomi), Micromax Informatics Ltd. (Micromax) and Intex Technologies (India) Ltd. (Intex), which are major handset and smartphone provider companies in India.

Contentions of Ericsson

Ericsson moved to the Delhi High Court against companies named above contending that licences on the standard essential patents were offered to be granted to these companies on fair, reasonable and non-discriminatory (FRAND) terms. However, these companies had refused to undertake such licences and were using these patents without licence and accordingly were infringing Ericsson's patents.

Decision of the High Court

The High Court held that prima facie Micromax and Xiaomi were dealing with a patent infringing product and therefore, granted ex-parte injunction orders against them. Furthermore, the court also directed the Customs Authorities to take note of any consignment of the products undertaken by these companies. In the case of Xiaomi, Flipkart was also impleaded in the order and was directed to get rid of all the products of Xiaomi that may be patent infringing. Although, Xiaomi managed to acquire an order allowing the company to import and sell the devices that use the chipsets imported from Qualcomm Inc., a licensee of Ericsson, it was asked to deposit an amount of Rs.100 for the sale of every device. Furthermore, the court also directed Micromax to pay certain royalty rates per set to Ericsson pending the final outcome of the patent infringement suit, if Micromax wanted to continue selling the devices.

The aforesaid ex-parte injunction orders by the High Court were with respect to selling, advertising, importing and/or manufacturing devices that infringed the patents owned by Ericsson.

CCI Investigation Orders

Some of the aggrieved parties like Micromax decided to file a complaint under section 19(1)(a) of the Competition Act, 2002 before the Competition Commission of India (CCI) against Ericsson. These parties claimed that Ericsson did not negotiate the terms of the licence for the standard essential patents as per FRAND terms.

The main contention raised by the parties was that the royalty rates prescribed by Ericsson were excessive and discriminatory and that Ericsson, being a dominant player in the relevant market with respect to the essential patents, had taken advantage of its position and charged exorbitant rates for royalty from the companies for use of its patents. The CCI considered this contention and after examining the evidence presented, agreed with the companies and passed an investigation order. However, this order suffered a blow as the Delhi High Court passed an order restraining the CCI from passing final orders with respect to the contention of the companies. The Delhi High Court held that the CCI's order resulted in raising a question of conflict of jurisdiction with the orders of the Delhi High Court. The High Court held that the order of CCI was adjudicatory and determinative due to the nature of the order being detailed and as a result of which the remedy available to Ericsson had been discarded.

After perusing the narrative above, answer the following questions :

- (i) Under what provisions of the Patents Act, 1970, can the court grant injunction orders ? Is the injunction order justified in this case ? (10 marks)*
- (ii) What are the likely implications of such ex-parte orders for the public ? (10 marks)*
- (iii) How does the Competition Act, 2002 deal with matters relating to IPRs ? (10 marks)*

Answer 2(i)

Section 108 of the Patents Act, 1970 provides the power of the Court to issue injunction orders for infringement, subject to such terms, if any, as the Court think fit. In the case of patent infringement, interlocutory order in the form of temporary injunction can be granted if facts indicate (a) a prima facie of infringement (b) balance of convenience is in favour of the plaintiff (c) insufferable damage for the plaintiff, if injunction is not granted.

The patents owned by Ericsson are considered to be Standard Essential Patents. Standard Essential Patents are those patents that form a part of a technical standard that must exist in a product as a part of the common design of such products. The Indian Patents Act, 1970 seeks to protect the rights of patent holders and the Courts too have displayed their willingness to protect such rights. In fact, the courts have often granted ex-parte injunction orders, without hearing any arguments on merits from the alleged infringers.

But in this case, the Court failed to reckon that the patents were Standard Essential Patents. As mentioned above, Standard Essential Patents form a part of a technical standard that must exist in a product as a part of the common design of such products. The alleged infringers were under the obligation to ensure that the Standard Essential Patents as a technical standard existed in their products as a part of common design. In the circumstances, it would have been in order if the Defendants (alleged infringers) had been given a hearing before order had been passed.

Answer 2(ii)

The High Court granted ex-parte injunction orders, without hearing any arguments on merits from the alleged infringers. Besides the fact that the court failed to observe that the patents in these cases were Standard Essential Patents, it cannot be gainsaid that it would have major implications with respect to development of technology and protection of consumers. Consumers in these circumstances are likely not given enough choice due to such ex-parte injunction orders.

In the case of Xiaomi, Flipkart was impleaded in the order and the Court directed Flipkart to get rid of all the products of Xiaomi that may be patent infringing. Although, Xiaomi managed to acquire an order allowing the company to import and sell the devices that use the chipsets imported from Qualcomm Inc., a licensee of Ericsson, it was asked to deposit an amount of INR 100 for sale of every device. Thus the consumers were deprived of the products of Xiaomi before even the charges of infringement were proved.

Furthermore, the Court also directed Micromax to pay certain royalty rates to Ericsson

pending the final outcome of the patent infringement suit, if Micromax wanted to continue selling the devices. The consumers impliedly would have to pay more for the products, as Micromax would pass on the royalty payments in the price payable by the former.

Answer 2(iii)

Section 3(5) of the Competition Act, 2002 deals with its applicability to matters relating to IPRs.

Section 3 of the Competition Act, 2002 dealing with anti-competitive practices. It states that

- (1) No enterprise or association of enterprises or person or association of persons shall enter into any agreement in respect of production, supply, distribution, storage, acquisition or control of goods or provision of services, which causes or is likely to cause an appreciable adverse effect on competition within India.
- (2) Any agreement entered into in contravention of the provisions contained in subsection (1) shall be void.

Section 3 (5) declares that nothing contained in this section shall restrict:-

- (i) the right of any person to restrain any infringement of, or to impose reasonable conditions, as may be necessary for protecting any of his rights which have been or may be conferred upon him under:-
 - (a) The Copyright Act, 1957
 - (b) The Patents act, 1970
 - (c) The Trade Marks Act, 1999
 - (d) The Geographical Indications of Goods (Registration and Protection) Act, 1999
 - (e) The Designs Act, 2000
 - (f) The Semi-Conductor Integrated Circuits Layout Design Act, 2000

Thus, the patent holder has every right to restrain the infringement of his rights. Section 3(5) of the Competition Act, 2002 cannot come in the way of the right of the patent holder to restrain infringement of his rights, unless he has imposed any unreasonable conditions while granting licence. In cases of unreasonable conditions in the licence, section 3 of the Competition Act can be invoked. This is the legal situation on a bare reading of the Competition Act, 2002 in conjunction with the Patent Act, 1970.

The decision of the Delhi High Court pertaining to the CCI's investigation orders shows that there is a possibility in patent cases that CCI's orders may result in the overlapping with the jurisdiction of the High Courts and result in intervening with the jurisdiction of the High Court. The role of CCI in patent cases needs to be clearer. The High Court has flagged the issue for adjudication.

Question 3

*Explain the restrictive trade practice of 'grant-back provisions' in IPR licensing.
(5 marks)*

Answer 3

The grant-back provisions provide for flow of technical information and improvements to the licensor. These provisions oblige the licensee company to transfer to the licensor of technology, free of cost, any invention or improvement made in the imported technology. The grant-back provisions may be characterised as 'unilateral', 'exclusive or non-exclusive'.

A unilateral grant-back provision establishes unilateral flow of technical information or improvement by licensee without any reciprocal obligation of the licensor. Therefore, such provisions oblige the licensee to provide to the licensor all future improvements made in the technology, on unilateral basis. While in the case of an exclusive grant back clause, though the licensee may be allowed to freely use the invention and improvement developed by it, yet the licensee is prohibited from transferring or licensing the same to the third party. Such clauses restrict the right of the licensee to license or transfer the invention developed through its own R&D activities. A Non-Exclusive Licence grants to the licensee the right to use the intellectual property, but the licensor remains free to exploit the same intellectual property.

The main reason behind the inclusion of grant-back provision appears to be rooted in the free of cost grant-back. Generally, the grant-back is not remunerated and thus, licensor has the advantage of securing access to all improvements made by the licensee. In this situation, the licensor receives the improved technology without sharing its risk or contributing in recipient's financial burdens. Therefore, these provisions constitute an abusive use of the licensor's dominant position and deprive the licensee of any possibility of improving its competitive position in the given market.

There are often pro-competitive reasons for including grant back provisions in an intellectual property licensing, and these generally do not pose competition concerns, especially where they are non-exclusive in nature. They may, however, have an adverse impact on competition, where they substantially reduce the incentives of the licensee to engage in R&D and thereby reduce innovation.

Question 4

What is not a design under the Designs Act, 2000 ? Explain with illustrations.

(5 marks)

Answer 4

Design does not include:

- (i) any trademark, as defined in Section 2(zb) of the Trademarks Act, 1999, or
- (ii) any property mark, as defined in Section 479 of the Indian Penal Code, 1860, or
- (iii) any artistic work, as defined in Section 2(c) of the Copyright Act, 1957.

Artistic Work means

- (i) A painting, sculpture, drawing (including a diagram, map, chart or plan), an engraving or a Photograph, whether or not any such work possesses artistic quality.
- (ii) Any work of architecture i.e. any building or structure having an artistic character or design or any mode for such building or structure.

(iii) Any work of artistic craftsmanship.

Illustrative of non-registrable designs are:

- book jackets, calendars, certificates, forms and other documents.
- dress making patterns, greeting cards, leaflets, maps and plan cards.
- post cards, stamps and medals.
- labels, tokens, cards and cartoons.
- any principle or mode of construction of an article.
- mere workshop alterations of components of an assembly.
- mere change in size of article.
- flags, emblems or signs of any country.
- layout designs of integrated circuits.

Question 5

How is valuation of intellectual property done ?

(5 marks)

Answer 5

Acceptable methods for the valuation of identifiable intangible assets and intellectual property fall into three broad categories. They are market based, cost based, or based on estimates of past and future economic benefits.

In an ideal situation, an independent expert will always prefer to determine a market value by reference to comparable market transactions. This is difficult enough when valuing assets such as bricks and mortar because it is never possible to find a transaction that is exactly comparable. In valuing an item of intellectual property, the search for a comparable market transaction becomes almost futile. This is not only due to lack of compatibility, but also because intellectual property is generally not developed to be sold and many sales are usually only a small part of a larger transaction and details are kept extremely confidential. There are other impediments that limit the usefulness of this method, namely, special purchasers, different negotiating skills, and the distorting effects of the peaks and troughs of economic cycles.

Cost-based methodologies, such as the “cost to create” or the “cost to replace” a given asset, assume that there is some relationship between cost and value and the approach has very little to commend itself other than ease of use. The method ignores changes in the time value of money and ignores maintenance.

The methods of valuation flowing from an estimate of past and future economic benefits can be broken down in to four limbs;

- (1) capitalization of historic profits,
- (2) gross profit differential methods,
- (3) excess profits methods, and
- (4) the relief from royalty method.

Discounted Cash Flow (“DCF”) Analysis sits across the last three methodologies and is probably the most comprehensive of appraisal techniques.

Question 6

The TRIPS agreement provides protection to trade secrets. Elucidate. (5 marks)

Answer 6

The TRIPS Agreement under Article 39 protects trade secret in the form of “undisclosed information”. The protection must apply to information that is secret, which has commercial value because it is secret and that has been subject to reasonable steps to keep it secret. The Agreement does not require undisclosed information to be treated as a form of property, but it does require that a person lawfully in control of such information must have the possibility of preventing it from being disclosed to, acquired by, or used by others without his or her consent in a manner contrary to honest commercial practices.

“Manner contrary to honest commercial practices” includes breach of contract, breach of confidence and inducement to breach, as well as the acquisition of undisclosed information by third parties who knew, or were grossly negligent in failing to know, that such practices were involved in the acquisition.

The Agreement also contains provisions on undisclosed test data and other data whose submission is required by governments as a condition of approving the marketing of pharmaceutical or agricultural chemical products which use new chemical entities. In such a situation the Member government concerned must protect the data against unfair commercial use. In addition, Members must protect such data against disclosure, except where necessary to protect the public or unless steps are taken to ensure that the data are protected against unfair commercial use.

INTERNATIONAL BUSINESS LAWS AND PRACTICES (Elective Paper 9.5)

Time allowed : 3 hours

Maximum marks : 100

NOTE: Answer **ALL** Questions.

Question 1

The growth of shopping via internet had been viewed by Japan's Seven-Eleven convenience store chain as an opportunity rather than a threat. Because of the conditions in the Japanese market place, Seven-Eleven Japan was not likely to be able to sell its own food and other products over the internet. The company could, however, provide service to a large number of Japanese who do not have credit cards or who do not have strong aversion to providing credit card information over the telephone. With over 10,000 outlets in Japan, Seven-Eleven has stores within a short distance of most of its customers and, in fact, of most Japanese. Their customers tend to visit the stores frequently for relatively small purchases.

Thus, Seven-Eleven Japan developed a plan to serve as a distribution point for the products of other companies that were selling over the internet. Customers who wanted goods from an internet marketer could order the goods over the internet, and the internet marketer would ship the goods to a Seven-Eleven store near to the customer. The store would then give the goods to the customer when he or she visits the store, accept in cash (as most Japanese customers prefer) or by credit card, and remit the money to the shipper. The ubiquitous and efficient delivery services available in Japan would facilitate quick delivery to the stores, which would, in fact, be easier than locating the often difficult-to-find address of individuals. Seven-Eleven would collect a small fee for this service. More importantly, the stores would bring in additional potential customers, or bring in regular customers for additional visits. These customers might buy some of Seven-Eleven's own products in addition to picking-up their internet order.

In November, 1999, the company started this system of handling merchandise for internet marketers, delivering goods to customers from their stores, accepting payments from the customers and remitting the payment to the seller. They entered into agreements with Softbank Corporation, Tohan book, Yahoo Japan and others to create a venture to sell using a website on Yahoo Japan. In February, 2000 Seven-Eleven partnered with seven others, including Sony, NEC, Mitsui trading company and Japan Travel Bureau to distribute a wide range of products, to provide music and photos online, and to handle booking and sale of tickets. In another venture, they were involved with internet automobile sales agencies. In July, 2000 they opened a virtual mall named 7dream.com allowing customers to order goods online and pick-up at the Seven-Eleven store of their choice. The service proved to be a great success increasing the sales of their own products while they also collected small fees from the sellers.

In 2001, Seven-Eleven extended this service to Taiwan. The service might also be

offered in additional markets if successful in Taiwan, and if target markets had appropriate characteristics.

In 2004, company opened its first outlet in China through a joint venture with local firms. Although, a Hong Kong company operates several Seven-Eleven stores in south-eastern China, this was the first time Seven-Eleven had made an equity investment and operated a store in the country. Seven-Eleven (Beijing) Co. expects to open 30 to 50 stores in the Chinese capital by mid-2005. By 2010, the company plans to have 500 stores in the nation.

Background

The Seven-Eleven chain has a long history of innovation and growth. It was originally a US company that was subsequently acquired by Japan's Ito-Yokado Co. Ltd. (Ito-Yokado). The original US Seven-Eleven, owned by a Corporation of the United States, was designed to meet the needs of the growing number of wage-earner families and single workers in the United States who worked on non-standard hours. These people often had difficulty in getting to large grocery stores and supermarkets during the hours that they were open. The increasing affluence in the United States, particularly among the target customers, suggested that they would be willing to pay something extra for the convenience of being able to shop at other times, and preferably 24 hours a day. The company opened a number of outlets, carefully selecting the items to be carried, used centralised purchasing to obtain low prices, monitored sales to improve the mix of products offered, carefully controlled inventories and used frequent delivery to achieve high turnover in limited spaces.

In 1973, Seven-Eleven's parent company, Southland Corporation (Southland) saw an opportunity in the Japanese market where many other companies saw only potential problems. The Japanese distribution system was very complex with multiple levels of wholesalers and many very small 'Mom and Pop' stores. Compared to the United States, there were twice as many wholesalers per capita and over twice as many retailers per capita in Japan. Though many of those in the distribution chain in Japan operated on very small margins, the multiple levels resulted in high distribution costs. Additionally, all participants in the distribution system were notoriously reluctant to change distributors or suppliers.

While many foreign markets viewed the Japanese market as too difficult to penetrate, Southland felt that they could set-up their own marketing chain and operate it more effectively than Japanese competitors who retained their existing systems. Japanese society appeared to be ripe for the Seven-Eleven concept. The number of women in the workforce had increased, and most men worked such long hours that they could not visit stores during the regular hours of operation. The typical neighbourhood food stores were small and carried a limited range of products, often specialising in only one type of food (fish, or vegetables, or rice, etc.). Traditional housewives were accustomed to visiting local shops once in a day to get fresh foods, but the number of households where women had the time to do so was decreasing. Japan was becoming increasingly affluent and people had always been willing to pay extra for convenience. The concentration of the population in a few metropolitan areas and the widespread use of trains and buses for commuting to major business districts meant that there were many locations with high traffic volumes.

Japan was still viewed as a very difficult place to do business if you did not have the right connections as well as detailed knowledge of the legal, political and social environment. Southland, therefore, formed a strategic alliance with Ito-Yokado, a large Japanese supermarket chain operator. The joint venture was highly successful, with Seven-Eleven becoming the largest convenience store operator in Japan. In an attempt to avoid being acquired by a Canadian company in 1987, Southland sold its shares of Seven-Eleven Japan to Ito-Yokado.

Seven-Eleven Japan thus became Japanese owned. Subsequent financial problems at Southland in 1990 led to the US company selling 75% of its stock to Ito-Yokado. In doing so, it turned its approximately 7,000 company-owned stores in 21 countries over to the Japanese company. (The name of Southland Corporation, now Japanese-owned, has been changed to Seven-Eleven Inc.)

Under Japanese Leadership

During the period of Japanese ownership from 1987 to the present, the company has enjoyed remarkable further growth and increasing profitability in Japan, and has expanded its overseas operations. The number of its stores in Japan has grown from 3,304 in 1987 to over 10,000 in 2004. Sales per store have steadily increased, market share has increased, and earnings have grown rapidly, with a record profit of over US \$1.6 billion in the fiscal year ended February, 2004. On an average, each store in Japan now attracts 950 customer visits per day.

Seven-Eleven Japan's performance is even more impressive when placed in the context of the whole industry. Several other Japanese companies, attracted by Seven-Eleven's early success, formed competing chains. Lawson Inc. is the second largest convenience store franchise operator, followed by Family Mart. While Seven-Eleven has prospered, the convenience store sector as a whole has suffered from a slowdown in sales growth. Seven-Eleven, however, remains the market leader.

The company's success appears to have been built on a commitment to innovation. It was the first in Japan to introduce a point-of-sale (POS) system for merchandising control. It was also the first to start accepting payments for utility companies, a service now earning commissions on US \$6 billion of such payments per year. It subsequently started handling insurance company payments, payments for NHK (the national broadcasting company) and others. Also, in 1987, the company introduced a control system to keep prepared rice food products at 20 degrees Centigrade through factory, delivery, and in selling cases. They continually upgrade their information systems (fifth generation via satellite communications in 1997) and their warehousing and delivery systems. They continually track sales data so as to determine the best mix of products and make changes in 70% of their products each year. The company develops tie-ups with manufacturers and producers, where mutual advantage can be attained in advertising or offerings. It is increasingly looking overseas for suppliers where superior products or lower prices for quality products can be obtained.

Taiwan and Beyond

The overall social, economic, and geographic environment in Taiwan appears to offer excellent potential for a profitable extension of Seven-Eleven's delivery and

payment service for items ordered on the internet. Taiwan has an even higher population density than Japan, with 611 people per square kilometer in Taiwan compared to 333 people per square kilometer in Japan. Both countries also have most of their populations concentrated in a few major cities. The ratio of stores to population is high in both nations, with over 10,000 stores in Japan for catering to its population of 126 million, and over 3,100 stores in Taiwan for its population of 22 million. Thus, in Taiwan as in Japan, there is easy access to Seven-Eleven stores for most of the population.

The per capita GDP in Taiwan is only approximately one-third of that in Japan. However, the Taiwanese also have an aversion to giving out private information over the internet. Many people cannot, or do not, want to stay at home waiting for delivery services. Thus, it is easier for them to pick-up items at the convenience stores.

Seven-Eleven Japan has outlets in 19 countries. Only 4 of these countries have more than 500 outlets per country. These are Japan, the United States, Taiwan, and Thailand.

Strategy in China

Seven-Eleven took a conservative approach in entering the Chinese market, determining market potential by licensing agreements with a Hong Kong firm opened stores in Shenzhen and Guangzhou. When decided to make an equity investment they did so in the capital city with local firms as partners. In operations, they will be similar in some ways to the approach in Japan. The outlet will be open 24 hours per day. It will handle mainly prepared dishes and foodstuffs in lunch boxes, although handling about 20% fewer items. The per capita income in China is low, but it is growing rapidly and there are increasing number of busy people with comfortable incomes in the larger cities.

Based on the above, answer the following questions :

- (a) What factors accounted for Seven-Eleven's success in Japan ? Discuss. (10 marks)
- (b) Is Seven-Eleven Japan wise in extending its delivery and payment services to Taiwan ? Justify. (10 marks)
- (c) If its extension of services to Taiwan is a success, should it extend such services to the United States, Thailand, or other countries ? Elaborate with reasons. (10 marks)
- (d) Does China offer good potential for Seven-Eleven ? Elucidate. (10 marks)
- (e) Was Seven-Eleven's entry strategy appropriate for the countries ? Explain why or why not. (10 marks)

Answer 1(a)

Japanese retail system comprised of very small 'Mom and Pop' stores as compared to United States. Further, there were twice as many wholesalers per capita and over twice as many retailers per capita in Japan. The Japanese neighbourhood food stores were small and carried a limited range of products, often specializing in only one type of

food. The company provided service for the large number of Japanese who did not have credit cards or who were not having strong aversion to providing credit card information over phone. With over 10,000 outlets in Japan, Seven-Eleven had stores within a short distance for most of its customers. The customers tended to visit the stores frequently and for relatively smaller purchases. In order to attract the customers, Seven-Eleven Japan developed a plan to serve as a distribution point for the products of other companies that were selling over the Internet. Customers who wanted goods from an Internet marketer could order the goods over the Internet, and the Internet marketer would ship the goods to a Seven-Eleven store nearest to the customer. More importantly, the stores would bring in additional potential customers, or bring in regular customers for additional visits. These customers might buy some of Seven-Eleven's own products in addition to picking up Internet order. In November 1999, the company started this system of handling merchandise for Internet marketers, delivering goods to customers from their stores, accepting payments from the customers, and remitting the payment to the seller. They entered into agreements with Softbank Corporation, Tohan book/wholesalers, Yahoo Japan, and others to create a venture to sell using a web site on Yahoo Japan. In February 2000, Seven-Eleven partnered with seven others companies including Sony, NEC, Mitsui Trading Company and Japan Travel Bureau to distribute a wide range of products, to provide music and photos online, and to handle book and ticket sales. In another venture, they are involved with Internet automobile sales agencies. In July 2000, they opened a virtual mall named 7dream.com allowing customers to order goods online and pick up at the Seven- Eleven store of their choice. The service proved to be a great success as it increased the sales of their own products while they also collected small fees from the sellers. These were the factors that made Seven-Eleven Japan successful in the Japanese market.

Answer 1(b)

The social, economic, and geographic environment in Taiwan appeared to offer an excellent potential for a profitable extension of Seven-Eleven's delivery and payment service for items ordered on the Internet. Taiwan has an even higher population density than Japan i.e. 611 people per square kilometer as compared to 333 people per square kilometer in Japan. There was another common feature for both countries as most of their populations concentrated in a few major cities. The ratio of stores to population was high in both nations, with over 10,000 stores in Japan with its population of 126 million, and over 3,100 stores in Taiwan with its population of 22 million. Thus, in Taiwan too, an easy access to Seven-Eleven stores was manageable as in Japan for majority population. Furthermore, though per capita GDP in Taiwan is just approx. one-third that of Japan. However, the Taiwanese also had an aversion to providing private information over the Internet. Many people did not prefer to stay at home waiting for delivery services. Thus, it is easier for them to purchase items at the convenience stores. Therefore, Seven-Eleven Japan took a wise decision in extending its delivery and payment services to Taiwan.

Answer 1(c)

The Seven-Eleven chain was originally a US company that was subsequently acquired by Japan's Ito-Yokado Co Ltd. The original US Seven-Eleven, owned by Corporation of the United States, was designed to meet the needs of the growing number of wage-earner families and single workers in the United States who worked non-standard hours. These

people often had difficulty in getting to large grocery stores and supermarkets during these hours. The increasing affluence in the United States, particularly among the target customers, suggested that they would be willing to pay extra for the convenience of being able to shop at 24 hours per day if provided. The company opened a number of outlets, carefully selecting the items to be carried, used centralized purchasing to obtain low prices, monitored sales to improve the mix of products offered, carefully controlled inventories, and used frequent delivery to achieve high turnover in limited spaces. In 1973, Seven-Eleven's parent company, Southland Corporation saw an opportunity in the Japanese market where many other companies saw only potential problems. Seven-Eleven Japan has outlets in 19 countries. Only 4 of these countries had more than 500 outlets per country consisting of Japan, the United States, Taiwan, and Thailand. Since, the Seven-Eleven Japan targeting to different customers and it was originally a US based company and had experience in US market, so, the Seven-Eleven Japan, should extend their service to United States and also to Thailand and other countries.

Answer 1(d)

In 2004, Company opened its first outlet in China through joint venture with local firms. Although, a Hong Kong Company already operating several Seven-Eleven stores in South-Eastern China, but this was for the first time Seven-Eleven had made an equity investment and operated a store in the country. Seven-Eleven took a conservative approach in entering the Chinese market, determining market potential by licensing agreements with a Hong Kong firm opened stores in Shenzhen and Guangzhou. When decided to make an equity investment, they did so in the capital city with local firms as partners. In operations, they will be similar in some ways to the approach in Japan. The outlet will be open 24 hours per day. It will handle mainly prepared dishes and foodstuffs in lunch boxes, although handling about 20 per cent fewer items. The per capita income in China is low, but has a rapid growing and increasing numbers of busy people with comfortable incomes in the larger cities. All this offers a good potential for Seven-Eleven to operate in China.

Answer 1(e)

Seven-Eleven Japan was very successful and performance was even more impressive when placed in the context of the whole industry. Several other Japanese companies, attracted by Seven-Eleven's early success, too formed competing chains. Lawson Inc. happened to be the second largest convenience store franchise operator, followed by Family Mart. While Seven-Eleven prospered, the convenience store sector as a whole suffered from a slowdown in sales growth. Seven-Eleven remained the market leader. Seven-Eleven's entry strategy proved to be appropriate for the country because the company made licensing agreement with a Hong Kong firm opened stores in Shenzhen and Guangzhou and later on they decided to make an equity investment in the capital city with local firms as partners. Entering through equity investment in China seemed to help the company in management control and extending the service to Taiwan through franchise was appropriate because the characteristics of Taiwan market being similar to Japanese market. Analyzing these factors, it seems the entry strategy adopted by Seven-Eleven Japan was appropriate.

Question 2

(a) (i) *India adopted special economic zone (SEZ) model from China in order to*

increase its exports. In this context, analyse the uniqueness of SEZ model and give your opinion as to why SEZ will increase India's exports.

- (ii) *Though SWOT analysis is a very old technique but still companies are using it. Explain why SWOT analysis is still very much relevant for the companies.*
- (iii) *One of the major key changes in the FDI Policy, 2013 was the approval of FDI in multi-brand retailing. Analyse the impact of the FDI policy in multi-brand retailing. (5 marks each)*
- (b) *Distinguish between the following :*
- (i) *'Economic union' and 'political union'.*
- (ii) *'WTO' and 'UNCTAD'.*
- (iii) *'Anti-dumping duties' and 'countervailing duties'.*
- (iv) *'Warehousing' and 'inventory management'.*
- (v) *'Commodity agreement' and 'international commercial arbitration'.*
(3 marks each)

Answer 2(a)(i)

India adopted SEZ model from China to increase its exports, but India's model represent uniqueness as:

- China's SEZ initiative is Government driven. But in India, the private sector is also allowed to set up SEZs.
- There is no minimum area requirement to set up an SEZ in China. However, in India, there exists such a requirement.
- China does not offer tax incentives across the board to all companies, but India does.

Reasons Why SEZ will Increase India's Exports:

Incentives and facilities available to units in SEZ such as exemption on duties on Indian capital goods and inputs, exemption, waiver or reimbursement of taxes, Duty-free imports of spares, raw materials, capital goods, and consumables etc. will give a competitive edge to the companies in terms of cost as well as quality, therefore, the companies' manufacturing in SEZ will able to compete in global market and can export more goods in international market.

Answer 2(a)(ii)

The SWOT analysis is usually described with a 2 x 2 Matrix. The boxes in this SWOT matrix are labelled 'Strengths' and 'Weaknesses' i.e. internal factors and 'Opportunities' and 'Threats' i.e. factors from external environment.

Though considered to a traditional technique, yet, SWOT analysis helps the companies in contemporary scenario as companies can design a marketing plan by analyzing their strengths, neutralizing their weaknesses, discovering new opportunities and creating a plan to deal with the threats. Therefore, SWOT analysis helps in effective

setting of goals, strategies and tactics for creating a 'Best Marketing Plan'. Particularly, SWOT analysis tries to answer the following questions:

- What is core strength of the company? Whether it is technical prowess, people, product or logistics.
- What opportunities exist out there? It could be expansion into a new vertical with an existing resources. Another could be taking business to a new geographical area. Or, it could be expanding your product portfolio with another product line.
- What sets the business apart from its competitors? Whether it is resources, greater experience, trustworthy supplier relationships or better technology.
- How the company does neutralize a threat?
- How a weakness if not treated and dealt with, could get worse, and could become a potential threat, which in long term could put an opportunity and/or a strength in jeopardy.

Answer 2(a)(iii)

Following are most probable impact of FDI Policy 2013 in Multi Brand Retailing:

FDI Policy 2013 sets a Minimum Investment Limit at \$100 million for foreign companies, out of which at least 50 percent must be in 'Backend Infrastructure' segment. This move is anticipated to result in improved transportation, distribution, storage and packaging facilities, agricultural processing, and develop farm allied infrastructure. Due to these, inflation is expected to come down. In addition, job opportunities in sectors above sectors are expected to thrive.

Foreign companies are expected to take some constructive steps for the creation of supply and logistic chain. Previously, the country use to suffer huge losses due to under developed refrigeration facilities. Now with the entry of foreign players, storage and refrigeration infrastructure are supposed to improve significantly.

Due the FDI initiative, the concept of the middleman, which has subjugated farmers in India for decades, can be eradicated. Farmers can now get the full benefit of their produce.

However, FDI in the retail sector may not have a beneficial impact on the MSME sector.

FDI in retail will also be beneficial for customers as this will increase one-stop shopping options with access to international brands.

Answer 2(b)(i)

'Economic Union' and 'Political Union'

Economic Union is created when countries enter into an economic agreement to remove barriers to trade and adopt common economic policies. An example is the European Union (EU).

Political Union more advanced integration steps are typically accompanied by unification of economic policies (tax, social welfare benefits etc). Political union is the

final stage in economic integration with more informal political link between the countries. The unification of West Germany and East Germany in 1990 is an example of total political union.

Answer 2(b)(ii)

'WTO' and 'UNCTAD'

The World Trade Organization (WTO) is an organisation for liberalizing and a forum for Governments to negotiate trade agreements and settlement of trade disputes with the help of a system of trade rules. WTO works through the agreements which are negotiated and signed by the bulk of the World's trading nations.

UNCTAD was established to promote the development friendly integration of developing countries into the World economy. It functions as a forum for intergovernmental deliberations and aims to help shaping current policy debates and thinking on development with a particular focus on domestic policies and international action for bringing about sustainable development. It provides technical assistance tailored to the specific requirements of developing countries with special attention to the needs of the least developed countries and of economies in transition.

Whereas, there is a strong participation of Non-Governmental stakeholders in UNCTAD, such a participation is limited in WTO.

Answer 2(b)(iii)

'Anti-dumping duties' and 'Countervailing duties'

Antidumping and Countervailing duties essentially seek to remedy the same problem i.e. artificially low priced imports. However, the root cause of the artificially low price is what differentiates antidumping and countervailing duties. Anti-dumping duties are for combating "dumping", which means that an exporter is setting prices at such a low point, that they are intentionally losing money in order to harm the domestic producers of the importing country. It is a 'predatory pricing model' where the exporter prices its goods below production costs or below what they sell for in their home market.

Countervailing duties seek to counteract artificially low prices that are a result of 'subsidies'. Governments often offer all sorts of subsidies on exports in the form of tax breaks and credits. Because of these subsidies, exporters are able to offer lower prices than domestic producers in the importing country. Countervailing duties level the playing field and negate the advantage that exporters get from subsidies. Despite of this, antidumping and countervailing duties go hand in hand.

Answer 2(b)(iv)

'Warehousing' and 'Inventory Management'

Warehousing activity is more complex than inventory management. It is a more focused and detailed system for the operations in a business's warehouses. Warehouse management divides warehouses into many compartments and bins.

Inventory management is the overseeing and controlling of the ordering, storage and use of components that a company will use in the production of the items it will sell as well as the overseeing and controlling of quantities of finished products for sale. As

compared to warehousing, inventory management takes a broader approach to tracking inventory by location and being more product-detail oriented.

Answer 2(b)(v)

‘International Commodity Agreement’ and ‘International Commercial Arbitration’

International Commodity Agreement is an agreement among producing and consuming countries to prove the functioning of the global market for a commodity, it may be administrative, providing information, or economic influencing world price, usually using a buffer stock to stabilize it. Arbitration is the more prominent of the private dispute settlement mechanisms, both domestically and for international commercial relations. *International Commercial Arbitration* is a particular means of settling disputes, i.e. by “arbitration” that is “commercial” in nature and has some international element to it. In other words, an international commodity agreement is an undertaking by a group of countries to stabilize trade, supplies and prices of a commodity for the benefit of participating countries.

Question 3

What is a Logistics Park ? Why has the government established free trade warehousing zone (FTWZ) and how will FTWZ facilitate India's export and import ? (5 marks)

Answer 3

A logistics park is a stipulated area that facilitates domestic and foreign trade by providing services such as warehousing, cold storage, multi-modal transport facility, CFS, ICDs, etc. Logistics parks facilitate loading and unloading of cargo for distribution, redistribution, and packaging and repackaging.

Free Trade Warehousing Zones (FTWZ) were established by the government to develop infrastructure to facilitate import and export of goods and services with the freedom to carry out trade transactions in the free currency.

FTWZ would be a key Link in Logistic and Global Supply chains and will provide warehousing for various kinds of products, handling and transportation equipment, providing commercial office space, all related utilities i.e. telecom, power, water, etc; and one stop clearance of Import and Export of goods etc.

Question 4

Licensing seems to be a fairly safe way for a manufacturer to produce in a foreign market for the first time. Comment. (5 marks)

Answer 4

Licensing is a common method of international market entry for companies with a distinctive and legally protected asset. It involves a contractual arrangement whereby a company licenses the rights to certain technological know-how, design, patents, trademarks and intellectual property to a foreign company in return for royalties or other kinds of payment.

“Licensing seems to be a fairly safe way for a manufacturer to produce in a foreign

market for the first time." This seems to be true to some extent as Licensing is widely considered as another form of "safe" market penetration as it Builds and strengthens the brand image beyond traditional boundaries without much involvement of the brand owner and still builds brand value. It is also a safer avenue for the customers in foreign country to acquire authorized rather than illegal or unauthorized products using the brand name, marks and logo. It also generates additional revenue through venturing in foreign country while protecting the trade marks.

Question 5

If a firm is planning a strategic alliance then how will it decide about the type of strategic alliance and how will it proceed through different stages of alliance formation. Discuss. (5 marks)

Answer 5

Strategic Alliances can be of various types depending upon the factors like capital commitment, type of industry, structure of organisation etc.

Strategic alliance on the basis of type of industry i.e.

- Horizontal Strategic Alliance
- Vertical Strategic Alliance
- Inter-sectoral Strategic Alliance

Strategic alliance on the basis of capital such as

- Joint venture,
- Equity strategic alliance,
- Non-equity strategic alliance, or
- Global Strategic Alliances

The type of strategic alliance has to be chosen keeping multiple factors in mind such as the overall business goal or objective, development or maintenance of a core competency or other source of competitive advantage, blocking a competitive threat, creating or maintaining strategic choices for the firm, mitigates a significant risk to the business etc.

Different stages of alliance formation:

- (i) Strategy Development
- (ii) Partner Assessment
- (iii) Contract Negotiation
- (iv) Alliance Operation
- (v) Alliance Termination

Question 6

A small and medium enterprise shoes manufacturing company is very successfully doing its business in Indian market. Now the company wants to export its products to international market. The company has hired you as an international business

consultant for preparing the detailed export plan so that the company can start exporting its products as early as possible. Suggest how the company can plan for the prospective export. (5 marks)

Answer 6

Integral aspect of starting a successful export business in India is to have a proper understanding of the products being exported through a thorough research of the market where they are to be exported. Good research can also help them determine which market is good for the type of products being exported by them. The markets should be approached on a priority basis and thorough research should be done on products and designs being done overseas. It is important to learn export related laws applicable in a country, state, or region before going ahead with the business.

Following are certain questions that form an important part of the entire process:

- Which products should be chosen for developing exports?
- Which specific steps should be taken regarding operations and what would be the right time to take them?
- What changes have to be made to the products so that they are at par with customer demands?
- What will be the amount of time needed to put to use each component of the export plan?
- Which countries can be considered as prospective markets?
- What resources and personnel will be used only for export related purposes?
- Which distribution and marketing channels should be used?
- What will be the expense in terms of money and time for every single procedure?
- What are the special challenges of the markets in terms of areas like competition, import control, differences in culture, and others?
- Which strategies can be used to counter them?
- How will results be evaluated and used for changing the plan?
- How shall the export sale price of the products be decided?
