CONTENTS

1. Corporate Laws — Imperatives for Future
— *U K Chaudhary* 1

2. Historical Perspective of Securities Laws
— *M S Sahoo* 5

3. New Corporate Governance Norms : An Analysis of Revised Clause 49 of the Listing Agreement
— *N K Jain* 33

4. Stock Market Benefit : For whom the Bell Tolls ?
— *Abul Khair Al-Muqtadir* 39

5. GATS : Impact on Company Secretaries
— *Parveen Nagree-Mahtani & Sandeep Farias* 44

6. Business Ethics and Professionalism
— *Justice S N Kapoor* 53

7. Business Ethics and Professionalism
— *Joshua W Wambua* 66

CORPORATE LAWS — IMPERATIVES FOR FUTURE

U K CHAUDHARY*

It is now universally recognized that for proper and smooth functioning of bodies corporate, it is essential to have progressive, liberal and simplified corporate laws to encourage disclosure of information and transparency in the working of the bodies corporate and Trans-National Corporations working beyond the national boundaries. Since liberalization of economy and globalization of Indian market and the efforts of the Government to harmonize the Indian economy with the global economy, appreciable changes have been made in the various economic and corporate legislations relating to the management of Foreign Exchange, Company Law with connected rules and regulations, Money Laundering, Competion, Trade marks, Patents and Designs laws, Cyber Laws, Laws relating to issues of securities by listed companies, Acquisitions and Mergers, Monopolies, Restrictive and Unfair Trade Practices, industrial licensing, rehabilitation of sick companies, recovery of dues and tackling of problem of non performing assets, establishment of new Tribunals, simplification of tax laws including the reduction of tax burden of individuals and corporates. These various appreciable changes in the economic, tax and corporate legislation have brought proper disclosure of information to shareholders, consumers and public at large, simplification of compliance of laws, reduction of tax burden of individuals and corporates and elimination of procedures and licensing, de-regulation, making it more convenient for the corporations to establish new business and carrying on the present business more efficiently and diligently. It will therefore, be pertinent to analyze the recent amendments in the corporate and other connected legislations and to examine as to whether sufficient work has been done in this regard by the Government and how much more is required to be achieved.

Urban Land (Ceiling and Regulation) Repeal Act,1999

The first step in the direction of liberalization was taken by the Ministry of Law, Justice and Company Affairs,when the Urban Land (Ceiling and Regulation) Repeal Ordinance, 1999 was promulgated (later on converted into Act) to repeal the existing Urban Land (Ceiling and Regulation) Act, 1976, paving way for efficient and proper use of Urban Land by commercial enterprises.

Companies (Amendment) Act, 1999

In the same year, the Companies (Amendment) Act, 1999 was enacted by the Parliament with an objective to allow the companies to buy back their own securities and to enable the companies to issue sweat equity shares issued at a discount for consideration other than cash or in lieu of for providing know-how or making available rights in the nature of Intellectual Property Rights or Value Addition. The Companies (Amendment) Act, 1999 also granted to the holders of the securities of a company a facility for nomination to the benefit of debenture/ deposit holders. The said Act of 1999 also made provision for establishment of Investor Education and Protection Fund and formation of the National Advisory Committee on Accounting Standards. The said Act of 1999 also took a progressive step freeing the companies from obtaining prior approval from the Central Government to grant corporate Investments and Loans. Accordingly, suitable amendments were made in Sections 4A, 58A, 78, 80,82, 205A, 205B , 211,217,227, 370,372 and 642. The said Act also added new sections such as, Section 77A, 77AA, 77B,79A, 109A and 109B, 205C,210 A and 372 A of the Companies Act, 1956.

Financial Companies Regulation Bill, 2000

In the year 2000, the Financial Companies Regulation Bill, 2000 was introduced to make this regulation of Non Banking Financial Companies effective and to protect depositors interest. The said bill *inter alia* provides :

* Senior Advocate and Past President, The ICSI

(a) constitution of an Advisory Council consisting of Deputy Governor, RBI as the Chairperson and other members of the Council to advise and make recommendations on matters referred to it by the RBI;

(b) compulsory registration of all financial companies with the RBI;

(c) requirement of prior approval of the RBI for any substantial change in the management, change in location of its registered office and change in name of a financial company;

(d) enhancement of the ceiling of minimum net owned fund required for registration of a financial company receiving public deposits being raised from rupees two crores to rupees ten crores;

(e) provision requiring owned funds for registration of every financial company which does not receive public deposits with a minimum owned fund of rupees twenty five lakhs which may be raised to rupees two crores by the RBI;

(f) creation of reserve fund and investment of twenty-five percent of such fund in specified unencumbered securities:

(g) provision for depositors to have first charge on certain assets of the financial companies which may default in repayment of public deposits and specified unencumbered securities created out of a part of reserve fund;

(h) regulating or prohibiting from issuing advertisement by any non-banking institution;

(i) conferring powers upon the RBI to direct a financial company or a class of financial companies to seek prior approval for appointment of statutory auditors in certain cases;

(j) empowering the RBI to appoint one or more Special Officers;

(k) prohibition of financial companies receiving public deposits for carrying on business other than the business of financial institution;

(l) giving more powers to Board for Company Law Administration constituted under the Companies Act, 1956 for redressal of depositor's grievances;

(m) conferring upon the Board the powers prohibiting alienation of assets by financial companies and attachment and sale of assets of the financial company for effecting repayment of the deposits;

(n) prohibiting all unincorporated bodies from issuing advertisement in any manner for soliciting public deposits;

(o) making certain offences relating to unauthorized acceptance of public deposits as cognizable offences;

(p) making acceptance of public deposits by unincorporated bodies as a cognizable offence.

The Companies (Amendment) Act, 2002

This amendment in the Companies Act also provided for the establishment, control and operations of producer companies adding new sections 581 A to 581 ZT. It was felt for quite some time that benefits of corporates in the form of incorporated companies be extended to co-operative societies engaged in the vocation, business and services of Agriculture and other produce as defined in the Act, in small cottage industry and agriculture sector.

The Companies (Second Amendment) Act, 2002

The Companies (Second Amendment) Act, 2002 further amended to incorporate the latest developments and innovations in corporate laws and provide for the following:-

(i) A National Company Law Tribunal will be set up. The powers and jurisdiction presently being exercised by various bodies viz, Company Law Board or Board for Industrial and Financial Reconstruction or Appellate Authority for Industrial and Financial Reconstruction or High Courts will now be consolidated and entrusted to the Tribunal. Thus, multiplicity of litigation before various Courts or quasi-judicial bodies or forums regarding revival or rehabilitation of merger or amalgamation or winding up will be avoided as all these matters will be heard and decided by the proposed National Company Law Tribunal;

(ii) All the parties will be bound by the Tribunal's orders and in case of non-availability of a workable proposal for revival or rehabilitation etc., the Tribunal can decide the matter on merits including introduction of its own scheme.

(iii) The Tribunal shall work through Benches. There shall be ten special benches which will deal with the matters relating to revival or reconstruction or rehabilitation or winding up of the companies;

(iv) This will reduce the entire process which is presently taking several years in winding up of the companies to about two three years or so;

(v) Stripping of assets of sick companies will be avoided;

(vi) Since individual affidavits will be filed with National Company Law Tribunal which will have powers of contempt of Court, there will be an in-built seriousness;

(vii) There will be a fund known as Rehabilitation and Revival Fund which will be used to make primarily:

(a) interim payment of the dues of workmen of the company which has been declared sick or is under liquidation;

(b) protection of the assets of sick companies;

(c) revival and rehabilitation of sick companies.

(viii) Industrial Undertaking in terms of sickness does not include:

(a) small scale industrial undertakings, as defined in clause (j) of Section (3) of the Industrial (Development and Regulation) Act, 1951;

(b) Public Sector Undertakings, unless a reference is made by the Central Government and / or State Government, as the case may be.

(ix) As a result of this enactment everyone including workers, creditors, investors and the economy as a whole will stand to benefit.

Competition Act, 2002

The Parliament has also enacted Competition Act, 2002 with an objective to foster and maintain competition in the Indian market so as to sub-serve the consumer interest while protecting the freedom of economic action of various market participants and to prevent practices which effect competition and to establish a Competition Commission of India therefor. With the enactment of Competition Act, the present MRTP Commission will be dissolved as and when notified by the Government and the new Commission will be conferred with the jurisdiction to deal with Monopolies and Restrictive Trade Practices, and large scale merger/ amalgamation and acquisitions leading to elimination of competition, whereas Unfair Trade Practices will be dealt with by the Consumer Courts in India.

Negotiable Instruments (Amendment and Miscellaneous Provisions) Act, 2002

The Government has also enacted Negotiable Instruments (Amendment and Miscellaneous Provisions) Act, 2002 to cover certain deficiencies and loopholes of the Negotiable Instruments Act, 1881 and for speedy and expeditious trial of dishonouring of cheques.

Consumer Protection (Amendment) Act, 2002

With the objective of sub-serving the consumer against the interest of business enterprises, further amendments are made by Consumer Protection Act.

SEBI (Amendment) Act, 2002 & Securities Laws (Amendment) Bill, 2003

To achieve transparency and de-mutualisation of Stock Exchanges, Government has made suitable amendments in the Securities and Exchange Board of India Act by enacting SEBI (Amendment) Act, 2002 and with the same purpose, recently the Government has introduced in the Lok Sabha, Securities Laws (Amendment) Bill, 2003 to further amend the Securities Contracts (Regulation) Act, 1956 and the Depositories Act, 1996.

Foreign Exchange Management Act, 1999

The Government also repealed the Foreign Exchange Regulation Act and substituted the same by liberal and progressive Foreign Exchange Management Act to promote direct foreign investments in India and to de-regulate, for the benefit Trans-National Corporations, their establishment of business in India. The provisions of Foreign Exchange Management Act, 1999 have acknowledged the requirement of liberal foreign investment rules and that it is beneficial to attract direct foreign investments in India and also the exposure of Indian bodies corporate outside India leading to the growth of Indian corporations and enabling them to meet with the Competition of Trans-National Corporations in true sense.

Information Technology Act, 2000

The Government of India has also enacted Information Technology Act to keep pace with the use of Technology and Information by the corporates and the business enterprises. This has also recognized the use of electronic mode of transmission of information and its authenticated use for legal purposes. This Act is framed to provide legal recognition for transactions carried out by means of electronic data interchange and other means of electronic communication, commonly referred to as E-commerce which involve the use of alternative to paper based methods of communication and storage of information, to facilitate electronic filing of documents with the Government agencies and to amend the Indian Penal Code, the Indian Evidence Act, the Bankers Book Evidence Act and the Reserve Bank of India Act.

Trade Marks Act; Patents Act; Designs Act and Copyright Act

With the same objective of harmonizing the business enterprises with their counterparts outside India and providing level playing field to Trans-National Corporations, suitable amendments have been made in the Trade Marks Act, Patent Act, Designs Act and Copyright Act.

Insurance (Amendment) Act, 2002

Insurance (Amendment) Act, 2002 is also a step in the direction to privatize the business of insurance and granting opportunities to the private sector to extent the benefit of life and General Insurance to the individuals and bodies corporates.

Arbitration and Conciliation Act, 1996 & Legal Services Authorities (Amendment) Act, 2002

It is pertinent to mention that the enactment of new legislations and amendments in the corporate legislations will be of not much use, if the enforcement of these legislations is not effective and corporate disputes are not resolved in the time bound manner. The Government is, therefore, emphasizing the need of resolving small and simpler disputes by Lok Adalats and Arbitrations for which new Act is enacted, namely Arbitration and Conciliation Act, 1996 and the amendment is made by the Legal Services Authorities (Amendment) Act, 2002 recognizing the decisions taken by Permanent Lok Adalats and making an arbitration award as a decree unless challenged within the specified period in accordance with the provisions of Arbitration and Conciliation Act, 1996 as amended up to date.

Securitisation and Reconstruction of Financial Assets & Enforcement of Security Interest Act, 2002

The Government is also aware that whereas lending and borrowing for commercial purposes is essential for economic growth, prosperity, production and distribution of goods, it is essential that the money borrowed by corporations and business enterprises is paid back to the lenders in time and as per the terms and conditions. With these objectives in mind, the Government has already established Debt Recovery Tribunals under the provisions of Recovery of Debts by Banks and Financial Institutions Act. In addition to the said Act, the Government has also enacted an elaborate legislation known as the Securitisation and Reconstruction of Financial Assets & Enforcement of Security Interest Act, 2002, which provides for expeditious and quicker remedies to the Banks and Financial Institutions to recover their dues from the defaulting companies and business enterprises by taking into their possession the assets of the company and the assets of the guarantors to the loans or financial assistance. Though the Act is under challenge for its constitutional validity and the outcome is still not clear but the point, cannot be lost sight off that the nation cannot afford the loss of funds to the extent of over Rs.75,000 crores not repaid by the borrowers to the Banks and Financial Institutions, which are the trustees of the public money. However, appropriate equilibrium is to be maintained to achieve this objective, so that the industrial and economic growth does not suffer by stoppage of production and distribution and the available assets created out of the borrowed funds are not destroyed just to recover the funds of the Banks and Financial Institutions.

In the end, it can be safely concluded that whereas Government has done considerable and appreciable work in enacting, modifying and amending the corporate legislations and issuing rules and regulations thereunder to achieve the objectives as discussed above but to achieve the objectives of expeditious disclosure and protection of consumers and shareholders there is no need to enact the laws which are retrograde steps in the achievement of the objective underlying the thinking of the Government. In this regard, special mention may be made to the Companies (Amendment) Bill, 2003 which is pending for consideration by the Parliament and which has a number of negative, restrictive and obstructive sections which will not only hamper growth but will start the process of retardation rather than achieving the desired progress.

HISTORICAL PERSPECTIVE OF SECURITIES LAWS

M S SAHOO*

The two exclusive legislations that governed the securities market till early 1992 were the Capital Issues (Control) Act, 1947 (CICA) and the Securities Contracts (Regulation) Act, 1956 (SCRA). The CICA had its origin during the war in 1943 when the objective was to channel resources to support the war effort. Control of capital issues was introduced through the Defence of India Rules in May 1943 under the Defence of India Act, 1939. The control was retained after the war with some modifications as means of controlling the raising of capital by companies and to ensure that national resources were channeled into proper lines, i.e., for desirable purposes to serve goals and priorities of the government, and to protect the interests of investors. The relevant provisions in the Defence of India Rules were replaced by the Capital Issues (Continuance of Control) Act in April 1947. This Act was made permanent in 1956 and enacted as the Capital Issues (Control) Act, 1947. Under the Act, the Controller of Capital Issues was set up which granted approval for issue of securities and also determined the amount, type and price of the issue. This Act was, however, repealed in 1992 as a part of liberalization process to allow the companies to approach the market directly provided they issue securities in compliance with prescribed guidelines relating to disclosure and investor protection.

Though the stock exchanges were in operation, there was no legislation for their regulation till the Bombay Securities Contracts Control Act was enacted in 1925. This was, however, deficient in many respects. Under the constitution which came into force on January 26, 1950, stock exchanges and forward markets came under the exclusive authority of the Central Government. The Government appointed the A. D. Gorwala Committee in 1951 to formulate a legislation for the regulation of the stock exchanges and of contracts in securities. Following the recommendations of the Committee, the SCRA was enacted in 1956 to provide for direct and indirect control of virtually all aspects of securities trading and the running of stock exchanges and to prevent undesirable transactions in securities. It has undergone several modifications since its enactment and even today an amendment is awaiting approval of the Parliament. It gives Central Government regulatory jurisdiction over (a) stock exchanges through a process of recognition and continued supervision, (b) contracts in securities, and (c) listing of securities on stock exchanges. As a condition of recognition, a stock exchange complies with conditions prescribed by Central Government. Organised trading activity in securities is permitted on recognised stock exchanges.

The authorities have been quite sensitive to requirements of the development of securities market, so much so that the last decade (1992-2003) witnessed nine special legislative interventions, including two new enactments, namely the Securities and Exchange Board of India (SEBI) Act, 1992 and the Depositories Act, 1996. The SCRA, the SEBI Act and the Depositories Act were amended six, five and three times respectively during the same period. The developmental need was so urgent at times, that the last decade witnessed five ordinances relating to securities laws. Besides, a number of other legislations (the Income Tax Act, the Companies Act, the Indian Stamps Act, the Bankers' Book Evidence Act, the Benami Transactions (Prohibition) Act etc.) having bearing on securities markets have been amended in the recent past to complement amendments in securities laws.

The legal reforms began with the enactment of the SEBI Act, 1992, which established SEBI with statutory responsibilities to (i) protect the interest of investors in securities, (ii) promote the development of the securities market, and (iii) regulate the securities market. This was followed by repeal of the Capital Issues (Control) Act, 1947 in 1992 which paved way for market determined allocation of resources. Then followed the Securities Laws (Amendment) Act in 1995, which extended SEBI's jurisdiction over corporates in the issuance of capital and

* FCS, Chief General Manager, SEBI. The explanation and understanding provided in this paper are of the author and not necessarily of his employer.

transfer of securities, in addition to all intermediaries and persons associated with securities market. It empowered SEBI to appoint adjudicating officers to adjudicate wide range of violations and impose monetary penalties and provided for establishment of Securities Appellate Tribunals (SATs) to hear appeals against the orders of the adjudicating officers. Then followed the Depositories Act in 1996 to provide for the establishment of depositories in securities with the objective of ensuring free transferability of securities with speed, accuracy and security. It made securities of public limited companies freely transferable subject to certain exceptions; dematerialised the securities in the depository mode; and provided for maintenance of ownership records in a book entry form. The Depositories Related Laws (Amendment) Act, 1997 amended various legislations to facilitate dematerialization of securities. The Securities Laws (Amendment) Act, 1999 was enacted to provide a legal framework for trading of derivatives of securities and units of CIS. The Securities Laws (Second Amendment) Act, 1999 was enacted to empower SAT to deal with appeals against orders of SEBI under the Depositories Act and the SEBI Act, and against refusal of stock exchanges to list securities under the SCRA. The next intervention is the SEBI (Amendment) Act, 2002 which enhanced powers of SEBI substantially in respect of inspection, investigation and enforcement. The latest and the ninth legislative intervention namely the Securities Laws (Amendment) Bill, 2003 introduced in the monsoon session of the Parliament to amend the SCRA to provide for demutualisation of stock exchanges is awaiting approval. The approval to this bill is a matter of time as it is a money bill. This paper explains the provisions in these nine legislative interventions in a historical perspective.

A. Repeal of Capital Issues (Control) Act, 1957

It is believed that a liberalised securities market helps promote economic growth. The more liberalised a securities market is, the better is its impact on economic growth. Interventions in the securities market were originally designed to help governments expropriate much of the seigniorage and control and direct the flow of funds for favoured uses. These helped governments to tap savings on a low or even no-cost basis. Besides government used to allocate funds from the securities market to competing enterprises and decide the terms of allocation. The result was channelisation of resources to favoured uses rather than sound projects. In such circumstances accumulation of capital per se meant little, where rate of return on some investments were negative while extremely remunerative investment opportunities were foregone. This kept the average rate of return from investment lower than it would otherwise have been and, given the cost of savings, the resulting investment was less than optimum.

The implication of the above regime is illustrated in Figure 1. The vertical axis represents cost of capital and rate of return on investment and the horizontal axis represents the amount of capital raised from the securities market. With intervention, the demand for investment is represented by DdD, which indicates lower average rate of return corresponding to sub-optimal resource allocation. As the level of investment increases to OD, the maximum permitted by the authorities, the average rate of return decreases as relatively less remunerative investments are approved. SS represents the supply of capital. This results in an investment of K. If, however, intervention is withdrawn, rate of return will go up causing a shift in demand for investment schedule to D_1D_1, which will be down ward sloping through out. This would result in higher investment and consequently income. This would shift supply schedule of capital to S^1S^1. The investment would further increase to K* and rate of return would improve to r*. Rate of return improves because removal of intervention rations out low yielding investments. As the cost of capital goes up, the entrepreneurs are likely to switch to less capital-intensive technologies. Such technologies may not only raise the average productivity of capital, but also represent appropriate technology provided by relative availability and cost of labour and capital in the economy. Letting rate of return be determined by the market mechanism would reduce or even eliminate the costs involved in credit rationing arrangements and thereby enhance the efficiency of the economy as a whole.

The allocation of resources by government, rather than by market, contributed to shrinkage of the securities market. When subject to effective expropriation through suppressed return on investment, people naturally seek a proper reward elsewhere, either through capital flight, through a retreat to underground or through the hoarding of goods. People keep their savings out of the markets. The underground sector allocates the resources, but relatively inefficiently.

As a part of the liberalisation process, the CICA was repealed by an Ordinance on May 29, 1992 paving way for market determined allocation of resources. With this the office of Controller of Capital Issues was abolished and the cost of rationing the resources was saved. The Act earlier required a firm wishing to issue securities to obtain prior approval from the government, which also determined the amount, type and price of the issue. Now the eligible firms comply with the specified requirements and access the market to raise as much resources and at such terms as the market can bear. In the issues made through book building, the investors have freedom to subscribe for the securities at the prices they consider appropriate.

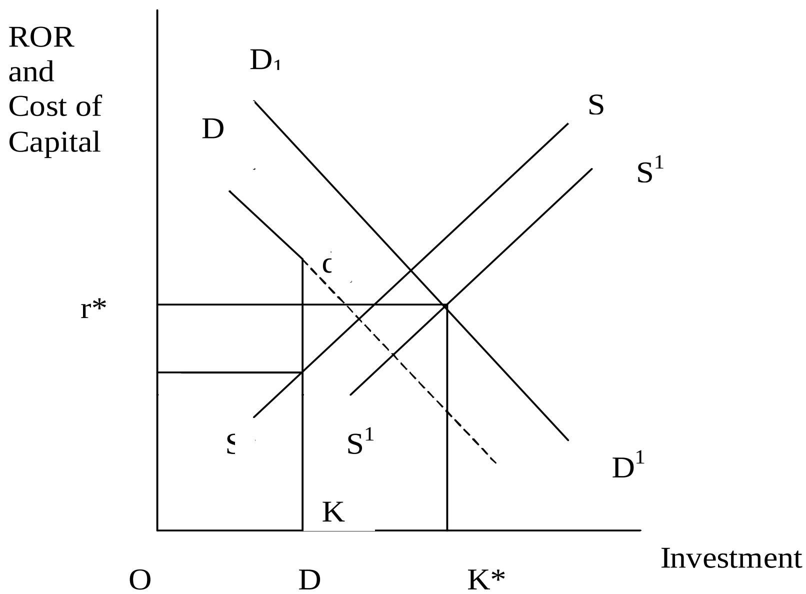


Figure 1: Effect of liberalisation of Securities Market

B. Enactment of the SEBI Act, 1992

Liberalisation does not mean scrapping of all codes and statutes. It rather means replacement of one set by another set of more liberal code / statute, which influence or prescribe the way the private sector agents should carry out their activities. In the context of securities market, the regulations are necessary for the following reasons:

(i) The correction of identified market imperfections and failures. There are many potential market imperfections in securities market such as inadequate information, asymmetric information, difficulty in ascertaining the quality of contracts at the point of purchase, imprecise definitions of products and contracts, under-investment in information, agency costs and principal agent problems. In a regulation free environment, these imperfections impose costs on investors in securities. A high degree of information disclosure is required to make investors effective in the market place. If the regulation requires the issuer or intermediaries to provide necessary information, this adds cost to them but reduces cost on consumers.

(ii) Substantial economies of scale to be derived from collective regulation and supervision of issuers and intermediaries. As investment contracts are long-term in nature and often involve a fiduciary role in a principal-agent relationship, there is need for continuous monitoring. In the absence of regulation and supervision by a specialist agency, which offers certain minimum standards, investors are required to spend time, effort and resources in investigating and monitoring issuers and intermediaries. This entails two types of costs: (a) substantial duplication and hence excessive social costs as all investors are duplicating the same process, (b) the loss of economies of scale that are derived through a specialist regulator/ supervisor acquiring expertise and establishing effective authorization and monitoring system. In the absence of such an agency, an occasional investor would find investigation and monitoring excessive and free-rider problem are likely to arise.

(iii) Signaling minimum standards of quality enhances confidence in markets. With a known asymmetric information problem, risk averse investors may exit the market altogether. In its extreme form the market breaks down completely as potential investors know there are high and low quality products but they cannot distinguish them ex ante, while the issuers can make the distinction but are unable or unwilling to communicate the distinction with credibility. When investors know there are low quality products in the market, good issuers and their products may become tarnished by the generalized reputation of poor products and suppliers. In such a case, the regulator is to set minimum standards and thereby remove the bad products from the market.

With these objectives, it was considered necessary to create a statutory agency, which would ensure fair play in the market, develop fair market practices, prescribe and monitor conduct of issuers and intermediaries so that the securities market enables efficient allocation of resources. The enactment of the SEBI Act, 1992 was an attempt in this direction.

Constitution : The Act established a Board, called Securities and Exchange Board of India (SEBI), to protect the interests of investors in securities and to promote the development of and to regulate the securities market. It prescribed that the Board would consist of a Chairman, one member each from amongst the officials of the finance ministry, the law ministry and the RBI and two other members. In order to avoid conflict of interest, it was provided that a member shall be removed from office if he is appointed as a director of a company.

Functions : In addition to its general responsibility, it was assigned the following specific responsibilities:

(a) regulating the business in stock exchanges and any other securities markets,

(b) registering and regulating the working of stock brokers, sub-brokers, share transfer agents, bankers to an issue, trustee of trust deeds, registrars to an issue, merchant bankers, underwriters, portfolio mangers, investment advisors and such other intermediaries,

(c) registering and regulating working of CIS, including mutual funds,

(d) promoting and regulating self regulatory organizations (SROs),

(e) prohibiting fraudulent and unfair trade practices relating to securities market,

(f) promoting investor education and training of intermediaries,

(g) prohibiting insider trading in securities,

(h) regulating substantial acquisition of shares and takeover of companies,

(i) calling for information from, undertaking inspection, conducting inquiries and audits of the stock exchanges, intermediaries and SROs,

(j) performing such functions and exercising such powers under the SCRA as may be delegated by the Central Government, (This was done in the interest of integrated regulation. Then all the powers under the SCRA were exercisable by Central Government. Until SEBI stabilizes, it was considered desirable that important powers are not transferred from Central Government, but delegated to SEBI.)

(k) levying fees or other charges for carrying the above purposes,

(l) conducting research for the above purposes and

(m) performing such other functions as may be prescribed.

The Board was empowered to delegate any of its powers and functions under the Act (except powers to make regulations) to any member, officer of the Board or any other person.

Autonomy and Accountability : The Central Government being accountable to Parliament, the SEBI Act granted powers of last resort to Central Government. It obligated SEBI, in exercise of its powers and performance of its functions, to be bound by the directions of the Central Government on questions of policy. Whether a question is one of policy or not shall be decided by the Central Government. Further, the Central Government was empowered to supersede the Board for a period not exceeding six months if it is of the opinion that the Board is unable to discharge the functions and the duties under the Act on account of grave emergency, or the Board has persistently defaulted in complying with any directions issued by the Central Government under the Act and as a result of such default the financial position or the administration of the Board has deteriorated, or the circumstances exist which render it necessary in the public interest to do so. The Board was obligated to furnish to the Central Government such returns and statements and such particulars in regard to any proposed or existing programme for the promotion and development of the securities market, as the Central Government may, from time to time, require. The Board was also obligated to submit to Central Government a report in the prescribed form giving a true and full account of its activities, policy and programmes during the previous year within 60 days (increased to 90 days by 1995 amendment) of the end of each financial year. A copy of this report shall be laid before each house of parliament. While the Act empowered Central Government to make rules for carrying out the purposes of the Act, it empowered SEBI to make regulations, with the previous approval of Central Government, consistent with the Act and the rules, to carry out the purposes of the Act. In order to ensure accountability, it was provided that all the rules and regulations made under the Act shall be laid before each house of parliament. It was also provided that any person aggrieved by an order of the Board under the Act may prefer an appeal to the Central Government. The Act empowered Central Government to exempt, in public interest, any person or class of persons dealing in securities from the requirements of registration.

In the interest of autonomy of SEBI, it was empowered to levy fees or other charges for carrying on the purposes of the Act. This power to levy fees has been upheld by the Supreme Court in the matter of *BSE Brokers' Forum and others* v. *SEBI and Others*.

It was provided that no court shall take cognisance of any offence punishable under the Act or any rules or regulations made thereunder except on a complaint made by the Board with the approval of Central Government. It was further provided that no suit, prosecution or other legal proceedings shall lie against central government or any officer of the Central Government or any member, officer or other employee of the Board for anything which is in good faith done or intended to be done under this Act or the rules or regulations made thereunder.

Amendments in SCRA : All the powers under the SCRA were exercised by Central Government. The SEBI Act, however, created a Board to regulate the securities market. In the interest of integrated regulation of securities market, it was felt that only one agency (SEBI) as far as possible, should regulate the securities market. In order to do so, the SEBI Act transferred some of the powers of the Central Government under the SCRA to SEBI and empowered Central Government to delegate other powers, except power to make rules, under the SCRA to SEBI. In exercise of this power, Central Government has delegated almost all the powers under the SCRA by notifications issued in 1992 and 1994. All the powers under the Securities Contracts (Regulation) Rules, 1957 have also been transferred to SEBI in 1996.

Trading of government securities was not subject to any regulatory framework as these were not 'securities' under the SCRA. In order to develop the market for government securities, the definition of 'securities' was amended to include government securities within its ambit so that the whole regulatory framework applicable to trading of securities could apply to trading government securities also. Further, in order to avoid frequent amendments, which is time consuming, the SCRA was amended to empower Central Government to declare any other similar instrument to be securities.

C. Securities Laws (Amendment) Act, 1995

In the light of experience gained with the working of the SEBI Act, 1992, it was considered desirable to expand the jurisdiction of SEBI, enhance its autonomy and empower it to take a variety of punitive actions in case of violations of the Act.

Composition of Board: As mentioned earlier, the SEBI Act made it obligatory for the central government to remove a member from the Board if he was appointed as a director of any company. This was presumably to ensure that a person would not be able to do justice to his roles as member of Board and as a member of board of directors of a company simultaneously. His interests as member of Board might clash with that of a director of a company. SEBI, being a quasi-judicial body, the members of the Board were not just expected to be impartial, they should also appear impartial. This was precluding the appointment of people with adequate knowledge and experience in the area of securities market to Board as many of them were also involved with corporate management in various capacities. The amendment Act deleted the provision relating to disqualification of a member of Board on his being appointed as a director of a company from the statute. It inserted a new provision to make it obligatory for a member of Board, who is director of any company and who has any direct or indirect pecuniary interest in any matter coming up for consideration at a meeting of the Board, to disclose the nature of interest and refrain from participating in the deliberations or decisions of the Board with respect to that matter. Now the government can appoint people of eminence with experience in matters relating to securities market to Board. This was expected to improve the decision making potential of SEBI and enable Board to lead and guide more effectively the team of professionals working for SEBI.

Jurisdiction of SEBI: The jurisdiction of SEBI was enlarged to register and regulate a few more intermediaries and other persons associated with the securities market. The amendment Act empowered SEBI to register and regulate the working of the intermediaries like depositories, custodians for securities and also certain other persons associated with the securities market like foreign institutional investors, credit rating agencies, venture capital funds etc. SEBI was also given blanket authority to regulate other intermediaries or persons, not named specifically in the statute, by specifying them through a notification. This obviated the need for amending SEBI Act every now and then to deal with a particular type of intermediary or a person associated with the securities market that may emerge in future.

Before the amendment Act, SEBI was being perceived as ineffective and toothless in protecting the interest of investors. This was essentially because SEBI did not have any power to control or regulate the issuers of securities. The SEBI Act listed all kinds of intermediaries to be registered and regulated by SEBI, but excluded the issuer of securities. As a result, SEBI could not directly regulate the issuers (Companies) on matters relating to issue and transfer of securities. In the absence of clear statutory mandate to SEBI to regulate issuers of securities which are governed by the Companies Act, 1956, SEBI was not able to compel the issuers to make adequate disclosures. It was rather directing its efforts only at the lead managers and merchant bankers who are intermediaries and signatories to prospectus requiring them to make adequate disclosures. Even this was being challenged in courts of law, as this was perceived beyond the jurisdiction of SEBI. This debilitating infirmity was done away with by the amendment Act which incorporated section 11A to SEBI's regulatory powers over corporates in the issuance of capital, transfer of securities and other related matters. SEBI can now specify by regulations the matters to be disclosed and the standards of disclosure required for the protection of investors in respect of issues made by bodies corporate.

Monetary Penalties : The SEBI Act originally provided for penalty of suspension and cancellation of a certificate of registration of an intermediary. Such suspension/cancellation led to cessation of business and affected innocent third parties, often adversely, who were dealing with the intermediary. Besides there were many persons other than intermediaries associated with the securities market on whom the penalty of suspension/cancellation had no bearing. In order to tackle this, the amendment Act provided for monetary penalties as an alternative mechanism to deal with capital market violations.

SEBI was empowered to adjudicate a wide range of violations and impose monetary penalties on any intermediary or other participants in the securities market. The amendment Act listed out a wide range of violations along with maximum penalties leviable. It provided for a highest penalty of Rs.10 lakh and the violations listed were failure to submit any document, information or furnish any return, failure to maintain required books of accounts or records, carrying on any CIS without registration, failure to enter into agreement with clients, insider trading, failure to redress the grievances of investors, failure to issue contract notes, charging excessive brokerage by brokers, failure to disclose substantial acquisition of shares and take-overs, etc. The amendment Act provided for three types of monetary penalties viz., - (a) a lump sum penalty for a specific violation of the Act, (b) a penalty for every day during which the violation continued, and (c) a multiple of the amount involved in the violation. The amount of penalty was determined, subject to the ceiling, by the adjudicating officer who would be guided by the factors including amount of disproportionate gain or unfair advantage wherever quantifiable made as a result of the default, the amount of loss caused to an investor or any group of investors as a result of default, and the repetitive nature of the default. It amended section 24 to provide that non-payment of penalty would be an offence punishable with fine or imprisonment under the Act.

The adjudicating officer is required to be appointed by SEBI. He shall not be an officer below the rank of a division chief of SEBI. He will hold an enquiry after giving a person reasonable opportunity of being heard for the purpose of determining if any violation has taken place and imposing penalty. To ensure fair enquiry and penalty, it was provided that appeal against the orders of adjudicating officers would lie to the SAT, which was also constituted by the amendment Act.

While the suspension or cancellation of registration continued to be regulated by regulations framed by SEBI and the appeal from the orders of the Board suspending or canceling a registration would lie to Central Government, the amendment Act provided that the monetary penalties would be imposed only in cases of violations listed in the Act by an adjudicating officer as per the Rules prescribed by the Central Government. Appeals from the orders of an adjudicating officer can be preferred to the SAT. The appeals against the orders of SAT can be preferred to the High Court.

Empowerment : The amendment Act inserted section 11B to empower SEBI to issue directions to all intermediaries and other persons associated with the securities market (i) in the interest of investors, (ii) in the interest of orderly development of the securities market, (iii) to prevent the affairs of any intermediary including a mutual fund from being conducted in a manner detrimental to the interest of investors or of the securities market, or (iv) to secure the proper management of any such entity. The Act also empowered SEBI to call for and furnish to any agency such information as necessary for efficient discharge of its functions. It vested SEBI with powers of a civil court under the Code of Civil Procedure, 1908 in respect of the following: (i) summon and enforce attendance of person and examine them on oath, (ii) inspect any books, register and other documents, (iii) discover and enforce production of books of accounts and other documents. These helped SEBI considerably to carry out investigations, conduct inquires and inspections and levy fines against the erring intermediaries, issuers of securities and other persons associated with the securities market. SEBI was also empowered to call for information and conduct enquiries, audits and inspection of mutual funds, and other persons associated with the securities market, in addition to stock exchanges, self regulatory organizations and intermediaries provided earlier.

Autonomy of SEBI: The autonomy of SEBI was reinforced by the following provisions: (i) SEBI was vested with the powers of a civil court; (ii) Section 20A barred the jurisdiction of civil court in respect of actions or orders passed by SEBI. One can, however, prefer an appeal to the Central Government against the orders of SEBI and the jurisdiction of the High Court was not barred. This made SEBI's functioning independent of the lower civil courts and allowed quick disposal of cases by SEBI without being hamstrung by stay orders from civil courts; (iii) Section 23 was amended to extend the immunity from suit, prosecution or other legal proceedings to SEBI or any of its members, officers or employees in respect of action taken in good faith; (iv) Section 26 was amended to permit SEBI to file complaints in Courts under section 24 in respect of offences under the SEBI Act without previous sanction of the Central Government which was mandatory then even for filing routine prosecutions; (v) By amendment to section 28, the power of last resort of the Central Government to exempt any person or class of persons dealing with securities market from the requirement of registration with SEBI was withdrawn; (vi) Sections 29 and 30 were amended to amended to provide that the conditions for grant of registration would be determined by Regulations and not by Rules; (vii) Section 30 was amended to provide that the SEBI can notify regulations without approval of the Central Government. These enabled SEBI to respond speedily to changing market conditions and enhanced its autonomy.

SEBI was armed with better weapons to regulate various participants in the securities market. The amendment Act provided that henceforth the conditions of registration shall be determined by Regulations and not under Rules as used to be before the amendment. The enactment of Rules under the Act is the prerogative of the Central Government and is a very time consuming process in contrast to Regulations which required only prior approval of Central Government. By this amendment, the requirement of prior approval was dispensed and the regulation making was brought within the exclusive domain of SEBI. This enabled SEBI to expeditiously notify and modify regulations to keep pace with rapidly changing market conditions, facilitate maintenance of market discipline, prudence and transparency and thereby strike on time.

Securities Appellate Tribunal : An efficient and effective system of regulation calls not only for firmness, but also for fairness. The amendment Act provided for establishment of one or more SATs to hear the appeals from the orders of the adjudicating officers. Anybody not satisfied with the orders of the SAT can prefer an appeal to the High Court. This ensured fairness in the process of adjudication.

Amendments in SCRA: The amendment Act also amended SCRA. In the last few years there has been substantial improvements in the functioning of the securities market. However there were inadequate advanced risk management tools. In order to provide such tools and to deepen and strengthen the cash market, a need was felt for trading of derivatives like futures and options. But it was not possible in view of prohibitions in the SCRA. Its preamble stated that the Act was to prevent undesirable transactions in securities by regulating business of dealing therein, by prohibiting options, etc. Section 20 of the Act explicitly prohibited all options in securities. Section 16 of the Act empowered Central Government to prohibit by notification any type of transaction in any security. In exercise of this power, government by its notification in 1969 prohibited all forward trading in securities. Introduction of trading in derivatives required withdrawal of these prohibitions. The amendment Act withdrew the prohibitions by repealing section 20 of the SCRA and amending its preamble.

Traditionally the operations of the stock exchanges were limited to the area earmarked at the time of its recognition. This prevented an exchange from expanding its operations beyond the area, though it was considered desirable to introduce competition among the exchanges and technology permitted such expansion. The SCRA was amended to allow an exchange to establish additional trading floor outside its area of operation with approval of SEBI.

The SCRA, before the amendment, provided that SEBI could compel a company to list its securities on any stock exchange. Such coercion from authorities was not considered desirable in the liberalised market environment. This provision was removed from the SCRA.

The exchanges enter into listing agreements with the listed companies. The agreement casts a lot of obligations on the listed companies in the interest of investors. However, this agreement was not having any statutory backing. As a result, in cases of non-compliance with listing agreement, the exchanges used to suspend / withdraw trading of the security, which was not in the interest of investors. In order to provide statutory backing to listing agreement, which is being increasingly used to improve corporate governance, it was prescribed that where securities were listed on the application of any person, such person shall comply with the conditions of listing with the stock exchange.

The rules made under the SCRA used to be published before formal notification. Though this practice helped to consult the regulated and the public on the proposed rules, it was time consuming and the regulated could derive regulatory arbitrage before the new rule came to effect. The Amendment Act did away with the requirement of previous publication.

D. The Depositories Act, 1996

The system of transfer of ownership of securities prevailing till mid 1990s was grossly inefficient as every transfer was required to be accomplished by the physical movement of paper securities to the issuer for registration and the ownership was evidenced by the endorsement on the security certificate. The process of transfer in many cases took much longer time than two months stipulated in the Companies Act, 1956 or the SCRA. A significant proportion of transactions ended up as ' bad delivery' due to faulty compliance of paper work, mismatch of signatures on transfer deeds with the specimen records of the issuer or for other procedural reasons. Theft, forgery, mutilation of certificates and other irregularities were rampant. The inherent right of the issuer to refuse the transfer of a security added to the misery of the investors. The cumbersome paraphernelia associated with the transfer of securities under section 108 of the Companies Act, 1956, along with huge paper work, printing of stationary, safe custody of securities, transportation and dispatch added to the cost of servicing paper securities, delay in settlement and restricted liquidity in securities and made investor grievance redressal time consuming and at times intractable. All these problems had not surfaced overnight but these were compounded by burgeoning trade volumes in secondary market and increasing dependence on securities market for financing trade and industry. This underscored the need for streamlining the transfer of ownership of securities which was sought to be accomplished by the Depositories Act, 1996. The Act provides a legal basis for establishment of depositories in securities with the objective of ensuring free transferability of securities with speed, accuracy and security by

(a) making the securities of public limited companies freely transferable; (b) dematerializing the securities in the depository mode; and (c) providing for maintenance of ownership records in a book entry form.

Legal Basis : The Depositories Act, 1996, read with section 12 of the SEBI Act, 1992, provides a legal basis for establishment of multiple depositories and entrusts them with responsibility of maintaining ownership records of securities and effecting transfer of securities through book entry only. The depositories render, through participants, any service connected with recording of:

(a) allotment of securities; and

(b) transfer of ownership of securities.

By fiction of law under section 10 of the Depositories Act, the depository is deemed to be registered owner of securities with the limited purpose of effecting transfer of ownership of security. In respect of securities held in a depository, the name of the depository appears in the records of the issuer as registered owner of securities. The depository has right to effect the transfer of securities and shall not have any other right associated with them. The owners of the securities become beneficial owners on the records of the depository in respect of the securities held in a depository. The beneficial owner has all the rights and liabilities associated with the securities. The depositories holding the securities maintain ownership records in the name of the each participant. Each such participant, as an agent of the depository, in turn, maintains ownership records of every beneficial owner in book entry form. The depository and participants have a principal and agent relationship and their relations are governed by the bye-laws of the depository and the agreement between them.

Both the depository and participant need to be registered with SEBI under section 12 of the SEBI Act, 1992, and are regulated by SEBI. Only a company formed and registered under the Companies Act, 1956 can be registered as a depository. However, before commencing business, the depository registered with SEBI has to obtain a certificate of commencement of business from SEBI. Such certificate is issued by SEBI on being fully satisfied that the depository has adequate systems and safeguards to ensure against manipulation of records and transactions. SEBI is empowered to suspend or cancel the certificate of registration of a depository as well as of the participants after giving a reasonable opportunity of hearing.

The ownership records of securities maintained by depositories/participants, whether maintained in the form of books or machine readable form, shall be accepted as prima facie evidence in legal proceedings. The depository is treated as if it were a bank under the Bankers' Books of Evidence Act, 1891.

The depository services shall be available in respect of the securities as may be specified by SEBI. The type of securities and the eligibility criteria for admission to the depository mode shall be determined by SEBI regulations. This provides the flexibility to SEBI, for example, to admit certain instruments like units of mutual funds and prohibit admission of certain securities like shares of private limited companies from depository mode.

Free Transferability of Securities : The securities of all public companies have been made freely transferable. The Act took away the companies' right to use discretion in effecting transfer of securities by deleting section 22A from the SCRA and by inserting section 111A in the Companies Act, 1956. These provisions, read with section 7 of the Depositories Act make the transfer of securities in any company, whether listed or not, other than a private company and a deemed public company, free and automatic. That is, once the agreed consideration is paid and the purchase transaction is settled, the buyer is automatically entitled to all the rights associated with the security. As soon as the intimation regarding delivery of security against the payment of cash (delivery v. payment) is received, the transfer will be effected by the depository or company and the transferee will enjoy all the rights and obligations associated with the security immediately. If the securities are in the depository mode, depository would effect the transfer on the basis of intimation (contract notes or some other suitable evidence) from the participants. If the securities are outside the depository mode, the company would effect the transfer on receipt of the transfer deed. For the securities in the depository mode, no transfer deed is required and other procedural requirements under section 108 of the Companies Act were dispensed with. The transferee in both the modes would be entitled to all the rights including voting rights and obligations associated with security.

However, if it is felt that the transfer of a security is in contravention of any of the provisions of the SEBI Act, 1992 or Regulations made thereunder or Sick Industrial Companies (Special Provisions) Act (SICA), 1985, the company, depository, participant, investor or SEBI can make an application to the Company Law Board (CLB) to determine if the alleged contravention has taken place. After enquiry, if the CLB is satisfied of the contravention, it can direct the company/ depository to make rectification in ownership records. In other words, transfer has to be effected immediately even if the transfer is contravention of SEBI Act, 1992 or SICA, 1985, subject to subsequent rectification by the direction of CLB. Pending the completion of enquiry, CLB can suspend voting rights in respect of securities so transferred. The transferee will continue to enjoy economic rights (bonus, dividend, rights etc) which cannot be suspended under any circumstances. During the pendency of the application with CLB, the transferee can transfer the securities and such further transfer will entitle the transferee to the voting rights also unless the voting rights in respect of transferee has also been suspended.

Partial Dematerialisation of Securities : Section 9 of the Depositories Act provides that the securities held by a depository shall be dematerialized and be fungible. The Act envisages dematerialization of securities in the depository mode as against immobilization of securities. The later refers to a situation when the depositories hold securities in physical form side by side with ownership records. In such a case physical movement of securities does not accompany the transfers but securities are in existence in the custody of the depository. What the Act envisages is that ownership of securities shall be reflected through book entry system and this will not require existence of securities certificates. However, the securities outside the depository would be represented by physical security certificate. Hence, the depository mode envisaged is one of the partial dematerialization, that is, a portion of securities is dematerialized and the other portion remains in physical form.

Supremacy of Investor : The investor has been given the option between holding physical securities as at present or opting for a depository based ownership records. At the time of fresh issue, the issuer is under obligation to give the option to the investors either to seek physical securities under the existing paper based system (non-depository mode) or opt for book entry system of recording ownership (depository mode). The decision on whether or not to hold securities within the depository mode, if in depository mode, which depository or participant, would be entirely with the investor. Such freedom can be exercised either at the time of the initial offer of the security by indicating his choice in the application form or at any subsequent time. He will also have the freedom to switch from depository mode to non-depository mode and vice versa.

At the time of initial offer, if the investor opts to hold a security in the depository mode, the issuer shall be intimate concerned depository the details of allotment of securities and record the depository as registered owner of the securities. On receipt of such information, the depository shall enter in its records the names of allottees as the beneficial owners.

An investor who holds physical securities and seeks to avail the services of a depository will surrender the certificates to the issuer. The issuer on receipt of certificates shall cancel them and substitute in its records the name of the depository as a registered owner in respect of that security and inform the depository accordingly. The depository shall thereafter enter the name of the investor in its records as beneficial owner.

If a beneficial owner or a transferee of securities seeks to opt out of a depository in respect of any security, he shall inform the depository of his intention. The depository in turn shall make appropriate entries in its records and shall inform the issuer. The issuer shall make arrangements for the issue of certificate of securities to the investor.

The depository shall record all transfers made within the depository mode on receipt of intimation from a participant. The type of intimation would be specified by SEBI regulations.

An investor, before availing the services of a depository, shall enter into an agreement with a depository through a participant. The participant is also required to enter into an agreement with the depository to act as the latter's agent. There will also be an agreement between the depository and the issuer of securities. The rights and obligations of depositories, participants, issuers and investors would be governed by the agreement among them, the bye-laws of the depository and the regulations of SEBI.

Amendments in Other Acts : To provide for the smooth operation of the depositories, the Depositories Act amended a few other Acts such as the Indian Stamps Act, 1989, the Companies Act, 1956, the Securities Contracts (Regulation) Act, 1956, the Income-tax Act, 1961, the Benami Transactions (Prohibition) Act, 1988 and the Securities and Exchange Board of India Act, 1992. The major amendments in these Acts are discussed below:

Amendment to the Indian Stamps Act : Section 8A was inserted in the Indian Stamps Act to provide for the following:

(i) At the time of issue of securities, shares or otherwise, the issuer shall pay the Stamp duty on the total amount of the security issued by it, whether through a depository or direct to investors, even though there will be no physical securities (instrument) which can be stamped (executed).

(ii) Entry into depository involves change of registered ownership as the investor becomes the beneficial owner and the depository becomes the registered owner in respect of the security. As it involves change in registered ownership, it attracts stamp duty under the existing provisions. The new section 8A, however, exempted such change of registered ownership of shares from an investor to a depository from the stamp duty.

(iii) All transactions of securities involving change in registered ownership and/or beneficial ownership of shares within the depository mode shall not attract any stamp duty.

(iv) If an investor opts to exit from the depository and seeks the issue of physical certificate of securities from the issuer, the issue of such certificates shall attract stamp duty as is payable on the issue of duplicate certificates.

(v) All transactions outside the depository mode shall attract stamp duty as at present.

Amendments to the Income Tax Act : Sub-section 2A was inserted in section 45 to provide that the depositories as well as the participants would not be liable to pay any capital gains tax in respect of profits or gains arising from transfer securities held in depositories and transacted from time to time since these securities are held on behalf of the beneficial owners. In other words, inter-se transfer of securities between the participants in the books of a depository as well as between the depositories in the records of an issuer shall not be treated as transfer unless it involves change in beneficial ownership. If it involves any change in the beneficial ownership, only the beneficial owner shall be chargeable to capital gains tax, not the registered owner.

Due to fungible characteristic of the securities, while calculating capital gains tax, the cost of acquisition of securities shall not be determined with reference to cost of acquisition of specific identifiable securities, but be ascertained on the principle of first in first out. That is, the securities acquired first by the beneficial owner would be deemed to have been transferred first irrespective of the intention of the investor. This principle would be applicable only in respect of securities held in a depository.

Amendment to the Companies Act : Section 83 of the Companies Act was deleted. This did away with the mandatory requirement of each company limited by shares to distinguish the shares by distinguishing numbers, in order to introduce the concept of fungibility. The abolition of section 83, however, did not prohibit a company from having distinct numbers, although there was no mandatory requirement to that effect.

Section 108 was amended to provide that the provisions of section 108 shall apply to transfer of securities effected outside the depository mode. The provisions of section 108 shall not apply to transfers of securities effected within the depository mode.

Section 111 was amended to provide that the provisions of section 111 shall apply to a private company and a deemed public company. The new section 111A was inserted to govern the transfer of securities of a public limited company. The shares or debentures and any interest therein of a company were made freely transferable and all the rights and obligations associated with them immediately accrue to the transferee. However, if the transfer violates any of the provisions of the SEBI Act, 1992 or SICA, 1985, the depository, company, participant, investor or SEBI can make an application to the CLB. The CLB, pending completion of enquiry may make an interim order to suspend the voting rights in respect of those securities, and on completion of the enquiry, may direct the company or depository to rectify the register or records if transfer is in violation of the aforesaid provisions. During the pendency of the application with CLB, the economic rights accrue to the transferee and the transferee has a right to transfer the securities further and such further transferee shall be entitled to voting rights also.

E. The Depository Related Laws (Amendment) Act, 1997

While amending the Depositories Act, 1996, this amendment Act amended the Companies Act, 1956, the Indian Stamp Act, 1899, the State Bank of India Act, 1955, the State Bank of India (Subsidiary Banks) Act, 1959, the Industrial Development Bank of India Act, 1964, the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1970, and the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1980 to facilitate dematerialization of securities. The Act amended the Depositories Act to provide that the provision of the Companies Act relating to securities held in trust shall not apply to a depository in respect of such securities, even though the depository is the registered owner of the securities. It restored section 83 in the Companies Act relating to distinct numbers for securities. However, the securities held in a depository may not have distinct numbers. It amended section 111A to restrict free transferability of securities provided originally in the Depositories Act, 1996. It provided that if a company refuses to register securities within 2 months, the transferee can appeal before the CLB for registration of securities in his favour. It also provided that if the transfer is in violation of any law for the time being in force, the depository, depository participant, company, SEBI or investor may apply to CLB within 2 months for rectification of register or records. It amended the Indian Stamp Act to exempt stamp duty on transfer of beneficial ownership of units of mutual funds dealt with by a depository. (Subsequently the stamp duty was exempted on transfer of beneficial ownership of debt securities.)

F. Securities Laws (Amendment) Act, 1999

This Act has inserted provisions relating to derivatives, units of CIS and delegation of powers under the SCRA to RBI.

Derivatives : Despite withdrawal of prohibitions on derivatives by the Securities Laws (Amendment) Act, 1995, the market for derivatives, however, did not take off, as there was no regulatory framework to govern trading of derivatives. SEBI set up a 24 member Committee under the Chairmanship of Dr. L. C. Gupta on 18th November 1996 to develop appropriate regulatory framework for derivatives trading in India. The Committee submitted its report on March 17, 1998 recommending among others, that the derivatives may be declared as securities under section 2(h) (ii)(a) of the SCRA, so that the regulatory framework applicable to trading of securities could govern trading of derivatives also. Section 2 (h) of the SCRA, which provides an inclusive definition of 'securities', empowers Central Government to declare "such other" instruments as "securities". Government, however, did not declare derivatives to be securities, rather amended the SCRA, to explicitly define securities to include derivatives, probably because it's power to declare any instruments as "securities" was limited by the words "such other".

The Securities Contracts (Regulation) Amendment Bill, 1998 was introduced in the Lok Sabha on 4th July 1998 proposing to expand the definition of "securities" to include derivatives within its ambit so that trading in derivatives could be introduced and regulated under the SCRA. The Bill was referred to the Standing Committee on Finance (SCF) on 10th July 1998 for examination and report thereon. The Committee submitted its report on 17th March 1999. The committee was of the opinion that the introduction of derivatives, if implemented with proper safeguards and risk containment measures, will certainly give a fillip to the sagging market, result in enhanced investment activity and instill greater confidence among the investors/participants. The Committee after having examined the Bill and being convinced of the needs and objectives of the Bill approved the same for enactment by Parliament with certain modifications. The Bill, however, lapsed following the dissolution of 12th Lok Sabha. A fresh bill, the Securities Laws (Amendment) Bill 1999 was introduced in the Lok Sabha on 28th October 1999 incorporating the amendments proposed in the Securities Contracts Regulation (Amendment) Bill, 1998 as well as the modifications suggested by the SCF. This Bill was converted into an Act on 16th December 1999.

The Act inserted clause (aa) in section 2 to define derivatives to include: (a) a security derived from a debt instrument, share, loan whether secured or unsecured, risk instrument or contract for differences or any other form of security, and (b) a contract which derives its value from the prices, or index of prices, of underlying securities. It also inserted sub-clause (ia) in section 2 (h) to include derivatives within the ambit of securities. Since derivative contracts are generally cash settled, these may be classified as wagers. The trading in wagers being null and void under section 30 of the Indian Contracts Act 1872, it may be difficult to enforce derivatives contracts. In order to avoid such legal uncertainties, a new section 18A was inserted to provide that notwithstanding anything contained in any other law for the time being in force, contracts in derivatives shall be legal and valid if such contracts are traded on a recognised stock exchange and settled on its clearing house in accordance with rules and bye-laws of such stock exchange. Section 23 was amended to provide that any body who enters into contract in contravention of section 18A shall be punishable.

By a notification issued on 1st March 2000, Government lifted the three-decade-old prohibition on forward trading in securities by rescinding 1969 notification. This prohibition was imposed by government in exercise of its powers under section 16 of the SCRA by a notification issued on 27th June 1969 in order to curb certain unhealthy trends that had developed in the securities market at that time and to prevent undesirable speculation. In the changed financial environment, the relevance of this prohibition had vastly reduced. Through appropriate amendments in the byelaws of the stock exchanges, carry forward transactions in securities were permitted. Similarly, periodic amendments to the aforesaid notification were made to permit repo transactions in government securities by authorised intermediaries. Even though the notification of 1969 was in force, exceptions had been carved out in course of time as market needs changed and some form of forward trading (carry forward/ready forward) was prevalent.

The provisions in the SCRA and the regulatory framework developed thereunder govern the trading in securities. The amendments of the SCRA to include derivatives within the ambit of "securities" in the SCRA made trading in derivatives possible within the framework of that Act.

Collective Investment Scheme : During mid 1990s, many companies especially plantation companies had been raising capital from investors through schemes, which were in the form of CIS. Though SEBI is authorised under the SEBI Act, 1992 to register and regulate CIS, there was no suitable regulatory framework to allow an orderly development of market for units/instruments by them. Since SEBI's jurisdiction is limited to protect the interests of investors in securities, it could not take steps to protect the interests of investors in CIS units which were not securities. In order to allow for this and to strengthen the hands of SEBI to protect interests of investors in plantation companies, the Act amended the definition of "securities" to include within its ambit the units or any other instruments issued by any CIS to the investors in such schemes. The Act empowered the Central Government to make rules to provide for the requirements, which shall be complied with by CIS for the purpose of getting their units listed on any stock exchange. Such rules have been incorporated in the Securities Contracts (Regulation) Rules. This is aimed at an orderly development of market for these units while protecting the interest of investors therein. The Act also inserted a definition of the CIS in the SEBI Act, 1992. The CIS was defined to mean any scheme or arrangement made or offered by any company under which (a) the contributions, or payments made by the investors, by whatever name called, are pooled and utilised solely for the purposes of the scheme or arrangement; (b) the contributions or payments are made to such scheme or arrangement by the investors with a view to receive profits, income, produce or property whether movable or immovable from such scheme or arrangement; (c) the property, contribution or investment forming part of scheme or arrangement, whether identifiable or not, is managed on behalf of the investors; and (d) the investors do not have day to day control over the management and operation of the scheme or arrangement. The CIS, however, does not include any scheme or arrangement (a) made or offered by a cooperative society, (b) under which deposits are accepted by non banking financial companies, (c) being a contract of insurance, (d) providing for any Scheme, Pension Scheme or the Insurance Scheme framed under the Employees Provident Fund and Miscellaneous Provision Act, 1952, (e) under which deposits are accepted under section 58A of the Companies Act, 1956, (f) under which deposits are accepted by a company declared as Nidhi or mutual benefit society under section 620A of the Companies Act, 1956, (g) falling within the meaning of Chit business as defined in clause (d) of section 2 of the Chit Fund Act, 1982 and (h) under which contributions made are in the nature of subscriptions to a mutual fund.

Delegation of Powers to RBI : The Government had power to delegate regulatory authority to SEBI. To provide additional flexibility, the Act amended section 29A of the SCRA so as to empower the Central Government to delegate powers to RBI also along with SEBI, to enable the former to regulate transactions under the SCRA as may be necessary. Now the Central Government, SEBI, and the RBI depending on their jurisdiction as may be mutually agreed upon can exercise the powers under the Act.

With the repeal of the 1969 notification in 2000, the then prevailing regulatory framework, which governed repo transactions, disappeared. It was, therefore, necessary to work out an arrangement whereby the regulators could regulate such transactions. In pursuance to this and in exercise of its newly acquired power, Central Government issued a notification on 2nd March 2000 delineating the areas of responsibility between RBI and SEBI. In terms of this notification, the powers exercisable by Central Government under section 16 of the SCRA in relation to the contracts in government securities, gold related securities, money market securities and in securities derived from these securities and in relation to ready forward contracts in bonds, debentures, debenture stock, securitised debt and other debt securities shall also be exercised by RBI. Such contracts, if executed on stock exchanges, shall, however, be regulated by (i) the rules and regulations or the byelaws made under the SCRA, or the SEBI Act or the directions issued by SEBI under these Acts, (ii) the provisions contained in the notifications issued by RBI under the SCRA, and (iii) the rules or regulations or directions issued by RBI under the RBI Act, 1934, the Banking Regulations Act, 1949 or the Foreign Exchange Regulation Act, 1973.

RBI and SEBI have also issued consequential notifications on 2nd March 2000 specifying the regulatory framework in their respective areas. In terms of RBI notification, no person can enter into any (a) contract for the sale or purchase of government securities, gold related securities and money market securities other than spot delivery contract or such other contracts traded on a recognised stock exchange as is permissible under the SCRA, rules and byelaws of such stock exchange, and (b) ready forward contracts in bonds, debentures, debentures stock, securities debt, and other debt securities. Ready forward contracts may, however, be entered into by permitted persons in all government securities put through the Subsidiary General Ledger Account held with RBI in accordance with terms and conditions as may be specified by RBI. SEBI by its notification has prohibited all contracts in securities other than such spot delivery contract or contract for cash or hand delivery or special delivery or contract in derivatives as is permissible under the SCRA or the SEBI Act and rules and regulations made thereunder and rules, regulations and byelaws of a recognised stock exchange.

G. The Securities Laws (Second Amendment) Act, 1999

The SCRA provided the right of appeal before the Central Government against refusal, omission or failure by a stock exchange to list the securities of any public company. The SEBI Act, 1992 provided for two kinds of appeals. Under section 20 of the Act, any person aggrieved by any order of the SEBI under the Act or rules or regulations made thereunder, may prefer an appeal to the Central Government. Accordingly, the Central Government had notified the SEBI (Appeal to the Central Government) Rules, 1993 and constituted an Appellate Authority for disposal of appeals. Section 15K of the Act provided for establishment of one or more SATs to hear appeals from orders of adjudicating officer of SEBI imposing monetary penalty as per Rules framed by the Central Government. Government has accordingly established a SAT at Mumbai to hear appeals from the orders of adjudicating officers. Under section 23 of the Depositories Act, 1996, any person aggrieved by an order of SEBI under the Depositories Act 1996 or Rules and Regulations made thereunder may prefer an appeal to the Central Government. Accordingly, the Central Government had notified the Depositories (Appeal to the Central Government) Rules, 1998 and constituted an Appellate Authority for disposal of appeals. Thus the Central Government was conferred with powers to dispose of appeals in respect of all matters (except disposal of appeals against the orders of adjudicating officer under the SEBI Act, 1992) under all the three Acts.

In addition, the Central Government was empowered to issue directions to SEBI and make rules under these Acts. It was empowered to approve / amend / make rules / byelaws / regulations of the stock exchanges. Further, Central Government was represented on the management of SEBI as well as of the stock exchanges. The powers of the Central Government to issue directions and to make rules and appoint members of the SEBI as well as all governing bodies of the stock exchanges were perceived as compromising on its appellate powers. The Appellate Authorities appointed by the government under the SEBI Act and the Depositories Act had been receiving and disposing of appeals in accordance with the Rules. However, since government constituted these, their orders were perceived at times as orders of the government. When an order of SEBI was struck down, even on merits, there was a feeling that SEBI's autonomy as the regulator has been compromised. In order to remove such misgivings and impart transparency and impartiality to the process of disposal of appeals and to make the administration of penal provisions in the securities laws by the regulators more accountable and impartial, the Securities Laws (Second Amendment) Act 1999 amended all the three Acts to transfer appellate functions from the Central Government to an independent body, SAT.

The Amendment Act freezed section 22 of the SCRA and inserted a new section 22A to provide for right of appeal before SAT against refusal, omission or failure by a stock exchange to list the securities of any public company within 15 days of such refusal, omission or failure. An obligation was cast on SAT to dispose off appeals as expeditiously as possible, and to endeavour to dispose of finally within six months. Section 23 was amended to provide penalty for failure to comply with orders of SAT. Similar amendments were effected in the SEBI Act, 1992 and the Depositories Act 1996. Section 15K of the SEBI Act was amended to expand jurisdiction of SAT to deal with appeals also under any other law. Section 15T was amended to empower SAT to deal with appeals from any person aggrieved by an order of SEBI as well as of an adjudicating officer under the SEBI Act. Section 20 of the SEBI Act, which provided for appeals to Central Government, was freezed. Section 23 of the Depositories Act, 1996, which provided for appeals to the Central Government, was also freezed. A new section 23A was inserted to provide for appeals to SAT under the Act. Hence, all appeals, namely the appeals against the orders of SEBI under the SEBI Act and the Depositories Act, appeals against the orders of the adjudicating officers under the SEBI Act, and appeals against refusal of stock exchanges to list securities were allowed to be preferred to SAT. It was further provided that any person aggrieved by the order of SAT may prefer appeal to High Court within 60 days.

Provisions were made in all three Acts to provide for appearance of the appellant in person or through one or more chartered accountants or company secretaries or cost accountants or legal practitioners or any of its officers before a SAT.

Central government was empowered to make rules to provide for the form in which an appeal may be filed before the SAT and the fees payable in respect of such appeals. Consequently, the SEBI (Appeal to the Central Government) Rules, 1993 and the Depositories (Appeal to the Central Government) Rules, 1998 were repealed. Government notified on 18th February 2000 three Appeal Rules, Viz. (a) Securities Appellate Tribunal (Procedure) Rules, 2000 under the SEBI Act, 1992, (b) The Depositories (Appeal to Securities Appellate Tribunal) Rules, 2000 under the Depositories Act, 1996, and (c) The Securities Contracts (Regulation) (Appeal to Securities Appellate Tribunal) Rules, 2000 under the SCRA. These rules provide for fees, form and procedure for filing appeal and the process of their disposal by the SAT. The appeals (except appeals against adjudication orders under the SEBI Act) under all three Acts need to be accompanied by a fee of Rs. 5,000/- only. The appeals against the adjudication orders need to be accompanied by a fee of Rs. 500/- if the penalty imposed is less than Rs.10,000/-, Rs.1,200/- if the penalty imposed is more than Rs. 10,000/- but less than Rs. 1,00,000/- and an additional Rs. 1,000/- for every additional one lakh of penalty or fraction thereof.

H. SEBI (Amendment) Act, 2002

While responding to a calling attention motion in early March, 2001 by the leader of the opposition on extreme volatility in the stock markets, Finance Minister had proposed legislative changes to further strengthen the provisions in the SEBI Act, 1992 to ensure investor protection. In pursuance to this, the SEBI (Amendment) Act, 2002 was enacted to make provisions to (i) strengthen the Securities Appellate Tribunal (SAT) and the SEBI in terms of organisational structure and institutional capacity, (ii) enhance powers of SEBI substantially, particularly in respect of inspection, investigation and enforcement, and (iii) strengthen penal framework by prescribing a few more offences in the SEBI Act and enhancing the monetary penalties for various offences.

Strengthening Organisations : Before the Amendment Act, 2002, SEBI consisted of a Chairman and five other members to be appointed by the Central Government. Of the five members, three represented Ministry of Finance, Ministry of Law and the RBI. In view of the growing importance of the securities markets in the economy and the responsibilities of the SEBI under the SEBI Act, it was necessary to strengthen it further. The Amendment Act strengthened it by increasing the number of members from five to eight, providing for at least three whole time members and substituting the representation of the Ministry of Law by the Ministry dealing with administration of the Companies Act, 1956. SEBI would now benefit from the expertise of three additional members, full time attention of at least three additional members, and the representation of the Department of Company Affairs whose operations have bearing on the working of the securities market.

The SEBI Act provides for establishment of one or more SATs to hear appeals against the orders of SEBI. Prior to this amendment, the SAT consisted of one person called the Presiding Officer. Since it hears appeals against the orders of SEBI which is a very high powered statutory body and which is strengthened further by this amendment, and in the interests of objectivity and potential work load, it was necessary to strengthen the SAT. The Amendment Act converted the SAT to a three member body consisting of a presiding officer and two other members to be appointed by the Central Government. It enhanced the level of the SAT by prescribing higher eligibility criteria for appointment of the presiding officer and the members. It provided that only a sitting or retired judge of the Supreme Court or a sitting or retired Chief Justice of a High Court would be eligible to be appointed as presiding officer of the SAT and such appointment shall be made in consultation with the Chief Justice of India or his nominee. The presiding officer will hold the office for a term of five years or until he attains the age of sixty eight years, whichever is earlier. It further provided that a person shall be qualified for appointment as member of the SAT if he is a person of ability, integrity and standing, who has shown capacity in dealing with problems relating to securities market and has qualification and experience of corporate law, securities laws, finance, economics or accountancy. A member of SAT can hold office for a term of five years or until he attains the age of sixty two years, whichever is earlier. A member of SEBI or a senior officer of SEBI at the level Executive Director shall not be eligible to be appointed as a member or Presiding Officer of the SAT during the tenure of his office with the SEBI or within two years from the date on which he ceases to hold such office. This will avoid conflict of interest in the sense that an official of SEBI responsible for a particular order should not uphold the order as a member of the SAT. Any person aggrieved by any decision or order of the SAT can prefer an appeal before the Supreme Court (it was High Court earlier) only on a question of law.

Empowering SEBI : The Amendment Act conferred on SEBI a lot of additional powers to deal with any kind of market misconduct and protect the investors in securities. For example, it can now prevent issue of any offer document if it has any misgivings about the antecedents of promoters / companies concerned. Under the amended provisions, SEBI can now:

(i) call for information and record from any bank or any other authority or board or corporation established or constituted by or under any Central, State or Provincial Act in respect of transactions in securities which are under investigation or enquiry by SEBI;

(ii) conduct inspection of any book or register or other document or record of any listed public company; If, however, the said company is not a registered intermediary, SEBI can inspect only if it has reasonable grounds to believe that such company has been indulging in insider trading or fraudulent and unfair trade practices relating to securities market.

(iii) issue commissions for examination of witnesses or documents while exercising powers to call for information or conduct inspection;

(iv) take any of the following measures in the interest of investors or securities market, either pending investigation or inquiry or on completion of such investigation or inquiry, but after giving an opportunity of hearing -

(a) suspend trading of a security in a recognised stock exchange;

(b) restrain persons from accessing the securities market and prohibit any person associated with securities market from buying, selling or dealing in securities;

(c) suspend any office bearer of a stock exchange or self-regulatory organisation from holding such position;

(d) impound and retain the proceeds or securities in respect of any transaction which is under investigation;

(e) attach for a period not exceeding one month, with the prior approval of a magistrate, one or more bank accounts of any intermediary or any person associated with the securities market in any manner involved in violation of any of the provisions of the Act or rules or regulations made thereunder; and

(f) direct any intermediary or any person associated with the securities market in any manner not to dispose of or alienate an asset forming part of any transaction which is under investigation.

In case of a listed public company, which is not a registered intermediary, the SEBI can exercise its powers of impounding and retaining proceeds or securities, attaching bank accounts or directing non-alienation of assets only if it has reasonable grounds to believe that the company has been indulging in insider trading or fraudulent and unfair trade practices relating to securities market.

(v) prohibit, for the protection of investors, any company from issuing any offer document including a prospectus or advertisement soliciting money from the public for the issue of securities, and specify the conditions subject to which such offer documents can be issued;

(vi) specify the requirements for listing and transfer of securities; and

(vii) pass an order requiring a person to cease and desist from committing or causing a particular violation of any of the provisions of the SEBI Act, or any rules or regulations made thereunder, if it finds, after an enquiry, that such person has violated or likely to violate the said provisions. In case of a listed public company, which is not a registered intermediary, the SEBI can exercise this powers only if it has reasonable grounds to believe that the company has been indulging in insider trading or market manipulation.

In addition, SEBI was armed with powers of investigation. If SEBI has reasonable grounds to believe that the transactions in securities are being dealt in a manner detrimental to the investors or the securities market or any intermediary or any person associated with the securities market has violated any of the provisions of the SEBI Act or the rules or the regulations made or directions issued by SEBI thereunder, it can appoint a person as investigating authority to investigate the affairs of such intermediary or persons associated with the securities market. In order to provide required teeth to the investigating authority, it has been provided that any person failing to produce any document or information to the investigating authority or appear before the investigating authority or sign the notes of examination shall be punishable with imprisonment or with fine or with both. Further, if the investigating authority has reasonable grounds to believe that the books, registers or documents or records of or relating any intermediary or any person associated with securities market in any manner, may be destroyed, mutilated, altered or falsified or secreted, he can obtain an authorisation from a Magistrate to (a) enter the place or places where such books or records are kept, (b) search the place or places and (c) seize the books or records, as considered necessary for investigation. Such authorisation would not be available to investigating authority in case of books or documents of any listed public company, which is not a registered intermediary, unless such company indulges in insider trading or market manipulation. Such search and seizure shall be carried out in accordance with the provisions of the Code of Criminal Procedure, 1973. The investigating authority can keep such record and documents in his custody till the conclusion of the investigation.

Strengthening Penal Framework : Section 11 of the SEBI Act, 1992 enjoins upon SEBI to take measures to provide for prohibiting insider trading in securities and fraudulent and unfair trade practices relating to securities markets, regulating substantial acquisition of shares and takeover of companies etc. However, these terms were not explained and these activities were not expressly forbidden in the Act. In order to clarify the matter, the Amendment Act added a new chapter, Chapter VA, relating to prohibition of manipulative and deceptive devices, insider trading and substantial acquisition of securities or control and empowered SEBI to regulate these practices by regulations. It now provides that it shall be unlawful for any person, directly or indirectly –

(a) to use or employ any manipulative or deceptive device or contrivance in contravention of regulations in connection with the issue, purchase or sale of any securities listed or proposed to be listed;

(b) to employ any device, scheme or artifice to defraud in connection with issue or dealing in securities which are listed or proposed to be listed;

(c) to engage in any act, practice, course of business which operates or would operate as a fraud or deceit upon any person, in connection with the issue, dealing in securities which are listed or proposed to be listed, in contravention of the provisions of the Act, or the rules or the regulations made thereunder;

(d) to engage in insider trading;

(e) to deal in securities while in possession of material or non-public information or communicate such material or non-public information to any other person, in a manner which is in contravention of the provisions of the Act, or the rules or the regulations made thereunder; and

(f) to acquire control or securities beyond threshold limit of a company, whose securities are listed or proposed to be listed, in contravention of the regulations made under the SEBI Act.

In order to equip SEBI with wherewithal to bring all types of culprits to book to ensure orderly development of market, the Amendment Act prescribed a few more offences along with associated penalties and enhanced penalties for the offences committed under the Act from a maximum of Rs. 5 lakh to a maximum of Rs. 25 crore or three times the amount of profit made out of violation, whichever is higher, and from imprisonment of one year to 10 years. Such enhanced punishment should serve as enough deterrent for the potential violators of law. Table 1 illustrates the scheme of penalties.

All the violations under section 15 shall be adjudicated by an adjudicating officer appointed by SEBI. The Amendment Act, however, provides that all sums realised by way of penalties would be credited to Consolidated Fund of India instead of SEBI. This is probably to avoid conflict of interest that SEBI may impose higher penalty when it needs more funds.

The Amendment Act empowered the SAT and the Courts to compound offences. They can compound any offence under the SEBI Act, not being an offence punishable with imprisonment only, or with imprisonment and also with fine, either before or after the institution of the proceeding.

In order to reduce delays, avoid unnecessary litigation and get cooperation of the accused, Central Government has been empowered to grant immunity, before institution of prosecution, to any person from prosecution for any offence under the SEBI Act or rules or regulations made thereunder or from the imposition of any penalty under the Act with respect to alleged violation. Such immunity can be granted only if SEBI recommends it and the person makes a full and true disclosure in respect of the alleged violation. If any person to whom immunity has been granted does not comply with the conditions on which immunity was granted or had given false evidence, the immunity can be withdrawn and on such withdrawal, the accused would face normal prosecution / penalty.

Any offence punishable under the Act or any rules or regulations made thereunder shall be tried by a 'court of session' instead of 'a metropolitan magistrate or a judicial magistrate of the first class' as provided earlier.

Table 1

Scheme of Penalties under the SEBI (Amendment) Act, 2002

Section	*Violations*	*Penalty*	
		Before Amendment	*After Amendment*
11C(6)	Failure to produce books, records, etc. or furnish information or appear before the investigating authority or to sign the note of any examination by investigating authority	New provision	Imprisonment for a term which may extend to one year or fine which may extend to Rs. 1 crore or both and a further fine which may extend to Rs. 5 lakh for every day after the first during which the failure or refusal continues
15A(a)	Failure by any person to furnish any document, return or report to SEBI required under the Act or any rules or regulations made there under	Not exceeding Rs.1.5 lakh / Failure	Rs. 1 lakh for each day during which such failure continues or Rs. 1 crore, whichever is less
15A(b)	Failure by any person to file any return or furnish any information, books or other documents within the time specified in the regulations	Not exceeding Rs. 5,000 for each day during which such failure continues	
15A(c)	Failure by any person to maintain books of accounts or records required under the Act or any rules or regulations made thereunder.	Not exceeding Rs. 10,000 for each day during which such failure continues	

Section	Violations	Penalty Before Amendment	 After Amendment
15B	Failure by an intermediary to enter into agreement with clients required under the Act	Not exceeding Rs. 5 lakh / Failure	
15C	Failure by an intermediary to redress the grievances of investors after having been called upon by SEBI to do so	Not exceeding Rs. 10,000 / Failure	
15C	Failure by a listed company to redress the grievances of investors after having been called upon by SEBI to do so	New provision	
15D(a)	Sponsoring or carrying on any CIS, including mutual funds, by any person, without obtaining a certificate of registration from SEBI	Not exceeding Rs. 10,000 for each day during which he carries on any such CIS or Rs. 10 lakh, whichever is higher	Rs. 1 lakh for each day during which he sponsors or carries on any such CIS or Rs. 1 crore, whichever is less
15D(b)	Failure by a registered CIS to comply with terms and conditions of registration	Not exceeding Rs. 10,000 for each day during which such failure continues or Rs. 10 lakh, whichever is higher	
15D(c)	Failure by a registered CIS to apply for listing of its schemes as provided in the regulations	Not exceeding Rs. 5,000 for each day during which such failure continues or Rs. 5 lakh, whichever is higher	
15D(d)	Failure by a registered CIS to despatch unit certificates in the manner provided in the regulations	Not exceeding Rs. 1,000 for each day during which such failure continues	
15D(e)	Failure by a registered CIS to refund application monies within the period specified in the regulations	Not exceeding Rs. 1,000 for each day during which such failure continues	
15D(f)	Failure by a registered CIS to invest money in the manner or within the period specified in the regulations	Not exceeding Rs. 5 lakh / Failure	
15E	Failure by any asset management company of a registered mutual fund to observe rules and regulations	Not exceeding Rs. 5 lakh / Failure	

Section	Violations	Penalty Before Amendment	Penalty After Amendment
15F(a)	Failure by a registered stock broker to issue contract notes in the manner specified by the exchange	Not exceeding five times the amount for which the contract note was required to be issued	No change
15F(b)	Failure by a registered stock broker to deliver any security or make payment of the amount due to investor in th e manner specified in the regulations	Not exceeding Rs. 5,000 for each day during which such failure continues	Rs. 1 lakh for each day during which such failure continues or Rs. 1 crore, whichever is less
15F(c)	Charging brokerage in excess of the amount specified in the regulations by a registered stock broker	Not exceeding Rs. 5,000 or five times the amount of brokerage charged in excess of the specified brokerage, whichever is higher	Rs. 1 lakh or five times the amount of brokerage charged in excess of the specified brokerage, whichever is higher
15G	Insider trading	Not exceeding Rs. 5 lakh	Rs. 25 crore or three times the amount of profits made out of insider trading, whichever is higher
15H	Failure by any person to disclose the aggregate shareholding in the body corporate or make public announcement as required under the Act or rules or regulations	Not exceeding Rs. 5 lakh	Rs. 25 crore or three times the amount of profits made out of such failure, whichever is higher
15H	Failure by any person to make a public offer or make payment of consideration to shareholders who sold their shares pursuant to the letter of offer, as required under the Act or rules or regulations	New provision	
15HA	Indulging in fraudulent and unfair trade practices relating to securities	New provision	Penalty which may extend up to Rs. 1 crore
15HB	Failure to comply with any provision of the Act, the rules or regulations made or directions issued by SEBI thereunder for which no separate penalty has been provided	New provision	
24(1)	Contravenes or attempts to contravene or abets the contravention of the provisions of the Act or of any rules or regulations made thereunder	Imprisonment for a term which may extend to one year, or fine, or both	Imprisonment for a term which may extend to ten years, or fine which may extend to Rs. 25 crore, or both

Section	Violations	Penalty Before Amendment	Penalty After Amendment
24(2)	Failure to pay the penalty imposed by adjudicating officer or to comply with any of his directions or order.	Imprisonment for a term which shall not be less than one month but which may extend to 3 years, or fine which shall not be less than Rs. 2,000 but which may extend to Rs. 10,000, or both	Imprisonment for a term which shall not be less than one month but which may extend to 10 years, or fine which shall not be less than Rs. 25 crore or both

I. The Securities Laws (Amendment) Bill, 2003

The Securities Laws (Amendment) Bill, 2003 was introduced in the monsoon session of the Parliament to provide for (a) demutualisation and corporatisation of the stock exchanges, (b) fill up certain identified regulatory gaps such as units of mutual funds, delisting of securities, clearing corporation, protection of client assets etc. for which there were no statutory provisions, and (c) strengthen penal framework. The Bill has been referred to Standing Committee on Finance for Examination.

Demutualisation of Exchanges

Historically the exchanges were formed as 'mutual' organisations. They are generally "not-for-profit" and tax exempted entities. The trading members who provide broking services, also own, control and manage such exchanges for their common benefit, but do not distribute the profits among themselves. In contrast, in a "demutual" exchange, three separate sets of people own the exchange, manage it and use its services. The exchanges frame and enforce rules, which may not always, further the public interest (interest of investors and society) and the private interest (interests of trading members) simultaneously. Theoretically, public interest gets precedence in a demutualised exchange while private interest gets precedence in a mutual exchange in formulation and implementation of the rules. As the self (private interest) sometimes gets precedence over regulation (public interest), mutual exchanges do not offer an effective model for self-regulatory organisations. Besides addressing this malaise, the demutualisation offers several advantages. The limitations of a mutual structure has been realised time and again by the exchanges and the regulators. Recent happenings, particularly the 2001 stock market scam, made it clear that failure of the 'mutual' stock exchanges to resolve conflict of interest satisfactorily contributed to undesirable transactions in securities, which the SCRA aims to prevent. In order to address the malaise, the Finance Minister in March 2001 proposed corporatisation of stock exchanges by which ownership, management, and trading membership would be segregated from each other. The Joint Parliamentary Committee on the Stock Market Scam called for expeditious corporatisation and demutualisation of the stock exchanges. The implementation of this proposal, however, required amendments in the SCRA. The Securities Laws (Amendment) Bill, 2003 proposes these amendments.

The SCRA permits different structures for stock exchanges. That is why some exchanges are association of persons, some are company limited by shares, and some others are company limited by guarantee. Since the law permits any form for a stock exchange, it may not be possible to mandate a particular form for all exchanges. Similarly, the SCRA does not prohibit brokers from owning and managing an exchange. It may not, therefore, be possible to mandate a demutualised structure for all exchanges. In order to mandate these, the Bill seeks to amend the SCRA to specify that only a corporate entity can be a stock exchange and the exchange must be demutualised. The process of demutualisation involves segregation ownership, management and trading rights. However, the process of corporatisation would involve offering shares to public, including brokers. It is possible that the brokers subscribe for the shares and in terms of their rights under the Companies Act, get themselves elected to the board of directors. It may so happen that a stock exchange has only broker shareholders in the general body and broker directors in the governing body. Thus, even though an exchange is corporatised, it would not be demutualised, as the same set of people would be owning and managing the exchange and also trading on the exchange. The Bill, therefore, seeks to restrict the participation of broker-shareholders in the general body as well as in the management of the exchange.

The Bill makes it mandatory that all stock exchanges, if not corporatised and demutualised, shall be corporatised and demutualised on and from a date appointed by SEBI. It obligates the exchanges to submit a scheme for corporatisation and demutualization to SEBI for approval. SEBI shall not approve any scheme of demutualization and corporatisation if the issue of shares for a lawful consideration or payment of dividend or provision of trading rights in lieu of membership card of the members of an exchange is proposed out of any reserves or assets of the exchange. If a scheme is approved, it shall be published immediately and shall be binding on all persons and authorities. SEBI may reject a scheme after giving a reasonable opportunity of hearing the concerned exchange and the persons. Any person aggrieved by an order of SEBI can prefer an appeal before SAT.

While approving the scheme, SEBI may, by order, restrict (a) voting rights of the broker shareholders, (b) the rights of shareholders or brokers to appoint the representatives on governing boards, and (c) the maximum number of broker directors on the governing board, which shall not exceed one fourth of the total strength of the governing board. Such order shall be published in the official gazette. Within 12 months of this publication, the concerned stock exchange shall, either by fresh issue of equity shares to the public or in any other manner as may be specified by SEBI, ensure that at least 51% of its equity shares is held by public other than shareholders having trading rights. SEBI may extend this period by another 12 months in public interest.

If an exchange is not corporatised and demutualised or fails to submit a scheme for the same or the scheme is rejected by SEBI, the recognition granted to such exchange shall stand withdrawn.

Regulatory Gaps

In view of so many regulators and so many statues governing securities market, it is quite natural that there are regulatory gaps and overlaps. The Bill seeks to remove a few regulatory gaps.

Units of Mutual Funds : Units of mutual funds (MFs) resemble securities. They represent the interest of the unit holder in the specific scheme just as securities represent the interest of the holder in the issuer. The unit holder has similar rights as a security holder has on the future performance of any underlying asset or group of assets. Special kinds of units (units of assured return schemes), which represent the rights of investors on a fixed income flow over the future years or a fixed maturity value at the end of a specified period, are similar to debentures issued by companies. The units are issued, dematerialised, listed, traded on exchanges in a manner similar to any other security. These are transferred from one holder to another or sold back to the issuer, at pre-specified or market determined values, just like shares, debentures and other securities are. The holders of units and securities have the same need for safety, liquidity and return. Despite such close similarities between units and securities, they are not explicitly treated legally at par. While the trading of securities issued by corporates is governed by SCRA and regulatory framework developed thereunder, while trading of units are not subject to similar regulatory framework. In fact, trading of units is not subject to any regulatory framework. This presents a case of regulatory gap and this is one of the reasons why the secondary market for units has not developed appreciably. The easiest way to develop the market for units of MFs and protect the investors investing in them is to consider the units to be securities so that the regulatory framework applicable to trading of securities would also apply to trading of units and SEBI which has the responsibility to protect the interests of investors in securities, can protect the interest of holders of units of MFs also. Since the jurisdiction of SEBI is limited to securities market and the units of MFs are not explicitly recognised as securities in law, the actions of SEBI in protecting the interests of investors in units of MFs and developing a market for them is being challenged before the courts of law. In an appeal before SAT, an appellant contended that he was not covered by the Rules as he was not dealing in securities, but in units of MFs which are not securities and hence the SEBI had no powers, authority or jurisdiction to conduct any enquiry or impose any penalty on him. While disagreeing with this, the SAT considered the units of MFs to be securities in view of the object and purpose underlying the SEBI Act. This judicial pronouncement needs to be codified in law. The Bill, therefore, proposes to expand the definition of 'securities' to include units or any such instrument issued to the investors under any mutual fund scheme.

Delisting of Securities : Listing and delisting are two sides of the same coin. There is a substantial body of law that governs listing. The Companies Act makes it mandatory for a company issuing shares to public to list its securities on a stock exchange. The SCRA obliges the company to comply with the conditions of listing. It also allows a company to prefer an appeal before Securities Appellate Tribunal if a stock exchange refuses listing. The SCRA prescribe requirements for listing on a stock exchange. It also regulates suspension and withdrawal of trading. So much care and concern about listing. Even there are provisions about suspension of listing in statutes, rules and regulations. Unfortunately, delisting does not find place in any statute, rules or regulations. It was so far being regulated through a circular of SEBI, now by guidelines. Since the delisting is at least as important as listing, it is necessary that both have same level of legal backing.

Since no such statutory provision exists, doubts are raised if delisting is at all permissible under the laws. It is argued in some circles that delisting should not be permitted at all. They argue that it is the intention of legislature, as there are statutes and rules to govern listing, but no statute/rule provides for delisting. It is probably considered that listing is so sacrosanct that once a security is listed, it should not be delisted. An investor subscribes to an issue on the basis of the contents in the prospectus which may state that the security would be listed on stock exchanges. Once he subscribes to the issue, he takes an irreversible decision, as the promises in the prospectus are irreversible. Hence if one considers investors interest to be predominant and sole factor, there should not be any delisting of securities. Another school argues that listing agreement is essentially a contract between a company and an Exchange. Like any contractual relations, it must have also a way to terminate the relationship in certain circumstances. If there is a way to get in, there must be also a way to get out. Should the exchange and the company consider terminating their relationship, after taking care of interest of the affected investors, they should be permitted to do so. In view of pros and cons of delisting, it may not be desirable to put an absolute ban on delisting but it may be regulated. The statute and rules must provide a framework for delisting, as it provides for listing. If it is in the interest of investors, it must be permitted. If it is not in the interest of investors, delisting may be allowed only if investors are adequately protected.

The Bill proposes a framework for voluntary and compulsory delisting. A stock exchange may delist securities, after giving the concerned company an opportunity of hearing, if (a) the company has incurred losses or its networth has been reduced to less than its paid up capital, (b) the securities have not been traded continuously, (c) the company has failed to comply with listing agreement or provisions of any law, (d) the company fails to redress complaints of investors, (e) the company or its promoters or directors indulge in insider trading or unfair trade practices in securities, (f) the promoters or directors or persons in management indulge in malpractices, (g) the addresses of promoters or directors are not known or false, (h) trading in securities has remained suspended for more than six months, and (i) public shareholding has come below the limits specified in the listing agreement. The Bill empowers SEBI to specify additional grounds on which securities may be delisted. A listed company or an aggrieved investor can file an appeal before SAT against the decision of the exchange delisting the securities. The Bill allows a company to delist its securities from an exchange. It can, however, do so only after it has obtained prior approval of the holders of securities by a special resolution passed at a general meeting, given an opportunity to the shareholders to exit at a fair price, and complied with such conditions as may be prescribed by the Exchange or SEBI.

Clearing Corporation : The securities laws do not explicitly recognise existence of clearing corporation. They talk only about trading and not about settlement, which is left to byelaws of the exchanges. The byelaws are supposed to provide for clearing house (not clearing corporation) for settlement of securities transactions. The anonymous order book ushered in by screen based trading system does not allow participants to assess the counter party risk. It is, therefore, necessary that the exchanges use a clearing corporation to provide novation and settlement guarantee.

The Bill inserts a new section to provide that an exchange may, with the approval of SEBI, transfer the duties and functions of a clearing house to a clearing corporation for the purpose of the periodical settlement of contracts and differences thereunder, and the delivery of and payment for securities. SEBI shall approve such transfer if it is in public interest or in the interest of trade. Every clearing corporation must be a company and its byelaws must be approved by SEBI. The various provisions in the SCRA such as grant and withdrawal of recognition, supersession of management, suspension of business etc. applicable to stock exchanges shall, *mutatis mutandis*, apply to clearing corporations.

Client Assets : The intermediaries handle the money and the securities on behalf of clients and hold these in their custody on their behalf. They have generally been advised by SEBI to segregate their assets from those of their clients and not comingle the assets of the clients. At times, the intermediaries like depositories hold the assets as registered owner on behalf of beneficial owners. However, there is a doubt if the assets of the clients can be attached in case of insolvency of the intermediaries. There is no statutory backing to protect the investors in case of insolvency of intermediaries. In order to provide this protection of assets held in trust on behalf of investors, the Bill proposes that an investor can entrust the money or securities to any intermediary (stock broker, sub-broker, share transfer agent, banker to an issue, trustee of trust deed, registrar to an issue, merchant banker, underwriter, portfolio manager, investment adviser, depository, depository participant, custodian of securities, FIIS, credit rating agencies and such other intermediary) to be dealt or held on behalf of and at the instance of the investor. The intermediary shall hold such assets in trust and shall not have any right, title or interest of any nature therein. He shall deal with such assets as directed by the investor and shall be accountable for the same. Such assets shall not form part of assets of the intermediary and no authority can attach or seize such assets. If a broker or sub-broker fails to segregate the assets of the client or clients or uses the assets of a client for self or any other client, he can be penalized by an adjudicating officer up to Rs. 1 crore.

Scheme of Penalty

The securities market is an integral part of the economy. It has the potential to destabilise other sectors. It is, therefore, necessary that the penalty for offences in the securities market is deterrent. The first step in this regard is to make all the offences in the securities market cognisable, as a few offences under the SCRA are. Accordingly the Bill proposes to make all the offences listed in section 23 cognisable.

The penalty prescribed under the SCRA is ridiculously low. Many of the offences under the SCRA attract a penalty of Rs. 1,000, on conviction. For example, non-compliance of listing agreement, which can put investors to untold miseries and make a mockery of corporate governance norms, can be punished upto Rs. 1,000. Listing agreement can be effectively used to discipline a listed company, if its non-compliance invites a deterrent penalty. Accordingly, the Bill proposes increase penalty from Rs. 1,000 to an imprisonment upto 10 years or fine upto Rs. 25 crore or both. The Bill empowers SAT and Courts to compound any offence punishable under the SCRA, not being an offence punishable with imprisonment only, or with imprisonment and also with fine, either before or after institution of any proceeding.

The Bill lists out a wide range of violations along with maximum penalties leviable. It empowers SEBI to appoint an officer not below the rank of a division chief of SEBI to be an adjudicating officer. He will hold an enquiry after giving the person concerned a reasonable opportunity of being heard for the purpose of imposing penalty under sections 23A to 23F. While adjudging the quantum of penalty, the adjudicating officer shall have due regard to amount of disproportionate gain or unfair advantage wherever quantifiable made as a result of the default, the amount of loss caused to an investor or any group of investors as a result of default, the repetitive nature of the default and seriousness of the offence or violation. Table 2 presents the penalties envisaged in the Bill for different violations.

Table 2

Penalties proposed in the Securities Laws (Amendment) Bill, 2003

Section	*Offence*	*Penalty*
23(1)	Various offences	Imprisonment upto 10 years or fine upto Rs. 25 crore or both
23A	Failure to furnish information, books etc. or maintain books, records etc. as required under listing agreement or byelaws of an exchange	Rs. 1 lakh for each day during which such failure continues or Rs. 1 crore, whichever is less
23B	Failure to enter into an agreement with client	

Section	Offence	Penalty
23C	Failure to redress the grievances of investors by a broker, sub-broker, a listed or proposed to be listed company, after being called upon to do so by SEBI or Exchange	
23D	Failure by a broker or sub-broker to segregate assets of clients or uses the assets of a client for self or another client	Penalty not exceeding Rs. 1 crore
23E	Failure to comply with listing agreement or delisting norms by a person or company managing CIS or Mutual fund	Penalty not exceeding Rs. 25 crore
23F	Dematerialisation in excess of the listed securities	
23G	Failure or neglect by an Exchange to furnish periodical returns or to comply with any direction of SEBI	
23H	Failure to comply with any provisions of the Act, rules, articles or byelaws of exchange or directions issued by SEBI, for which no separate penalty has been prescribed	Penalty not exceeding Rs. 1 crore

The Bill provides that non-payment of penalty imposed by an adjudicating officer or non-compliance with any of his orders or directions would be an offence punishable with imprisonment for a term between one month and ten years, or with fine upto Rs. 25 crore or with both. All sums realized by way of penalties shall be credited to Consolidated Fund of India.

To ensure fair enquiry and penalty, the Bill provides that appeal against the orders or decision of SEBI rejecting the scheme of demutualisation submitted by an exchange, of an adjudicating officer imposing monetary penalty or of an Exchange regarding listing or delisting of securities can be preferred before SAT. Any person aggrieved by an order of SAT can prefer an appeal before Supreme Court only on a question of law.

The Bill provides that that no court shall take cognisance of any offence punishable under the Act or any rules made thereunder except on a complaint made by Central / State Government, SEBI, a stock exchange or a person. Any offence punishable under the Act shall be tried by a 'Court of Session' instead of 'a Presidency Magistrate or a Magistrate of the First Class' as provided now.

The amendment Bill inserts section 12A to empower SEBI to issue directions to any stock exchange, clearing corporation, any agency or person providing trading, clearing or settlement facility in respect of securities and to any company whose securities are listed or proposed to be listed on a stock exchange. Such directions can be made only being satisfied after inquiry that it is (i) in the interest of investors or orderly development of securities market, (ii) to prevent the affairs of any exchange, clearing corporation etc. from being conducted in a manner detrimental to the interest of investors or of the securities market, or (iii) to secure the proper management of any such entity.

Other Amendments

The amendment Bill also proposes the following amendments:

Derivatives : It amends the definition of 'derivatives' to include swap, options and hybrid instruments and other contracts for differences. These are not securities as such and not based on underlying securities, but can be traded and regulated under SCRA, if these are considered derivatives and consequently securities. This will help the market for these instruments to develop.

Spot Transactions : Market has moved to T+2 rolling settlement in April 2003 and is scheduled to move to T+1 by April 2004. Since T+2 is as good as spot transactions, there is no need to allow spot transactions or exempt them from the regulatory framework. Besides, the spot transactions have been alleged misused for manipulative purposes. It may, therefore, be desirable to regulate spot transactions. The Bill proposes to withdraw the exemption for spot transactions in general. It grants the exemption only in respect specified types of spot transactions from the regulatory framework. It also empowers Central Government to regulate spot transactions, including exempted transactions, in the interest of trade or public interest.

Depositories Act : The Bill amends the Depositories Act to provide that any person aggrieved by an order of SAT can prefer an appeal before Supreme Court on a question of law arising out of the order.

Further Reforms

Nine special legislative interventions since 1992 indicate generosity of authorities. This has built up expectations of the market participants. This is a perfect example of more we get, more we ask or expect. The following further changes in law could be considered:

Regulatory Issues

There are several statutes regulating different aspects of the securities market. The four main legislations are: the SEBI Act, 1992, the Companies Act, 1956, the SCRA, 1956, and the Depositories Act, 1996. The larger the number of laws, higher is the scope for inconsistency among them and the possibility of regulatory overlaps and gaps. For example, listing is provided for in the Companies Act, SCRA and SEBI Act, while law does not provide for delisting, clearing corporation etc. as on date.

There are also as many regulators as the number of laws. The responsibility for supervision and development of the securities market is shared by Department of Economic Affairs, Department of Company Affairs, RBI and SEBI. In view of involvement of so many regulators, there is scope for confusion among the regulators and the regulated, regulatory gaps and overlaps, and duplicate and inconsistent regulations. For example, no regulator regulated CIS till it assumed scandalous dimensions when it was explicitly assigned to SEBI. Similarly, there is hesitation among regulators to regulate private placement of securities.

Not only the regulatory jurisdiction among different agencies is blurred, but also there is no statutory provision to provide for regulatory cooperation / sharing information among the domestic regulators and between overseas and domestic regulators. Powers of the regulator to assist / seek assistance from overseas regulators or to enter into MOUs or other co-operation arrangements with them to deal with cross border misconduct are not explicitly provided in any legislation, though these are also not forbidden.

The protection of the interests of investors requires consolidation of all laws relating to securities market into a single piece of legislation, preferably called the Securities Act which should prevail over general laws. The administration of the Act may assigned to one agency with clearly defined regulatory jurisdiction and accountability. And the agency works in close coordination with other regulators, domestic or foreign.

If a regulator is also a participant in the market, it may not always be possible to avoid conflict of interest. For example, RBI, which is manager of the monetary policy, acts as regulator for government securities market, and also participates in the market simultaneously as manger of government debt, issuer of securities, merchant banker to issue, registrar and transfer agent, clearing and settlement agent, depository for securities, provider of trading platform, and subscriber to securities. The decisions relating to debt management, interest rate and regulation of market should be taken independently to avoid perceived conflict of interest.

The SROs are expected to share the responsibility with the regulator in framing and administering regulations. However, the SROs have not developed appreciably in India. Most of the associations of intermediaries like, AMFI, AMBI do not exactly regulate, though promote the activities of their members. The stock exchanges are SROs in true sense. However, the current ownership and governance structure of many stock exchanges do not seem adequate to deal with conflict of interest objectively. The imminent demutalisation should address this. This requires approval to the Securities Laws (Amendment) Bill, 2003.

While formulating regulations, no conscious effort is made to estimate cost of compliance of regulations and if the benefits from regulation outweigh the costs of regulation. There has also not been any study to estimate the cost of regulation / compliance. In order to prevent over regulation, it is necessary that the regulators are mandated to explicitly take into account the costs of regulation.

There is no provision in law requiring regulator to consult the regulated while formulating regulations. SEBI has, however, recently instituted a consultative process before framing regulations. All major policy / regulatory proposals are evolved through a committee comprising of experts and market participants and are posted on SEBI web site for comments from market participants and public. This needs to be codified.

Penal Provisions

The SEC lets off the offenders who simply pay up without admitting to an offence. This prevents every case being locked up in a Court. Given the number of cases pending in the Indian Courts and intangible nature of securities market offences, SEBI requires similar facilities if the offenders are to be punished on priority. This would help to bring all the co-accused to book or solve difficult cases if one accused provides lead by agreeing to plea bargain in exchange of a linient sentence.

The SEBI Act provides for two alternative types of punishment. They are: (a) suspension or cancellation of certificates of registration to be imposed by SEBI, or (b) monetary penalty to be imposed by an adjudicating officer. These two types of punishments are mutually exclusive. If a violation is assigned to an adjudicating officer for adjudication or monetary penalty is imposed, penalty of suspension or cancellation of certificate of registration can not be imposed and vice-versa. This happens because SEBI does not have power to impose monetary penalty and the adjudicating officer does not have power to suspend or cancel a certificate of registration. A corollary of this is that mind is made up about the type of punishment to be imposed on the erring party when the alleged violation is referred to an adjudicating officer for adjudication or taken up by SEBI for imposition of suspension or cancellation of registration, that is, at a stage when the nature and gravity of the violation has not been fully ascertained. What would, therefore, be desirable is to authorise the adjudicating officers to try all offences under the SEBI Act, rather all securities laws, and award all types of penalties so that SEBI can concentrate on developmental and regulatory work.

Investor Protection

Investors are the backbone of the securities market. Protection of their interest is essential for sustenance of their interest in securities and hence development of market.

The consumer fora provide an expeditious remedy to a consumer who has suffered loss on account of deficiency in goods/services purchased by him. A system ombudsman is working well in the banking and insurance sector. A similar arrangement is called for redressal of investor grievances.

The investor forum as well as other authorities should have power to dispose off the cases summarily and to award compensation to the investor. It is not enough if the culprit is punished. The culprit needs to be punished in an exemplary manner, while investor should have means to recover his loss caused by the culprit. The law should empower the authorities not only to levy penalties, but also award compensation to investor.

The depositors are protected up to Rs. 1 lakh in the event of liquidation/bankruptcy of a bank. This protects innocent depositors and thereby contributes to the stability of the financial system. A similar mechanism may be insituted to compensate an investor up to Rs. 5 lakh if he suffers a loss on account of the failure of the system or mischief by any market participant. An organisation called Securities Investor Protection Corporation operates in the USA to provide similar protection to investors.

A large number of shares in the hands of a large number of shareholders is essential for sustenance of a continuous market for listed securities to provide liquidity to investors and to discover fair prices. To ensure this, a public company seeking listing of its securities on a stock exchange is required to offer at least 10% of securities to public. This framework suffers from following limitations: (i) 10% offer to public is too low to prevent price manipulation. (ii) The public offer is of no consequence unless the public are actually allotted shares. Even allotment has no meaning, unless sizeable number of shares remains in the hands of public to provide a continuous market. The law should speak in terms of allotment to public and public holding. (iii) The units of CIS are securities. But there is a different standard for listing of units of CIS. The same requirement (10% + 20 lakh + Rs. 100 crore or 25%, as the case may be) as applicable to listing of securities, should also apply to listing of units of CIS. The units of MFs are being considered as securities and are being traded like securities on exchanges. The requirement of public holding may apply to units of MFs as well. The investors in securities – shares, units of CIS or units of MFs – have need for same level of protection and hence the conditions of listing for all kinds of securities should be uniform. (iv) There should not be any discrimination between a government company and a non-government company. The powers of the stock exchange to relax this requirement in respect of a government company needs to be withdrawn. The powers of SEBI to relax or waive strict enforcement of listing requirement may also be withdrawn. (v) The words 'public' or 'offer to public' have not been defined. The Rules permit 10% public offer subject to the condition that 60% of the issue is allocated to QIBs. Since QIBs are part of public, allocating 60% to QIBs would automatically constitute 60% public offer and the retail public would not get any share. Or, if 60% of public offer of 10% is allocated to QIBs, the retail public would be left with just 4%. It is, therefore, necessary to define 'public' and other terms and explicitly exclude allocation to QIBs from the public offer.

To ensure availability of reasonable floating stock on continuous basis, the listing agreement requires a company to maintain the minimum level of non-promoter holding at the level of public shareholding as required at the time of listing. If, however, the non-promoter holding of an listed company as on April 1, 2001 was less than that is required at the time of initial listing, the company was required raise the level of non-public holding to at least 10% within one year. This arrangement prescribes different standards for continued listing for companies listed before April 2001 and for companies listed thereafter. A company listed before April 2001 can have non-promoter holding of at least 10%, if as on April 1, 2001 it had non-promoter holding less than that is required at the time of initial listing. Otherwise it will have non-promoter holding as required at the time of initial listing, which may be 60% if it was listed before 1993. A company listed after April 2001 would maintain a minimum level of non-promoter holding at the level of public holding as required at the time of listing, that is, at 10% plus 20 lakh securities plus Rs. 100 crore or 25%, as the case may be. Thus existing listed and would be listed companies and consequently investors in these companies are treated differently.

Non-promoter holding required at the time of listing is quite vague as it has changed over time. If we follow the listing agreement, the companies listed before 1993 would maintain non-promoter holding at 60%, the companies listed between 1993 and 2001 would maintain at 25% and the companies listed after 2001 would maintain at 10% + 20 lakh + Rs. 100 crore or 25%, as the case may be. If minimum non-promoter holding is prescribed in the interest of investors and investors in all companies are to be treated uniformly, regulation has to be uniform and all companies should be required to maintain non-promoter holding of 10% + 20 lakh + Rs. 100 crore or 25%, as the case may be.

The confidence of the investors can be maintained and enhanced by making provision for professional intermediation services. Industry/SROs/Regulators have made a modest beginning, but not adequate given the dimensions of the market. There must be a formal and adequate arrangement to equip the personnel working with the intermediaries with the skills required to operate in the securities market. Probably an institute like ICSI or ICAI is necessary for securities market.

An investor normally deals in securities through an intermediary, whose acts of omission and commission can cause loss to him. In order for the investor to choose the right intermediary through whom he may transact business, it may be useful to help him in taking informed decision by making details of intermediaries available to him. Even, the intermediaries may be rated and their ratings are disseminated.

The sustenance of investors' interest and confidence in the securities market depends crucially on corporate governance. An investor, however, is generally not equipped to form an idea about the level of corporate governance in a company. As he is helped by credit rating in respect of his investments in debt instruments, he needs to be helped by a summary figure such as corporate governance index in respect of his investments in the concerned company.

NEW CORPORATE GOVERNANCE NORMS : AN ANALYSIS OF REVISED CLAUSE 49 OF THE LISTING AGREEMENT

N K JAIN*

Introduction

Good Governance in capital market has always been high on the agenda of SEBI. Corporate Governance is looked upon as a distinctive brand and benchmark in the profile of Corporate Excellence. This is evident from the continuous updation of guidelines, rules and regulations by SEBI for ensuring transparency and accountability. In the process, SEBI had constituted a Committee on Corporate Governance under the Chairmanship of Shri Kumar Mangalam Birla. The Committee in its report observed that "the strong Corporate Governance is indispensable to resilient and vibrant capital markets and is an important instrument of investor protection. It is the blood that fills the veins of transparent corporate disclosure and high quality accounting practices. It is the muscle that moves a viable and accessible financial reporting structure."

Based on the recommendations of the Committee, the SEBI had specified principles of Corporate Governance and introduced a new clause 49 in the Listing agreement of the Stock Exchanges in the year 2000. These principles of Corporate Governance were made applicable in a phased manner and all the listed companies with the paid up capital of Rs 3 crores and above or net worth of Rs 25 crores or more at any time in the history of the company, were covered as of March 31, 2003.

SEBI, as part of its endeavour to improve the standards of corporate governance in line with the needs of a dynamic market, constituted another Committee on Corporate Governance under the Chairmanship of Shri N. R. Narayana Murthy to review the performance of Corporate Governance and to determine the role of companies in responding to rumour and other price sensitive information circulating in the market in order to enhance the transparency and integrity of the market. The Committee in its Report observed that "the effectiveness of a system of Corporate Governance cannot be legislated by law, nor can any system of Corporate Governance be static. In a dynamic environment, system of Corporate Governance need to be continually evolved."

With a view to promote and raise the standards of Corporate Governance, SEBI on the basis of recommendations of the Committee and public comments received on the report and in exercise of powers conferred by Section 11(1) of the Securities and Exchange Board of India Act, 1992 read with section 10 of the Securities Contracts (Regulation) Act 1956, revised the existing clause 49 of the Listing agreement vide its circular SEBI/MRD/SE/31/2003/26/08 dated August 26, 2003. It clarified that some of the sub-clauses of the revised clause 49 shall be suitably modified or new clauses shall be added following the amendments to the Companies Act 1956 by the Companies (Amendment) Bill/Act 2003, so that the relevant provisions of the clauses on Corporate Governance in the Listing Agreement and the Companies Act remain harmonious with one another.

Schedule of Implementation

The circular specifies following schedule of implementation of the revised clause 49 :

(i) All entities seeking listing for the first time, at the time of listing,

(ii) All listed entities having a paid up share capital of Rs 3 crores and above or net worth of Rs 25 crores or more at any time in the history of the company.

* Secretary, The ICSI, Views expressed are personal views of the author and do not reflect those of the Institute.

The companies are required to comply with the requirements of the clause on or before March 31, 2004. The companies which are required to comply with the requirements of the revised clause 49 have been put under an obligation to submit a quarterly compliance report to the stock exchanges as per sub clause (IX) (ii), of the revised clause 49, within 15 days from the quarter ending 31st March, 2004. The report is required to be submitted either by the Compliance Officer or the Chief Executive Officer of the company after obtaining due approvals.

Application of Revised Clause 49

The revised clause 49 is applicable to the listed companies, in accordance with the schedule of implementation given above. However, for other listed entities, which are not companies, but body corporates (e.g. private and public sector banks, financial institutions, insurance companies etc.) incorporated under other statutes, the revised clause will apply to the extent that it does not violate their respective statutes, and guidelines or directives issued by the relevant regulatory authorities. The revised clause is not applicable to the Mutual Fund Schemes.

Obligations on Stock Exchanges

The Stock Exchanges are put under obligation to ensure that all the provisions of Corporate Governance have been complied with by the company seeking listing for the first time, before granting any new listing. For this purpose, it would be satisfactory compliance if these companies set up the Boards and constitute committees such as Audit Committee, shareholders/ investors grievances committee, etc. before seeking listing. The stock exchanges have been empowered to grant a reasonable time to comply with these conditions if they are satisfied that genuine legal issues exists which will delay such compliance. In such cases while granting listing, the stock exchanges are required to obtain a suitable undertaking from the company. In case of the company failing to comply with this requirement without any genuine reason, the application money shall be kept in an escrow account till the conditions are complied with. The Stock Exchanges have also been required to set up a separate monitoring cell with identified personnel to monitor the compliance with the provisions of the Corporate Governance, and to obtain the quarterly compliance report from the companies which are required to comply with the requirements of Corporate Governance. The stock exchanges are required to submit a consolidated compliance report to SEBI within 30 days of the end of each quarter.

HIGHLIGHTS OF THE NEW AMENDMENTS

1. Widening the Definition of Independent Director

Under the revised clause 49, the definition of the expression 'independent director' has been expanded. The expression 'independent director' mean non-executive director of the company who —

(a) apart from receiving director's remuneration, does not have any material pecuniary relationships or transactions with the company, its promoters, its senior management or its holding company, its subsidiaries and associated companies;

(b) is not related to promoters or management at the board level or at one level below the board;

(c) has not been an executive of the company in the immediately preceding three financial years;

(d) is not a partner or an executive of the statutory audit firm or the internal audit firm that is associated with the company, and has not been a partner or an executive of any such firm for the last three years. This will also apply to legal firm(s) and consulting firm(s) that have a material association with the entity.

(e) is not a supplier, service provider or customer of the company. This should include lessor-lessee type relationships also; and

(f) is not a substantial shareholder of the company, i.e. owning two percent or more of the block of voting shares.

It has been clarified that the Institutional Directors on the boards of companies are independent directors whether the institution is an investing institution or a lending institution.

2. Compensation to Non Executive Directors and Disclosure thereof

As per earlier clause 49, the compensation to be paid to non-executive directors was fixed by the Board of Directors, whereas the revised clause requires all compensation paid to non-executive directors to be fixed by the Board of Directors and to be approved by shareholders in general meeting. There is also provision for setting up of limits for the maximum number of stock options that can be granted to non-executive directors in any financial year and in aggregate. The stock options granted to the non-executive directors to be vested after a period of at least one year from the date of retirement of such non-executive directors.

Placing the independent directors and non-executive directors on equal footing, the revised clause provides that the considerations as regards compensation paid to an independent director shall be the same as those applied to a non-executive director. The companies have been put under an obligation to publish their compensation philosophy and statement of entitled compensation in respect of non-executive directors in its annual report. Alternatively, this may be put up on the company's website and a reference thereto in the annual report. The company is also required to disclose on an annual basis, details of shares held by non-executive directors, including on an "if-converted" basis.

The revised clause also requires non-executive directors to disclose prior to their appointment their stock holding (both own or held by / for other persons on a beneficial basis) in the listed company in which they are proposed to be appointed as directors,. These details are required to be accompanied with their notice of appointment.

3. Periodical Review by Independent Director

The revised clause 49 requires the Independent Director to periodically review legal compliance reports prepared by the company and any steps taken by the company to cure any taint. **The revised clause specifies that no defence shall be permitted that the independent director was unaware of this responsibility in case of any proceedings against him in connection with the affairs of the company.**

4. Code of Conduct

The revised clause 49 requires the Board of a company to lay down the code of conduct for all Board members and senior management of a company and the same to be posted on the website of the company. Accordingly, all Board members and senior management personnel have been put under an obligation to affirm compliance with the code on an annual basis and a declaration to this effect signed by the CEO and COO is to be given in the Annual Report of the Company.

It has been clarified that the term senior management will include personnel of the company who are members of its management / operating council (i.e. core management team excluding Board of Directors). Normally, this would comprise all members of management one level below the executive directors.

5. Non–Executive Directors – Not to hold office for more than Nine Years

Revised clause 49 limits the term of the office of the non-executive director and provides that a person shall be eligible for the office of non-executive director so long as the term of office does not exceed nine years in three terms of three years each, running continuously.

6. Audit Committee

Two explanations have been added in the revised clause 49. The first explanation defines the term "financially literate" to mean the ability to read and understand basic financial statements i.e. balance sheet, profit and loss account, and statement of cash flows. It has also been clarified that a member is considered to have accounting or related financial management expertise if he or she possesses experience in finance or accounting, or requisite professional certification in accounting, or any other comparable experience or background which results in the individual's financial sophistication, including being or having been a Chief Executive Officer(CEO), Chief Financial Officer(CFO), or other senior officer with financial oversight responsibilities.

7. Review of information by Audit Committee

The Audit Committee is required to mandatorily review financial statements and draft audit report, including quarterly / half-yearly financial information, management discussion and analysis of financial condition and results of operations, reports relating to compliance with laws and to risk management, management letters/ letters of internal control weaknesses issued by statutory / internal auditors, and records of related party transactions.

The appointment, removal and terms of remuneration of the Chief Internal Auditor shall be subject to review by the Audit Committee.

8. Disclosure of Accounting Treatment

The revised clause 49 requires that in case a company has followed a treatment different from that prescribed in an Accounting Standards, the management of such company shall justify why they believe such alternative treatment is more representative of the underlined business transactions. Management is also required to clearly explain the alternative accounting treatment in the footnote of financial statements.

9. Whistle Blower Policy

Companies have been required to formulate an Internal Policy on access to Audit Committees. Personnel who observe any unethical or improper practice (not necessarily a violation of law) can approach the Audit Committee without necessarily informing their supervisors.

Companies are also required to take measures to ensure that this right of access is communicated to all employees through means of internal circulars, etc. The employment and other personnel policies of the company should also contain provisions protecting "whistle blowers" from unfair termination and other unfair or prejudicial employment practices. Companies have also been required to affirm that it has not denied any personnel access to the Audit Committee of the company (in respect of matters involving alleged misconduct) and that it has provided protection to "whistle blowers" from unfair termination and other unfair or prejudicial employment practices. Such affirmation should form part of the Board's report on Corporate Governance that is required to be prepared and submitted together with the annual report.

10. Subsidiary Companies

The revised clause 49 provides that the provisions relating to the composition of the Board of Directors of the holding company are also applicable to the composition of the Board of Directors of subsidiary companies. The clause further requires that at least one independent director on the Board of Directors of the holding company should be a director on the Board of Directors of the subsidiary company.

The Audit Committee of the holding company has been empowered to review the financial statements, in particular the investments made by the subsidiary company and the minutes of the Board meetings of the subsidiary company to be placed for review at the Board meeting of the holding company. It is further required that the Board's report of the holding company should state that they have reviewed the affairs of the subsidiary company also.

11. Disclosure of contingent liabilities

The revised clause 49 requires the management to provide a clear description in plain English of each material contingent liability and its risks, which shall be accompanied by the auditor's clearly worded comments on the management's view. This section is required to be highlighted in the significant accounting policies and notes on accounts, as well as, in the auditor's report, where necessary.

12. Additional Disclosures

The revised Clause 49 of the Listing Agreement requires the following additional disclosures:

(A) Basis of related party transactions

A statement of all transactions with related parties shall be placed before the Audit Committee for formal approval/ratification. If any transaction is not on an arm's length basis, management is required to justify the same to the Audit Committee.

(B) Board Disclosures –Risk management

The Board members should be informed about the risk assessment and minimization procedures. These procedures shall be periodically reviewed to ensure that executive management controls risk through means of a properly defined framework.

Management shall place a quarterly report certified by the compliance officer of the company, before the entire Board of Directors documenting the business risks faced by the company, measures to address and minimize such risks, and any limitations to the risk taking capacity of the corporation. This document shall be formally approved by the Board.

(C) Proceeds from Initial Public Offerings (IPOs)

When money is raised through an Initial Public Offering (IPO), it shall disclose to the Audit Committee, the uses / applications of funds by major category (capital expenditure, sales and marketing, working capital, etc), on a quarterly basis as a part of their quarterly declaration of financial results. Further, on an annual basis, the company shall prepare a statement of funds utilized for purposes other than those stated in the offer document/prospectus. This statement shall be certified by the independent auditors of the company. The Audit Committee shall make appropriate recommendations to the Board to take up steps in this matter.

13. Certification by CEO/CFO

CEO (either the Executive Chairman or the Managing Director) and the CFO (Whole-Time Finance Director or other person discharging this function) of the company has been put under an obligation to certify that, to the best of their knowledge and belief, they have reviewed the balance sheet and profit and loss account and all its schedules and notes on accounts, the cash flow statements as well as the Directors' Report and these statements do not contain any materially untrue statement, omits any material fact or do they contain statements that might be misleading. Further they are required to certify that these statements together present a true and fair view of the company, and are in compliance with the existing accounting standards and/or applicable laws/regulations.

The revised clause requires them to be responsible for establishing and maintaining internal controls, to evaluate the effectiveness of internal control systems of the company, and to disclose to the auditors and the Audit Committee, deficiencies in the design or operation of internal controls, if any. They are also required to disclose to the auditors as well as the Audit Committee, instances of significant fraud, if any, that involves management or employees having a significant role in the company's internal control systems, whether or not there were significant changes in internal control and / or of accounting policies during the year.

14. Report on Corporate Governance

The companies have been required to submit a quarterly compliance report in the prescribed format to the stock exchanges within 15 days from the close of the quarter. The report has to be submitted either by the Compliance Officer or the Chief Executive Officer of the company after obtaining due approvals.

15. Company Secretary in Practice to Issue Certificate of Compliance

This is a landmark amendment authorizing Company Secretaries in Practice among other professionals to issue certificate of compliance of clause 49. The revised clause requires the company to obtain a certificate from either the auditors or practicing company secretaries regarding compliance of conditions of corporate governance and annex the certificate with the directors' report, which is sent annually to all the shareholders of the company. The same certificate is also required to be sent to the Stock Exchanges along with the annual returns filed by the company.

16. Additional disclosure in the Report on Corporate Governance

The following additional items are required to be disclosed in the suggested list of Items to be included In the Report on Corporate Governance in the Annual Report of Companies.

(i) Disclosure of accounting treatment, if different, from that prescribed in Accounting Standards with explanation.

(ii) Whistle Blower policy and affirmation that no personnel has been denied access to the audit committee.

17. Additional Disclosures under Non-Mandatory Requirements

The following additional disclosures are required to be made under the non-mandatory requirements :

(i) Audit qualifications

Company may move towards a regime of unqualified financial statements.

(ii) Training of Board Members

Company shall train its Board members in the business model of the company as well as the risk profile of the business parameters of the company, their responsibilities as directors, and the best ways to discharge them.

(iii) Mechanism for evaluating Non-Executive Board Members

The performance evaluation of non-executive directors should be done by a peer group comprising the entire Board of Directors, excluding the director being evaluated; and Peer Group evaluation should be the mechanism to determine whether to extend / continue the terms of appointment of non-executive directors.

Conclusion

The recent events worldwide, particularly in the United States have renewed the emphasis on Corporate Governance the worldover. These events have highlighted the need for ethical governance and require management to look beyond their systems and procedures. Reacting swiftly and spontaneously, the United States enacted Sarbans Oxley Act, 2002 bringing out fundamental changes in every dimension of Corporate Governance. Back home in India, the need for strengthened norms for Corporate Governance is also felt. The revised clause 49 of the Listing Agreement is, therefore, most timely and provides much needed disclosure requirements, widened definition of independent director, periodical review by independent director, whistle blower policy, quarterly compliance report in the prescribed format and issue of certificate of compliance. It is hoped that the revised clause 49 would go a long way in providing corporates good governance framework

STOCK MARKET BENEFIT : FOR WHOM THE BELL TOLLS ?

ABUL KHAIR AL-MUQTADIR*

Perhaps one of the important elements in opting for public floatation by a corporate concern is participation in the capital market. Generating unfettered fund from the 'public' may be an imperative consideration. But 'floatation' does involve contemplation about mingling in the stock traffic. Well then, why should companies want to mingle in the stock market ? The best answer may be - for the reason that it is the only source that can provide interest free funds for the company. Yes, the conventional approach of debt based business is fudged by the advent of public floatation, a process fundamentally based on the perception of a forum called the stock exchange. This is because, the concept would not have come out successful without an open avenue for selling and buying of shares and securities.

But interestingly, this buying and selling again is done not by the issuers of shares. That, being a different discipline, is left alone for a separate set of beneficiaries known as the brokers and dealers etc. rolling on the floors of the stock exchange. They are the operators who thrive on securities issued by companies, leaving aside the companies. To complement, the arrangement does not include the investors either. Rather they are the onlooker to the fishing and finishing ! But then who fetches the actual benefit of the mechanism. In direct terms, the query should be as to who makes the market and who reaps the real benefit, or rather who moves the bell and for whom the bell tolls ?

So far, so many companies have fetched fund from the Bangladesh capital market by primary offers, some even to a tremendous extent. And mentionably, the secondary performances of some of such shares are rather mesmerizing. If we remember well, it was late in 1996 when the stock market gush in Bangladesh surpassed all contemporary records in comparison with even the neighbouring countries. To mention a few, shares of the nominal value of Tk. 100 each of a company in the engineering group and also one in the food and allied sector soared up to Tk. 25,000 and 17,000 each respectively. A maddening craze indeed ! It was simply a trying situation, helpful only to beguile the gullible investors and baffling all, even those in the monitoring helms, it went on. But as obviously, the bubbles did not last long. It got fused down and soon made the bumpy burst ! But by then, millions of fund slipped out of Bangladesh. However, slowly it settled down. After that jolt, now the situation is rather stable. Although, a trailing wail for lack of investors confidence is there, but the stock price situation appears to be somewhat fair and steady, atleast for the time being !

With that stable scenario in the background, however, more companies were expected to brave ahead to go and exploit the stock market benefit through the process of market capitalization. But from the last few years' experience it can be said that companies are rather shaky to participate in the process of so-called market capitalization. Why is it so ? Companies should rather volunteer to go and raise its much needed fund free of interest from the capital market. But it is true and well known that there is a remarkable decline in the trend.

Now then, a reverse question may as well be raised - why should a company go to the capital market for funds? Does it really make sense for it ? Given the context of an on-field scenario jammed with so many perplexing and paradoxical regulatory obligations, it is rather a mazing situation for a 'privately managed public company to go for initial public offer or IPO. The consequences follow in a way as if a sin has been committed by

* The writer is a Fellow and Founder Member and the Senior Vice President of the Institute of Chartered Secretaries and Managers of Bangladesh. He is also the Company Secretary of SABINCO, a joint venture financial institution. As a freelance activist, he also performs as a corporate consultant. (muqtadir@sabincobd.com).

the company so that it is now subjected to so many harassments - let alone venturing for AGMs. Why should a company go for much hassles and botherations ? Just for the 'fault' that it has raised interest free fund from the capital market ? If that were so, then there are alternative rights for the company as well to consider aloud.

There are other considerations to ponder about in the game. Why do the prices of shares enlarged in the stock market gallop over the days ? It is said that the prices of shares depend on the respective company fundamentals. But company fundamentals come out in the published financial statements of the company, which are presented only periodically and not daily. Whereas, prices change daily. They change because they float on the flows of market forces governed by the market operators. Now, it is these market operators only who actually cash on the change of prices - often through speculation or by manipulation. They cash on the throbbing prices of shares, an item that originates from the issuing companies. But the sorry story for the poor companies is that they are left alone and apart from the benefit, although it is they who create the securities.

The Ground Rules

In the arena of stock market, investment and trade have got two different meanings. While one goes to the offerer of shares, the other to the dealer. Supposing, X company floats shares to the tune of Tk. 50,000,000 and the response being overwhelming, it is over subscribed. So, the conventional outgrowth in Bangladesh is refund of excess subscription and allotment of shares to the extent of Tk. 50,000,000 only. To the company, the people who have bought its shares are treated as investors and the subscription as investment. The new share scrips will be issued in the name of the shareholders. Now let us say, one of the shareholders decides to sell a portion or full of his holdings. The share certificate concerned then goes to a new hand. This 'new' hand, in the members' register of the company will be treated as a shareholder with the same bearing and status as in the case before, but definitely not like an investor. This is because, at the time of share subscription the deal was between company and the investors. That position has now changed and the company has got nothing to do with the present cash transaction between two individuals. The only and obvious development necessitated for the company is to update its record. It would, however, be quite wrong to conclude at this point that the second kind of deal or trade has got no bearing on the shares of the company. But that again, is a separate aspect and different from our current concept.

The regulatory background in this respect may also be studied. In Bangladesh, it is the Securities and Exchange Commission, generally known as the SEC, which is responsible to or not to allow public floatation of shares. The SEC campaign for stronger corporate equity base, but then it does not allow retention of the excess subscription received from public floatation, that is capitalization of the oversubscribed amount for any company. That may, however, be apparently for the reason that such an action may vitiate and debase the prospectus basics of the company and could change the background of the floatation, to the detriment of the general investors. But then, the SEC does allow shares to be floated at premiums, much as a decorative for the sponsors on the one hand and with all likelihood to be for 'mutual' benefit, on the other.

The Securities and Exchange Ordinance 1969 provides the basic set of laws governing the capital market in Bangladesh. The SE Ordinance together with the Securities and Exchange Commission Act 1993 gives SEC, the control over the issue of capital by companies in Bangladesh. According to the law, no company incorporated in Bangladesh shall, except with the consent of SEC make an issue of capital outside Bangladesh. Further, no company, whether incorporated in Bangladesh or not, shall, except with the consent of SEC make an issue of capital in Bangladesh, or any public offer of securities for sale or renewal or postponment of the maturity or repayment of any security maturing for payment in Bangladesh.

About the current situation, it is to be added that the SE Ordinance 1969 has been amended several times recently to give the SEC more and more apparently unfettered rights to issue directions to the capital market stakeholders. Two of the important provisions in this respect are Sections 2CC and 20A. Accordingly, an anomalous and potentially undesirable situation is being created whereby the regulatory agency is in effect amending the provisions of an Act of Parliament i.e. the Companies Act, without any further reference to the legislature and often swift reactions to the emergent situations in the capital market.

The SEC during 2002, using the powers granted under the above quoted sections of the SE Ordinance 1969, instituted a categorization formula of companies on the basis of their regularity in holding AGMs and the regularity and quantum of dividends. Accordingly, stocks were classified in category A, B or Z. Now, category A stocks are companies that held their AGM during the last year and declared dividends above 10%. Category B includes companies that held an AGM during the last year, but declared dividends less than 10%. Those companies that either did not hold an AGM or did not declare dividends are considered category Z companies. New issues are also placed in categories based on their earnings per share. The SEC notifications declared that companies which remain in the Z category for over one year must reconstitute their Board by holding an EGM within six months. Further, their Managing Director and Chairman should be appointed with SEC approval and new directors must be appointed in proportion to groups of shareholders. Now, it is important to note here that by the above categorization, the SEC is infact trying to regulate companies with the benchmark of dividend payout ratio and thus considering performance as a proxy for compliance.

Capital Market Scenario in Bangladesh

There are two stock exchanges operating in Bangladesh, one at Dhaka and the other at Chittagong. The Dhaka Stock Exchange Limited (DSE) is the pioneer bourse and far more older in the scene, although the Chittagong one is relatively more organized and updated in terms of technical awareness. However, both are modestly active in their business. The Chittagong Stock Exchange can be operated from the capital city and Sylhet, a north eastern town notable for home of the affluent non-resident Bangladeshis.

After the surge of events in mid 1990s - starting from a general upturn in 1994 and leading to a boom that eventually crashed in 1996 - there have been various piecemeal and adhoc attempts to rejuvenate the market and bring back the investors, without mentionable success in sight.

As of the end of 2002, there are 239 listed companies on the country's main bourse, the DSE. Market capitalization was Tk. 68,677 million (US$1,184 million) in 2002, an increase of only 0.68% over 2001. The DSE market capitalization amounted to 2.52% of GDP at the end of 2001. DSE's performance over the last year has been lackluster as well. The DSE All Share Price Index gained only 2.27% between 2001 and 2002. There were eight IPOs during 2002, a decline from eleven in the previous year. The number of companies holding AGMs was similar over the last two years : 79% of the total listed companies held AGM regularly in 2002, compared to 77% holding AGM in 2001. During 2002, there were a number of reform measures undertaken at the DSE. Twelve non-brokers were included as members of its policy-making council. But there is no representation from the investors or issuing companies in the DSE council. Conspicuously enough as well, the DSE does not also include in its council anybody as representative from the Institute of Chartered Secretaries and Managers of Bangladesh (ICSMB), which is more apposite in terms of its objectives, although the ICAB is well represented there.

It may be relevant here to look at some key data of the prime bourse, the DSE :

Dhaka Stock Exchange select statistics

Particulars	*Dec 1999*	*Dec 2000*	*Dec 2001*	*Dec 2002*	*'01 -'02 change*
No. of listed companies	221	230	231	239	3%
Market capitalization (in million Dollar)	870	1,165	1,176	1,184	0.68%
Market capitalization as % of GDP	2.04%	2.65%	2.52%	NA	—
DSE all share price index	647.95	853.75	829.61	848.41	2.27%

Source : Bangladesh Enterprise Institute (Aug. 2003) & AIMS of Bangladesh

The overall performance measures of the stock exchange show low trading volume, intermittent and very few new offerings and declining valuation. This lack of depth in equity market makes it feebly transparent and resultantly less attractive.

The Impediments

In Bangladesh, the fundamental spokes of an efficient capital market wheel are not in place. The average non-controlling shareholder in this country is an individual who does not possess sufficient level of education, understanding and sophistication required to exert pressure on a company to change its corporate behaviour. Institutional activism is also not there owing to poor outgrowth. As a result, market prices of shares fail to have any kind of disciplining impact on management and companies have no incentive to be transparent.

Because of the built-in weaknesses in the stock market, corporate entities see few benefits in becoming a public company and listing on the stock exchange. The capital market does not appear to offer adequate incentives to become a public company and enlist on the stock exchange. On the cost side, listing involves the expenses of filing the voluminous appropriate documents, bureaucratic obstacles and bothersome additional disclosure obligations. The SEC requirements for proportionate board composition are a further impediment to local conglomerates and the multinationals.

In contrast to the capital market, Bangladesh has by now developed a moderately ranked banking network with relatively unutilized cash resources and with that kind of a competitive backdrop, banks these days tend to be venture-hungry. Accordingly, as far as benefits are concerned, capital can be more easily raised through bank borrowing since companies with good reputations face little problems in obtaining adequate capital from banks. Bank financing is readily available now as a result of excess liquidity and extensive competition in the banking sector due to the fact that new private bank incences had been issued mostly on political considerations. Banks therefore are reluctant to enforce additional requirements or strict conditions of lending. This phenomenon is amply substantiated by a recent survey, which revealed that equity requirement had been the prime motivator for only 10% of the public companies, which came under the survey interview. The remaining corporates had cited reasons like, tax advantage and legal compulsions for going public. All the private companies interviewed expressed their total dissatisfaction with the state of the capital market and hence preferred to continue as private companies. That situation further indicates that the companies, which cannot obtain bank financing, may go to the equity market, which means in ultimate effect that listed companies are prone to be weaker companies. There is an optimum level of debt in a company's capital structure after which point debt should become more expensive and the risk of committing to fixed debt servicing becomes too high. This question, however, appears not to hold true in the case of Bangladesh. Here, banks do not increase lending rates for companies that carry high debt loads and there is little hazard in high levels of leverage. Companies are comfortable with high fixed debt payments because they know that the penalties for debt-default are not necessarily severe. Banks, as a consequence, end up with high levels of non-performing loans and resultantly there is a low demand of equity financing. Thus in Bangladesh companies are neither disciplined by the market forces, nor by the agencies tasked with regulating their behaviour. The end result, therefore, is : weak control breeds weaker entities whereas lack of benefits shy the firm-footers away from the capital market.

Sharing the Benefit

Now, why should a company envisage to go for public floatation undergoing so many hazards as mentioned above ? And why should it allow its shares to be traded on the stock exchange riddled with problems ? Just for the sake of raising interest free fund from the capital market ! Well, that kind of a perspective will be quite an incomplete contemplation. There has to be a mechanism whereby companies can also reap atleast some of the market benefits of share trading. The concept that - shares issued and later traded are infact matters of the company - must be given the value it weighs. Companies also need to raise their status from the primary market to the secondary market. Playing intermediaries should share their market benefits, whatsoever there is, with the respective issuers, since their trading item i.e. the securities originate from them. The old role of companies merely to watch price manipulation and then issue press release protecting their position has to be revised. So, companies should also be allowed their due share of benefits from the stock market. This can be instituted by a formula what may be designated as Stock Market (Benefit) Formula acronymed as the SMF. The formula works out on the volume of trade of shares of respective companies.

To accommodate such a scheme, the old way of looking at the system has to be changed. It is the stock exchange that has to play a reciprocating role towards the company. A levy on the total volume of trade of a company's share, to be paid to the company, is the guiding factor in this case. For example, the total turnover of trade of XYZ Company's share amounts to Tk. 50,000,000 in a month. Now, it is certainly because of the company's market reputation, strength in its balance sheet fundamentals and business performance put together in a given period, that matters on the volume of trade of shares of that company. The shares of that company are bought and sold by brokers, traders, and above all, by investors not just because of the so called stock market mechanism. The forces of the market do play its part. But, by and large, the success or failure of a company is one of the main influencing factors behind the volume of trade of stocks of any particular company. So, there is no reason why the company should not be rewarded for the high volume of trade of its shares. In the given case, a market premium of say 1%, to be fixed on the scale of volume of trade, may be considered payable to the company as its part of trade. Since all shares are now tradable only on floors of the stock exchange, such market premium should be paid ideally by the respective stock exchange to the company. It may be paid monthly or annually as decided by the policy makers. However, there should also be some minimum ceiling on the volume of trade of any particular stock in a given period that would invoke the premium fee payable. The policy makers may also decide about that ceiling initially. But the rules and the formula have to be clearly defined for smooth trading in the stock exchange and for contentment of the companies.

It is to be added that since companies do not directly engage themselves in the day-to-day trading of their shares, there will be no conflict of interest in the arrangement. The Stock Market (Benefit) Formula is aimed to bring about change in the market concept on securities trading. The objective of the scheme is to include the main partner of a share issue programme i.e., the company into the fold of secondary market trading. The scheme is likely to defuse the tendency of price manipulation of securities since there will be an understandable check and balance between market operators and the company. At the same time, it is also likely to imbue more companies to go public and get into the secondary market.

Bibliography

1. Securities and Exchange Ordinance 1969.
2. SEC Notifications.
3. Listing Regulations of Dhaka Stock Exchange.
4. DSE & CSE publications.
5. ‘A Cluster of Concepts’ (book on finance and commerce).
6. ‘Charting Roadmap for Bangladesh’ (a publication of the Bangladesh Enterprise Institute, August, 2003).

GATS : IMPACT ON COMPANY SECRETARIES

PARVEEN NAGREE-MAHTANI & SANDEEP FARIAS*

A. Introduction

A company secretary is essential to the Board of a company as well as in charge of the day-to-day compliance related activities of a company. The Secretary is privy to all the information made available to the Board, as well as the decision making of the Board. Apart from statutory duties, a company secretary may also have duties assigned to him under the Articles of Association of a company or under a contract with the company.

The General Agreement on Trade in Services (GATS) of the World Trade Organization regulates trade in services and company secretaries would fall within the purview of the GATS. The opening of the company secretarial practice by India could have considerable impact on the entry of foreign players, resulting in increased competition. In addition, the liberalization of the company secretarial practice by other nations would also determine the extent to which company secretaries in India would be able to globalize and offer services abroad as well as establish their presence in such nations.

However, the profession of company secretaries is peculiar only to certain countries as their terminology differs. Additionally, in certain countries there is an overlap in the performance of the functions of a company secretary. This ambiguity can lead to several interpretation issues as to the extent of market access and national treatment that a nation offers to the company secretarial practice under the GATS. This paper seeks to explore some of these issues.

But first it is important to provide an understanding of certain basic issues pertaining to the GATS.

1. THE BASIC AGREEMENT

The GATS emerged from the Uruguay Round of Negotiations (1986-1994), establishing the rules governing trade in services and providing a framework for multilateral negotiations. The GATS comprises of 6 parts and 29 Articles. Part I sets out the scope of the terms used therein and definitions of the agreement. Part II deals with the general obligations and disciplines that apply to services and to all Members. Part III sets out rules governing the specific commitments in the Schedule of Commitments. Part IV deals with future negotiations in relation to the Schedule of Commitments. Parts V and VI cover institutional and final provisions.

Article I of the GATS defines the scope of the agreement, specifying that it applies to measures adopted by WTO Members which affect trade in services. The GATS encompasses not just measures imposed by the central governments, but also includes measures taken by regional and local governments, as well as non-governmental bodies exercising powers delegated to them by governments. Any service in any sector is covered by the GATS, except those services "supplied in the exercise of governmental authority".[1] Services "supplied in the exercise of governmental authority" are defined as any services which are supplied neither on a commercial basis nor in competition with one or more service suppliers.[2] Although the scope of the GATS is very wide, some of the following matters lie outside the GATS disciplines, provided, measures adopted in these matters are not used by a Member as a means to circumvent its obligations:[3]

---

* Nishith Desai Associates

1. GATS, Article I: 3(b).
2. GATS, Article I: 3(c).
3. European Commission Info Point on World Trade in Services; "To what does GATS apply?"; available at http://gats-info.eu.int/gats-info/guide.pl?MENU=bbb-2 accessed on November 28, 2002.

— Immigration rules;
— Services supplied under Government Authority;
— Fiscal policy and taxation measures;
— Customs systems;
— Certain aspects of investor protection concerning the movement of capital;
— The exchange rate management, the WTO will work with the IMF and World Bank to create conditions of greater economic stability, including exchange rate management (e.g. by setting interest rates);
— Privatisation forms of ownership as such are not addressed, but there are disciplines for state-owned trading entities and monopolies.

2. MODES OF SUPPLY

Article I (2) of the GATS sets out four different modes of supply of services viz. cross-border, consumption abroad, commercial presence and presence of natural persons.

(a) *Mode 1: Cross Border Supply*

Cross-border supply of services or "Mode 1" covers services flowing from the territory of one Member to the territory of another Member, for example, banking, architectural services or postal services transmitted via telecommunications or mail. It is in many ways the most straightforward form of trade in services, because there is a clear geographical separation between the seller and buyer and only the service crosses national frontiers.

(b) *Mode 2 : Consumption Abroad*

Consumption abroad or "Mode 2" is the supply of a service in the territory of one Member to the service consumer of another Member. Typically, this will involve the consumer travelling to the country where the service supplier is located, for example, tourism, education, medical services or the repair of a ship or aircraft outside its home country.

(c) *Mode 3 : Commercial Presence*

Commercial presence or "Mode 3" is the supply of a service through the commercial presence of the foreign supplier in the territory of another WTO Member. Examples would be the establishment of branch offices or agencies to deliver services such as banking, legal advice or communications. A large proportion of service transactions require that the provider and the consumer be in the same place. Mode 3 does not necessarily require the presence of foreigners in the Member country. The foreign supplier's office may be staffed entirely by local personnel. However, in the event the supplier needs to employ some foreign personnel, Mode 3 would be read together with "Mode 4" which deals with the presence of natural persons.

(d) *Mode 4: Presence of Natural Persons*

"Mode 4" relates to the admission of foreign nationals to another country to provide services there. Mode 4 may exist by itself, without any commercial presence (Mode 3) and the persons involved may be employees of a foreign service supplier or may provide services as independent individuals. The Annex to the GATS on Movement of Natural Persons specifies that Members are free to determine measures regarding citizenship, residency or access to the employment market on a permanent basis. Therefore, even if Members undertake Mode 4 commitments to allow natural persons to provide services in their territories, they may still regulate the entry and stay of the persons concerned, for instance, by requiring visas. Such regulations should not prevent the commitments from being fulfilled.

The four modes of supply may be explained by way of an example of postal services as follows[4] :

MODE	*DESCRIPTION OF MODE*	*POSTAL SERVICES EXAMPLE*
1.	CROSS-BORDER SUPPLY	FAX, E-MAIL
2.	CONSUMPTION ABROAD	USE OF INTERNATIONAL MAIL SERVICES OF THE CONSUMER'S DOMESTIC POSTAL SERVICE
3.	COMMERCIAL PRESENCE	DOMESTIC POST OFFICE REPRESENTATIVE OFFICE, AGENT ETC.
4	PRESENCE OF NATURAL PERSONS	POSTAL CONSULTANCY SERVICE

3. GENERAL OBLIGATIONS

(a) *Most Favoured Nation Principle*

The Most-Favoured-Nation ("MFN") principle is embodied in Article II of the GATS which states:

"With respect to any measure covered by this Agreement, each Member shall accord immediately and unconditionally to services and service suppliers of any other Member treatment no less favourable than it accords to like services and service suppliers of any other country".

4. Tim Walsh, Consignia; "The WTO, GATS & Posts: Issues for Postal Operators" available at http://www.posteurop.org/newspdf/gats.pdf accessed on December 30, 2002.

However, particular measures inconsistent with the MFN obligation can be maintained.[5] More than 70 Members have made a list of exemptions under Article II to their scheduled service commitments.

Each country is required to provide five types of information for each exemption:

(i) Description of the sector or sectors in which the exemption applies;

(ii) Description of the measure, indicating why it is inconsistent with Article II;

(iii) The country or countries to which the measure applies;

(iv) The intended duration of the exemption;

(v) The conditions creating the need for the exemption.

The list of MFN exemptions were submitted at the end of the Uruguay Round of Multilateral Trade Negotiations and by the conclusion of extended negotiations on certain sectors for which the delayed submission of related exceptions has been expressly authorized. Certain exemptions are subject to a specified time limit. For those which are not, the Annex on Article II exemptions provides that, in principle, they should last no longer than ten years (that is, not beyond 2004) and in any case, they are subject to negotiations in future trade-liberalizing rounds.

It is a basic principle of the GATS that specific commitments are applied on an MFN basis. Therefore, where commitments are entered into, the effect of an MFN exemption can only be to permit more favourable treatment to be given to the country to which the exemption applies than is given to all other Members. Where there are no commitments, however, an MFN exemption may also permit less favourable treatment to be given.

Apart from services specified in individual MFN exemption lists, the only permitted departure from MFN treatment under the GATS is among countries which are Members of regional trading arrangements as per Article V of the GATS, which deals with "Economic Integration". Article V permits any WTO Member to enter into an agreement to further liberalize trade in services with other countries, provided such an agreement has substantial sectoral coverage and provides for non-discriminatory measures which are in line with the provisions of national treatment under Article XVII of the GATS.

(b) *Principle of Transparency*[6]

One of the basic principles of the GATS is the principle of transparency embodied in Article III. Each Member is required to publish all relevant measures of general application, that is, measures other than those that involve only individual service suppliers, which affect the operation of the GATS. Members are also required to notify the Council for Trade in Services of new or changed laws, regulations or administrative guidelines that affect trade in services covered by their specific commitments under the GATS. Each Member was required to establish an enquiry point by the end of 1996, to respond to requests from other Members for information on the aforesaid matters. Developed countries (and other Members, if possible) are required to establish contact points to which the service suppliers and not merely the governments of developing countries can approach for information about commercial and technical aspects of the supply of services, professional qualifications required and the technology available.

4. SPECIFIC COMMITMENTS

Part III of the GATS lays down rules for specific commitments of Members. Article XVI and XVII of the GATS deal with market access and national treatment, respectively. Members are required to specify the extent to which they undertake commitments in their respective Schedule of Commitments ("Schedule of Commitments").

5. Please refer to Article II: 2 and the Annex on Article II Exemptions for the list of exemptions to the MFN obligations and the measures inconsistent with the MFN obligations of the Members.

6. GATS, Article III.

(a) *Method of Scheduling Commitments*

The Council for Trade in Services adopted the "Guidelines for the Scheduling of Specific Commitments under the General Agreement on Trade in Services" on March 23, 2001 ("Scheduling Guidelines")[7] . The Schedule of Commitments lists twelve broad sectors, which correspond to the GATT Secretariat classification. These twelve sectors are further sub-divided into 160 sub-sectors or service activities. The twelve basic sectors are:

— Business services
— Communication services
— Construction and related engineering services
— Distribution services
— Educational services
— Environmental services
— Financial services
— Health-related and social services
— Tourism and travel-related services
— Recreational, cultural and sporting services
— Transport services; and
— Other services not included elsewhere.

For each service sector or sub-sector, the Member must indicate any limitations on market access or national treatment, which are to be maintained, with respect to each of the four modes of supply. The following is the diagrammatical representation of the Schedule of Commitments:

COUNTRY NAME — SCHEDULE OF SPECIFIC COMMITMENT

Modes of supply :

(1) Cross-border supply (2) Consumption abroad (3) Commercial presence

(d) Presence of natural persons

Sector or sub-sector	*Limitation on market access*	*Limitation on national treatment*	*Additional commitments*
I. HORIZONTAL COMMITMENTS			
	(3) (4)	(3) (4)	
II. SECTOR SPECIFIC COMMITMENTS			
Sector	(1) (2) (3) (4)	(1) (2) (3) (4)	

The first column contains the sector or sub-sector which is the subject of the commitment; the second column contains limitations on market access and the third column contains limitations on national treatment. In the fourth column, Members may enter any additional commitments, which are not subject to scheduling

7. Please refer to Annexure 2 of this Report for the Scheduling Guidelines.

under market access or national treatment. Where commitments do not cover the entire national territory, the entry should describe the geographical scope of measures taken, according to Article I: 3(a)(i).

In nearly all schedules, commitments are split into two sections. The first section contains "horizontal" commitments, which stipulate limitations that apply to all of the sectors included in the Schedule of Commitments. These often refer to a particular mode of supply, mainly commercial presence and the presence of natural persons. Any evaluation of sector-specific commitments must therefore take the horizontal entries into account. In the second section of the Schedule of Commitments, commitments which apply to trade in services in a particular sector or sub-sector are listed.

(b) *Market Access*

Article XVI states that each Member is to give no less favourable treatment to the services and service suppliers of other Members than is provided in its Schedule of Commitments. Members may set out the minimum treatment that will be accorded to the foreign services or its supplier. Article XVI also sets out six types of measure affecting free market access that shall not be applied in respect of foreign services and service suppliers unless they are clearly provided for in the Schedule of Commitments. Therefore, measures beyond these six types of measures may be imposed on foreign services and service suppliers.[8]

(c) *National Treatment*

Article XVII provides that subject to any conditions and qualifications set out in the Schedule of Commitments, each Member is obligated to accord treatment to foreign services and service suppliers in measures affecting supply of services, treatment no less favourable than it gives to its own like, services and suppliers.

(d) *Terminology used in the Schedule of Commitments to denote the Extent of Commitment of Members*

A Member may inscribe the limitations to market access and national treatment through a particular mode in the relevant sector. The entries in the Schedule of Commitments use uniform terminology:

(i) **NONE** – In this case, the Member makes a full commitment and does not seek in any way to limit market access or national treatment in a given sector through a particular mode of supply of services. The Member will specify 'NONE' in the appropriate column of the Schedule of Commitments.

(ii) **UNBOUND** – The Member is free to introduce measures inconsistent with market access and national treatment and records 'UNBOUND' in the appropriate column under a specified mode of supply. This case is only relevant where a commitment has been made in a sector with respect to at least one mode of supply.

(iii) **UNBOUND**[9] – Where it is not technically feasible to give access through a particular mode of supply, for instance, hair-dressing services through cross-border supply, 'UNBOUND*' is used under the relevant mode of supply.

In many cases, Members have not followed the aforesaid uniform terminology but have adopted one of following approaches:

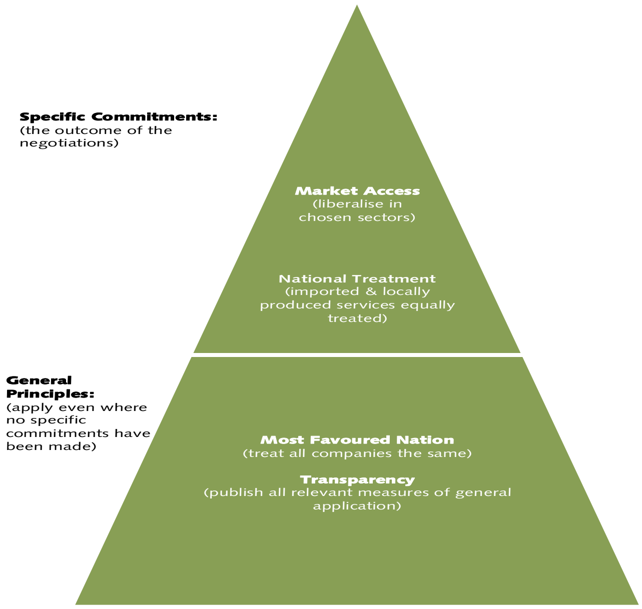
— The entry describes in the appropriate space the nature of the limitation, indicating the elements, which make it inconsistent with Articles XVI and XVII of the GATS.

— In some cases, Members have chosen to indicate a limited commitment by describing what they are offering rather than the limitations they are maintaining. Such an approach is often used to indicate the market access opportunities for the entry of certain categories of foreign natural persons who supply services.

8. Please refer to Section 3.2 of this report for a further discussion on this subject.

9. Raja Ghosal; WTO Request List to be Ready Soon; November 29, 2002; available at http://in.news.yahoo.com/021103/58/1xbuh.html accessed on September 4, 2003.

The general obligations and specific commitments under the GATS can be diagrammatically explained as follows:



B. Classification of Company Secretary Service

The profession of company secretaries is peculiar only to a few countries such as India, UK, Malaysia and Australia. They are known as "chartered secretaries" in UK, Malaysia etc., while come countries do not have a specific post for this kind of service.

India has made commitments in only 6 out of the 12 sectors in the GATS Schedule i.e. (i) business, (ii) construction and related engineering, (iii) financial, (iv) tourism and travel related services, (v) communication services and (vi) health and related services. India has not made commitments in (i) educational services (ii) transport (iii) distribution (iv) environmental services (v) recreational, cultural and sporting services (vi) other services not included elsewhere.

The company secretarial practice would fall within the "Business Services" sector category and the sub-sector "professional service". The following are the sub-sectors in the "professional services" sub-category: (i) legal (ii) taxation (iii) engineering (iv) urban planning and landscape architectural (v) vetinerary (vi) accounting, auditing and book keeping (vii) architectural (viii) integrated engineering (ix) medical and dental (x) services provided by midwives and physiotherapists (xi) others. India has made commitments only in the engineering services category.

The "professional" service category does not specifically provide for the sub-sector for company secretaries. As the classification of the service would determine the obligations of any Member country, there could be some ambiguity on the classification of the company secretarial service. For example, one could argue that company secretarial service is included in the "accounting, auditing and bookkeeping service" sector of the GATS or the "other" service sub-category under the "professional services" category. From an Indian point of view, however, it is useful to point out that India has currently made no commitments in both the "accounting, auditing and bookkeeping service" sector or the "other" sector.

Further, Member Countries have included other professions and services in this sector, which has led to further ambiguity of the scope of this sector. For example, Australia has included limitations for "liquidators" in this sector. Mongolia has included "management" services in this sector. Cuba has specifically provided for a "other" category within the accounting, auditing and bookkeeping service sub-sector. This kind of residual classification within a sub-sector, such as provided by Cuba, could lead to an interpretation whereby a company secretarial practice could be classified in the other category of this "accounting, auditing and bookkeeping service" sector, or could be classified within the "other" sub-sector in the main category of "professional services.

In the "other" category of the "professional services" sector, only five countries have made commitments viz. Iceland, Singapore, Peru, Trinidad and Tobago, and Sierra Leone. Iceland has applied no limitations in this residual category. Therefore, in the event that the company secretary service is classified in the residual "other" category, there would be no limitations to market access and national treatment in Iceland except for market access in Mode 4 (movement of natural persons). Singapore has included interior design services in the "other category". Peru has limited this sector only for management consultancy in the tourism sector. Similarly, Trinidad and Tobago has limited this sector to patent agents.

Hong Kong has included in the "accounting, auditing and bookkeeping services" auditing and advisory services on matters such as financial management consultancy, company formation and restructuring, raising of capital, debt-rescheduling, receivership and liquidation. In the case of Mode 4 (movement of natural persons), it has specified that it is "unbound" in the market access column in this category except for intra-corporate transfer of general managers, senior managers and specialists as set out in the Attachment to the Schedule of Commitments. The Attachment defines a "specialist" as a person within an establishment of a service supplier of a Member who possesses knowledge at an advance level of expertise, possesses proprietary knowledge of the organization's service, research equipment, techniques, or management and who is essential to the operation of the establishment of that service supplier in Hong Kong. It is not clear whether the company secretary service is included in this category by virtue of the service falling within the definition of a "specialist" since a company secretary has a level of expertise in his area of practice and possesses proprietary knowledge about an organization. Hong Kong has made no commitments in the "other" category of the "professional services" sector.

A survey was conducted by a Malaysian university with the permission of the accountant and company secretaries associations of Malaysia to get responses for the impact of the liberalization of the GATS on the accountancy services. Malaysia has included the company secretarial practice within the accountancy service. According to the report, there are three types of accounting professional services that are perceived to be most susceptible to competition via internet: accounting and taxation services, company secretarial services and management advisory or consultancy services. If this analysis is adopted whereby the company secretary service is included in the accountancy service, then the obligations of each country within the accounting sector would need to be examined to understand the impact on the company secretary service. India has currently made no commitments in the accounting sector.

The report states that the Malaysian accounting sector (which would include the company secretary sector) would face competition basically from two groups of professional service providers. The first group comes from the advanced economies as their members are perceived to have higher skills and expertise than local counterparts. The second group is from lower-cost economies, like Phillipines and India, and their members who are able to offer their services at a much lower cost. Further, restrictions on supply of service through commercial presence and movement of natural persons were considered the most necessary measures, followed by the requirement of membership in domestic professional bodies for the issuance of licenses. Requirement of specific local educational qualifications was rated the least necessary measure.

A total of 57% of people surveyed suggested varying forms of government protection against foreign competition, such as insisting on local equity in foreign professional firms, requirement to pass local professional exams, obtaining licenses to practice and restriction on employment of foreign professionals.

It is interesting that other countries see Indian company secretaries as a potential threat.

C. Nature of services of a company secretary: Companies Act, 1956

As per Section 2(45) of the Companies Act, 1956, a "secretary" has been defined to mean

> *"a company secretary within the meaning of clause (c) of sub-section (1) of Section 2 of the Companies Secretaries Act, 1980 and includes any other individual possessing the prescribed qualifications and appointed to perform the duties which may be performed by a secretary under this Act and any other ministerial or administrative duties".*

Therefore, broadly speaking, the practice of a company secretary could be classified as an "administrative" service. In such a case, there is no specific sector under the Schedule of Commitments of the GATS for "administrative" services. In such a case, it could be classified in the residual "other" sub-sector within the "professional services" sector. However, in certain countries, a director performs the role of a company secretary. This could lead to a overlap in the obligations that a Member country has made.

D. Recommendations of the Bhargava Committee

The Bhargava Committee was formed by the Department of Company Affairs (headed by Sunil Bhargava) to advise on the services sector (mainly the accountancy service sector). The Institute of Company Secretaries is also a part of the Bhargava committee.

The Committee has not only proposed a bar on the entry of foreign accountants, lawyers and company secretaries, but has also recommended a framework similar to that for trade in merchandise with safeguard mechanisms to check dumping, subsidization of services exports and emergency protection measures. In its report, the Committee has noted that in the present scenario where developed countries have placed stringent restrictions even on Mode IV (temporary movement of personnel), India should refrain from opening up its market for services by not allowing overseas services companies to operate in India.[9]

E. Conclusion

Member countries have not adopted a specific standard to classification of services. Due to the nature of service provided by a company secretary, it could be classified in the "accounting, auditing and bookkeeping services" sector or the residual "other" sector. The classification would directly relate to the market access and national treatment obligations of a Member country. The analysis of a unique service such as the company secretary service is an example of the ambiguity that can arise in relation to services that are unique only to a few countries.

What does the Indian company secretary need to do? The profession needs to examine where its opportunities lie. If, for example, there is clear evidence of opportunities in foreign markets for Indian company secretaries, it would be useful for India to negotiate accordingly and seek commitments from other nations to open up and permit Indian company secretaries to provide services in these foreign countries. However, the liberalization of the services sector for company secretaries whether in India or abroad is likely to be on a reciprocal and non-discriminatory basis – which would effectively increase competition in India.

Several strategies would need to be adopted to capitalize on the opportunities offered and to compete effectively with the foreign professional service providers when the sector is liberalized. The strategy that could be most appropriate is to develop the human resources and to enhance the professional knowledge and skills. Additionally, the service sectors should adopt IT-enabled tools to compete in a more liberalized environment. The third most important strategy for professional firms is to consolidate or merge to become bigger and more capable of offering a wide variety of services. A paradigm shift to "global thinking" or changing mindset as well as a greater transparency and professional work ethics will prepare the company secretarial service in India to compete more effectively post- liberalization and to capitalize on global opportunities.

BUSINESS ETHICS AND PROFESSIONALISM

JUSTICE S N KAPOOR*

The Ailment and Need Of Panacea

Corporate America reeled under a Spate of Scams

The Enron scandal has already spawned countless scandals, jokes and gags. One of them relates to period after Enron scandal and before Saddam's debacle in IRAQ.

Colin Powell walks into George W. Bush's office and says,

"Mr. President, I have some good news and some bad news." "What's the good news?" asks Dubya.

"Saddam has decided to allow UN inspectors to come in and check his research facilities for nuclear bombs."

"That's great." Says the President. "What's the bad news?" Replies Powell: "He is insisting on inspectors from Arthur Andersen.

To see some slightly more bizarre humour, check out the number of offers on E-bay, the auction site, by ex-Enron employees. They run into several pages, including this priceless gem: 'A mint condition edition of the Enron code of ethics, described as "unopened, untouched, just like the ones owned by most Enron executives." This collector's item- mint condition edition - had been snapped up by eager buyers for around $46 (considerably more than the price of Enron stock).

It is not a laughing matter. The biggest bankruptcy in the American history has destroyed the life of thousands of employees holding worthless Enron stock given as part of their wages and their pension plans. The Enron scam of 2001 was followed by several large U.S. companies like the **World Com scam, Global Scam, Cruising scam, Xerox scam and the collapse of the Audit firm Anderson**, are too familiar too be ignored.

INDIAN CORPORATES- Scams since 1992

The Indian editions of Enron scandal are several but we have no dearth of Benami Partnerships, front companies and siphoning away of hard earned money of poor investors. Forget the hundreds of companies that collect money from gullible investors and then disappear, even some of the more reputed names in our corporate firmament blatantly indulge in conflict interest.

"Missing from BSE: Rs. 10000 Crores" was the headline of the Sunday Express of 25th May 2003. Express investigation claimed that nearly half the Bombay Stock Exchange's 5651 companies had been banned from trading and 11 million investors have at least lost Rs 10000 Crores.

To appreciate **plight of poor victims** of such fraud, take the case of **Pal-Peugeot Limited**. It crashed in an early 1997 implosion leaving thousands of workers in its Kalyan plant jobless, saddling financial institutions with huge non-performing assets (NPAs) and investors with dud shares. Shares and debentures helped them raise a total of Rs. 200 Crores in February 1996.Financial institutions took the biggest hit of Rs. 160 crores (investment of Rs. 120 crore in company debentures and another Rs. 30 crores in its shares) Small investors lost another Rs. 41.7 Crores. S Kale a worker at Pal Peugeot's Kalyan Plant tried selling *chapattis* at Kalyan railway station after loosing Rs. 35 thousands in salary and wondered what mistake did he make in working with Pal Peugeot for free. Doshis continue to live in Mumbai's posh Peddar Road while the European partner has quit India.

---

* Former Judge of High Court of Delhi, Dealing with Company Matters.

One Pied Piper Rakesh Kant Syal set up **Golden Forest** India Limited befooled 24 lakh investors in 11 states; and collected Rs. 3000 Crores by selling a dream of doubling the money within three and a half years; increasing into ten fold in ten years and two hundred twenty two times in 25 years. He took their money and he took their land as well. According to Punjab Vigilance Department, he hived off more than Rs. 3000 crores. He got a helicopter to fly from his house to office, all within Chandigarh. He has thousands of acres of land. But the Vigilance Department got nothing. It is said that even liquidator has not ben appointed for Mumbai and Punjab and Haryana High Court matters are pending consideration before Supreme Court, as reported in Indian Express. Today Syal's lavish life style is slightly toned down in Model Jail in Chandigarh where he is cooling his heels with his wife Neena, father Amrit Lal Syal brother Rajesh Syal and sister Pameela Syal. The investors are waiting since long to collect their money and land back.

In the **CRB Capital's case**, C R Bhansali similarly raised Rs. 1100 Crores and made it vanish into thin air. With 133 companies he had dream run; and neatly tipped Rs. 1100 crores into a funnel of dud companies.

Name of Harshad Mehta and Ketan Parekh are so well known that you may not forget them. List of companies who sailed in same kind of boats, sank the boats and swam away from the scene with stolen treasure and took it to unknown places.

Such colossal frauds caused shockwaves, temporarily. One good rainy season and Sensex is rising and flying again likes a Phoenix. What a wonderful resilience has been shown by unblemished companies and Indian Economy? But pause and imagine if this amount of Rs 10000 Crores has not been lost by about 11 million investors, what would have been sentiment of the money market and Sensex?

MODUS OPERANDI

In these scams, crooks and powerful players, in connivance with the promoters of the company: -

(a) Manipulated the Stock Market;

(b) Diverted money raised through public offerings to the stock markets or through borrowings or by making false statements in the offer documents with a view to manipulate and make quick personal gains;

(c) Made defaults in repayment of deposits and debentures and other debt instruments;

(d) Allowed off -the book activities to make financial condition appear better than it was;

(e) Failed to ensure adequate public disclosure of material off the books liabilities;

(f) Failed to ensure independence of companies' auditors by allowing internal and external audit by personnel of virtually the same company or its sister concerns; and

(g) Allowed Directors and officers of the Company to use corporate funds as private equity fund.

Efficacy of the Panacea-Statutory Amendments and Rules and Regulations

If Enron led to passing of Sarbanes-Oxley Act in June 2002; its Indian versions also led to formation of Naresh Chandra Committee as well as Narayan Murthy Committee. Thank God this time due to Globalisation, the more sensitive Government and the pressure of investors by virtually shunning the money market, the reports of Naresh Chandra Committee and Narayan Murthy committees were seriously taken, acted upon and converted into statutory provisions, rules and regulations. All these suggestions related to Corporate Governance but a serious question about efficacy of corporate governance has been raised.

Narayan Murthy in this regard observed:

"Effectiveness of a system of corporate governance cannot be legislated by law nor can any system of corporate governance be static. In a dynamic environment, systems of corporate governance need to be continually evolved. The Committee believes that its recommendations raise the standards of corporate governance in Indian firms and make them attractive for domestic and global capital. These recommendations will also form the base for further evolution of the structure of corporate governance in consonance with the rapidly changing economic and industrial environment of the country in the new millennium".

If law, rules and regulations could prevail in all matters there would be no breach of such laws, rules and regulations, no action, no prosecution and no proceedings would have been required against any person. **Basic reason of all such scams was greed to become as rich and as powerful as King Midas overnight; it was and it is crisis of character and lack of vigilance and checks and balances.**

If these are limitations of statutory provisions, rules and regulations, we need something more, some self-regulating conscience, some sensibility, and some sensitivity of a human heart.

And, in the above backdrop we are discussing here business ethics.

WHAT IS BUSINESS ETHICS?

When we discuss "Business Ethics and Professionalism" at the 31st National Convention of Company Secretaries, we must appreciate the context in which we are supposed to talk about the subject.

One may feel it desirable here to appreciate meanings of these three words. As regards **"Business"** according to Chambers 20th Century Dictionary, it means **'employment; trade, profession or occupation; tasks or errand incumbent or undertaken; matter requiring attention; dealings, commercial activity, a commercial or industrial concern; one's concern or affairs, a matter or affairs, actions as distinguished from dialogue'**: In the present context it means commercial activities of a concern or an organisation where the company secretary is working.

"Ethics" means '**the science of morals, that branch of philosophy which is concerned with human character and conduct: a system of morals, rules of behaviour: a treatise on morals'**: Forgetting about **Swami Vivekanand's** philosophical definition of ethics; " **Ethics is unity; its basis is love"**. In the present context it would mean both philosophy of the concerned organisation and rules of conduct of business.

As regards **professionalism** one has to appreciate the term **profession** first. According to **Chambers Dictionary** the term **Profession** means 'The act of professing; an open declaration; an avowal; religious belief; a pretence; an employment not mechanical and requiring some degree of learning; a calling; habitual employment, the collective body of persons engaged in any profession'. On the other hand in the Webster's New world Dictionary, the term 'Profession' has been described as an occupation requiring advanced education and involving intellectual skills, as medicine, law, theology, engineering, teaching etc. Another definition of 'Profession' is that it is the body of persons in any such occupation. The random House Dictionary defines it as a vocation requiring knowledge of some department of learning or science.

The term **Professional** means ' pertaining to a profession; engaged in a profession or in the profession in question; competing for money prizes or against those who sometimes do so; undertakes as a means of subsistence; showing the skill; artistry, demeanour or standard of conduct appropriate in a member of a profession or of a particular profession; one who makes his living by an art; or makes it his career.

Finally, the most important term **Professionalism**, according to Chambers Dictionary, means 'the status of professional; the competence, or the correct demeanour; of those who are highly trained and disciplined; the outlook, aim, or restriction of the mere professional…'

BUSINESS ETHICS: DHARMA IN BUSINESS DEALINGS

Business ethics is gene and in law or codified ethics and concepts of Corporate Governance and Corporate Excellence and species thereof and as such these three facets of business ethics alongwith moral duty towards society are tributaries and sources of Ganga of Business Ethics.

Concepts of Corporate Governance

Our **Prime Minister Sri A.B. Vajpayee,** while describing "Corporate Governance", observed as under:

" Numerous debates, discussions, discourses and documentations, have broadly projected Corporate Governance as a multifaceted as well as multidimensional phenomena. And it involves Board of Directors, Shareholders, Stakeholders, Customers, Employees and Society at large. To build up an environment of trust and confidence amongst all the components, though having competing as well as conflicting interests, is a celebrated manifesto of the Corporate Governance. . On a tree, one may visualize fruits of more than one variety. And he may find himself in Wonderland"

In this regard what **Narayan Murthy Committee** has observed is also noteworthy:

"Corporate Governance is about ethical conduct in business. Corporate governance is beyond the realm of Law. It stems from the culture and mindset of Management and cannot be regulated by legislation alone."

It implies transparency of management systems in business and industry, be it private sector, public sector or the financial institutions, all of them being corporate entities. It encompasses the entire gamut of directions, controls, mechanics of the functioning of a company. It attempts to put in place a system of checks and balances between the shareholders, directors, auditors and the management.

The key to corporate governance practice is to set a goal for attaining the highest standard of good governance, meticulously pursue it and thereby maximise value for the shareholders, customers, employees, general public and last but not the least, the Government.

It is heartening to note that Indian Corporate world is making constant endeavour to improve the standards of corporate governance, to meet the requirements of a dynamic market. The Capital Market regulator SEBI has constantly been "improving" terms of listing Agreement and other regulations. In order to protect interest of all shareholders; and to ensure that the management complies with all legal norms; SEBI has ensured that the number of independent directors on the Board is increased and they do not shirk their responsibility, by making them accountable. Audit Committee would now be comprised only of independent directors, and they are expected to check all details of accounts and see that proper procedures were followed; they are supposed to quarry the auditors on various points and issues without having the management around.

Now, focus of the management is shifting rapidly from just looking after the interest of shareholders, to the job of looking after interest of all stakeholders, i.e. creditors, distributors, customers, employees, society at large, and the Government as well. Otherwise, a chemical company or say Union Carbide, can maximize their profit for benefit of shareholders, but can violate all environmental laws and may even endanger lives of the people living in its vicinity. Along the coastal Gujarat, numerous companies have maximized profits, but at the cost of livelihood of people living in the vicinity of their factories.

An example in this regard has been set by Infosys, by ensuring compliance of regulations of as many as six countries, and also the first company whose shares are listed in New York Stock Exchange.

The Indian Government has taken a very laudable step. On 2ndSeptember 2003 Union Cabinet approved a proposal to set up a Government-private venture, "National Foundation for Corporate Governance." It would be registered as a non-profit trust under the Indian Trust Act, 1882. Government will make a one-time contribution of Rs. Ten Crores as a grant, while CII would contribute Rs.3 crores; Rs.1 Crore each by ICAI & ICSI; and Rs.1 Crore by others. This Foundation intends to encourage good corporate governance and for this purpose, to ensure Research and Studies, Education, promotion and development; accreditation and awards, to provide a platform to deliberate upon issues relating to good corporate governance and the Foundation would virtually do everything in this regard. ICSI must be congratulated for its contribution and its determination to see that its members remain ahead of professionals of other countries in professional excellence keep.

It gives an impression that the entire business philosophy of capitalism is supposed to change from the business philosophy of the Merchant of Venice to the business philosophy of Trusteeship propagated by Mahatma Gandhi, or say from Darshan of Charvak to Visishthadwait.

My hunch is that too much of idealism may not be in larger interest of growth of all. We must opt for middle path to ensure that entrepreneurs do not start losing initiative on account of fast track of too many checks and reduced business secrecy. Suspecting bona fides of all business leaders is a negative approach and coupled with lower interest rates and constantly fluctuating stock market, it may impair, (a) domestic savings for capital generation; (b) growth of Indian industry; and (c) may encourage

consumerism in imported consumer durables. This aspect should not be ignored and needs threadbare discussions on impact of new regulations about increasing interference in management by independent directors.

CONCEPT OF CORPORATE EXCELLENCE

Dr. P.L. Sanjeeva Reddy, former Secretary DCA, while acting as Chairman of a study group to suggest ways and means of achieving corporate excellence, constituted a Task Force under the chairmanship of S. Rajagopalan, former Chairman, MTNL after having an in-depth study and interactive discussions with various chambers of commerce and professional bodies made certain key recommendations which read as under;

(a) Setting up of an independent, autonomous centre for corporate excellence, with a view to accord accreditation and promote policy research and studies, training and education and awards etc. in the field of corporate excellence through improved corporate governance;

(b) Introducing measures for greater shareholders participation, through multiple location meetings, or meeting through electronic media etc.

(c) Introducing formal recognition of corporate social responsibility with Triple bottom Line Accounting and Reporting.

(d) Clear distinction between direction and management that would ensure that the executive directors are held responsible for legal and other compliance with non- executive directors being charged with strategic and overall responsibilities.

(e) Highlighting directional commitment and accountability through fewer and more focused board and committee membership, tighter delineation of independence criteria and minimization of interest – conflict potential.

(f) Suggesting application of corporate governance principles to public sector undertakings, certainly in the case of listed companies and preferably even in the case unlisted companies, in terms of their board with independent directors.

These recommendations fall short of aim, purpose and objective of Business Ethics of total fairness to all for growth of all stakeholders, including society, government and of necessity of meeting environmental responsibility.

In the above background Business ethics could not be confined to just compliance of codified law or corporate governance for it does include social obligation. If it was confined to codified law, then it was not required as it would be just a surplus. Business Ethics of conscientious person in a conscientious society, is supposed to have **two sources of Business Ethics: one emanating from the conscience of the society and an other from the conscience of an individual,** One must not forget that Conscience of the society could cover only general situations, out of innumerable situations. . Consciousness of an individual should and does have freedom to act to meet peculiar situation according to his capacity, intelligence and conscience.

Similarly conscience of a company has to act as conscience of an individual and would neither be just satisfied with the compliance of codified law, nor would be able to meet the requirements of growth for benefit of all; nor it would be concerned with social obligations to serve its own larger self interest of prolonged period of few decades. Consequently Business Ethics has to include codified law to follow rules of corporate governance as well as an aspiration and will and determination to achieve corporate excellence. Corporate excellence is equally essential to explore the possibility of putting in place and implement able system and to develop firm infrastructure for business excellence to the satisfaction of all.

BUSINESS ETHICS –TO REGULATE HUMAN BEHAVIOUR

Every knowledge, law or rule or religious edict has to conform to the basic requirement of optimizing human happiness by reconciling conflicting claims between an individual and the society. Society itself would not exist in absence of individuals. Consequently, one has to appreciate factors deciding human behaviour, particularly when he indulges in business activities.

Before we consider further about other facets of business ethics recent studies may help us appreciate why do people react differently to the same situations.

According to **Kevin McCabe**, an economist and director of the Behavioural and Neuroeconomics Laboratory at George Mason University, underlying biological mechanisms effect the economic decisions and it leads people to act or not to act in accordance to new science of **Neuro Economics.** He observed in an answer to a question**: "Why do people react differently to the same situations?"** in the following words:

"Experimental economists have mapped out these anomalies and tested how much they affect economic interactions. Now a new field, called neuroeconomics, is using the tools of neuroscience to find the underlying biological mechanism that lead people to act, or not act, according to the economic theory."

Recently **Daniel Kahneman**, a professor of psychology at Princeton University, was awarded the Bank of Sweden Prize in Economic Sciences in Memory of Alfred Nobel on Wednesday by the Royal Swedish Academy for **research showing how quirks in human behaviour, such as a tendency to avoid risk or to be over-confident, lead people to behave in ways economist would consider irrational or that don't always bring positive outcomes.** Kahneman is the first psychologist to win economics' honour.

The other winner of the Nobel prize in economics was, **Vernon L Smith,** a George Mason University economist who took abstract economic theory and put it to the test in experimental labs, where he used students as guinea pigs to **demonstrate how financial bubbles could be created or how electricity markets can be deregulated.** It was the third year in a row that Americans were awarded the prize. The presentation of the award to Kahneman and Smith underscored a point that many economists have been slow to appreciate; **Markets are more complicated animals than Adam Smith might have led you to believe. They can overshoot or break down when not regulated well – a point all too familiar to many investors today**. Both researchers have spawned new fields in economics that are today among the hottest areas for younger academics.

An important insight in their work was that people are averse to recognising their losses, a point that helps to explain stock-market behaviour.

In April 2001, **the American Economic Association** awarded its prestigious **John Bates Clark** medal to **Mathew Rabin**, a University of California Economist. Mathew Rabin has developed a mythical model why people do irrational things such as procrastinate. An other Genius Award $ 5 lakhs, was given to Sendhil Mullainathan, a behavioural economist of **Massachusetts Institute of Technology.He** has studied how traits like will power and a sense of self-interest affect economic behaviour.

Vernon L. Smith, 75, a George Mason University economist pioneered the field of experimental economics, which is increasingly popular in academic departments around the US Smith's early work found **markets behaved with surprising efficiency**; when he asked students to simulate trading, prices in experiments tended to converge around an equilibrium that economists would expect.

The **Harvard Business Review** conducted a survey of top executives of leading business organisations to find out most basic and common characterstic of chief executives of America. The studied survey indicated that **most basic common factor in all the chief executives was self-control and steadfastness of mind. This implies setting up of process, precise goals and a consistent and persevering attempt to reach that goal again without wavering from the set objective or go after minor satisfactions without pursuing it further.**

Joseph Massie in his book "**Essentials of Management**" also advocates the same. "The increase in the complexity of relationships in modern society demands that managers become an elite of brains and educations. Entrance into this class is based more and more on education and knowledge. The Theologian would study the spiritual implications of managerial actions". He also says that **the managers typically face moral dilemmas in their decisions and actions and further observes that management must be concerned with questions of philosophy, which help it make value judgment** in its day-by-day activities.

The **behavioural science school of management** studies the forces, which drive men to action. They consider two concepts of "drive" and "habit" "Drive" is internal state of mind. Under conditions of drive an individual is aroused or his behaviour to pursue an objective is energized and activated. Habit is a connection between a condition or event and the individual's response to that event**; it follows that unless drive and habit are controlled, one will not be able to achieve one's objectives.**

Dr. Sarvapalli Radhakrishanan, in his book says: "Man knows only a part of his being, his surface mentality. We are sometimes completely overcome by emotions, instinctive and involuntary reactions that upset the role of conscious reason.….Under the stress of strong emotions, we say or do things, which we regret afterwards**. Unless the individual has complete self-awareness, he cannot become master of his life; by developing purity of intentions, man marches to success".**

LAW OF KARMA, GENES, HABIT AND SAMKALP & DRIVE

I believe that one has to understand above said concepts of drive and habit in larger concept of law of Karma. Firstly, one cannot escape effect of composite karma manifesting in the shape of birth of a child and his relation with a particular person as father and another particular person as his mother to take birth on genes inherited from them. Although humans mostly inherit the same basic sets of genes, the human genome, there are small variations in the structure of each gene. These inherited variations can result in considerable differences in the way brains of different individuals function because specific genes are needed for the production of neurotransmitters. While personality is shaped by many different influences through life, the biological component of personality/ temperament is present from birth and so is likely to be influenced by genes in addition, for behavioural characteristics and environmental factors.

Environmental factors such as parenting, education, lifestyle and diet will probably have at least as strong an influence as genetic inheritance. Neuroscientists do not claim that individuals inherit through genes, a business empire, or inherit anything in the shape of infrastructure, finance and other resources.

But even in worst situations one has to act like Arjun or Churchil who said 'we shall never surrender' and make an attempt to match effort with fate in the shape of aforesaid working forces. Only in this way one shall be able to achieve his objectives.

BUSINESS ETHICS, PHILOSOPHY AND MOTIVATION

What motivates a person to act .in different modes and moods? According to our Hindu **Philosophy** there are six schools of thoughts embedded in one's subconscience, which consciously or unconsciously predominate his thinking, inclinations, drives and habits and in short motivation of a person, leading him to act or respond in different, and in his own unique way. Without elaborating, for the sake of convenience we may divide these **six Darshanas** into two classes: one which takes into consideration welfare not just of the physical self but considers the welfare of the broader self which in addition to physical self also includes those also who directly or indirectly help him in his material and spiritual growth. This broader self includes all friends, relations, one's colleagues, social and economic order, environment and his society and community. . The other philosophy is that of Charavak Darshan. Those who are inspired by this Charavak Darshan have neither time nor inclination to think about welfare of others. They believe in "Yaavat Jeevet Sukham Jeevet, Rinam Krutwa Ghrutam Peevet". This latter one could not be a philosophy for a Business organisation; naturally, the "Business Ethics" of a giant concern could and would not be governed by such a restricting philosophy. Modern Business expects a philosophy, which helps an organisation to blossom into a giant **Kalpa Vraksha** from a tiny plant to fulfill desires of all who come under its shelter.

BUSINESS ETHICS OF ALL ROUND GROWTH: NOT AN IDLE TALK

This kind of all round growth is neither a pipe dream nor it is daydreaming. Infosys, Wipro, Reliance, Tata and ITC assiduously pursued this approach of ensuring all round growth in their organisations and you may see that each one of them is vying with world leaders in competition.

USE OF COLLECTIVE INTELLIGENCE

The combined and innovative intelligence of entire team of management and workforce would lead to innovation and cost reduction, quality improvement, increased sales, better market, easy availability of funds and other resources, speedier consequential geographical expansion.

This kind of approach was found valid by Ford, when he insisted on jotting down all good ideas whenever they occurred for he respected intelligence and views of each and every member of his work force. Microsoft and Bill Gates have gone beyond their expectations by chasing intelligence and knowledge, wherever they could get it by pooling it and marketing it. This would be of great help in encouraging professionalism.

So, in case you want to be in global business and want to find whether you are capable or incapable of taking appropriate decision in a given situation, first find out a neuroeconomist of Neuroeconomics Laboratory at George Mason University. May I suggest one may go to an astrologer who knows how to please his clients and to force one to pay through nose on account of fear created by plying on one's weak psyche by glib taking.

Neurons are certainly influenced by cosmic forces in the shape of the influence of the heat of the Sun, the gravitational pulls of earth and the Moon, Mars, Saturn, Mercury, and Rahu etc and their mutual motional and positional relationship. But you must appreciate how right conduct is insisted upon in Astrological works by our Seers.

Business ethics is dharma of determined and steadfast warriors in economic Kurukshetra, who would like to retrace few steps or at the most, may like to loose the battle for strategic reasons but would continue to fight to win the war. It is not the business conduct of a temporary profit-seeker. It is neither dharma of a fatalist, nor of an escapist.

Business ethics, being professional Dharma, can not go beyond the scope, heart and soul of Dharma. Naturally it is as dynamic and as complex as the concept of Dharma is. Firstly, it is a matter of one's own fitness to discharge his professional responsibilities. Secondly, for the same purpose, it is a matter of constant mental alertness, complete awareness of nicities and nuances of one's business on one hand and on the other, a matter of intellectual capability to take right decision at right time. Right decision at right time needs spiritual advancement to develop intuitive faculty and to understand human psych. It is not only a matter of adopting correctional and remedial measures for putting back an individual on his own track, but also a matter of putting back others on their track. It is a matter of creating fine-tuned team of motivated, determined, broad minded, forward-looking optimists. And this team is to be formed out of those, who have been brought up in different families, different environmental and social setups, different educational and perceptional backgrounds, having their own individual philosophies. If one is having deep rooted faith in philosophy, then it would becomes easier for a company to fine- weave a homogeneous team working for mutual growth of each other as well as their own and their organisation. Then they understand easily that their own growth not only lies in their own growth, but also in the growth of their organisation, growth of their seniors, juniors, colleagues and subordinates, rather all those who come in their contact. In short, it is a thoughtful and effective action to ensure all round growth of all. In other words it is a technique of management of all round and mutual growth of all.

CORPORATE Vis-a Vis POLITICAL INTERPERSONAL RELATIONS

Communication between corporate world and Political leadership is not only desirable, rather essential for ensuring favourable climate for economic growth. The business world can not run in isolation and naturally should always be vigilant about fiscal policies of the government to ensure business expansion and economic growth. Inmate should both, concepts of Economic and Political democracies require constant dialogue on "How to accelerate Process of economic growth?' No exception could be taken to it.

But there is a seamy side of political hobnobbing leading to political corruption in the shape of arm twisting of corporates for project clearance and political favor of making ordinary facilities for a price of "contribution to Election Funds of the ruling party or of the party which could be expected to win, or financial supports to as many candidates of various parties" to act and play different roles the behest of a group of companies to put pressure on the government to the extent of covert threats of changing the government, as is being loudly whispered. . If there is truth in it, such a political and corporate climate fertilizes the concept of "Money makes the Mayor Go".

In the vision of Woodro W Wilson, prosperity is necessarily the first theme of every political campaign. This kind of prosperity has hardly any proximity with values or Business Ethics. In a workshop on Corporate Excellence caution rang that such a dubious political corporate nexus is enimical and runs against the basic principles of corporate governance, leave aside corporate excellence and Business Ethics.

Current Provisions have bestowed on the Board of Directors to pass on certain portion of profits to political funds. In large number of cases this provision has been reportedly misused. Way back in 1957,Justice M.C.Chhagla warned against the then existing similar provisions that the so called sanction of the company was a mere camouflage for either the directors or some powerful person holding some large block of shares so as to control the voting.

Sensibly gravity of the danger was realised and Companies (Amendment) Act, 1969 was brought in, Statement of Object and Reasons read:

"A view has been expressed that such a contribution has a tendency to corrupt political life and adversely affects the democracy in the country"

In view of past experiences would it not be desirable that the companies instead of funding elections are allowed to fund several projects of NGOs or various cells of political parties to show their worth by executing and running successfully in their vicinity. At least the trust and confidence in the management of the company would not be shaken by falsification of accounts.

What is known as political hobnobbing would become redundant if the projects submitted by any corporate body are not cleared within three months or any other reasonably specified period of few months, and the Government of India and the State Government or any other authority does not inform its objections, it should be deemed to have been provisionally cleared. Whatever objections are to be raised by concerned authority, all those objections must also be informed in one go and not in piecemeal.

I would strongly favour even a judicial intervention if any project is delayed by any department for a period over six months, then the Secretary of the concerned Legal Service Authority must approach the concerned High Court and in case of necessity the Supreme Court to issue directions to the concerned executive authority to explain the reason of each days delay in processing the project. One could not be oblivious to the heavy social cost involved in such delays in the shape of escalation in cost of the project, loss of man hours lost in such delays, loss to the company and the economy in the shape of GDP and its spiraling effect and loss of foreign exchange foreign exchange. This may also involve loss of excise duty, income tax and money spending and the local economy. Virtually it is colossal neglect on the entire department dealing with the project. Neither Indian economy nor any corporates body could afford such delays implying colossal loss.

In such circumstances, it is the duty of the Secretary of concerned Legal Services Authority to act and to seek legal remedies on behalf of the would be beneficiaries of such projects by approaching the concerned High Court and even Supreme Court in case of need. The High Court concerned, being a court of equity and good conscience would surely not lag behind in protecting the invisible beneficiaries and in the interest of National Economy, by looking into the matter after calling a report about delay and provisionally allowing the project to go ahead on giving an undertaking to remove all just objections in a period of three months.

B.T. AND A.T. KEARNEY STUDY

A recent **study "to discover and share with its readership the secrets of success of India Inc.'s best managed companies,"** jointly conducted by Business Today and A.T. Kearney reveal four kinds of companies, **Value builders, profit seekers, simple growers and under-performers**. **Profit seekers** show revenue growth rates below their industry's average although they still create significant shareholder value in the short term. On the other hand **Value-Builders** achieve above average revenue and shareholder value growth over a long period. These companies constantly try to extend their advantage by constantly finding ways to stay ahead of their peers in the race for growth opportunities, capital and talent.

The **profit seekers usually decide to shut down the growth engine and opt for a profit-oriented focus** that involves heavy cutting of cost to meet earnings target. In sharp contrast, Value Growers or **"Best Managed Companies" never slow down their growth engine, even if it means sacrificing the bottom line** for a certain period of time. These companies make intentional investments either on acquisitions or people or systems. They recognise that sinking into profit-seeker territory can make the eventual return both slower and more difficult.

This growth philosophy was exemplified well by TVS Motors and Reliance. During the down turn, T.V.S. Motors made extensive investment in distribution network, internal quality systems, manufacturing units and R&D facilities. Similarly reportedly Reliance has continued to make investments in existing as well as new businesses. The best-managed companies optimise growth rates rather then maximise them. They avoid the dangerous yet alluring trap of 'more and better', and instead maintain a sustainable speed and time for their growth to effectively ride the spiral.

What goes into the making of India's Best Managed Companies?

Here are some insights offered by the BT-A.T. Kearney study.

Fundamental 1: Value-building is possible in any industry, in any region and at any phase of a business cycle.

Fundamental 2: Growth is spiral-shaped, not linear.

Fundamental 3: Best-managed companies use innovation, geographic expansion and risk taking to fuel value-building growth.

Fundamental 4: Best-managed companies use clearly laid out systems and processes in areas of strategic review, operations and people management to sustain superior performance and growth.

Fundamental 5: Best-managed companies have a strong leadership team to help broad-base strategic thinking and 'fire their growth engine on all cylinders'.

Key areas for improvement

The study highlighted two areas where corporate India appears to be weak : governance and social responsibility. While both have started getting management's attention, substantial initiatives are required to not just meet the requirements but also consciously exceed tough global standards. Transparency and corporate governance not only helps attract quality global investors but also build credibility with customers.

Best managed companies like Infosys, Dr. Reddy's and Hindalco have made extra efforts in the area of corporate governance. Infosys complies with the corporate governance guidelines of six countries.

Similarly, corporate social responsibility is also an area to which the average corporate has not given adequate attention till recently. Despite increasing regulations, the need for being environment friendly is still in its nascent stages.

THREE GREAT HURDLES IN TAKING RIGHT DECISIONS AT RIGHT TIME

First great hurdle is **lack of knowledge of latest professionally required information.** Two other great obstacles in all round physical, mental, and spiritual growth- of an individual or an organisation or a developing market or economy, are **inhibitions and suspicions.** These are not insurmountable, at least in a business organisation and a group of sensible market players.

However, in order to avoid the first, one has to read professional journals like **Business Today and Chartered Secretary, in addition to Economic Times etc. One would do well by remaining in constant touch with the concerned Ministries and at least Booksellers who could supply on their own latest Amendment Bills, Notifications, Rules and Regulations.**

As regards, obstacles of inhibitions and suspicion in proper growth, they originate from internal and external sources. As regards internal sources, one feels inhibited and remains suspicious, if he **lacks spiritual strength or say Atmabala**, and **sad experiences in the past leaving a scar on one's psyche**. Yogik Asanas including Namaj, Pranayam, Sandhya and recital of Gayatri Mantra may help in 90% cases. They are also helpful in stress management. In rest of the cases, one may be required to consult a Vaidya or a Neuro-physician. As regards external sources, it lies in "**hush, hush" approach and secretive conduct of concerned person.** **C**rystal clear transparency, honesty, integrity probity, in short high state of business ethics would be essential. to relieve a person from inhibition and suspicion to enable him to take right decision at a right time.

WHISTLE BLOWER

The Company Secretary, the Audit Committee and concerned Directors, being conscious keepers of the management, are supposed to collect all information and all data, to martial and analyse it and to present analytical report with suggestions for prompt action to the concerned director and if he deems it desirable, he may bring it to the notice of MD, Chairman, all other Directors and the shareholders, consumers, promoters, the society at large, and the Government depending on situational necessity. As conscious keepers they are supposed to secure the aim and objectives of the organisation by timely informing the directors and for taking remedial measures.

SEBI'S EXPECTATIONS

In an interview G N Bajpai, Chairman of the Securities & Exchange Board of India (SEBI) about accounting procedure, suggested that the first step should be investors education by clearly telling him about the method of investment in the market; the risk, returns and trade offs associated with investing in stocks, the functioning of stock markets, depositories and grievance of redressal mechanism. SEBI was supposed to launch a nationwide campaign to spread awareness amongst investors. In terms of the directions issued by the SEBI he expected the corporates to disseminate real time information in easily understandable language. Every corporation listed in Indian stock exchanges and on market intermediaries has to follow corporate governance norms. Corporate governance is expected to go beyond the rulebook and encompass a principal approach, which requires focus on fundamentals. The fundamentals would be like why a corporate comes into being, how wealth is increased and more importantly how this wealth is shared. SEBI has asked its rating agencies to prepare a mathematical process for measuring corporate governance in terms of wealth creation, management and sharing, accounting principles. It is expected that the corporates follow that spirit of the law and not just letters of law. The corporate is supposed to furnish every conceivable form of information, which has a bearing on the stock price. SEBI intended to track down every case of misconduct by companies and they would take every possible action against company. Now, the companies would not be able to say they were not aware of the implication of a particular rule for the SEBI has taken steps pertaining to advance ruling. Supposing a company is planning to take over but is not sure whether it would be in accordance with SEBI regulations. These companies can take now the opinion of the SEBI for certain fee to avoid any post acquisition anxiety. Violation of any negative advise of the SEBI would lead SEBI to issue warnings. However, the correspondence relating thereto would be kept confidential. Consequently the business ethics require that the companies should adhere to the norms prescribed by the SEBI to avoid issuance of warning and ultimately de-listing of their stock.

Since the directors and managers of the company are just trustees of the shareholders, they are supposed to take all possible due care and caution to display their good faith. Display of due care and caution indicating good faith would enhance the credibility in investors and shareholders. It would further enhance the credibility otherwise while dealing with financial institutions and while entering into business transactions.

REVISED CLAUSE 49 OF LISTING AGREEMENT

On 26th August 2003,after considering public comments on N.R.Narayan Murthy Committee recommendations, SEBI has approved certain amendments in clause 49. The revised clause 49 contains both the existing sub-clauses as well as new clauses. The amendments have been inter-alia carried out for strengthening the responsibilities of audit committees, improving the quality of financial disclosures including those related to related party transactions and proceeds from initial public offerings, requiring boards to adopt formal code of conduct, whistle blower policy and improving disclosures related to compensation paid to non-executive directors. All listed entities, having a paid up share capital of Rs. three crores and above or net worth of Rs. twenty five crores or more at any time in the history of the entity, are required to comply with the requirements of the clause by 31st March 2004.

The clause may require to be amended after passing of the Companies (Amendment Bill) 2003 to ensure harmony in both.

RISK MANAGEMENT

Like God risk is omni present and omni potent; but does it call pressing of the panic button continuously. It has **different facets of risks** in so far as business is concerned :

(a) Total or partial damage to the goods sent through railway or transport or by air on account of accident

(b) Non-payment by a purchaser after receipt of goods

(c) Loss of goods on account of fire or vis major or act of God or by mischief monger.

One has to differentiate between **pure risk and speculative risk** or one may call it **pessimist's risk and optimists' risk.** Degree of risk being a matter of perception of an individual; but a comparison or the statistic and calculation of the actual risk would help decide in appreciating the impact of likely risk. There could be different kinds of situation indicating the degree of risk; say a community may find it **acceptable to live with the carcinogenic risk of smoking** while they may find a significantly lower **risk associated with a nuclear power plant unacceptable.** One must keep in mind that the actuarial tables have not been updated in India the way they are required to be updated in view of increased mechanized safety devices and increased awareness about prevention of accidents, thefts and frauds.. Consequently one has to take into consideration this aspect also while deciding to take insurance cover or the extent of the insurance cover. There is another facet; management is trustee of the assets to the organisation not owner. A pessimist manager may be inclined to have all sorts of insurance cover while an optimist manager may like to avoid to a great extent. In such a circumstances a collective wisdom based decision would be much more helpful. That will outweigh both extremes of pessimistic and optimistic outlook.

While considering the risk factors however, the following factors are required to be considered for considering industrial pure risk:

— Tangible costs

— The losses suffered due to an accident

— The investment in safety and good practice to minimise accidents, training and fire protection

— Lost revenue due to loss of production

— Insurance premiums

— Intangible costs

— Loss of market share following an accident

— Loss of public goodwill due to a product defect and environmental problem

— Loss of morale in staff due to repeated losses and stoppages.

Risk is the sugar and spice of life. This is a simple and effective definition bringing out the dual nature of risk. Risk is essential for the survival and growth of mankind. The sound understanding of its nature, the way it is perceived and its impact on business, are necessary to ensure that opportunities are harnessed, while the downside is managed. In a nutshell, this is the scope and purpose of risk management.

BUSINESS ETHICS: "HOLISTIC VALUE MODEL FOR ALL ROUND GROWTH"

Our economy has reached such a stage of globalization as well as liberalization that it is ready to enter the third and more challenging phase of economic transition i.e. playing a decisive role in the turbulently competitive global economy. We have to meet the requirement of time and the stage of global competition. For this purpose, we will have to create a credible, trustworthy and internally strong corporate India which values business more than just the economics of give and take. Hence this calls for our organisations to build an organisational culture characterised by "Value" in its true spirit. To set itself apart, it becomes imperative for India to show up a unique and united representative face of an Indian organisational value system. Hence, organisations should aim at evolving a culture, based upon a **"Holistic Value Model for All Round Growth**" which should embody the following determinant factors and coronary stones:

(i) Qualitative Value Addition focusing customer's satisfaction;

(ii) Creation of mutually beneficial customer supplier, distributor link for business intelligence collection and prompt responses;

(iii) Deep commitment to protect preserve and nurse and nurture interest of shareholders and investor,

(iv) Employees' satisfaction coupled with their material and intellectual and spiritual growth to serve the organisation for mutual benefit for all round growth of all;

(v) Deep commitment to welfare of society at large by

(a) Employment and infrastructure creation and addition in the vicinity;

(b) Creating purchasing power and investing capacity for further growth;

(c) Environmental protection;

(d) Encouraging literacy, health care and "Shramdan" for creating growth oriented infrastructure by extending a helping hand to local NGOs, Resident Welfare Associations or Panchayats etc.

It would be a vibrant **"Holistic Value Model for All Round Growth".** When it is institutionalized by organisations individually and as clusters, it can give a distinction to organisational culture.

In the light of their aforesaid legislative amendments creating office of CAO, independent directors, advisory committee as visualized by the management Gurus; business ethics arising in natural course of business dealings not covered otherwise by statutory provisions of law and the social environmental obligations; would be three facets of business ethics. Business ethics is heart and soul of corporate excellence and is all embracing and all pervasive. This is as good as dharma or codified ethics; dharma of an ordinary human being in mutual course of business dealings and dharma of a sensible, sensitive and spiritually conscious person who realizes his obligation to the society and the environment in which he lives.

All the three facets of business ethics as has been explained, depend on philosophy, basic inclination, habit, education, self-control and steadfastness which determine responses and actions positive and negative of an individual and an organisation, in a given situation. For faster and accelerated pace of growth rate - encompassing physical, material and spiritual growth of an individual as well that of organisation(s), society and the economy - one has no option but to insist on the concept of mutual growth of all taken together and one has to follow the concept of **SARVA BHOOT HITE RATAH or SARVE BHUVANTU SUKHINA, SARVE SANTU NIRAMAYA.**

BUSINESS ETHICS AND PROFESSIONALISM

JOSHUA W WAMBUA*

1.0. Preamble

It is a great pleasure and honour to be invited by the Institute of Company Secretaries of India (ICSI) to attend, participate and present a Technical Paper in the 31st National Convention of Company Secretaries of India. On behalf of the Institute of Certified Public Secretaries of Kenya (ICPSK) and on my own behalf, let me register our appreciation for this gesture by the ICSI. We do hope that this co-operation will continue to flourish for the benefit of our members. However, as a young Institute, the ICPSK has a lot to learn from the ICSI, which is apparently an older and already well established Institute, compared to ICPSK which started operations in 1989 after the enactment of the Certified Public Secretaries Act, Cap 534 of the Laws of Kenya. To date we have 1,534 registered members, out of whom only about 1000 are active.

I leave you to compare the above strengths with that of ICSI, which I understand is quite gigantic, which I know you know better than I do.

Turning to the topic " Business Ethics and Professionalism", It would be prudent to start with definitions of these terms.

2.0. Business Ethics

2.1. Business may be referred to as a set of activities that are employed towards producing products and/or services to be made available to a consumer.

2.2. Ethics in General

Ethics is a quest for, and understanding of those factors that lead to a good life.

Barclay defines ethics simply as "the science of behaviour " (p13) while Gichira defines it as " the systematic study of human actions from the point of view of their rightness or wrongness as means for the achievement of man's ultimate happiness." (p 16)

The term "ethics" is generally used to mean "the discipline (area of learning) dealing with what is good and bad." The term encompasses the " … study concerned with the principles of human duty … that moral principles or system of a particular: the moral principles by which a person is guided: the rules of conduct recognized in certain association or department of human life."

For our purposes in this discussion, we may settle for ethics to mean the principles of conduct governing an individual or conduct that is characteristic of an individual or group or persons. The only elaboration that we need to make is to emphasize the fact that the moral principle involves the guidelines of right and wrong behaviour: right behaviour being ethical and wrong behaviour being unethical.

It might also be fitting at this point to point out that the " the codes of ethics of a profession offer an object lesion in self-discipline, and in the restraint of selfish impulses for the general good." (Carey, p 18) Thus, one gives up their selfish wants, desires and wishes for the sake of the "common good." The challenge is the attainment and maintenance of the balance between me and us.

* BSC(BA), CPS(K), Chief Executive & Secretary, Institute of Certified Public Secretaries of Kenya (ICPSK).

3.0. Professionalism

3.1 What is a Profession ?

Whereas a profession is precisely defined as an occupation or vocation requiring advanced study in specialized field, it is quite fair to point out that " There is much more in a profession than a traditionally dignified calling. The term refers to a group of men (generic) pursuing a learned art as a common calling in the spirit of public service… gaining a livelihood is incidental."

Historically, there are three ideals involved in a profession: organization, learning and public service." (in Carey p.257)

In their concerted and comprehensive efforts to capture and document the common body of Knowledge for Certified Public Accountants, Ray and Neil (Horizons for Profession, 1966) identified the qualities and the characteristics that are common to all professions as:

(i) Service to society.

(ii) Ethical Principles which emphasize the virtues of self-subordination, honesty, uprightness, and devotion to the welfare of those served.

(iii) Legal regulations for admission and entry into the profession

(iv) Disciplinary procedures for those whose conduct violated ethical standards.

(v) A body of specialized and organized knowledge acquired through formal education and training.

(vi) A language of its own, which, in its more sophisticated forms is understandable by only those initiated.

Certified Public Secretaries share in these features and should be justifiably proud of the usefulness and importance of the services they render to the society, even though the value of such services may not always be apparent.

The study on the common body of knowledge that gave a profession the foregoing six characteristics was published in 1966. In 1998, International Federation of Accountants (IFAC), gave the qualities and characteristics of a profession as including:

(i) Mastery of a particular intellectual skill, acquired by training and education.

(ii) Adherence by its members to a common code of values and conduct established by its administrating body, including maintaining an outlook which is essentially objective; and

(iii) Acceptance of duties to society as a whole (usually in return for restriction in use of a title or in the granting of a qualification)

Even if the delineation of a profession in 1966 is not congruent to that of 1998, the qualities and characteristics given in both cases are not at all in conflict.

3.2. Qualification of a Certified Public Secretary of Kenya (CPSK)

Mastery of a particular intellectual skill, acquired by training and education is quite profound and demanding of personal effort.

In Kenya, to become a Certified Public Secretary of Kenya (CPSK), one must have, as a minimum High school level of general education. To register as a Kenya Accountants and Secretaries examination Board (KASNEB) candidate, one must attain a C+ overall in the Kenya Certificate of Secondary Education (KCSE) examination, together with a C+ in English and a C+ in Mathematics. However, one may attain a minimum of D plain but must start training at the equivalent of Kenya Accounting Technician Certificate (KATC) level. The KATC level has ten examination papers that one must pass in order to acquire and form the knowledge background in order to study for CPS, which has eighteen (18) papers.

In most countries of the world and probably this includes India, these occupations have become graduate professions. Thus candidates for either specialization are required to have a University degree as the minimum level of educations. This educational level makes it relatively easy for one to master " A body of specialized and organized knowledge acquired through formal education and training." This educational level and training (and passing the prescribed examinations) is the evidence of "Mastery of a particular intellectual skill, acquired by training and educations."

In Kenya, even if one starts at the equivalent of KATC level, by the time one succeeds in passing the 18 papers, one would certainly have fulfilled the educational and training requirements. Conclusively then, administration is a profession of world repute.

4.0. Corporate Governance

4.1. Definition of Corporate Governance

Corporate Governance has been defined in various ways by different authorities. Nevertheless, " Corporate Governance refers to the manner in which the power of a corporation is exercised in the stewardship of the corporations total portfolio of assets and resources with the objective of maintaining and increasing shareholder value with the satisfaction of other stakeholders in the context of its corporate mission {Principles for corporate governance in Kenya (November 1999) }.

4.2. Good Corporate Governance seeks to enhance

(i) Efficient, effective and sustainable corporations that contribute to the welfare of society by creating wealth, employment and solutions to emerging challenges.

(ii) Responsive and accountable corporations.

(iii) Legitimate corporations that are managed with integrity, probity and transparency.

(iv) Recognition and protection of stakeholder rights.

(v) An inclusive approach based on democratic ideals, legitimate representation and participation.

4.3. What is the need for Good Corporate Governance ?

The Global Corporate Governance forum noted in its mission statement that; " Corporate Governance has become an issue of worldwide importance. The Corporation has a vital role to play in promoting economic development and social progress. It is the engine of growth internationally, and increasingly responsible for providing employment, public and private services, goods and infrastructure. The efficiency and accountability of the corporation is now a matter of both private and public interests, and governance has hence come to the head of the international agenda."

4.4. Good Corporate Governance is necessary in order to

(i) Attract investors. They get assured that their investments will be secure and efficiently managed and in a transparent and accountable process.

(ii) Create competitive and efficient companies and business enterprises.

(iii) Enhance the accountability and performance of those entrusted to manage corporations;

(iv) Promote efficient and effective use of limited resources.

Let me now pose a few questions which will help us address some issues touching on Business Ethics, Professionalism and Corporate Governance.

Question one : Do Business Ethics and Professionalism contribute to Good Corporate Governance?

The answer is definitely yes.

(i) Business Ethics is about what is perceived as good or bad in the business world.

If there is "good" Business Ethics, which is acceptable by the norms of a given society, (nowadays we have a global society) then this will definitely contribute to Good Corporate Governance, which will be good corporate leadership to satisfy the norms of the society as perceived by the very society.

(ii) Professionals apply their professionalism on corporations in order for such corporations to realize their objectives.

The society, through its beliefs, norms and practices sets expectations to professional who in turn inculcate such expectations into their professional ethics.

The professionals therefore are guided by their ethics as they apply their professionalism into corporations.

The ethicalness upheld by such professionals, as they work for corporations, therefore promotes good Corporate Governance.

Both business ethics and professionalism are founded on the sense of right and wrong, what is fair and just, accountability and transparency.

Question Two : Do Good Ethics Translate to Good Business and hence Business Sustainability

A reputation for "sharp" business practices is not an asset at all to any business.

Customers and employees are value sensitive and require consistency.

Consistency builds predictability and trust. And indeed all other stakeholders, be it the Government, the suppliers, the neighbours and society at large value consistency in doing the right thing. Questions which touch on various issues are constantly asked by the stakeholders which helps them to evaluate whether actions and practices of a given corporation are good actions and therefore ethical.

It is on the basis of this decision that the corporation is viewed either as good and trustworthy one or not.

Once a corporation is trusted by the stakeholders, the following benefits accrue:

(i) If there is a competitor, the consumers will prefer goods and/or services of the trusted company.

(ii) The law enforcers will deal with the corporation positively and therefore it will not be subjected to a lot of scrutiny in attempts to catch it on the "wrong-footing".

(iii) Credit rating of such a corporation may increase, since it is a trusted company and hence enable it to obtain favourable credit terms.

There are may more advantages including "the corporation being forgiven by the society for any mis-deeds it does, even long before it argues its case".

It is therefore apparent that Ethics translate to Good Business and hence business sustainability as the customer and all other stakeholders will view the corporate body positively which translates to advantages to the business in turn.

Question Three : Are Societal Ethics and Business Ethics alienatable ?

The Societal Ethics are reflected in the business Ethics, since the business is part of the larger society. In addition, the persons who help the business. The same constitute the business. The same members of the society are the customers to the business, the government is part of the same society, the suppliers of goods and materials come from the same society and therefore, if the business pursues any principles which are repugnant to that of the society, which may not be easy, then a friction will ensure and since business draw their power from the society, such a business will definitely fail.

Question Four : Can Legislation change codes of Ethics and Standards result to desired holistic change ?

Legislation, Code of Ethics and Standards are guidelines by which if a person is accused on an issue touching on any of them. Such a person will be judged based on the benchmarks set.

It is disturbing to note that when subjects are forced through a legislation or some sort of a set standard to observe a given behaviour, if such subjects are not willing to observe that desired behaviour, they merely end up obeying the law by exhibiting actions that manifest the minimum desired behaviour to avoid the penalties.

As stated earlier in this paper there is much more in a profession than a traditionally dignified calling. If the Legislation, the code of ethics and standards are set by willing people then such person, who do not necessarily set such benchmarks to convince others of existence of the rules, then it would be expected that the players would go beyond their performance benchmarks and excel quite well.

Therefore there is a lot of benefit of ownership of the values that people are expected to exhibit and very little effort would be required to enforce such values.

It is important that Business and professional do act responsibly, transparently with fairness. They should also be efficient and effective, because it is in the interest of the very society they serve, who are their Masters, to do so.

It is inevitable not to have Codes of Ethics and Standards of practice so that they can be used to net the deviants.

Altogether, these should be viewed as mere lines making the minimums, but professionals and businesses alike, should endevour to achieve higher and higher performances in matters of Ethics.

The Role of Government and the Society

Every Government has a major duty to play if its citizens are going to benefit from Good Corporate Governance.

In the first instance, the Government must be composed of people who are themselves ethical, so that they can be listened to and emulated.

The society is the population which votes in governments and therefore it is a major influencing agent of what kind of a government they end-up with, which in turn, sets the tone on governance on citizens and indirectly on corporate bodies.

With Globalization, it is not possible to have major differences in levels of delivery and expectations by the Society. People all-over the world are sharing information very quickly and therefore, they are now able to tell whether the delivery of services and treatment they get be it from the government or the corporations, measures to what their furthest counterparts in other countries get.

It is even more serious that under the WTO treaties, professionals will be able to move freely and deliver services anywhere in the world and hence this means that time has come for professionals trained in different countries to unify their Ethical codes to meet the global society expectations.