

**GUIDELINE ANSWERS**  
**PROFESSIONAL PROGRAMME**

**JUNE 2023**

**MODULE 3**

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The Guideline Answers contain the information based on the Laws/Rules applicable at the time of preparation. However, students are expected to be updated with the applicable amendments which are as follows:

**CS Examinations    Applicability of Amendments to Laws**

December Session    upto 31 May of that Calender year

June Session    upto 30 November of previous Calender Year

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**PROFESSIONAL PROGRAMME EXAMINATION**

JUNE 2023

**CORPORATE FUNDING & LISTINGS IN STOCK EXCHANGE**

Time allowed : 3 hours

Maximum marks : 100

**NOTE :** Answer **ALL** Questions.

**PART-A**

**Question 1.**

ABC Limited is a trading company. Its annual turnover is ₹ 4000 lakhs out of which ₹ 2800 lakhs is on credit. Its average collection period is 90 days and presently its receivable collection cost is ₹ 35 lakh p.a. The company needs immediate funds to finance its growth projects and it has an option to take short-term loans at interest rate of 18% p.a. Recently, one of the factoring company visited the Chief Executive of ABC Limited and offered him to provide the factoring services on recourse basis. As per terms of factoring arrangement, factoring company will provide for an advance payment of 80% (maintaining factor reserve of 20% to provide for disputes and deductions relating to the bills assigned) of the value of factored receivable and for guaranteed payment after 90 days from the date of purchasing the receivables. The advance will carry a rate of interest of 12% per annum. In addition to interest, factoring company will charge factoring commission @ 2.5% of the value of factored receivables. Both the interest and commission shall be collected by factoring company on upfront basis. You are the Company Secretary of ABC Limited and you have been requested to prepare a report containing the following aspects. (a) What is the net annual cost of funding through factoring of receivables assuming 360 days in a year?

(5 marks)

(b) Whether it is appropriate to choose the factoring of receivable in comparison to short term bank loan?

(5 marks)

(c) Whether your advice would be changed if the clause of 'on recourse basis' is negotiated 'on non-recourse basis' keeping the other terms of agreement with factoring company as same. The experience indicates that bad debt losses on sales are 2% of sales.

(5 marks)

**Part -A**

**Answer 1(a)**

Net Annual Cost of Funding from the Factoring of receivables

Particulars	₹ lakh
Average level of Receivables= ₹ 2800 lakh x 90/360	700.000
Less: Factoring commission= ₹ 700 lakh x 2.5%	17.500
Less. Factoring reserve = ₹ 700 lakh x 20/100	140.000
Amount available for advance	542.500
Less: Interest on advance @ 12% ₹ 542.50 Lakhs x 12 x 90 100 x 360	16.275
Amount of advance received from the factoring company after deducting commission and interest	526.225

Total cost of factoring for 90 days = ₹ 17.500 Lakhs + ₹16.275 Lakhs)	33.775
Annual Cost of factoring - ₹ 33.775 * 360/90	135.100
Less: saving in cost of receivable collection cost	35
Net Cost of factoring of receivables on annual basis	100.100

### Answer 1(b)

Effective annual cost of factoring $\frac{\text{₹ } 100.10 \text{ Lakhs} \times 100}{526.225}$	19.02%
Cost of Short Term Loan	18%
Since the effective annual cost of factoring i.e. 19.02% is higher than the cost of short term loan i.e. 18% , it is not appropriate to choose the factoring of receivables in comparison to short term loan.	

### Answer 1(c)

If terms of agreement are negotiated from Recourse Factoring to Non-Recourse Factoring keeping the other terms of agreement same, it is advisable to opt for 'on Non-recourse basis' clause since it will reduce the effective cost of factoring to 17.02% (19.02% -2.00%) which is lower than the cost of Short Term Loan i.e 18%.

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

#### Question 2.

- (a) In reference to public issue of specified securities, what are the different conditions related to differential pricing ?
- (b) What are the conditions to be fulfilled for issue of sweat equity shares? Explain the lock in period with regard to sweat equity shares. Whether sweat equity shares may be issued to the non-whole time directors?
- (c) What are the eligibility conditions for being identified as "Social Enterprises" under chapter X of SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018?

(5 marks each)

### OR (Alternate question to Q. No. 2)

#### Question 2A.

- (i) Explain the differences between abbreviations "ADR" and "GDR".
- (ii) Explain the term REIT. State the major difference between REIT and Mutual Funds.
- (iii) In reference to the Import Finance, explain the difference between the term "Buyer's Credit" and "Supplier's Credit".

(5 marks each)

## **Answer 2 (a)**

### **Differential Pricing**

1. Under Regulation 30 of the SEBI (ICDR) Regulations, 2018, an issuer may offer its specified securities at different prices, subject to the following:
  - a) A retail individual investors or retail individual shareholders or employees entitled for reservation made under Regulation 33 of the SEBI (ICDR) Regulations 2018, may be offered specified securities at a price not lower than by more than 10% of the price at which net offer is made to other categories of applicants, excluding anchor investors.
  - b) In case of a book built issue, the price of the specified securities offered to an anchor investor shall not be lower than the price offered to other applicants.
  - c) In case the issuer opts for the alternate method of book building as specified under ICDR Regulations, 2018, the issuer may offer the specified securities to its employees at a price not lower by more than 10% of the floor price.
  - d) As per Regulation 128 of the SEBI (ICDR) Regulations, 2018, in case of a further public offer which is part of a composite issue, the price of the specified securities offered in the public issue may be different from the price offered in rights issue and justification for such price difference shall be given in the offer document.
2. Discount, if any, shall be expressed in rupee terms in the offer document.

## **Answer 2 (b)**

A company whose equity shares are listed on a recognised stock exchange may issue sweat equity shares in accordance with section 54 of the Companies Act, 2013 and SEBI (Share Based Employee Benefits and Sweat Equity) Regulations, 2021 to its employees for providing know-how or making available rights in the nature of intellectual property rights or value additions.

According to Section 54 of the Companies Act, 2013, a company may issue sweat equity shares of a class of shares already issued, if the following conditions are fulfilled.

- i. The issue is authorized by a special resolution passed by the company.
- ii. The resolution specifies the number of shares, current market price, consideration if any and the class or classes of directors or employees to whom such equity shares are to be issued.
- iii. Where the equity shares of the company are listed on a recognized stock exchange, the sweat equity shares are issued in accordance with the Regulations made by SEBI in this regard and if they are not listed, the sweat equity shares are to be issued in accordance with Rule 8 of the Companies (Share Capital and Debenture) Rules, 2014.

The rights, limitations, restrictions and provisions as applicable to equity shares for the time being, shall also be applicable to the sweat equity shares issued under the Section 54 of Companies Act, 2013 and the holders of such shares shall rank *pari passu* with other equity shareholders.

## **Lock-in**

The Sweat Equity shares shall be locked in for such period of time as specified in relation to a preferential issue under the SEBI (ICDR) Regulations, 2018. These Regulations shall apply if a company makes a public issue after it has issued sweat equity shares.

Regulation 29 of SEBI (Share Based Employee Benefits and Sweat Equity) Regulations, 2021 provides the definition of employee in relation to issue of sweat equity shares and covers:

- (i) an employee of the company working in India or abroad; or
- (ii) a director of the company whether a whole time director or not.

Hence, Sweat Equity shares can be issued to a director of the company whether a whole time director or not.

## **Answer 2 (c)**

### **Eligibility conditions for being identified as a Social Enterprise**

Regulation 292E of SEBI (ICDR) Regulation, 2018 specifies the eligibility conditions for being identified as a Social Enterprise. As per above said regulations, a Not for Profit Organization or a for Profit Social Enterprise, to be identified as a Social Enterprise, shall establish primacy of its social intent.

In order to establish the primacy of its social intent, such Social Enterprise shall meet the following eligibility criteria:

- a) the Social Enterprise shall be indulged in at least one of the following activities:
  - (i) eradicating hunger, poverty, malnutrition and inequality;
  - (ii) promoting health care including mental healthcare, sanitation and making available safe drinking water;
  - (iii) promoting education, employability and livelihoods;
  - (iv) promoting gender equality, empowerment of women and LGBTQIA+ communities;
  - (v) ensuring environmental sustainability, addressing climate change including mitigation and adaptation, forest and wildlife conservation;
  - (vi) protection of national heritage, art and culture;
  - (vii) training to promote rural sports, nationally recognised sports. Paralympic sports and Olympic sports;
  - (viii) supporting incubators of Social Enterprises;
  - (ix) supporting other platforms that strengthen the non-profit ecosystem in fundraising and capacity building;
  - (x) promoting livelihoods for rural and urban poor including enhancing income of small and marginal farmers and workers in the non-farm sector;
  - (xi) slum area development, affordable housing and other interventions to build sustainable and resilient cities;
  - (xii) disaster management, including relief, rehabilitation and reconstruction activities
  - (xiii) promotion of financial inclusion;
  - (xiv) facilitating access to land and property assets for disadvantaged communities;
  - (xv) bridging the digital divide in internet and mobile phone access, addressing issues of misinformation and data protection;
  - (xvi) promoting welfare of migrants and displaced persons;
  - (xvii) any other area as identified by the Board or Government of India from time to time
- b) the Social Enterprise shall target underserved or less privileged population segments or regions recording lower performance in the development priorities of central or state governments.

- c) the Social Enterprise shall have at least 67% of its activities, qualifying as eligible activities to the target population, to be established through one or more of the following:
- (i) at least 67% of the immediately preceding 3-year average of revenues comes from providing eligible activities to members of the target population.
  - (ii) at least 67% of the immediately preceding 3-year average of expenditure has been incurred for providing eligible activities to members of the target population.
  - (iii) members of the target population to whom the eligible activities have been provided constitute at least 67% of the immediately preceding 3-year average of the total customer base and/or total number of beneficiaries.

Corporate foundations, political or religious organizations or activities, professional or trade associations, infrastructure and housing companies, except affordable housing, shall not be eligible to be identified as a Social Enterprise.

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

**Answer 2 A(i)**

Typically, companies in India issue securities in the form of depository receipts (DR) viz. American Depository Receipts (ADR), Global Depository Receipts (GDR) etc. Both ADRs and GDRs are equity based instruments. "American Depository Receipt (ADR)" means a security issued by a bank or a depository in United States of America (USA) against underlying rupee shares of a company incorporated in India.

"Global Depository Receipt (GDR)" means a security issued by a bank or a depository outside India (other than the United States of America) against underlying rupee shares of a company incorporated in India (E.g. DRs issued on the Luxembourg Stock Exchange). The difference between American Depository Receipts (ADR) and Global Depository Receipts (GDR) is that ADRs are US \$ denominated and traded only in US while GDRs are traded in various places such as London Stock Exchange.

**Answer 2 A(ii)**

The Real Estate Investment Trust (REIT) is an investment vehicle that invests in rent-yielding completed real estate properties which has the potential to transform the Indian real estate sector.

REITs help attracting long-term financing from domestic as well as foreign sources, thereby improving fund availability to real estate developers and reduce some burden on completed assets by allowing owners of such assets to raise capital from investors against issue of units. Further, for the investors, the REIT can provide a new investment vehicle with ongoing returns, elevated transparency and governance standards.

**Difference between REITs and Mutual Funds**

<b>Basis</b>	<b>REITs</b>	<b>Mutual Funds</b>
Meaning	A REIT is a corporation, trust, or association that invests directly in real estate through properties or mortgages. REITs are traded on a stock exchange and are bought and sold like stocks.	Mutual funds are professionally managed pooled investments that invest in a variety of vehicles, such as stock and bonds.
Investment	A large amount of funds to be shelled out if one wishes to invest in real estate.	Mutual funds require small amounts to be invested.

Diversification	An Investor can invest only real estate related stocks through REITs.	Mutual funds, however, allow to diversify the portfolio by investing in various sectors.
Legal	The SEBI (Real Estate Investment Trusts) Regulations, 2014 applies to REITs	The SEBI (Mutual Funds) Regulations, 1996 applies to Mutual Funds

### Answer 2 A(iii)

Buyers' Credit	Suppliers' Credit
Buyers' credit refers to loans for payment of Imports into India arranged by the importer from overseas bank or financial institution.	Suppliers' credit relates to the credit for imports into India extended by the overseas supplier.
Imports should be as permissible under the extant Foreign Trade Policy of the Director General of Foreign Trade (DGFT).	In this case too, imports should be permissible under the extant Foreign Trade Policy of the DGFT.
For the overseas exporter, it is converted into a Cash transaction.	The importer pays an agreed amount of down payment and the balance amounts are paid in instalments over a deferred period.
Since the facility is provided by an overseas bank the interest rates may be slightly high.	Since the facility is provided by the supplier itself, interest rates are comparatively low.

### Question 3.

(a) What do you understand by the term ASBA ? Is it mandatory for investor to submit application for "Right Issue" through ASBA?

(b) SEBI has issued guidelines for overseas investment by Alternative Investment Funds (AIFs) /Venture Capital Funds (VCFs) vide its circular No. SEBI/HO/AFD-1/PoD/ CIR/P/2022/108 dated August 17, 2022. In reference to above referred circular, in which overseas entities, An AIF/VCF may not invest?

(c) A bond with a face value of 100 is paying an annual coupon of 12 percent and trading in the markets for 109.50 per bond. What is the effective percentage yield of the bond?

(5 marks each)

### Answer 3(a)

#### Application supported by Blocked Amount (ASBA)

ASBA stands for "Application supported by Blocked Amount" which is a mechanism whereby an application is made for subscribing to a public issue or rights issue, along with an authorization to self-certified syndicate bank to block the application money in a bank account. Under ASBA process instead of moving the application money from the bank account of applicant in an IPO to an escrow account, same is blocked in applicant's own bank account and if the shares are allotted to him in IPO, same is released to the issuer company.



The concept of ASBA was introduced by SEBI through the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009 (now SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018). The advantage is that until the money moves out of the investor's account, the investor continues to earn interest, which was not the case earlier since the money used to move out of the investor's account to that of the issuer.

SEBI vide its circular dated January 22, 2020 made it mandatory that Application for a rights issue shall be made using ASBA facility.

### **Answer 3(b)**

As per the asked circular, AIFs/VCFs shall not invest in an overseas investee company, which is incorporated in a country identified in the public statement of Financial Action Task Force (FATF) as:

- (a) a jurisdiction having a strategic Anti-Money Laundering or Combating the Financing of Terrorism deficiencies to which counter measures apply; or
- (b) a jurisdiction that has not made sufficient progress in addressing the deficiencies or has not committed to an action plan developed with FATF to address the deficiencies.

### **Answer 3(c)**

Effective yield = (Coupon rate/ Market price) \*100

$$= (12/109.50) \times 100 = 10.96\%$$

### **Question 4.**

(a) *Commercial Paper is an important debt instrument used by eligible organisation for raising the funds. There are certain advantages of raising funds, through commercial paper along with some disadvantages. Explain the demerits/disadvantage of raising funds through Commercial Paper.*

(b) *Explain the obligations of issuer of Green Debt Securities.*

(c) *What are the different types of Private Equity Investments?*

(d) *Explain the different purposes for which bank guarantees are issued.*

(e) *What are the different rights of the units holders in an Infrastructure Investment Trust?*

(3 marks each)

### **Answer 4(a)**

#### **Demerits of Commercial Paper**

- 1) Commercial Paper is a short term instrument. The duration generally ranges from 7 days to 364 days. Thus it is suited for short term borrowings only.
- 2) Commercial Paper is an unsecured instrument.
- 3) Since by nature Commercial paper is unsecured, only financially secure and highly rated organizations can raise money through Commercial Paper. New and moderately rated organizations may not be as successful in raising funds through Commercial Paper
- 4) The amount of money that can be raised through commercial paper is limited to the deductible liquidity available with the suppliers of funds at a particular point.
- 5) The duration of commercial paper cannot be extended.

- 6) Mutual Funds, which are the largest investors, invest only in listed Commercial Paper. Thus in case the Commercial Paper is unlisted, it may lose out on Mutual Funds as investors.

#### **Answer 4(b)**

An issuer of Green Debt Securities shall:

- 1) Maintain a decision-making process which it uses to determine the continuing eligibility of the project(s) and/or asset(s). This includes, without limitation a statement on the environmental objectives of the Green Debt Securities and a process to determine whether the project(s) and/or asset(s) meet the eligibility requirements.
- 2) Ensure that all project(s) and/or asset(s) funded by the proceeds of Green Debt Securities, meet the documented objectives of Green Debt Securities.
- 3) Utilize the proceeds only for the stated purpose, as disclosed in the offer document.

An issuer of Green Debt Securities or any agent appointed by the issuer, if follows any globally accepted standard(s) for the issuance of Green Debt Securities including measurement of the environmental impact, identification of the project(s) and/or asset(s), utilisation of proceeds, etc., shall disclose the same in the offer document/disclosure document and/or in continuous disclosures.

#### **Answer 4(c)**

Private equity investments can be divided into the following categories:

*Leveraged Buyout (LBO):* This refers to a strategy of making equity investments as part of a transaction in which a company, business unit or business assets is acquired from the current shareholders typically with the use of financial leverage. The companies involved in these type of transactions that are typically more mature and generate operating cash flows.

*Venture Capital:* It is a broad sub-category of private equity that refers to equity investments made, typically in less mature companies, for the launch, early development, or expansion of a business.

*Growth Capital:* This refers to equity investments, mostly minority investments, in the companies that are looking for capital to expand or restructure operations, enter new markets or finance a major acquisition without a change of control of the business.

#### **Answer 4(d)**

Some of the purposes for which Bank Guarantees are issued are:

- (i) To secure any claims by the buyer on the seller arising from default in delivery or performance of the terms of the contract (e.g. construction, assembly, execution).
- (ii) Due performance of a specific contract undertaken by a customer in favour of Government bodies/ Others. For example supply of materials, Construction of Roads, Buildings Dams, Civil Work, etc.
- (iii) Due performance of an equipment/project after completion for a specific period due to possible defects appearing after delivery during warranty period of the equipment's.
- (iv) Execution of Long Term Infrastructure Projects such as Seaports, Airports, Road Construction, Bridges, Sanitation and Sewerage Projects, Telecommunication Services, Construction of Educational Institutions and Hospitals, Generation/ Transmission/ Distribution of Power, etc.

#### Answer 4(e)

#### Right of Unit holders in InvITs

- (i) Right to receive returns through cash distributions made by the trust
- (ii) Rights to vote on matters pertaining to acquisition of new assets or borrowing
- (i) Right to vote on related party matters
- (ii) Right to vote on matters such as appointment or change of the Investment Manager
- (v) Right to vote on induction of a Sponsor, with the opportunity to exit for dissenting voters
- (vi) Right to vote on exit of Sponsor
- (vii) Right to receive periodic disclosures like annual report, valuation report, quarterly/semi-annual financials etc.

#### Part B

#### Question 5.

*(a) ABC Limited is within the top 1000 listed entities in India. It has 10 directors out of which there is one-woman executive director and 6 non-executive directors. All the non-executive directors are men. Assess whether the company has been complying the requirement of SEBI (LODR) Regulations, 2015.*

*(5 marks)*

*(b) Mrs. R is a director of XYZ Company Limited which is a listed company. She holds membership/chairperson in following companies as per details given below :*

*(1) Chairperson of Audit Committee of XYZ Company Limited.*

*(2) Chairperson of Nomination & Remuneration Committee of XYZ Company Limited.*

*(3) Chairperson of Stakeholders' Relationship Committee of ABC Company Limited.*

*(4) Chairperson of Audit Committee of ABC Company Limited.*

*(5) Chairperson of Audit Committee of PQR Limited Company.*

*(6) Chairperson of Stakeholders' Relationship Committee of XYZ Company Limited. She is seeking appointment in RRR Company Limited as the chairperson of Nomination Committee of the board of RRR Company Limited. Check whether her appointment as the Chairperson of the Nomination Committee of the RRR limited is valid in view of the provisions of the SEBI (LODR) Regulations, 2015.*

*(5 marks)*

*(c) M/s AAA Limited is a public listed company. The company is undergoing into a high growth phase and its shares are highly traded in the recognized stock exchanges.*

*You are the Company Secretary of M/s AAA Limited. It is reported to you on 4th January, 2023 that one of the members from promoter group has made trading of approx. ₹ 20 lakh in the shares of M/s AAA Limited on 30th December, 2022. As a Company Secretary of M/s AAA Limited, state the compliance requirements applicable with regard to trading in the shares of company by one of the members from promoter group.*

*(5 marks)*

*(d) M/s PQR Limited is a non-listed company. It has plan of raising finance through public issue of shares. M/s POQ Limited has appointed M/s Fair Issue Merchant Bankers. You are working with M/s Fair Issue*

Merchant Bankers as operation in-charge. You are given the task for preparing the offer document for public issue of M/s PQR Limited. In this context, explain the relevance of “Virtual Data Room”.

(5 marks)

### Answer 5(a)

As per Regulation 17 (1) (a) of SEBI (LODR) Regulations, 2015, Board of Directors shall have an optimum combination of executive and non-executive directors with at least one-woman director and not less than fifty per cent of the board of directors shall comprise of non-executive directors.

However, the Board of directors of the top 500 listed entities shall have at least one independent woman director by April 1, 2019 and the Board of directors of the top 1000 listed entities shall have at least one independent woman director by April 1, 2020.

In the given case, the Company doesn't has one independent woman director hence it is not in compliance with the requirement of SEBI (LODR) Regulations, 2015.

### Answer 5(b)

Regulation 26(1) of SEBI (LODR) Regulations, 2015 states that a director shall not be a member in more than ten committees or act as chairperson of more than five committees across all listed entities in which he /she is a director which shall be determined as follows:

(a) the limit of the committees on which a director may serve in all public limited companies, whether listed or not, shall be included and all other companies including private limited companies, foreign companies, 'high value debt listed entities' and companies under Section 8 of the Companies Act, 2013 shall be excluded;

(b) for the purpose of determination of limit, chairpersonship and membership of the audit committee and the Stakeholders' Relationship Committee alone shall be considered.

In the given case, Mrs. R is chairperson of five committees which are relevant for the purpose of the compliance of above referred provisions. Since holding the Chairpersonship of the Nomination Committee is not considered in the limit for compliance of above referred provisions, she may accept the chairpersonship of the Nomination committee of RRR Limited.

### Answer 5 (c)

In case of insider trading in the shares of the company by promoter or member of the promoter group or by any director of the company, the under given provision of SEBI (Prohibition of Insider Trading) Regulations 2015 would be relevant which are as under:

Regulation 7(2) - Continual Disclosures a) Every promoter, member of promoter groups and director of every company shall disclose to the company the number of such securities acquired or disposed of within two trading days of such transaction if the value of the securities traded, whether in one transaction or a series of transactions over any calendar quarter, aggregates to a traded value in excess of ten lakh rupees or such value as may be specified: b) Every company shall notify the particulars of such trading to the stock exchange on which the securities are listed within <b>two trading days</b> of receipt of the disclosure or from becoming aware of such information.	Within 2 trading days of such transaction
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<p>(Transaction type include buy/sales/pledge/revoke/ invoke)</p> <p>The above disclosures shall be made in such form and such manner as specified by SEBI from time to time.</p>	
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Since the transactions were made on 30<sup>th</sup> December, 2022 while it is reported to the company after the expiry of 2 days, it would be non-compliance of the above referred provisions by the members of the promoters group. It would be appropriate that the company report such transactions to the concerned stock exchange within 2 days of the receipt of such information i.e. 6<sup>th</sup> January, 2023,

**Answer 5(d)**

Preparation for an offer document involves humungous documentation and paper work. At the time of commencement of due diligence Merchant Banker and the Legal Advisor circulate the 'Compliance Manual enumerating detailed requirements along with various formats and undertakings to be submitted by the Company. Only on compiling the majority of documents the process of diligence actually starts.

Companies set up specific location where all the documents and the copies of the same are made available for examination & verification. Such location is popularly known as 'Data Room' In the present scenario these data rooms are also set up in virtual space and are called as 'Digital Data Room' or 'Virtual Data Room' on various drives such as google drive. All the concerned executives will have access to the Data Room while drafting the offer document. Essentially, a virtual data room is a secure online repository for document storage and distribution used in the due diligence process – used by a merchant banker / lawyers / intermediaries in relation to a public / rishis issue.

**Attempt all parts of either Q. No. 6 or Q. No. 6A**

**Question 6.**

*(a) The Company, Secretary Profession has got wide recognition under different laws in India. SEBI has recognized the Company Secretary under different regulations of the SEBI (LODR) Regulations, 2015. In view of above, explain the recognition of the Company Secretary as the “Senior Management” of the company.*

(5 marks)

*(b) London Stock Exchange is one of the world's most reputed stock exchange and it provides an active and efficient secondary market for trading in a wide range of security. Its main market is the flagship market for larger and more established company. The main market of London Stock Exchange has different segments for catering different business and securities. In view of this, explain the different segments of the main market of the London Stock Exchange.*

(5 marks)

*(c) Explain the term "Designated Securities" in relation to SEBI (LODR) Regulations, 2015.*

(5 marks)

*(d) You are the Company Secretary of XMP Limited. XMP Limited wanted to get itself listed on the “SGX Main Board”. You are asked to list down the quantitative requirements related to listing on the “SGX Main Board”.*

(5 marks)

**OR (Alternate question to Q. No. 6)**

**Question 6A.**

(i) You are the Company Secretary of M/s Fair Ventures Limited which is a Public Unlisted Company. M/s Fair Ventures Limited is undergoing a high growth phase and it requires funds for financing the growth opportunities available to it. The company has been weighing various options of raising funds and one of the options is to raise the funds through the public issue of its shares. The managing director of M/s Fair Ventures Limited asked you to list down the important documents which the company would be needed for going ahead with the public issue. In view of above, mention at least 10 documents which would be needed for public issue.

(5 marks)

(ii) Explain any 5 (five) "Event based compliance requirements" related to SME Listed entities.

(5 marks)

(iii) One of the measures of the principles of the corporate governance and protection of minority shareholder is "Equitable treatment to all shareholders". Explain the manner in which a listed company shall ensure equitable treatment to all shareholders.

(5 marks)

(iv) You are the Company Secretary of M/s Professional Limited. The Board of your company wants to get your company listed on the Luxembourg Stock Exchange. Your company is eligible for listing on both markets of Luxembourg Stock Exchange i.e. BdL Market and Euro MTF Market. The board of the directors asked you to compare both the market of Luxembourg Stock Exchange.

(5 marks)

**Answer 6(a)**

Regulation 16 (1) (d) of SEBI (LODR) Regulations, 2015 provides that "Senior Management" shall mean Officers/Personnel of the listed entity who are members of its core management team excluding the Board of directors and shall comprise all the members of management one level below Chief Executive Officer or Managing Director or Whole Time Director or Manager (including Chief Executive Officer and Manager, in case they are not part of the Board of Directors) and shall specifically include the functional heads and the Company Secretary and Chief Financial Officer.

**Answer 6(b)**

The Main Market has four segments that cater for a range of businesses and securities.

- *Premium Segment:* It is the part of the Financial Conduct Authority's (A financial regulatory body in the United Kingdom) Official List. This segment is home to some of the world's largest corporations that are subject to the highest standards of regulation and governance.
- *Standard Segment:* Subject to EU minimum standards and part of the Official List, open to shares and debt securities.
- *Specialist Fund Segment:* Designed for highly specialised investment entities that wish to target institutional, highly knowledgeable investors or professionally advised investors only.
- *High Growth Segment:* A new addition to the Main Market offering, this segment is specifically designed for equity securities of high growth, revenue generating businesses that are over time seeking to become Premium listed companies.

### **Answer 6 (c)**

#### **Regulation 2(h) of SEBI (LODR) Regulations, 2015**

'Designated Securities' means specified securities, non-convertible debt securities, non-convertible redeemable preference shares, perpetual debt instrument, perpetual non-cumulative preference shares, Indian depository receipts, securitized debt instruments, security receipts, units issued by mutual funds, Zero Coupon Zero Principal Instruments and any other securities as may be specified by the SEBI.

### **Answer 6(d)**

#### **Quantitative Requirements related to listing on SGX's Mainboard**

Companies intending to join SGX's Mainboard must meet one of the following quantitative requirements:

1. Minimum consolidated pre-tax profit of at least S\$30 million for the latest financial year with operating track record of at least 3 years;
2. It should be profitable in the latest financial year, and has a market capitalisation of not less than S\$150 million based on the issue price and post-invitation issued share capital with operating track record of at least 3 years; or
3. Operating revenue in the latest completed financial year and a market capitalisation of not less than S\$300 million based on the issue price and post-invitation issued share capital. Real Estate Investment Trusts and Business Trusts who have met the S\$300 million market capitalisation test but do not have historical financial information may apply under this rule if they are able to demonstrate that they will generate operating revenue immediately upon listing.

### **Answer 6A (i)**

#### **Material Documents which would be required for the IPO**

1. Certified copies of the updated Memorandum of Association and Articles of Association of Company, as amended from time to time.
2. Certificate of Incorporation of Company.
3. Certificate of commencement of business.
4. Copies of the Board and shareholder's resolutions authorizing the Issue.
5. Report of the Statutory Auditors/Peer Review Auditor on Company's Restated Financial Statements (Standalone) for past 3 financial years and stub period not older than 6 months from the date of filing & opening of IPO.
6. Report of the Peer Review Auditor on Company's Restated Financial Statements (Consolidated) for past 3 financial years and stub period not older than 6 months from the date of filing & opening of IPO.
7. Statement of Tax Benefits from Chartered Accountants.
8. Copies of annual reports of Company for the past three Financial Years.
9. Consents of Statutory Auditors, Peer Review Auditors, Bankers to Company, Merchant Banker, Registrar to the Issue, Legal Advisor to the Issue, Directors of Company, Company Secretary and Compliance Officer, as referred to, in their respective capacities.
10. In-principle approval from the Stock Exchanges for listing of the securities.
11. Due Diligence certificate to SEBI from the Merchant Banker.
12. Observation Letter issued by the Securities and Exchange Board of India and reply to the observation by Merchant Banker.

**Answer 6A (ii)****Event Based Compliances related to SME Listed Entities**

<b>S. No.</b>	<b>Regulation reference</b>	<b>Timeline</b>
1.	Regulation 7(5) – Intimation of appointment of Share Transfer Agent	Within 7 days of Agreement with RTA
2.	Regulation 28 (1) - In-principle approval	Prior to Issuance of Security.
3.	29(1) (a) –Prior Intimations of Board Meeting for financial Result.	At least 5 clear days in advance (excluding the date of the intimation and date of the meeting).
4.	Regulation 29 (1) (b) to (f) - Prior intimation of Board meeting for Buyback, Dividend, Raising of Funds, Voluntary Delisting, Bonus etc.	At least 2 clear working days in advance (excluding the date of the intimation and date of the meeting).
5.	Regulation 29(3) –Prior intimation of Board Meeting for alteration in nature of securities etc.	At least 11 clear working days in Advance.
6.	Regulation 30 (6) – Disclosure of events specified in Part A of Schedule III (Material events)	Not later than twenty four hours from occurrence of event.
7.	30(6) – Disclosure of events specified in sub-para 4 of Para A of Part A of Schedule III.	Within 30 minutes of conclusion of board meeting.
8.	Regulation 31(1)(a) – Shareholding Pattern prior to listing of securities	One day prior to listing of securities.
9.	Regulation 31(1)(c) – Shareholding Pattern in case of capital restructuring	Within 10 days of any change in capital structure exceeding 2% the total paid up share capital.
10.	31(A)(2) – Disclosure of class of shareholders and conditions for reclassification.	Prior approval.
11.	Regulation 37(2) – Draft Scheme of arrangement & Scheme of arrangement.	Prior approval before filing with Court.
12.	Regulation 39(3) - Loss of share certificates and issue of the duplicate certificates	Within two days of getting information.
13.	42(2) – Record date or Date of closure of transfer books.	At least 7 clear working days in advance (excluding the date of intimation and the record date).
14.	42(3) – Record date for declaring dividend and / or cash bonus.	At least 5 clear working days in advance (excluding the date of intimation and the record date).
15.	Regulation 44(3) - Voting Results	Within two working days of conclusion of Meeting
16.	Regulation 45(3) – Change in name	Prior approval from Stock Exchange before filing application with Registrar of Companies.



### Answer 6A (iii)

#### Equitable treatment

SEBI (LODR) Regulations, 2015 provides for the equitable treatment to shareholders as one of the principles. This is also one of the OECD principles of corporate governance.

As per the Regulations, the listed entity shall ensure equitable treatment of all shareholders, including minority and foreign shareholders, in the following manner:

- (i) All shareholders of the same series of a class shall be treated equally.
- (ii) Effective shareholder participation in key corporate governance decisions, such as the nomination and election of members of board of directors, shall be facilitated.
- (iii) Exercise of voting rights by foreign shareholders shall be facilitated.
- (iv) The listed entity shall devise a framework to avoid insider trading and abusive self- dealing.
- (v) Processes and procedures for general shareholder meetings shall allow for equitable treatment of all shareholders.
- (vi) Procedures of listed entity shall not make it unduly difficult or expensive to cast votes.

### Answer 6A (iv)

<b>BdL market EU-regulated market</b>	<b>Euro MTF market Exchange-regulated market</b>
<ul style="list-style-type: none"><li>• The Commission de Surveillance du Secteur Financier (CSSF), Luxembourg's supervisory authority, is in charge of prospectus approval.</li></ul>	<ul style="list-style-type: none"><li>• The Luxembourg Stock Exchange is in charge of prospectus approval.</li></ul>
<ul style="list-style-type: none"><li>• Eligible for a European passport.</li></ul>	<ul style="list-style-type: none"><li>• No European passport provided.</li></ul>
<ul style="list-style-type: none"><li>• Entry for issuers is subject to the Prospectus and Transparency Obligation Directives.</li></ul>	<ul style="list-style-type: none"><li>• Outside the scope of the Prospectus and Transparency Obligation Directives.</li></ul>
<ul style="list-style-type: none"><li>• Issuers subject to International Financial Reporting Standards (IFRS), or an equivalent, for non-EU issuers.</li></ul>	<ul style="list-style-type: none"><li>• Financial reporting is in line with IFRS. However, other accounting standards, such as Generally Accepted Accounting Principles (GAAP), are accepted.</li></ul>

## MULTIDISCIPLINARY CASE STUDIES

Time allowed : 3 hours

Maximum marks : 100

**NOTE :** Answer **ALL** Questions

### Question 1.

*Premium Resorts Limited maintains a five-star deluxe facility under the brand name Diamond Palms, with 150 rooms of various categories ranging from Standard to Presidential Suites, spanning 15 acres of land, and surrounded by lush vegetation on all sides. Tariffs vary based on the room category. In addition to a 24-hour coffee shop and specialty restaurants serving cuisine from various areas, such as Indian/Chinese/Italian cuisine, etc., the resort features 7 banqueting facilities ranging from a Board Room to halls that can accommodate 1,000 guests. In addition, the property features one of the large swimming pools, dining options in the open air adjacent to the pool area, facilities for various games, a well-laid badminton court, an excellent SPA offering wellness treatments, a health club, and a well-appointed bar selling premium spirits. The hotel has been operating for close to fifteen years, and its brand is well-known.*

*Being located outside of the city, it is mostly a resort that caters to corporate clients that hold one- to three-day courses for their employees. As a result of its expansive size, the resort also a popular wedding location. These events provide a consistent source of revenue for the resort. In addition, outside catering is provided for important events, such as international cricket matches and trade shows. The resort is preferred for outdoor catering for exhibitions due to its proximity to the International Exhibition Centre, which is only three kilometres away. Additionally, the resort operates a membership loyalty programme with an outside firm. Members who enrol in the programme and pay a set price receive benefits and privileges. Marketing has been outsourced to an external organization that is responsible for bringing in business for rooms, banquets, and corporate events such as day trips or Sunday brunch, etc. for the entire property. Additionally, the agency is responsible for collecting consumer payments. The agency receives commission on sales based on monthly statements reviewed by Finance, the Front Office manager, and the Food & Beverage manager. The agency is not responsible for marketing the SPA; instead, business is generated through in-house visitors and word of mouth. The resort has also partnered with online travel sites to generate hotel bookings, primarily for leisure travellers.*

*Despite all the above agreements, location and amenities, business has been dismal and consistently falls short of the budget. Being a sprawling resort property, maintenance and upkeep are challenging. In addition, age-related malfunctions of equipment result in substantial repair and maintenance expenses on a regular basis. Besides this, there are further issues that are High fixed costs that necessitate continual occupancy levels of 70% to achieve Breakeven. Dependence on outsourced marketing activities places the business at the mercy of the agency, which may have additional agreements with other companies. In addition, they frequently complaint about the poor maintenance which attributes to low business Resort.*

*The loss of revenue and the selection of unsuitable members resulted from the selection of an incompetent agency to manage the Loyalty Program, which failed to appropriately market the initiative. Memberships were sold to anyone without verification of their background. Membership requirements included clearly specified advantages. This was disregarded the agency, which promised benefits beyond the ordinary. In addition, the Agency has not remitted the sum collected from Members and owed to the Resort, citing various issues. Simultaneously, they issued cards to Members and granted them access to the program's benefits. The agreement required the agency to provide weekly updates on the number of members enrolled and the amount collected, but they did not comply. This resulted in a loss for the resort, and members who paid the membership price were unable to utilise the advantages since the resort did not get its portion of the cost, resulting in negative publicity from potential members who were made to suffer through no fault of their own.*

*It was discovered that the resort lacked a proper system to monitor the programme, including the number of members, the amount of money due and collected, and the monitoring of member-by-member benefit utilisation, which posed further issues. Frequent breakdowns disrupted service to customers.*

*Due to a lack of business, much-needed expenditures on equipment, including replacement, were not made since management was unwilling to contribute further Rupees.*

*In the hotel industry, it might be challenging to find trained personnel. This is especially true with vacation properties located away from the major metropolis.*

*Despite the enormous potential to market the resort as a weekend escape, online agencies that were intended to generate more revenue did not bring in the anticipated amount of bookings.*

*Resort had delegated the management of its website, including comments and/or inquiries, to an outside organisation. It is to the credit of this organisation that they did the best they could, but they did not fulfil their obligations in full. The agency's location in a distant city did not assist the situation.*

*Realisations were delayed as a result of the marketing agency's inadequate collection follow up, resulting in cash flow concerns. This resulted in delayed payments to suppliers, who consequently increased the cost of supplies to offset their expenses. This resulted in an increase in procurement costs and frequent supply disruptions.*

*The problem was exacerbated by the regular resignations of department heads who were tasked with overseeing operations. Added to this resort's responsibilities were legacy difficulties resulting from the property's previous owners. This strained the available resources.*

*Certain ideas to cut costs and increase operating efficiency, such as the conversion of diesel-fired boilers to LPG and the adoption of enhanced gas consumption technologies, were not implemented. This would have saved the property approximately ₹ 3 million per year. Additionally, the resort did not have the practise of generating a Profit & Loss Account by event. Thus, it was impossible to determine the profit or loss of a particular event in order to make an informed choice. Management accepted all of Marketing Agency's leads regardless of their feasibility. Staff unionisation was another unstable aspect.*

*The resort obtained Duty Credit Scrip under the Serve from India Scheme in exchange for ₹ 7 million in free foreign exchange earned over a three-year period. Almost fifty percent of the unused scrip could not be utilised correctly by the resort. This may have saved the resort a significant duty sum and much-needed funds.*

*Similarly, ensuring reasonable accommodation rates, banquet prices, and F & B costs is crucial for sustaining and growing revenue. Marketing is essential, because attempts to sell at any cost in order to fill a facility will fail.*

*The management approaches you and demands a comprehensive report covering the following areas as well as recommendations for resolving the issues.*

- (a) Various risks to which the resort is subject and their repercussions.*
- (b) Evaluate the identified risks and their ability to cause harm to the firm.*
- (c) Risk mitigation strategy with accompanying checkpoints.*
- (d) How Premium Resorts Ltd. fulfil the needs of corporate clients?*

*(10 marks each)*

### **Answer 1(a)**

The Resort faces a wide range of potential dangers, each with potentially devastating results. In today's unpredictable environment, running a business comes with a number of inherent hazards. The only real difference is that the dangers faced by each industry are unique. In light of this, the dangers to which Premium Resorts is vulnerable are as follows:

- i. All parts of money management are susceptible to financial hazards, including but not limited to: revenue management, accounts receivable and payable, financial asset and its management. Working capital management, risk assessment and management of third-party services, and so on and so forth. Things will only get worse if the risks aren't identified and adequate resources aren't allocated. It is clear from the case study data that poor accounts receivable administration is limiting the company's ability to run smoothly
- ii. Daily operations involve a certain amount of risk. such as the possibility that essential resources won't be available when they're needed, that key personnel will let you down, that crucial internal processes will be lacking, that external factors like economic uncertainty, political upheaval leading to lost business, sudden changes in tax rates, natural calamity, etc. will adversely affect your operations
- iii. Threat from Human Resources is one of the most important threats to any business. This is especially true at all stages of operation in the hospitality business, where finding trained and skilled workers is difficult. Because demand continues to surpass supply, hotels are frequently forced to hire trainees or contract them out. These workers are uninformed about the hotel business, and as a result they cannot provide the level of service necessary to keep customers happy. Since the focus of the sector is on providing a service, skilled workers are crucial
- iv. When we talk about strategic risk, we're referring to the plan that needs to be made to cope with things like contingencies, new practices, competitive pricing, compliance regulations, contract management, governance problems, and so on.
- v. Failure to comply with numerous regulations and Governance can result in substantial damage, including loss of reputation, making compliance management one of the most significant threats to any organisation.

### **Answer 1(b)**

#### **Risk Assessment and Prioritization**

Probability of severe monetary loss: 4

Extremely likely and highly risky operations: 4

Staffing Level: Most Likely 3

Extremely likely strategic risk level 4

Chances of Compliance Management Success, Level 3

(5 stands for highest, 4 stands for higher, most likely stands for 3) Candidates can write also, or reversal scale can be used by them, then also credit to be given.

#### **Results of Danger-**

Critical-Monetary, Has the potential to generate major problems for the company.

The operational significance is high enough that it has the potential to result in a loss of business and a suspension of operations.

Human Resources- Medium might lead to service interruptions in the short term.

Strategic Management of Compliance the consequences of noncompliance can be disastrous, both monetarily and in terms of reputation.

## Answer 1 (c)

Risk mitigation strategy with accompanying checkpoints.

Preparedness measures, include a system for keeping tabs on potential dangers-

The resort has many problems, including an inefficient control system, a poorly implemented contract that allows the service provider to disregard the agreement without repercussions, a weak marketing structure, and a lack of internal control and auditing. Despite the resort's convenient location and stellar reputation, business has suffered as a result.

Having said that, it is advised to establish a reliable mechanism for monitoring, complete with built-in controls and processes, and to ensure tight adherence to process with zero tolerance for non-adherence.

### Recommended Actions-

1. **Money Fiscal:** Clearly, the lack of responsible financial management has put a significant pressure on resources, causing disruptions in supplies and services. Ineffective means of collection are one such example. Bad fee-collecting mechanisms for loyalty programmes, etc.

**2 Establish a procedure for holding periodic reviews of collections with the marketing agency:** The agency should be held accountable for any delays or failures in the collection of past or present debts. Customers may withhold payment if they have outstanding issues with billing or service that have not been resolved. Taking care of this quickly will prevent any financial difficulties.

**3. All signed agreements, including any provisions made to protect the resort, should be reviewed:** The agreement concerning the Membership loyalty programme appears to have been badly structured, putting the resort at danger. An illustration of this would be the agency's ability to avoid paying the resort fee while yet granting the benefit to members. It is necessary to reconsider the entire agreement, fire the responsible agency, and take legal action to recoup the overdue payments. A clause allowing the property to receive the money straight into a designated account should be included in any newly executed agreement. The agency's fees can be paid over on a regular schedule if both parties agree to this.

4. It's likely that the resort is paying more than necessary because of a backlog in collecting dues to suppliers, therefore it should review all of its contractual commitments, particularly those involving outsourced activity like security services, car rental services, supply contracts for perishables, etc. This issue must be resolved through negotiations with relevant vendors and service providers on terms that are acceptable to all parties.

5. Build a comprehensive budgeting system that accounts for all expenses, and use a detailed management information system (MIS) to analyse the numbers every month, identifying who is to blame if goals aren't met.

6. The operational obstacle is more of an issue that affects the whole and must be dealt with effectively.

7. Keep all of the food and other consumables as well as the supplies used to entertain guests on hand at all times. To achieve this goal, coordination between the operations and supply departments is essential. Regular planning is required, with the results conveyed to the procurement team and enough time allotted to actually acquire the necessary supplies.

8. The resort's declining revenue can be traced to the inefficiency of the outside marketing firm. Their commission may be withheld if drastic action is required. They need to be provided clear parameters for minimum allowable rates, below which they are not to go unless market conditions necessitate quoting of lower rates. Such an action requires the prior consent of Management.

9. Establish a system of checks and balances to ensure that all operational aspects, including deviations, are reviewed on a regular basis. Serious problems call for urgent meetings to be called in order to find a solution.

10. Establish a monthly evaluation of Food & Beverage expenses to ensure they are staying within budget. Recipe costs and guidelines must be in place to guarantee accurate food and beverage pricing.

11. A Profit and Loss Account that details earnings for each individual event, with projections for the future as needed, is essential. This will allow for more precise price decisions and the elimination of any operational deficiencies.

12. Each division must have its own set of standard operating procedures (SOPs), which must not be altered under any circumstances. Standard Operating Procedures need frequent reviews and updates.

13. Establish an Internal Audit system that focuses on identifying and communicating risks in order to prompt preventative measures.

14. There should be strong internal controls and solid financial policies in place.

15. Employees are the backbone of the hospitality business. A major obstacle is the lack of available skilled labour at all levels. In order to attract and keep the best employees, the HR department must implement effective HR practices, such as a competitive wage strategy. All costs must be made to suppress union activities.

16. **Strategic Danger.** The present-day business climate is loaded with danger on all fronts: Only forward-thinking leadership can ensure the company's success. There needs to be discussion about hiring a Chief Strategy Officer.

17. Noncompliance with a variety of regulations has been the downfall of many a company, causing irreparable harm to their brand and bottom line. Establish and review on a regular basis a comprehensive checklist for ensuring compliance with all requirements. New compliance needs should be reflected in the compliance calendar. It is imperative that the Chief Compliance Officer be given authority over compliance matters.

#### **Answer 1 (d)**

Being located outside of the city, it is mostly a resort that caters to corporate clients that hold one-to three-day courses for their employees. As a result of its expansive size, the resort also a popular wedding location. These events provide a consistent source of revenue for the resort. In addition, outside catering is provided for important events, such as international cricket matches and trade shows. The resort is preferred for outdoor catering for exhibitions due to its proximity to the international Exhibition Centre, which is only three kilometres away. Additionally, the resort operates a membership loyalty programme with an outside firm. Members who enroll in the programme and pay a set price receive benefits and privileges. Marketing has been outsourced to an external organisation that is responsible for bringing in business for rooms, banquets, and corporate events such as day trips or Sunday brunch, etc. for the entire property. Additionally, the agency is responsible for collecting consumer payments.

The agency receives commission on sales based on monthly statements reviewed by Finance, the Front Office manager, and the Food & Beverage manager. The agency is not responsible for marketing the SPA; instead, business is generated through in-house visitors and word of mouth. The resort has also partnered with online travel sites to generate hotel bookings, primarily for leisure travellers. The companies also used the resort for organising marketing promotion for distributors, dealers and retailers meeting and training, Diwali festival event for employees and their family and annual general meeting for shareholders.

Corporate clients refers to travel where the primary motivation is business-related. This may include, for example, employees traveling to a conference, or a manager traveling to another branch. Corporate travel is a growing market, with the increased availability of flights and the growing popularity of business events and conferences.

To fulfill the need of corporate client Premium Resorts Ltd. can do the following:

One of the ways hotels can ensure they attract more corporate travelers is by connecting with the main Global Distribution System (GDS) systems. Increasingly, businesses outsource travel management responsibilities to professional travel management companies or corporate travel agents. This often means booking accommodations for corporate travelers, and agents usually turn to global distribution systems to find the best hotels and room rates for a destination.

Ask if they would like to book a meeting room. Promote your Wi-Fi or the views of previous corporate travel guests.

Providing amenities that will appeal to these customers is vital for hotels looking to benefit from business travel. The most obvious examples are private meeting areas and easy access to laptop or phone charging ports.

Corporate travelers will likely be busy and may need to fit things in when they can, so any 24-hour services or facilities you can offer will appeal.

Analyze your existing corporate travelers. Use data in your property management system, look at feedback on online review platforms, and turn to Google Analytics to understand online habits. Try to identify some trends or details that help you to understand your business travel guests.

## **Question 2.**

(a) *You have recently been promoted to head of risk management at a steel casting company. ABC Steel Castings Ltd. [ABC] is the company's name.*

*ABC has assured you that it will continue to enhance its risk management capabilities in order to better protect and increase shareholder value. As stated earlier, the risk management system ensures compliance with Clause 49, as amended, of the Listing Agreement. With this structure in place, the Company will be able to apply standardised risk management practises across all of its divisions and departments. Risks are managed in accordance with a well-defined framework that is periodically verified and doublechecked.*

*In addition, you are informed that the company has implemented a Risk Management Manual, compiled a comprehensive profile of the most major risks facing the organisation, identified the most significant gaps in managing these risks, and developed preliminary action plans to address them. With this work, the following aims are achieved.*

*(a) Meets the Board's requirement for a more comprehensive understanding of risks and a more robust strategy for mitigating those risks; provides the means to identify, assess, and respond to business risk; and integrates an effective internal control and management reporting system with the formalised, specific requirements for conducting risk assessments on a regular basis.*

*(b) Through backward integration, the company has grown into coal and iron mines, and through brownfield expansions, it has constructed a sinter plant, sponge iron plant, coke oven plant, and power plant from waste head recovery. Additionally, it launched research and development to boost production capacity and reduce costs.*

*You discovered that the Company is ISO-14001-2004 certified and strictly adheres to industry-wide emission norms. In addition, the Company tells you that demand for DI Pipes is likely to increase significantly and that it is confident of maintaining its market position due to the Indian government's emphasis on water and water-related projects, as well as the anticipated increase in water demand.*

*This year, worker relations have remained stable and friendly despite the expanding number of unions. The lack of lost man-days over the past eight years is directly attributable to the mutual respect and cooperation between the two sides. From the company's perspective, labour relations can only improve from here. The company additionally provides credit insurance coverage.*

*Now, the Company's management has requested you to give a report outlining the most pressing dangers to the company and the preventative measures that can be taken to mitigate their impact. Provide a list of at least six tasks for the role of risk management.*

(b) *The credit portfolio of The Gargi Bank Ltd. (Bank), is approximately ₹ 10 billion. The following are some of the most important characteristics of the portfolio.*

*The construction industry accounts for twenty percent of the portfolio's exposure (other sectors include cement/steel manufacturers, building material distributors, real estate developers/builders, automotive manufacturers, tyre makers and investment companies). 30% of revenues are generated by just two clients (they belong to the construction and building materials sector). The loan portfolio consists exclusively of Indian debtors. The bank offers a variety of loan terms, ranging from short-term to long-*

*term, with the latter being 60% of the portfolio. Over 75% of total finance needs were met by short-term deposits and inter-bank borrowings.*

*Even though all loans were denominated in Rupees, 45% of all time deposits were held in non-Rupee currencies. Real estate is the only acceptable form of security. The overall risks that this portfolio confronts must be discussed. Does this credit portfolio contain any significant undiversified risks? Include some suggestions for boosting diversity if this is the case.*

(6 marks)

### **Answer 2(a)**

The risk manager's responsibilities are as follows:

1. Implement methods, techniques, and systems to identify, assess, measure, manage, monitor, and report risks, and ensure that they are followed.
2. Need to pick the best methods and tools for spotting risks.
3. Take charge of determining risk rules and procedures, thresholds, and approval levels.
4. Always keep an eye on the most pressing risks as well as the less pressing ones.
5. Oversee the procedure for notifying higher-ups about potential control risks.
- 6 Reporting on risks, including to higher-ups, is something that needs to be managed.
7. Assist in writing the Project Initiation documents by drafting the project's high-level user requirements.
8. Collaboration with end-users in the business world in order to draught functional risk standards. Provide business/reporting/ and system specifications based on a thorough understanding of business requirements and functional demands. Verify that the requirements of the business as described in the technical specifications are met.
- 9 Produce paperwork for the project manager.
10. Conduct User Education for Internally Developed Risk Management Tools.
11. Carry out audits of regulations and potential threats.
- 12 Perform risk-related compliance audits and record results.
- 13 Identify and create necessary ret policies, processes, and documentation.
14. Put the plan for handling danger into action Verify that the risk management strategy is seamlessly included into the product creation and distribution process.
- 15 Take part in regional and international dialogues aimed at developing and refining methods, strategies, and standards for managing risk.

### **Answer 2 (b)**

There are substantial portfolio risks, including those listed below.

1. The construction industry accounts for twenty percent of the portfolio at present, making it too heavily weighted. This percentage should be lowered to, say, five percent. The portfolio could suffer heavy losses if, for example, the construction industry was to experience a downturn. Banks run on razor-thin margins and are highly leveraged, so any threat to either of them may be disastrous.

2 Additionally, there is high name concentration, with only two clients making almost 30% of the portfolio. Again, it's hardly comfortable that the leading companies are in the construction and building materials industries. It's common knowledge that the construction industry heavily influences the building materials market. It is important to diversify the portfolio such that no more than five names account for more than ten percent of the total, while also guaranteeing that all of these names have excellent credit (AAA category). It is also conceivable to pursue credit assets in industries with which they have a negative correlation.



3. The liabilities in the form of deposits other than the Indian rupee creates a substantial exposure to currency risk. Because all assets are denominated in the local currency (in this case, rupees), it is possible to attempt appropriate hedging.
4. Given that 75% of the deposits and interbank borrowings are short-term, and only 40% of the credit assets are short-term (i.e., 60% of the portfolio is long-term), maturity concerns are clear. If there is an event that reduces market liquidity, the significant disparity in maturities could cause problems. It's crucial to pair people of similar ages.
5. The concentration of collateral is also not recommended
6. As long as the bank's portfolio manager is using his or her brains there's no reason to worry about the institution going under Systemic risk then becomes the primary concern Companies with well-diversified portfolios can even weather systematic shock to some extent.

**Question 3.**

(a) *Rule 10MA (2) (i) of FEMA states that the rollback provisions must be applied if the international transaction covered by the agreement (other than the rollback provision) is identical to the international transaction covered by the rollback provisions. It is unclear what the phrase "same" means. Also unknown is whether this constraint applies to the FAR analysis of functions, assets and risks. Explain.*

(6 marks)

(b) *A meeting of members of Joka Agricultural Equipment's Limited was convened under the orders of the Court for the purpose of considering a scheme of compromise and arrangement. The meeting was attended by 200 members holding 500000 shares. 70 members holding 400000 shares in the aggregate voted for the scheme. 120 members holding 90000 shares in aggregate voted against the scheme. 10 members holding 10000 shares abstained from voting. Examine with reference to the relevant provisions of the Companies Act, 2013 whether the scheme was approved by the requisite majority?*

(6 marks)

**Answer 3 (a)**

If a rollback provision is to be authorised, it must be for the same international transaction that is planned to be carried out in the foreseeable future and in regards to which an agreement has been reached. Finalizing a rollback for a transaction that isn't covered by the agreement for subsequent years is not permitted. In order to qualify as the "same international transaction," the previous year's transaction must be of the same character and be conducted with the same affiliated enterprises as the transaction that is planned for future years and for which an agreement has been made.

The limitation would function to ensure that rollback provisions would only apply if the Functions, Asset, Risk (FAR) analysis of the rollback year does not differ materially from the FAR validated for the purpose of reaching an agreement in respect of international transactions to be undertaken in future years for which the agreement applies. In the Advance Pricing Agreements that CBDT is negotiating, "materially" is being defined in a broad sense. The term "materially" is to be defined in a way consistent with its ordinary meaning and such that a change in facts and circumstances is to be viewed as a change that may reasonably have resulted in an agreement with considerably different terms and conditions.

**Answer 3 (b)**

According to section 230 of the Companies Act, 2013, the scheme of compromise and arrangement must be approved by a resolution passed with a majority in number representing three-fourths in value of the creditors, or members, or class of members, as the case may be, present and voting either in person or, by proxy.

The majority is dual, in number and in value. A simple majority of those voting is sufficient. Whereas the 'three-fourths' requirement relates to value. The three-fourths value is to be computed with reference to paid-up capital held by members present and voting at the meeting.

In this case 200 members attended the meeting but only 190 members voted at the meeting. As 70 members voted in favour of the scheme the requirement relating to majority in number (i.e., 95) is not satisfied.

190 members who participated in the meeting held 4,90,000 shares, three-fourth of which works out to 3,67,500 while 70 members who voted for the scheme held 4,00,000 shares. The majority representing three-fourths in value is satisfied

Thus, in the instant case, the scheme of compromise and arrangement of Joka Agricultural Equipment's Limited is not approved as though the value of shares voting in favour is significantly more, the number of members voting in favour do not exceed the number of members voting against.

#### **Question 4.**

*(a) The Reserve Bank of India (RBI) began adjusting its liquidity management in February, 2020. How does the RBI utilise the reverse repo rate or variable reverse repo rate auction as its primary liquidity management operation?*

*(b) Examine the following circumstance in light of the Real Estate (Regulation and Development) Act, 2016. Vivaan booked a 4 BHK apartment in the Flower Valley development for 2 crore. Jiyu is in charge of directing the project. Before engaging into a written agreement for sale with Vivaan, Jiyu stipulated that an application fee of ₹ 50 lakh be paid. Determine whether Jiyu's claim is valid.*

*(6 marks each)*

#### **Answer 4(a)**

The rebalancing of liquidity management by the Reserve Bank of India (RBI) began in February 2020, when the central bank changed its liquidity absorption mechanism from the fixed-rate overnight reverse repo window to longer duration variable rate reverse repo (VRRR) auctions. To absorb extra system liquidity, the RBI has announced the implementation of a VRRR programme, which has higher yield prospects than overnight reverse repo at a fixed rate.

The Reserve Bank of India (RBI) has increased the number of VRRR auctions as it transitions away from the overnight reverse repo auction with a fixed interest rate and re-establishes VRRR as its primary liquidity management operation. Accrual returns on very short-term, low-market-risk products such as overnight and liquid funds may increase as a result of the substantial withdrawal of liquidity from the system, according to market participants.

The reverse repo rate is the interest rate at which the Reserve Bank of India borrows funds from commercial banks. Since the Reserve Bank of India is considered the lender of last resort and has minimal need for funds from other sources, the VRRR appears to be a method to absorb surplus liquidity from the market, which in turn helps to control inflation in the country. Moreover, through VRRR auctions, the RBI absorbs the market's excess liquidity. The RBI conducts 1-day, 3-day, 14-day, and 28-day auctions, in which banks participate. RBI chooses the bank that accepts the lowest VRRR quote for a certain amount of money to store its reserves. The bank that quotes the lowest rate of interest above the Reverse Repo Rate is deemed to have won the VRRR auction. As it earns a greater return than the Reverse Repo Rate, it is a good place for banks to store their money, and the RBI would be able to control the money supply and reduce the inflation risk in the economy.

#### Answer 4(b)

Section 13 of the Real Estate (Regulation and Development) Act, 2016 (the Act) provides the provisions relating to “No deposit or advance to be taken by promoter without first entering into agreement for sale”. Section 13(1) of the Act states:

A promoter shall not accept a sum more than ten per cent. of the cost of the apartment, plot, or building as the case may be, as an advance payment or an application fee, from a person without first entering into a written agreement for sale with such person and register the said agreement for sale, under any law for the time being in force.

In the given case, the cost of apartment is Rs. 2 Crore, and Jiyu stipulated that an application fee of Rs. 50 Lakhs be paid prior to entering into a signed agreement for sale with Vivaan. This is not valid, as a promoter is only permitted to accept Rs. 20 lakh (10% of 2 Crore) as an advance or application fee before entering into a signed agreement for sale.

#### Question 5.

*(a) Forex Dealers Ltd. qualifies as an Authorized Person under the Foreign Exchange Management Act of 1999. The Reserve Bank of India instructed the aforementioned Authorized Person to file specific returns, which it failed to do. Specify the penal provisions to which the mentioned Authorized person has been subjected.*

(6 marks)

*(b) The Chief Executive Officer of DEF Ltd. an up-and-coming firm with a snappy name, has reached out to you for your input on a limited range of topics pertaining to their company and a few others within the Group. He is also a member of the Board of Directors for STU Ltd. (STU), a subsidiary of the Group involved in the production of table salt that is publicly traded. Huge cash reserves are held by STU. Directors of STU have been contemplating a possible buy-back of the company's equity for the past two board meetings. After analysing the prospective channels, the Board will likely give its approval at the following meeting. You have established a solid reputation as an expert in investment banking, advising investors and companies on capital raising, financing strategic acquisitions etc. As a result of your wide network of venture capitalist and Private Equity providers (PE) connections, you are highly sought after in the industry for advice regarding return, the optimal combination of investments, investor exit strategies etc. The Managing Director (MD) of the company has planned a first orientation meeting for you to become acquainted with DEF Ltd. and the other members of the Group. He provided a complete overview of firm organisation and discussed probable future prospects. Specifically, he was seeking your input on the following: He hopes to attract Private Equity (PE) investors or Venture Capitalists (VC) to further grow DEF Ltd. He is curious in the criteria used by private equity and venture capital firms to select whether or not a finance a start-up. To effectively raise cash for DEF Ltd. he requires your assistance in selecting the appropriate course of action and decisions to make. He is contemplating a variety of options for repurchasing STU shares. He is curious about the Group's second publicly traded company, Peps Ltd., and its aspirations to expand its sugar-producing subsidiary via a follow-on offer. As he is not a financial specialist, he has heard from his co-workers that term-sheet that PE investors typically provide is extremely complicated. When he reaches that moment, he expects you to assist him. He is also curious about the break-fee, as it is commonly utilised in the field of private investing. He learned that a relative was having difficulty in identifying the suitable exit path for PE investors. He desired your advice on how he should approach his discussions with investors. The MD is interested in discovering all of his or her choices for escaping PE. What are some potential exit routes for a PE?*

(6 marks)

### **Answer 5 (a)**

Section 11(3) of the Foreign Exchange Management Act, 1999 states that if an Authorised person contravenes any direction given by the Reserve Bank of India under the said Act or fails to file any return as directed by the Reserve Bank of India, the Reserve Bank of India may, after giving reasonable opportunity to be heard, impose on Authorised Person, a penalty which may extend to ten thousand rupees, and in the case of continuing contraventions, an additional penalty which may extend to two thousand rupees for every day during which such contravention continues.

Since, according to the facts presented in the inquiry, the Authorized person, Forex Dealers Ltd., has failed to file the required returns with the Reserve Bank of India. According to the aforementioned requirements, it has exposed itself to a fine of up to ten thousand rupees and, in the case of ongoing contraventions of the sort of failure to file the returns, an additional fine of up to two thousand rupees for each day such infringement persists.

### **Answer 5 (b)**

The various Exits a PE could take are as follows:

When a private equity investor's horizon term ends or they are asked to leave by the company's management, they have following options:

#### *1. Initial Public Offer (IPO)*

With a solid business plan and solid finances in place, going public can be a lucrative exit option. The return can be immediate if the owner sells their shares soon after the company is listed.

#### *2. Partnership Strategy or Strategic Purchase*

A larger company in the same industry as the PE buys out its minority stake. This is one of the most typical ways out for investors and it benefits everyone involved (the current investor and the company's leadership).

#### *3. Secondary Purchase*

Investor PE will sell its stake to another PE in order to quit. A similar transaction occurs when a larger PE sees potential in the enterprise and offers a more favourable deal to the smaller PE, or when the business needs more capital than the existing equity fund can provide.

#### *4. Repurchase by current management or the company's founder*

There would be a golden handshake with the current PE and the founders would regain control of the company. Sometimes the term "Management Buy Out" is used to describe this scenario.

#### *5. Liquidation*

The investor suffers a net cash loss and must withdraw the money, making this the least desirable exit option. To put it simply, this occurs when a financier is unable to bear any more losses, overestimated his or her potential profits, or discovered that the market was not enthusiastic about the venture's central concept.

### **Question 6.**

*Ramanandan Bank was the state's third largest Bank. It maintained a vast branch and ATM network in order to serve its broad retail clientele. Despite Ramanandan Bank's size, that bank's commercial success was highly reliant on local economic trends. Two years of economic downturn resulted in two years of subpar loans, and Ramanandan Bank fell into dire straits. There were numerous layoffs in order to minimise and cut overhead expenses. A new executive management team anticipated achieving faster, superior results with fewer assets. Everyone at Ramanandan Bank feared termination, despite that bank's gradual return to profitability. There was still pressure to perform or face consequences.*

Ramanandan Bank's six-person Spring Hill Branch was managed by G. Revathi. Spring Hill, complete with an ATM and a newly renovated lobby, stood in the parking lot of a new suburban shopping centre. The mall, which was anchored by a store from the largest grocery chain in the region, contained approximately twenty modest retail shops. In addition, a big hospital was only across the street and a significant manufacturing factory (with around 3,000 employees) was located in a nearby industrial park. Numerous customers of the branch worked in these areas.

Revathi was promoted to her current position around one year ago. Prior to that, she had served as Assistant Manager at another branch in the region. In the past year and a half, Revathi had mastered her managerial duties. She enjoyed her work and performed well.

In any case, I used to enjoy it, she reflected to herself. She was seated at her desk at 6:00 p.m., observing the onset of night. "I wish I could get out of here before 5:30. These layoffs are extremely painful, the strain is too great, and nobody cares if I'm here or not." Revathi was aware that she was in a foul, depressed mood.

Six months had passed since the layoffs she was contemplating, but their full impact was just now being felt. The Spring Hill Branch of Revathi was a popular location, with nine employees previously appointed. There were now only six positions available, two New Accounts posts (including Revathi's) and four tellers. One teller could divide their time between the teller line and the back office.

The issue was that there were an excessive number of consumers. Revathi chuckled at the inconsistency. Here, the bank wants more customers, but we cannot service the existing ones. On nearly every day and hour, there were three or four clients waiting in line. The fact that the majority of them simply wanted to cash a check or make a deposit did not seem to matter: by the time they reached the teller, they were brusque or harsh, demanding, and occasionally confrontational and aggressive.

Revathi vividly recalled an event that occurred just two days prior. Twenty minutes had passed while a consumer waited to pay a utility payment. When he finally reached the window, he began criticising the tellers for their tardiness and the bank for its incompetence. When he finished, the teller was in tears. Revathi recalled their conversation after he left. The cashier stated: "We exert so much effort, but no one seems to appreciate it. I simply cannot work in this state."

Revathi began to receive significantly more complaints, seemingly from everyone. Customers were grumbling about bad services, tellers were moaning about pressure and "downtown" was beginning to protest about the branch's high amount of mistakes, errors, and shortages.

Revathi was scheduled to hold one of her monthly "sales meetings" with the team tomorrow. These conferences were mandated by "downtown." Revathi despised them because they usually seemed to last forever and nothing was ever done. Revathi was scheduled to deliver a 15 to 20 minutes presentation on a product, and she imagined the audience members fidgeting or staring at the floor. There would be no inquiries, but there would be occasional complaints about "the consumers yelling at us" or "the need for extra assistance".

Revathi dreaded tomorrow's meeting and pondered how she could focus on the branch's actual issues and generate tangible outcomes. Answer the following questions.

- (a) Can Revathi use this meeting to assist in resolving some of the branch's issues?
- (b) (b) What types of broad techniques may Revathi employ to assist in resolving these issues?
- (c) (c) Describe the procedure Revathi and her staff can follow to address productivity and quality issues.

(Each question is of 4 marks = Total 12 marks)

### Answer 6(a)

Absolutely, Revathi can use this meeting to assist in resolving some of the branch's issues. However, it is likely that a series of staff meetings will be required to find a solution to these issues. The fundamental issue is that the current setup of workers and consumers is unbalanced: the demand for services exceeds their capacity to meet customer needs. Reconfiguring the branch's service and customer mix is essential for enhancing its productivity

**Answer 6 (b)**

Revathi has the following alternatives to resolving this issue:

She can first request extra personnel from her management. In addition to requesting full-time employees, she might also recommend part-time positions or staff sharing with another department. Even on her own initiative, she may pursue the latter choice with the help of friendly branch manager peers.

Secondly, Customers using tellers for transactions that could be done through other, more efficient channels contributes to the problem with productivity. There are numerous strategies to encourage clients to use more productive methods, such as direct deposit of payroll cheques and use of automated teller machines (ATMs). Since her branch is in close proximity to a lot of employers, she may suggest a marketing campaign to contact these employers in order to set up direct payroll deposit. She could also collaborate with Marketing to develop branch- based promotional programmes designed to promote ATM usage.

Thirdly, she must collaborate with her workers to discover ways to enhance service. This latter strategy would include the personnel in identifying reoccurring issues and developing suitable solutions for them.

**Answer 6 (c)**

Essentially, Revathi should initiate a quality circle or productivity improvement programme with her workers. Several significant stages are required to implement such an initiative.

She must explain the programme to her employees and convey that this is one means by which they can attempt to better their condition. She could describe some of the initiatives she is currently pursuing. She ought to explain that this procedure would be ongoing.

She should acquire training in quality and productivity enhancement measures for herself and her staff. Additionally, she should acquire the habit of providing performance reports to the workforce. She should utilise regular meetings to identify issues and generate solutions.

Her measures should include enhancing the training of staff. This can arise in two areas: dealing with challenging clients and technical aspects of branch operations. She would require training assistance in these areas.

## **BANKING – LAW & PRACTICE**

### **(Elective Paper 9.1)**

*Time allowed : 3 hours*

*Maximum marks : 100*

**NOTE :** 1. Answer **ALL** Questions.

2. Working notes should form part of the answer.

#### **Question 1**

**Read the following case study and answer the questions that follow:**

*Consumer Protection and Banks The Consumer Protection Act was enacted in India in the year 1986 to protect the interest of the consumers of goods and services. The basic thrust of the Act is on speedy and inexpensive redressal consumer's grievances. For this purpose, the Act provides for establishment of Special Tribunals at three levels namely the District, the State and the Nation. The Act applies to both Goods and Services, Banking, Financing, and Insurance are included amongst the services, in respect of which a complaint can be filed by a consumer. Over the period of time different sections of consumers as well as the providers of goods services brought under its scope. Post liberalization of economic reforms in the year 1991 and fall out over trade and commerce in India, necessitated amendments into Consumer Protection Act 1986 and which is done in the year 2002. In the past two decades seen tremendous in e-commerce and online based delivery of goods and services necessitated to repeal and replace by Consumer Protection Act 2019. The New Act aims at safeguarding and reinforcing the rights of the consumers by establishing regulatory authorities, spelling out strict liabilities and penalties on manufacturers and various service providers including electronic service providers, misleading advertisers, and by providing additional settlements consumer disputes through mechanism such as mediation. The New Consumer Protection Act, 2019 had received the assent of the President of India on 9th August 2019. However, while exercising power conferred by sub-section (3) of section 1 of the Consumer Protection Act 2019, the Central Government had fixed 20th day of July, 2020 as the appointed date that is the date on which provisions of the said Act came into force. The Act was applicable to the whole of India.*

*Banker renders various services to his customers as well as general public. The act applies to all the services rendered by a banker to both the categories of persons. Provided the service is rendered for a consideration that is a fee, commission or like. So far, the main functions of the banker are concerned with acceptance of deposits and lending of funds to the customers, the banker-customer relationship is that of debtor-creditor or creditor-debtor. Any deposit received from depositor is legally speaking a loan taken by the banker from the customer and when a customer draws a cheque on his deposit account, it deemed as repayment of the loan taken by the banker. Similar is the legal position of banker in relation to loans granted to the account holders. Hence in such transaction with the customers, a banker does not render a service for a consideration as envisaged in the Act. However, any negligence on the part of the banker in such cases do attract the provisions of the Act.*

**(A) Redressal of Customer Grievances :**

*There are many types of grievances felt by the bank customers. Some of them may relate to minor mistakes or irregularities or acts of omission or commission on the part of the bank employees. Other grievances may be in connection with serious irregularities or wrong decisions/steps taken by the bank, resulting losses to the customer. The customer has the following options available for redressal of his complaints. There are two levels of grievances which can be filed with bank concerned and at Reserve Bank of India level. In 2006 Reserve Bank of India set up a separate customer department includes administering Banking Ombudsman Scheme, acting as nodal department for Banking Codes and Standard Board of India and ensuring redressal of complaints directly by Reserve Bank of India.*

**(B) Various Authorities Under Consumer Protection Act 2019:**

*The following is a list of various authorities created under Consumer Protection Act 2019 as advisory bodies includes:*

National Consumer Protection Council, State Consumer Protection Council and District Consumer Protection Council protecting the interest of consumers.

(C) Deficiency in Service Rendered by Banker :

Various deficiencies in service namely Unlawful dishonour of cheque, Negligence in collection of cheques, Negligence in case of Safe Deposit Lockers, Negligence in issuing drafts, Negligence in case of guarantee, Negligence in case of Granting Advances and Negligence in remitting premium to Insurance Company.

*Unlawful Dishonour of Cheque :*

In this case the cheque of an applicant for convertible debenture on right basis was unlawfully dishonoured by the payee banker on the ground of deficiency of funds. Consequently, no debentures could be allotted to him. The Consumer forum awarded him compensation based on the market price of the shares that the applicant has got on conversion of debentures, if the same were allotted to him.

*Negligence in Collection of Cheque :*

In case of collection of cheques, drafts, bills etc. from outstations, the bankers render this service for a consideration. Hence any negligence on the part of the banker resulting in loss to the customer will make the banker liable for compensation under the Act. Reserve Bank of India has already directed the banks to pay interest in case of undue delays in the collection of cheques. The compensation payable under the Act will be in addition to the interest payable under Reserve Banks directive, provided negligence in the collection of cheque and the resultant loss to the customer are proved.

*Negligence in case of Safe Deposit Locker:*

Negligence in taking all the necessary precautions by the banker in ensuring the safety of the safe deposit lockers/safe custody lockers is another ground for action by the customer under the Act. The Consumer Disputes Redressal Commission in Maharashtra indicted one of the nationalized banks of negligence to render service to safeguard the custody of ornaments locked in its safe deposit vaults. The bank was ordered to pay ` 1.26 lakh towards cost of ornaments. Bank plea that the relationship between the banker and the customer was that landlord and tenant was rejected by the Commission and it was found guilty of gross negligence.

*Negligence in Issuing Demand Drafts:*

Banks issue demand drafts for a commission. At some of the branches, the staff ask the customer to collect draft after some time. The customer might miss some important transactions in the meanwhile and thus make the banker liable for compensation. If the drafts are issued without the signature of bank manager or his code number and the draft is dishonoured by the drawee branch on this ground, the customer may take recourse against the banker under the Act. If he suffers loss due to such dishonour.

*Negligence in case of Guarantee:*

In case of a bank guarantee, the bank charges a service charge from the customer and thus renders a service for a fee. If the customer does not fulfil his obligation, banker is bound to comply with the provisions of the guarantee given by him. The banker must be conscious of his additional obligations and liabilities under the Act.

*In case of Granting Advances:*

While granting an advance, banker undertakes to lend money to his customer. He does not render any service for a consideration. A banker may justifiably apply his discretion in such cases, which will not fall within the purview of the Act.

*Negligence in Remitting Premium to Insurance Company:*

If the bank has debited the account of the borrower (Customer) with insurance premium in respect of his assets, but has not remitted the same to the insurance company in time, and in the meanwhile customers assets are damaged due to natural calamity, the bank shall be liable to pay compensation to the borrower.

*Reserve Bank of India and Consumer Protection:*



The Reserve Bank of India have come long way since then recognised the significance of customer service and consumer protection in banking sector early on. The Reserve Bank of India taken measures in the area of Consumer Protection. Consumer confidence and trust in a well-functioning market for financial services promotes financial stability, growth, efficiency and innovation over the long term. Effective customer protection regulations together with an easily accessible mechanism to resolve disputes between customers and the regulated entities in a timely manner are essential for promoting consumer confidence. Further awareness measures for customers on financial matters instils in them knowledge about their rights and responsibilities and helps them to make right decisions.

Specifically, in its pursuit of the objective of consumer protection, the Reserve Bank of India introduced the Banking Ombudsman Scheme on June 14, 1995, for the customers of banks which has been reviewed periodically so that it retains relevance as an apex level complaint redressal mechanism for customer of banks. Reserve Bank has launched this Ombudsman Schemes to include the customers of non-banking financial companies and Prepaid Payment Instrument, Mobile/Electronic Fund Transfers, System providers to System Participants on payment transactions through Unified Payment Interface, Bharat Bill Payment Systems, Bharat QR Code, UPI QR Code. These schemes have evolved over time as apex level complaint redressal mechanisms for customers of entities regulated by Reserve Bank. This Schemes provide a cost free and expeditious redressal of complaints relating to deficiency in the services by eligible entities covered under respective Schemes.

Based on the above information, answer the following questions:

- (a) What is the main objective of Consumer Protection Act?
- (b) What is Product Liability? Discuss the grounds the Product Liability arises. (c) What is various Deficiency in services defined under the Consumer Protection Act?
- (d) What are various Authorities created under Consumer Protection in protection of consumers?
- (e) What are various levels for redressal of Customer Grievances?
- (f) Enumerate the types of complaints which may be referred to Banking Ombudsman?
- (g) Give some examples of negligence on the part of banker in respect of services rendered, in respect of which a complaint can be filed with a consumer forum.
- (h) What do you understand by Banking Ombudsman? Who appoint him and why?

(5 marks each)

### Answer 1 (a)

The Consumer Protection Act was enacted in India for the first time in the year 1986 to protect the interest of the consumers of goods and services. Several shortcomings have been noticed while administering the various provisions of the Consumer Protection Act, 1986. With the advent of technological development in E-commerce and online-based dispensation of goods and services and have provided new options and opportunities for consumers for which the Consumer Protection Act, 1986 was repealed and Parliament enacted the Consumer Protection Act, 2019. Consumer Protection Act, 2019 a path breaking socio economic legislation and most important milestones in the area of consumer movement in India. Preamble of the Consumer Protection Act, 2019 provides for protection of the interests of consumers and for the said purpose, to establish authorities for timely and effective administration and settlement of consumers' disputes and for matters connected therewith or incidental thereto.

### Answer 1(b)

Product liability means the responsibility of a product manufacturer or product seller, of any product or service, to compensate for any harm caused to a consumer by such defective product manufactured or sold or by deficiency in services relating thereto.

Section 84 of the Consumer Protection Act, 2019 enumerates the situation where a product manufacturer shall be liable in a claim for compensation under a product liability action for harm caused by a defective product manufactured by the product manufacturer.

Following defects manufacturer shall be liable in product liability action:

- i. The Product contains a manufacturing defect.
- ii. The product is defective in design.
- iii. There is a deviation from manufacturing specifications.
- iv. The product does not conform to the express warranty.
- v. The product fails to contain adequate instructions for correct usage to prevent any harm or any warning regarding improper or incorrect usage.

**Answer 1 (c)**

According to Section 2(11) of the Consumer Protection Act, 2019, "service" means service of any description which is made available to potential users and includes, but not limited to, the provision of facilities in connection with banking, financing, insurance, transport, processing, supply of electrical or other energy, telecom, boarding or lodging or both, housing construction, entertainment, amusement or the purveying of news or other information, but does not include the rendering of any service free of charge or under a contract of personal service.

A complaint in relation to a service may be filed if the service suffers from deficiency in any respect. The term deficiency has been defined under section 2(11) of the Consumer Protection Act, 2019, as any fault, imperfection, shortcoming or inadequacy in the quality, nature and manner of performance which is required to be maintained by or under any law for the time being in force or has been undertaken to be performed by a person in pursuance of a contract or otherwise in relation to service and includes-

- (i) any act of negligence or omission or commission by such person which causes loss or injury to the consumer; and
- (ii) deliberate withholding of relevant information by such person to the consumer;

**Answer 1 (d)**

Consumer Protection Authorities established under Consumer Protection Act, 2019 are as follows:

**I. Advisory Bodies**

- i. National Consumer Protection Council;
- ii. State Consumer Protection Council;
- iii. District Consumer Protection Council.

**II. Consumer Rights Protection Authorities**

- i. The Central Consumer Protection Authority
- ii. The Director-General of Investigation Wing appointed under sub-section (2) of section 15 under Central Authority known as "Director-General".

**III. Commissions Dispute Redressal Forum**

- i. District Consumer Dispute Redressal Commission;
- ii. State Consumer Dispute Redressal Commission;
- iii. National Consumer Dispute Redressal Commission.

**Answer 1(e)**

The grievance first of all brought to the notice of the branch manager, preferably in writing. If satisfactory answer is not received within a reasonable period and where complaint is not resolved in stipulated time the customer may take recourse to the mechanism set up by Reserve Bank of India or alternatively through judicial machinery.

In the year 2006 Reserve bank of India set up a Customer Service Department regarding customer service and grievance redressal by banks, administering Banking Ombudsman Scheme, acting as nodal

department for the Banking Codes and Standard Board of India. If the customer is not satisfied, then they can file a suit in the civil court/criminal court.

### **Answer 1 f)**

There are various complaints which are referred to the Banking Ombudsman are:

Any person may file a complaint with Banking Ombudsman having jurisdiction on anyone of the following grounds alleging:

- (i) Deficiency in banking including internet banking or other services.
- (ii) Non-Payment or inordinate delay in the payment or collection of cheques, drafts, bills etc.
- (iii) Non-acceptance, without sufficient cause of small denomination notes tendered for any purpose and for charging commission in respect thereof.
- (iv) Failure to honour guarantee/letter of credit by banks.
- (v) Complaints from exports in India.
- (vi) Concerning loans and advances in so far as they relate to non-observance of Reserve Bank Directives.
- (vii) New grounds of complaints with effect from January 2006 relating to credit cards failure in providing the promised facilities and levying excessive charges without prior notice.
- (viii) New grounds of complaints include deficiency arising out of internet banking etc.

### **Answer 1 g)**

The negligence on the part of the banker do attract the provisions of the act:

- (i) Unlawful dishonour of cheque;
- (ii) Negligence in collection of cheque;
- (iii) Negligence in case of Safe Deposit Lockers;
- (iv) Negligence in issuing demand Draft;
- (v) Negligence in case of Guarantee;
- (vi) Granting of advances.

### **Answer 1 (h)**

The *Banking Ombudsman* is a quasi-judicial authority formed with the aim to address and resolve complaints of the *Bank's* customers.

As per the Banking Ombudsman Scheme, 2006 'Banking Ombudsman' means any person appointed under Clause 4 of the Scheme.

As per clause 4 of the Banking Ombudsman Scheme, 2006, the Reserve Bank shall appoint one or more of its officers in the rank equivalent to that of a Chief General Manager to be known as Banking Ombudsman in the public interest to carry out the functions entrusted to them under the Scheme. The Banking Ombudsman can be appointed for any specified local area or for the whole or such part of the country.

**Appointment:** The Reserve Bank may appoint one or more of its officers in the rank of Chief General Manager or General Manager to be known as Banking Ombudsmen to carry out the functions entrusted to them by or under the Scheme. The appointment of a Banking Ombudsman under the above Clause may be made for a period not exceeding three years at a time.

**Aim to appoint:** The Main object of this scheme is introduced with the object of enabling resolution of complaints relating to certain services rendered by banks and facilitating the satisfaction and settlement of such complaints.

**Question 2.**

(a) Discuss in brief the important aspects of Payments and Settlement Act 2007 in day-to-day banking activities and lending process of Banks.

(6 marks)

(b) Suppose you as a Banker entered into a Forward Purchase Contract for US \$ 50,000 on 5th March with an export customer for 3 months at the rate of ₹ 59.6000. On the same day you also covered yourself in the market at ₹ 60.6025. However, on 5th May your customer comes to you and requests extension of the contract to 5th July. On this date (5th May) quotation for US\$ in the market is as follows:

Spot	₹ 59.1300/1400 Per US\$
Spot/June	₹ 59.2300/2425 Per US\$
Spot/July	₹ 59.6300/6425 Per US\$

Assuming a margin 0.10% on buying and selling, determine the extension charges payable by the customer and arrive the New Rate quoted to the customer.

Note: Rates to be rounded off to 4 decimals in multiples of 0.0025.

(3+3=6 marks)

**Answer 2 (a)**

The objectives of the Payment and Settlement Systems Act, 2007 are to provide regulation and supervision of payment methods in India Section 58 empowers the bank to make regulations for giving effect to the provisions of the Act and Clause (g) and sub section (2) thereof provides for making provisions for regulation of clearing houses for the banks including post office saving banks. The regulation of payment systems has become important in the context of electronic payment systems and probability of complication in the absence of a suitable regulatory framework with statutory backing. The Information Technology Act amended the Reserve Bank of India act, inserting the clause in Section 58(2) empowering the Reserve Bank to frame regulations relating to payments system of banks and financial institutions. The Act also provides the legal basis for netting and settlement finality. This is of great importance as in India, other than the Real Time Gross Settlement system all made by the Reserve Bank of India namely, the Board for Regulation and Supervision of Payment and Settlement System Regulation 2008 and Payment and Settlement of System Regulations 2008. Both these regulations came in to force along with Payment Settlement Act, 2007 and 12th August 2008.

The Payment and Settlement Systems Regulations covers matters like form of application for authorization for commencing /carrying on a payment system and grant of authorization, payment instruction and determination of standards of payment systems, furnishing of returns/documents/ other information, furnishing of accounts and balance sheets by system provider etc.

**Answer 2 (b)**

**Cancellation of Original Contract**

The forward purchase contract shall be cancelled for the forward sale rate for delivery June:

Particulars	Amount in Rs.
Inter Bank Forward Selling Rate	Rs. 59.2425
<b>Add:</b> Exchange Margin	Rs.0.0592

Net amount payable by customer Per USS	Rs.59.3017
Rounded off, the rate applicable is	Rs.59.3025

Particulars	Amount in Rs.
Buying USS under original contract at original price	Rs.59.6000
Selling rate to cancel the contract	Rs.59.3025
Difference in USS	Rs.00.2975

Exchange difference for US\$ 50,000 payable by the customer is Rs. 14,875 (50,000\*0.2975).

#### Rate of booking New Contract

The forward contract shall be rebooked with the delivery 15th July as follows:

Particulars	Amount in Rs.
Forward buying rate (5th July)	Rs.59.6300
Less Exchange Margin	Rs.0.0596
	Rs.59.5704

**Rounded off to Rs.59.5700**

#### Question 3.

(a) The details Current Assets and Current Liabilities of M/s Shine & Company is as follows:

Total Current Assets required by the borrower	₹ 50,000
Current Liabilities (Excluding Bank Borrowing)	₹10,000
Core Current Assets (Assumed)	₹ 4,000

Work out permissible bank borrowing as per Tandon Committee I, II and III methods of lending.

(2+2+4=8 marks)

(b) What is meant by Off-Balance Sheet exposures of Banks?

(2 marks)

(c) Bankers' Lien is called Implied Pledge. Comment.

(2 marks)

#### Answer 3 (a)

##### I. Method

In the first method of lending, 25% of the working capital gap [Current Assets - (Current Liabilities, Excluding Bank Borrowings)] should be contributed by the borrower through long term funds and remaining 75 percent can be financed through bank borrowings.

<b>Particulars</b>	<b>Amount in Rs.</b>
Total Current Assets required by the borrower	50,000
Current Liabilities (Excluding bank borrowings)	10,000
<b>Working Capital Gap</b>	<b>40,000</b>
<b>Less: 25% from borrower through long term source</b>	10,000
<b>Maximum Permissible Bank Borrowing (i.e. 75% of Working Capital Gap)</b>	<b>30,000</b>

## **II. Method**

Under this method, the borrower should provide 25% of the total current assets through long term funds.

<b>Particulars</b>	<b>Amount in Rs.</b>
Total Current Assets required by the borrower	50,000
<b>Less: 25% to be provided by borrower through long term funds</b>	12,500
<b>Less: Current Liabilities (Excluding bank borrowings)</b>	10,000
<b>Maximum Permissible Bank Borrowing (i.e. 75% of Current Assets – Current Liabilities other than Bank Borrowings)</b>	<b>27,500</b>

## **III. Method**

In this method, borrower shall contribute from long term sources to the extent of core current assets (Fixed Current Assets) and 25% of the balance of current assets. The remaining of the working capital gap can be met from the bank borrowings. This method will further strength the current ratio.

<b>Particulars</b>	<b>Amount in Rs.</b>
Total Current Assets required by the borrower	50,000
Less: Core Current Assets	4,000
<b>Balance (A)</b>	<b>46,000</b>
25% to be provided by the borrower through long term sources	11,500
<b>Balance (B)</b>	<b>34,500</b>
Less: Current Liabilities (excluding bank borrowings)	10,000
<b>Maximum Permissible Bank Finance</b>	<b>24,500</b>

**Answer 3 (b)**

Off-Balance Sheet exposures are contingent in nature. Where banks issue guarantees, committed or back up credit lines, letter of credit etc., bank face payment obligations contingent upon some event. These contingencies adversely affect the revenue generation of banks. Banks may also have contingent assets. For example, a bank may have purchased insurance to protect against certain negative events. Here banks are the beneficiaries subject to certain contingencies, derivatives are off-balance sheet market exposures. They may be swaps, futures, forward contracts, foreign currency contracts, options etc.

**Answer 3 (c)**

Under Section 171 of Indian Contract Act, 1872, the lien of banker is called the general lien which is available to the bank for the overall balance in different loan accounts rather than for a particular lien transaction. The banker's general lien is also called as implied pledge as a result the banker has the right to sell the goods and securities under its possession when these are retained under lien. There is no written pledge agreement between the bank and the debtor, but this right is available under a contractual obligation, due to which it is called implied pledge.

**Question 4.**

(a) Vivek deposited some amount in the bank for 7.5 years at the rate of 6 per cent per annum at Simple Interest. Vivek received ₹ 1,01,500 at the end of the term, Compute the initial deposit of Vivek.

(3 marks)

(b) Arun invests ₹ 10,000 every year starting from today for next 10 years. Suppose interest rate is 8 per cent per annum compounded annually. Calculate the Future value of Annuity. Given that  $(1 + 0.08)^{10} = 2.15892500$

(3 marks)

(c) Cash Credit and Overdraft classified as Non-Performing Assets if it is "Out of Order" as per New guidelines of Reserve Bank of India. Discuss.

(6 marks)

**Answer 4 (a)**

$$A = P(1+it)$$

$$1,01,500 = P(1 + 6/100 \times 15/2)$$

$$1,01,500 = P(1 + 45/100)$$

$$1,01,500 = P(145/100)$$

$$P = 1,01,500 \times 100 / 145 = 70,000$$

Initial Deposit of Vivek = Rs. 70,000

**Answer 4 (b)**

Calculate future value as through it is an ordinary annuity

$$= \frac{10,000 (1 + 0.08)^{10} - 1}{0.08} = \frac{10,000 (2.15892500 - 1)}{0.08}$$

$$= 10,000 \times 14.4865625$$

$$= 1,44,865.625$$

Then multiply the result by (1 + i)

$$= 1,44,865.625(1 + 0.08)$$

$$= 1,56,454.875$$

**Answer 4 (c)**

Cash Credit/Overdraft is classified as NPA if it is 'Out of Order'. An account should be treated as 'Out of Order' if:

- I. The outstanding balances in the cash credit and overdraft account remains continuously in excess of the sanctioned limit /drawing power for 90 days.
- II. The outstanding balance in the cash credit and overdraft account is less than the sanctioned limit/drawing power but there are no credits continuously for 90 days or the outstanding balance in the cash credit and overdraft account is less than the sanctioned limit drawing power but credits are not enough to cover the interest debited during the previous 90 days.

The definition out of order is clarified in circular issued on February 15, 2022 shall be applicable to all loan products being offered as an overdraft facility, including those not mean for business purposes and or which entail interest repayments as the only credits.

The Previous 90 day's period for determination of out of order status of a cash credit and overdraft account shall be inclusive of the day for which the day end process is being run.

In case of borrowings have more than one credit facility from a lending institution, loan accounts shall be upgraded from Non-Performing Assets to standard asset category only upon repayment of entire arrears of interest and principal pertaining to all the credit facilities.

#### **Question 5.**

*(a) Discuss the 'Credit Risk Assessment Approach' in Credit Risk Weighted Assets.*

*(b) Discuss the New Guidelines issued by Reserve Bank of India on 'Risk Assessment' procedure in 'Know Your Customer' norms.*

*(6 marks each)*

#### **Answer 5 (a)**

Under Basel II, Basel Committee on Banking Supervision has devised three approaches for calculation of credit risk weighted assets under Credit Risk Assessment.

- (i) Standardized Approach to Credit Risk:** The standardized approach has fixed risk weights which vary from 0 to 150 per cent, corresponding to various risk categories based on rating agencies. Loans which are unrated carry 100 percent risk weight. The approach has widened risk sensitivity by taking into account a broad range of collateral, guarantees and credit derivatives. The residential mortgage exposure carries a lesser risk weight related to Basel I.
- (ii) Foundation Internal Rating Based Approach:** Credit risk under this approach is based on internal ratings of a bank instead of external credit rating agencies. The ratings correspond to risk characteristics of borrower and the transaction. Expected loss arrived at based on Probability of Default of borrower Loss Given Default, Banks exposure at Default and remaining Maturity of exposure.
  - Probability of Default is a measure of (PD) likelihood that a borrower's default over a time horizon.
  - Loss Given Default (LGD) computes the proportion of the exposure that will be lost if Defaults occurs.
  - Exposures at Default (EAD) gives an estimate of loan amount outstanding at the time of default.
  - Maturity (M) measures the remaining economic maturity of the exposure.
- (iii) Advanced Internal Rating Based Approach:** It is an improved version of Foreign Investment Promotion Board Under the Loss Given Default, Exposure of Default are estimated based on historical data by the bank itself.



### Answer 5 (b)

In Master of Direction on Know Your Customer (vide Reserve Bank of India Circular dated April 20, 2020) added new section (5A) requiring Reporting Entities to carry out Money Laundering and Terrorist Financing, Risk Assessment exercise periodically to identify, assess and take effective measures to mitigate its money laundering and terrorist financing risk for clients, countries or geographic areas, products services, transactions or delivery channels, etc. While assessing the Money Laundering and Terrorist Financing Risk, Reporting Entities are required to take cognizance of the overall sector specific vulnerabilities, if any, that the regulator/supervisor may share with Reporting Entities from time to time. Further, the internal risk assessment carried out by the Reporting Entities should be commensurate to its size, geographical presence, complexity of activities/ structure etc. Also, the Reporting Entities shall apply a Risk Based Approach for mitigation and management of the identified risk and should have Board approved policies, controls and procedures in this regard.

As per recent amendment done by the Reserve Bank of India through amendments in Master Direction on May 10, 2021, Reporting Entities (REs) may undertake V-Customer Identification Procedure to carry out

- Customer Due Diligence in case on boarding for individual customers, proprietor in case of proprietorship firm, authorised signatories and Beneficial Owners in case of Legal Entity customers.  
Provided that in case of Customer Due Diligence of a proprietorship firm, Reporting Entities shall also obtain the equivalent e-document of the activity proofs with respect to the proprietorship firm, as mentioned in Section 28 apart from undertaking Customer Due Diligence of the proprietor.
- Conversion of existing accounts opened in non-face to face mode using Aadhaar One Time Password based e-Know Your Customer authentication as per Section 17.
- Updating/ Periodic updating of Know Your Customer for eligible Customers.

### Question 6.

(a) Discuss the compliance functions and role of 'Chief Compliance Officer' in NonBanking Financial Companies in Upper Layer and Middle Layer.

(b) Customer Mr. X of Branch Y deposited an outstation cheque of ₹ 2.50 lakh to the branch for collection. The cheque was not sent for collection instead it was stitched with the voucher. During the 'Voucher Verification Report' checking the concerned person observed the mistake. He was to leave the branch as it was already late. He kept the voucher in the drawer for the disposal on next day. Next day he forgot about the cheque. After 15 days Mr. X visited the branch to check if it was collected. Then the concerned staff immediately recollected about the cheque. The customer was told to wait for some more days and the staff promised that he would follow up. It took further 10 days in collection of the cheque. He gave complaint to the bank bank citing that he had incurred a loss of ₹ 3 lakhs due to the delay in collection as he could finalize a deal to purchase a property. Earnest Money given by him was lapsed due to the delay. He also provided evidence to that. The aggrieved customer filed a complaint in District Consumer Court Complain Online. Customer demanded a compensation of ₹ 5 lakh for the loss and mental anguish suffered by him. Discuss the position of Banker and quote the case.

(6 marks each)

### Answer 6 (a)

As part of robust compliance system banks are required inter-alia, to have an effective compliance culture, independent corporate compliance function and strong risk management programme at bank and group level. Such an independent compliance function is required to be headed by a designated Chief Compliance Officer through a suitable process with an appropriate fit and proper evaluation /selection criteria to manage compliance risk effectively.

The Reserve Bank of India has place following guidelines on Scale Based Regulation applicable to all Non-Banking Finance Companies in Upper Layer and Middle Layer regarding Compliance Function and role of

Chief Compliance Officer to align the supervisory expectations on Chief Compliance Officer with best practices.

The Compliance Function is an integral part of effective governance a, along with the internal control and risk management processes. The Non-Banking Finance Companies in Upper Layer and Middle Layer shall treat the prescription in the circular as set of minimum guidelines only and accordingly frame their guidelines taking into account their corporate governance framework, the scale of operations, risk profile and organizational structure, etc.

Compliance risk is the risk of legal or regulatory sanctions, material financial loss or loss of reputation a Non-Banking Finance Companies (NBFCs) may suffer, as a result of its failure to comply with laws, regulations, rules and codes of conduct etc., applicable to its activities.

Compliance Function shall ensure strict observance of all statutory and regulatory requirements for the Non-Banking Finance Companies, including standards of market conduct, managing conflict of interest, treating customers fairly and ensuring the suitability of customer service. The Board/Board Committee shall ensure that an appropriate Compliance Policy it put in place and implemented. Further, the Board/ Board Committee shall prescribe the periodicity for review of Compliance risk.

The Senior Management shall carry out an exercise at least once a year, to identify and assess the major Compliance risk facing the Non-Banking Finance Companies and formulate plans to manage it, submit to the Board/Committee a review at prescribed periodicity and a detailed annual review of Compliance and report promptly to the Board/Committee on any material compliance failure while ensuring that appropriate remedial or disciplinary action is taken.

The Chief Compliance Officer shall be the nodal point of contact between the Non-Banking Finance Companies and the regulators/supervisors and shall necessarily be participant in the structured or regular discussions held with Reserve Bank of India. Further, compliance to Reserve Bank of India necessarily through the office of the Compliance Function.

In some Non-Banking Finance Companies there may be separate departments/divisions looking after compliance with different statutory and other requirement. In such cases the departments concerned shall hold the prime responsibility for their respective areas, which shall be clearly outlined Adherence to applicable statutory provisions and regulations is the responsibility of each staff member. However, the Compliance Function would need to ensure overall oversight.

The Non-Banking Finance Companies shall lay down a Board-approved Compliance policy clearly selling outs Compliance philosophy, expectations on Compliance culture, structure and role of the Compliance Function, the role of Chief Compliance Officer, processes for identifying, assessing, monitoring, managing and reporting on Compliance risk. The policy shall be reviewed at least once a year.

The Compliance Department shall be headed by the Chief Compliance officer meeting the requirements prescribed in this circular issued by Reserve Bank of India Non-Banking Finance Companies are free to adopt their own organizational structure for the Compliance Function. However, the function shall be independent and sufficiently resourced, its responsibilities shall be clearly specified, and its activities shall be subject to periodic and independent review.

#### **Answer 6 (b)**

The duty of the collecting banker is to present the cheque for collection in reasonable time, else will be liable for damages if customer incurs, due to delayed presentation.

#### **Decision:**

Bank received the communication from the Consumer Court. The branch manager met with the customer and convinced him for compensation of Rs. 1 lakh only in full settlement of account. The customer gave him it in writing. The banker is liable for compensation through settlement as part of Negligence of banker (*State Bank of Patiala vs. Rajinder Lal (Revision Petition no 2510 of 2002)*).

## INSURANCE – LAW & PRACTICE

### (Elective Paper 9.2)

Time allowed : 3 hours

Maximum marks : 100

**NOTE :** 1. Answer **ALL** Questions.

2. Suitable assumptions, if considered necessary, may be made while answering a question. However, such assumptions must be stated clearly.

#### Question 1.

Many proponents feel that filling up of the proposal form is a boring and tiresome job and the agent of the insurance company should take care of that. But actually, that should not be the case. The proposer himself is supposed to fill up the same on his own. Despite that, many prefer the agent to do the job and most of the times the agents do it without asking for any details of the health status of the proponent. This innocent act may run into a nightmare, if the policyholder dies within two years from the date of commencement of the policy. In such a situation, mandatory investigations are carried out before passing such claims and the insurer may reject the claim, if the probe reveals that the policyholder had withheld some information which was material information for the purpose of underwriting by the insurer. It is the responsibility of the proponent to fill up the proposal form while the agent may only help him. Regulations too do not allow an agent to go beyond this." Thus, an insurance policy is a contract, and it must, therefore, conform to the rules of general contract law. Through a contract of insurance, the insurer agrees to make good any loss on the insured property or loss of life that may occur in course of time in consideration for a small premium to be paid by the insured. The business of insurance aims to protect the economic value of assets or economic value of life of a person.

On the basis of the above facts, answer the following questions :

- (a) Despite a contract, how can the insurer repudiate its liability ?
- (b) How can you apply the concept of warranty in this context ?
- (c) How can you differentiate between a warranty and a representation ?
- (d) Discuss the legal authority of the insurer to repudiate its liabilities.
- (e) "It is therefore the duty of the proposer to disclose, clearly and accurately, all material facts relating to the proposed insurance." Discuss the facts that are to be disclosed by the proponent as well as the facts that are not need not be.

(8 marks each)

#### Answer 1(a)

Insurance contracts are contracts of utmost good faith, based on the principles of "Uberrimae Fidei". The person taking the insurance policy is expected to disclose the information required in the application form concerning his health, occupation, family history, habits and all other material questions truthfully without withholding any information required. This is to enable accurate assessment of the risk and fixing of the premium by the insurer accordingly. Repudiation is a breach of a contract by the one-party that justifies cancellation. Repudiation is conduct that exhibits the clear and unequivocal intention of the party concerned to no longer be bound to the contract. Since only the person taking the insurance is privy to the personal information, obligation to truthfully disclose lies with the person taking the insurance. If there is any misstatement or concealment of a material fact (any information which would have impacted the decision to accept the risk), the insurance company has the right to cancel the contract (repudiation) and deny the policy benefits.

In this case, there is a high possibility that the agent may commit mistake and that may turn into a misrepresentation on the part of the policy holder. Moreover, the policyholder has to provide a warranty regarding the correctness of all the facts mentioned therein. Therefore, the contract will be treated as voidable at the option of the insurer owing to misrepresentation, if anything wrong is written in the proposal form.

A Life Insurance Policy cannot be repudiated on the ground of fraud if the insured can prove that the misstatement of or suppression of a material fact was true to the best of his knowledge and belief or that there was no deliberate intention to suppress the fact or that such misstatement of or suppression of a

material fact are within the knowledge of the insurer and in such a case, the onus of disproving lies upon the beneficiaries, in case the policyholder is not alive.

#### **Answer 1(b)**

A warranty is a promise collateral to the main contract, so that if there is a breach, it merely gives a right to damages and does not go to the root of the contract. In insurance contracts, however, a warranty corresponds to a condition in ordinary commercial law, that is to say, it entitles the party aggrieved by the breaking of a warranty, to repudiate the contract either ab initio or from the date of the breach, according to the terms of the contract. A warranty must be complied with strictly and literally. It makes no difference whether the breach of warranty is material or immaterial, fraudulent or innocent, or whether the insurer would have been equally ready to insure at the same premium if aware of the breach.

A warranty in an insurance policy is a statement attesting that something the insured person says is true. An insurance contract is written on the principle of utmost good faith, meaning each party must trust that the other is being completely truthful. For the contract to be valid, you may have to warrant that an assumption the insurer is making is true. For example, if you are applying for life insurance, you must make a warranty that you are not terminally ill. If the insurer discovers that one of your warranties is untrue, it generally has the power to void the contract and not honor any claims you make. This is the only instance where the term "insurance warranty" is accurate.

So in this case if the agent has declared the wrong information, then the insurance company has the power to void the contract and not honor any claim to the client.

#### **Answer 1(c)**

A warranty is a statement that is considered guaranteed to be true and, once declared, becomes an actual part of the contract. Typically, a breach of warranty provides sufficient grounds for the contract to be voided. Conversely, a representation is a statement that is believed to be true to the best of the other party's knowledge. In order to void a contract based on a misrepresentation, a party must prove that the information misrepresented is indeed material to the agreement. According to the laws of most states and in most circumstances, the responses that a person gives on an insurance application are considered to be a representations, and not warranties.

The differences between a representation and a warranty are as follows:

- i. A representation, even when material, need only be substantially correct whereas a warranty must be strictly and literally complied with.
- ii. Before a misrepresentation can be held to be sufficient to enable the insurer to avoid the contract, it must be shown to be material to the risk. On the other hand, with a warranty, any breach is sufficient to avoid the contract, whether it is material or not.
- iii. Whereas a representation does not appear in the policy, a warranty must be incorporated in the policy whether expressly or by reference.

#### **Answer 1(d)**

Insurance laws and the terms and circumstances stated in the insurance policy are normally what regulate an insurer's legal right to repudiate its obligations or deny a claim. There are several fundamental principles that can help clarify the insurer's authority in this case, even though precise rules and regulations may vary among regions.

- i. **Terms and Conditions of the Policy:** Insurance policies are contracts that the insurer and the insured enter into. The parameters of coverage and the situations in which the insurer may reject a claim are specified in the policy's terms and conditions. Both parties are expected to abide by these conditions, which are typically included in the policy document.
- ii. **Misrepresentation or Non-Disclosure:** If insurers can prove that the insured made false statements or omitted material information during the application procedure, they have the right to refuse a

claim. This is typically founded on the idea of absolute good faith, which calls for accurate and thorough information to be provided by both parties. The insurer may have grounds to reject the claim if they can demonstrate that the insured willfully provided inaccurate information or concealed pertinent facts.

- iii. **Policy Exclusions and Limitations:** Exclusions and restrictions that describe the scenarios and dangers that the insurance policy does not cover are frequently included in insurance plans. Depending on the type of insurance, such as health, property, or liability insurance, these limitations may differ. The insurer may be able to reject the claim based on such terms if the exclusion listed in the policy applies to the claim.
- iv. **Breach of Policy Conditions:** In the event that the insured does not adhere to specific policy requirements, insurers may reject a claim. These requirements could include giving prompt notice of a loss, helping with the claims investigation, or adhering to particular safety precautions. The insurer may contend that it is released from its duties under the policy if the insured violates these terms.
- v. **Fraud or Illegal Activities:** The insurer may be able to repudiate their obligations if they can show that the insured committed fraudulent or criminal activity that were related to the claim. Insurance policies frequently don't cover damages brought on by unlawful or dishonest behaviour.

Further, Section 45 of the Insurance Act, 1938, also called Indisputability or Incontestability Clause, has given the authority to the insurer to repudiate a claim in the following cases:

The policyholder suppressed certain facts and those facts were material for the underwriting decision-making by the insurer if death claim arises within two years from the date of commencement of risk. But if any death claim occurs after two years from the date of commencement of the risk, an insurer has to prove the following three points in order to repudiate any policy benefit:

- i. Statement(s) made in the proposal for insurance or in any medical report or any other document leading to issue of policy was inaccurate or false on a material matter (i.e. on a matter which could have affected judgment of underwriter)
- ii. The statements were made with fraudulent intention
- iii. The policyholder knew at the time of making the statement that it was false or knew that material facts were suppressed

It is significant to remember that the insurer's power to repudiate obligations is not unqualified. If an insured person feels that a claim was unfairly denied or that the policy's conditions were broken, they have the right to contest the decision and pursue legal action. Depending on the relevant laws and the insurance policy's conditions, disputes over claim denials may be settled through negotiation, arbitration, or, if required, litigation in the court system.

### **Answer 1(e)**

The duty of disclosure must be observed throughout the negotiations and continues until they are completed and the contract is operative. The contract is deemed to be operative when the proposal is accepted by the insurer. This is called the "condition of continued insurability" which operates from the date of the proposal and the date of its acceptance.

Material facts, which are to be disclosed, include the following:

- i. Facts, which show that a risk represents a greater exposure than would be expected from its nature e.g., the fact that a part of the building is being used for storage of inflammable materials.
- ii. External factors that make the risk greater than normal e.g. the building is located next to a warehouse storing explosive material.
- iii. Facts, which would make the amount of loss greater than that normally expected e.g. there is no segregation of hazardous goods from non-hazardous goods in the storage facility.

- iv. History of Insurance (a) Details of previous losses and claims (b) if any other Insurance Company has earlier declined to insure the property and the special condition imposed by the other insurers; if any.
- v. The existence of other insurances.
- vi. Full facts relating to the description of the subject matter of Insurance

In the absence of an enquiry, the following facts need not be disclosed. Consequently, they have no effect on the validity of the contract:

- i. Facts which lessen the risk proposed for insurance
- ii. Facts which could or should be inferred by the insurer in the wake of the particulars being actually disclosed.
- iii. Facts of public knowledge, such as the existence of a state of war, or facts which should be known to the insurer in the ordinary course of his business.
- iv. Matters of law.
- v. Facts with the possibility of discovery where the insurer has been given enough information to provoke enquiry on his part. The details furnished by the proposer in such circumstances must be adequate to fulfil his duty of disclosure.
- vi. Facts which can be reasonably concluded are a matter of indifference to the insurer, or regarding which he has waived information. e.g. if the proposer inserts a disk in an answer to a proposal form question and the insurer makes no further enquiry.
- vii. Facts which are superfluous to disclose by reason of a warranty in the proposed insurance.
- viii. Any fact as to which information is waived by the insurer.

## Question 2.

*(a) A top equestrian, Sundar Raj, insured his prize show horse, Karishma, for ₹ 2.5 lakh. After a series of lack lustre performances, Karishma died suddenly from what appeared to be colic, a common killer disease of horses. However, the underwriters settled the claim of ₹ 2.5 lakh although many observers felt that the settlement was more than the horse was worth alive due to its poor performance just prior to its death.*

*During the same time, the Fraud Investigation Department of the Insurance Company was involved in an investigation regarding horse killings and related insurance fraud. They arrested one Salim, who said that he was paid to kill horses so that their owners could collect any insurance proceeds. Further, Salim also revealed the names of his clients wherein Sundar Raj was also mentioned. During the trial, the owner testified that Karishma had not died of a natural cause, but instead died of electrocution which can be easily disguised as colic.*

*From the information provided, answer briefly, the following questions:*

- (i) How as a responsible underwriter, you would evaluate the risk factors while issuing such a policy? (2 marks)*
  - (ii) Is moral hazard present in the case? (2 marks)*
  - (iii) Can the company call back the insurance settlement of ₹ 2.5 lakh? (2 marks)*
  - (iv) Identify the damage compensation liability of the owner. (2 marks)*
- (b) Gopal quit smoking about 18 months ago. How much time should have lapsed before insurers would consider him a non-smoker for a term life insurance policy? (4 marks)*

### **Answer 2(a)(i)**

The underwriting process follows a series of stages, at the end of which the status of a risk is decided. An important part of the insurance underwriting process is assessing risk variables as a competent underwriter. It is only after the risk has been weighed and all possible alternatives evaluated that the final underwriting is done.

There are different types of hazard which can influence the decision to accept or reject a risk:

- **Physical hazards:** These are hazards that affect the physical characteristics of whatever is being insured. For example a building made of wood represents a higher level of physical hazard than the one made of bricks.
- **Moral hazards:** These hazards refer to the defects that exist in a person's character that may increase the frequency or the severity of loss. Such a character may tend to increase the loss for the company.
- **Financial hazards:** If the value of the risk is beyond the capacity of the insurer he may reject the risk, or share the same.

In this case, as a prudent underwriter, at the time of issuance of the policy, besides the cost of the horse, the character of the owner and his past loss record are some of the factors to be considered. Underwriters can issue insurance policies with more knowledge and assurance that the insurer will be able to manage potential losses while providing coverage to those who fulfil the risk criteria by carefully examining risk variables.

### **Answer 2(a)(ii)**

**Moral hazards:** These hazards refer to the defects that exist in a person's character that may increase the frequency or the severity of loss. Such a character may tend to increase the loss for the company.

**Intentional Loss or Damage:** Insured individuals or entities may be tempted to intentionally cause damage or losses to their insured property to receive insurance payouts. As per this clause the moral hazard is present in this case as Sunder Raj has intentionally taken the insurance of Karishma, his horse and paid Salim to kill his horse to get insurance benefits.

### **Answer 2(a)(iii)**

In this case, due to fraudulent activity involved, an insurance company have the power to call back an insurance compensation of Rs 2.5 lakhs. When an insurance company learns that an insured person purposefully provided false information or acted fraudulently to secure the settlement, they may file a lawsuit to recoup the money paid out.

It is crucial to remember that the insurance company must offer proof to back up any allegations of fraud. Usually, they have to file a lawsuit and argue their case in court. The insured person will have a chance to argue their case and offer their own proof. The result will be determined by the particular facts, the evidence offered, and the relevant laws and rules governing insurance contracts.

### **Answer 2(a)(iv)**

The owner can be convicted for a clear case of fraud, with a liability of fine and imprisonment as per the rules of the criminal code procedure. Further he is also guilty of manipulating the cause of death with a wilful intention to cheat the insurance company.

### Answer 2(b)

After giving up smoking, different insurance companies have different requirements for how long they will consider a person to be a non-smoker. However, insurers frequently use a 12-month smoke-free period as their benchmark. This indicates that a person who has been smoke-free for at least a year may qualify for non-smoker prices or policies.

Gopal would normally satisfy the time limit established by many insurers to be regarded as a non-smoker because he stopped smoking 18 months ago. It's crucial to remember that each insurance company has its unique underwriting standards and procedures. To qualify as a non-smoker, certain insurers may need a longer smoke-free period, such as 24 months or more.

It is advised that Gopal speak with insurance companies directly to learn more about the exact requirements and eligibility for a term life insurance policy as a non-smoker. They will give you the most precise details about their individual plans, underwriting requirements, and premiums for non-smokers.

### Question 3.

(a) *What steps would you suggest for minimization of losses in Health Sector?*

(b) *In an Agriculture Cultivating Land, the loss occurrence yearly, in Rupees and the Probability of loss occurrence also are given below. Find the mean amount of loss and Expected Value of Loss for 5 years :*

Year	Loss in Rupees (₹) lakh	Probability of Loss
1	6	0.05
2	28	0.18
3	30	0.28
4	15	0.35
5	58	0.14
Total	137 Lakh	1.00

(6 marks each)

### Answer 3 (a)

There is robust growth of business in "Health Sector" and this trend is expected to continue in future also. Unfortunately, Ratio of Loss in this sector has increased with the business growth. Hence, there exists urgency of minimizing losses.

- Aggressive Marketing of Health Policies to the people of Younger Age by introducing new products, training to the Agents and Greater incentives for procuring this Business.
- Loading of Premium on Group Policies based on their Past Claim Experiences.
- Careful Selection of Third Party Administrators (TPA) having Professionals and favorable past records.
- Monitoring the working of TPAs on regular basis as the loss ratio in the Health Sector increases considerable after the introduction of TPA.
- The benefits under various heads like Room Rent, Doctors fees and Diagnostic materials etc. should have individual limits instead of overall Sum Insured without any Sub Limits.
- Maximum Limits of compensation may be fixed for treatment of common diseases like Cataract, Kidney Stone, and Heart Ailments etc.
- While empaneling Hospitals for cashless service, insurance companies may negotiate for discounts.
- Prompt investigation of doubtful cases to detect fraud.
- Blacklisting of hospitals and third party administrators found resorting to fraudulent means.



**Answer 3 (b)**

Year	Loss in Rupees (Rs.) lakhs	Probability of Loss	(Loss x Probability loss)
1	6	0.05	0.30
2	28	0.18	5.04
3	30	0.28	8.40
4	15	0.35	5.25
5	58	0.14	8.12
<b>Total</b>	<b>137</b>	<b>1.00</b>	<b>27.11</b>

- a) Means amount of loss =  $137 / 5 = 27.40$   
b) Expected amount of loss = 27.11

**Question 4.**

(a) What is the difference between subject-matter of insurance and the subject-matter of a contract of insurance?  
(3 marks)

(b) What are the underwriting factors to be considered for a fire insurance cover?  
(3 marks)

(c) Three friends, Ashok, Lalit and Hari-teamed up to start a lobster export business. Ashok owned a ship which was used in the business for fishing as well as for transporting the processed lobsters to foreign shores. They insured their ship, the cargo, freight, profits and commission, for a total of ₹ 80 lakh. Expecting to obtain enormous profits on their cargo, it was overvalued by the insured. A few months later, the ship sank in mid-ocean as it had a hole. Consequently, the cargo was also lost. The insured approached the insurance company to file a claim for compensation for the lost cargo. However, the insurance company refused payment of the entire claim amount. It only made partial payment of the claim stating that the cargo was insured for an amount more than its actual market value. Moreover, investigation by the insurance company surveyor revealed that the insured had intentions to sink the ship. The vessel was retrieved by the insurance company and was offered for sale as salvage. The insured approached the court to prevent the sale of the ship. Based on the above facts:

(i) Was the insurance company violating the insurance contract by refusing payment to the insured? Justify your answer.  
(4 marks)

(ii) Discuss the duty of an insurer pertaining to salvage.  
(2 marks)

**Answer 4 (a)**

The subject matter of insurance and the subject matter of a contract of insurance refer to different aspects within the context of insurance.

- i. **Subject Matter of Insurance:** The precise item or danger being covered is referred to as the subject matter of the insurance. It serves as the focus of the insurance policy and serves as the entity or piece of property that is the subject of insurance coverage. A building, a car, or any other tangible object that is being insured against certain risks could be the subject matter of insurance in the case of property insurance, for instance.
- ii. **Subject Matter of a Contract of Insurance:** The agreement between the insurer and the insured is referred to as the subject matter of an insurance contract. It serves as a representation of the terms and conditions of the insurance contract, including both parties' rights and duties. It includes all of the clauses that control the insurance relationship, including the coverage that is offered, the premium that must be paid, policy limitations, deductibles, and exclusions.

In conclusion, the subject matter of insurance refers to the particular thing or risk that is insured, whereas the subject matter of an insurance contract refers to the conditions that are specified in the actual insurance

contract. The object of coverage is the topic of insurance, whereas the agreement that forms the insurance relationship and specifies the rights and obligations of both parties is the subject of an insurance contract.

#### **Answer 4 (b)**

Underwriting the peril of fire focuses on the physical hazards presented by a particular loss exposure. To assure a thorough review of these hazards' property underwriters use an approach that scrutinizes four specific areas. These are traditionally referred as COPE-Construction, Occupancy, Protection and External Exposures.

Construction of the covered property is of primary concern to the underwriter. The building construction is directly related to its combustibility when exposed and its construction as fuel once ignited. The Insurance Services Office (ISO) divides building construction into Six Classifications:

- i. Fire Resistive.
- ii. Modified Fire Resistive.
- iii. Masonry Non-combustible.
- iv. Non-combustible.
- v. Joisted masonry.
- vi. Frame.

Occupancy factors affect the frequency and severity of losses. These factors which vary from one occupancy to another can be grouped into three headings:

- i. Ignition sources or fire causes.
- ii. Combustibility.
- iii. Damageability.

Fire protection can be of two types: public or municipal protection provided by towns and cities- and private protection provided by the property owner or occupant.

External exposures are those outside the area owned or controlled by the insured. These exposures fall into the following categories:

- Single-Occupancy Exposures.
- Multiple-occupancy Exposures

When the property being underwritten consists of a single building, fire division or group of buildings owned and controlled by the same policyholder, a single- occupancy exposure exists. A multiple-occupancy exposure occurs whenever other portions of the same fire division are owned and controlled by persons other than the policy holder.

#### **Answer 4 (c) (i)**

An insurance contract legally binds an insurer to pay the policyholder for the damages or losses caused by the perils against which the policyholder has insured himself. In the given case, the sinking of the ship and the loss incurred by the insured was due to willful or fraudulent act of the insured and not by the perils against which the ship was insured. An insurer is not liable for refusing to accept a claim pertaining to a loss caused by the fraudulent act of the insured. Such losses are not covered by insurance policies.

However, in taking over the ship to sell as salvage, the insurer was violating the insurance contract because salvage belongs to the insurer only after he has made the payment of the loss suffered to the insured. In this case, the insurer should have rejected any further dealings with the insured once it was apparent that the insured had involved in fraudulent act by intentionally causing the ship to sink to claim the insurance amount. Instead, the insurance company took over the insured's property for salvage without the latter's approval.

Thus, the insurer was not acting within the framework of the insurance contract and was liable to be legally penalized.

#### **Answer 4 (c) (ii)**

Salvage refers to the process of recovering or preserving insured property that has been damaged or lost. The duty of an insurer pertaining to salvage involves several key aspects:

- i. **Duty to Preserve Salvage:** Insurance companies have a responsibility to make every effort to preserve salvage. This involves attempting to safeguard and salvage the insured property in the event of a loss. For the purpose of evaluating the damage and determining the salvageable value of the property, insurers may use surveyors or adjusters.
- ii. **Right of Subrogation:** After paying a claim, insurers have the option to assume the role of the insured and seek all appropriate legal remedies to recoup their expenses from liable parties. This is known as the right of subrogation. This includes the right to salvage damaged property and recoup any remaining value. To lessen their losses, insurers may decide to sell recovered products, salvage rights, or other recoverable assets.
- iii. **Salvage Value Considerations:** When resolving disputes, insurers must take salvage value into account. The estimated worth of the damaged item or its remaining parts that can be recovered or sold is known as the salvage value. Usually, this sum is subtracted from the total claim settlement given to the insured.
- iv. **Salvage Disposition:** The way the recovered items or assets are handled is up to the insurers. They could decide to auction off salvage, bargain salvage deals with specialised salvage firms, or give salvage rights to interested parties. The type of property, the state of the market, and the possibility of recovering value are frequently taken into consideration when choosing a salvage disposition.

#### **Question 5**

*(a) Sumit gifted a brand new car to his wife Devi on her birthday. The car was insured against damage or loss with Wheels Insurance Company for an amount of ₹ 5 lakh with a deductible of ₹ 75,000 from her coverage.*

*One day, Devi, who was an experienced, driver, took the car out to visit her friend. On the way to her friend's place, she had to stop at a traffic signal. Although she stopped her car to avoid jumping the signal, a speeding driver from behind rammed into her car. The impact of the collision was such that Devi suffered severe injuries and she had to be hospitalized. Her car was reduced to a wreck. Investigations revealed that the car that hit Devi's car was being driven by Amit Garg.*

*Devi filed a claim for loss with her insurance company and received ₹ 4,25,000 as damage claim. The insurance company, in turn, sued Amit on behalf of its policy holder, Devi for the same amount that it had paid her. Amit Garg approached the court challenging the validity of the Insurance Company's suit*

*(i) What is the principle on the basis of which the Insurance Company accepted Devi's claim and later filed a suit against Amit Garg ?*

*(4 marks)*

*(ii) What is a deductible ? How does an insured benefit by having a deductible clause in his insurance coverage ?*

*(4 marks)*

*(b) Gopal Singh had engaged a driver for his car, who had negligently driven the vehicle and caused damage to a third party. Is Gopal responsible in the above situation ?*

*(4 marks)*

#### **Answer 5 (a) (i)**

The Insurance Company paid the claim amount to Devi and later filed a suit for claiming the same from Amit Garg by following the process of subrogation. In common parlance, subrogation is the process of legally substituting a person in place of another.

According to the principle of subrogation, when the insured is compensated for the losses due to damage to his insured property, then the ownership right of such property shifts to the insurer. This principle is applicable only when the damaged property has any value after the event causing the damage. The insurer can benefit out of subrogation rights only to the extent of the amount he has paid to the insured as compensation.

In subrogation, legal proceedings are initiated by the insurance company against a third party that has a liability to the policyholder. Subrogation gives the insurance company, the right to collect the claim amount from a third party after paying the insured's claim. It is one of the most effective procedures of post-loss claims handling. Subrogation is common in claims that pertain to automobile damage, property insurance and worker's compensation claims. Although the Policyholder's deductible may be included in the claim, other losses suffered by the policyholder such as medical expenses, which are not included in the coverage are not taken into account during subrogation.

### **Answer 5 (a) (ii)**

Deductible is the amount that an insurer deducts from the amount of loss before paying the remaining amount to the policyholder. For example, if a certain company has a Rs. 50,000 deductible in its fire insurance policy, the insurer will only pay for claims that exceed Rs. 50,000. Thus, a loss of Rs. 1,00,000 caused due to a fire or some other insured peril would produce a payment of only Rs. 50,000 from the insurer.

The rule related to a deductible clause is "the higher the deductible, the lower is the insurance premium for a loss exposure". This means increasing the deductible amount in the insurance policies leads to considerable savings in the premium. Businesses too stand to benefit from increasing the size of the deductible in their insurance policies. By doing so, they can achieve a savings in their insurance premiums. However, in the process, the deductible portion in the insurance must not be increased to such an extent that it becomes financially difficult for the individual or firm to bear the risk assumed.

### **Answer 5 (b)**

As per the common Law, the master is liable for the tortious acts of the servant provided the servant does such act in the course of his employment. The common law also recognizes the vicarious liability of the owner of the motor car. In the law of torts, if a person negligently drives his vehicle and causes injury or death to the third party, the driver whose negligence caused the damage is liable to the third party. The driver is the servant of the owner, and since he is a person of no means, the owner is liable for all his acts so far that he has done such acts in the course of his employment.

In the above case, based on the provisions of the common law, Gopal is held liable for the damage caused to the third party. [Pushpabai Sudershin v Ranjit G and P Co].

### **Question 6.**

- (a) How is the professional liability cover different from other liability covers?*
- (b) Is a doctor also equally liable for the negligence of his Assistant and Nurse?*
- (c) What is the protection assured under a Crime Insurance Policy?*
- (d) Differentiate between a Fidelity Bond and Crime Insurance?*

*(3 marks each)*

### **Answer. 6 (a)**

The professional liability insurance differs from other liability insurance policies in a few ways. These are as follows:

- i. While other liability insurance policies usually specify the per occurrence limit, (there is usually a maximum limit for each claim), there is no limit per occurrence in case of a professional liability policy Further, no distinction is made between bodily injury and property damage liability.

- ii. Professional liability insurance is not restricted to accidental acts, faulty diagnosis or faulty performance is also covered. Deliberate acts giving unintended results are also covered in the policy.
- iii. Professional liability policies usually cover the damage caused to the property in the custody or care of the insured as well.
- iv. Professional liability insurance does not allow the settlement of the claim without the prior approval of the insured

### **Answer 6 (b)**

The circumstances, applicable legislation, and the doctor's connection with the assistant and nurse will all play a role in determining whether a doctor is responsible for the actions of their assistant and nurse. Here are some crucial things to remember:

- i. Vicarious Liability: If the negligent conduct occurred while the assistant or nurse was performing their job duties, many jurisdictions will hold the doctor vicariously accountable for the negligence of those individuals. This means that the doctor may be held accountable for the assistant's or nurse's acts if they were performing their job obligations and acting under the doctor's direction or supervision when the negligence happened.
- ii. Standard of Care: Medical professionals have a responsibility to give their patients an acceptable quality of care. A doctor may be held accountable for their own negligence in the supervision or training of assistants and nurses if that failing to do so contributed to the negligence or harm that resulted.
- iii. Independent Contractors: The doctor's liability for the assistant's or nurse's carelessness may differ if they are independent contractors as opposed to employees. In general, doctors may not have as much direct control and oversight over independent contractors, and their accountability may be restricted to their own acts or omissions rather than those of the independent contractor.
- iv. Non-Delegable Duties: In some circumstances, such as when it comes to patient safety and specific medical treatments, doctors may have non-delegable responsibilities. Even if they were not actively involved or supervising at the time, non-delegable obligations ensure that the doctor cannot escape responsibility for the actions or inactions of their helpers and nurses. The doctor is still in charge of making sure the patient is given the right care and is safe.

### **Answer 6 (c)**

There are two types of financial protection that are available against the losses caused by crime. They are fidelity and surety bonds and burglary, robbery and theft insurance.

A bond is a legal instrument in which a third person (surety) ensures the performance of contract properly by the principal or the obligator. A fidelity bond deals with assurance of bonafide behavior by an employee during the course of his employment. In fidelity bond, the surety assures the employer of trust worthiness and honesty of the employee and agrees to pay the damages that arise due to the dishonest acts of that employee.

Money and security coverage pays for money and securities taken by burglary, robbery, theft, disappearance and destruction.

### **Answer 6 (d)**

A fidelity bond and crime insurance are both types of insurance coverage that protect against financial losses resulting from fraudulent or dishonest acts committed by employees or third parties. However, there are some differences between the two:

#### **Fidelity Bond:**

A fidelity bond, often referred to as an employee dishonesty bond or employee dishonesty insurance, is a type of insurance that guards against losses incurred by enterprises due to employee dishonesty. It usually compensates company losses brought on by employee theft, embezzlement, forgery, fraud, or other unethical behaviour. Employers typically buy fidelity bonds to protect themselves against monetary losses resulting from wrongdoing on the part of their workforce. Main characteristics fidelity bond's are:

Fidelity bonds explicitly cover damages brought on by an employee's dishonest behaviour, such as theft or embezzlement.

- i. Fidelity bonds typically demand the participation of an employee in order to activate coverage.
- ii. Customizable Coverage: Fidelity bonds can be made to fit a company's particular requirements, including coverage limitations, the kinds of dishonest acts that are covered, and the personnel or positions that are covered.

### **Crime Insurance:**

On the other hand, crime insurance is a broader category of insurance protection that guards against monetary losses brought on by a variety of illegal activities. It covers losses brought on by both third parties and employees, going beyond employee dishonesty. A wide range of criminal behaviours that could cause a firm financial harm are covered by crime insurance. Crime insurance's key characteristics are as follows:

- i. Coverage for Various Criminal activities: Losses brought on by employee dishonesty, forgery, theft, robbery, computer fraud, extortion, and other criminal activities are often covered by crime insurance.
- ii. Greater Coverage: Unlike fidelity bonds, crime insurance can also cover losses brought on by third parties, like customers, suppliers, or outside fraudsters.
- iii. Protection that is Complete: Crime insurance offers a more complete coverage option, addressing several criminal dangers that a firm may encounter.

## INTELLECTUAL PROPERTY RIGHTS – LAWS AND PRACTICES

### (Elective Paper 9.3)

Time allowed : 3 hours

Maximum marks : 100

**NOTE** : Answer **ALL** Questions.

#### Question 1.

**Read the following case study carefully and answer the questions given at the end:**

Care and Cure Limited was established in Hyderabad in 1998. It was a manufacturer, exporter and importer of drugs and pharmaceutical formulations such as anti-hypertensives, anti-fungals, anti-depressants, anti-obesity treatments, bulk drug intermediates, active pharmaceutical ingredients, pellets and granules. Apart from India, the company marketed pharmaceuticals to many countries including the United States, Canada, Germany, Spain and Sweden. Despite its global marketing reach, the company was relatively lesser known in India.

Saxagliptin is a dipeptidyl-1 peptidase-4 inhibitor used for lowering blood sugar levels in type 2 diabetes, a condition of high blood-sugar levels in the human body that occurred when the body did not produce or use enough insulin in the pancreas. Other comparable drugs are available in the Indian market and can be used for controlling blood sugar levels by inducing higher production of insulin in patients suffering from diabetes. Generic alternatives for comparable drugs are also available in the Indian market.

Bristol-Myers Squibb (BMS), a multinational company founded in the United States of America in 1858 developed the molecule that was used in Saxagliptin. BMS received the patent for Saxagliptin in India in 2007. AstraZeneca (AZ) another global company founded in Sweden, joined with BMS in 2007 to further develop the drug and commercialize its uses. During the codevelopment period AstraZeneca (AZ) bore the entire development cost. Subsequently in 2014, as a part of a broader diabetes market strategy, AZ acquired BMS's entire diabetes business, which gave AZ complete ownership of all the intellectual property rights of BMS's diabetes drugs, including Saxagliptin. This drug was marketed in stand-alone form under the brand name ONGLYZA and in combination with another active ingredient for enhanced diabetes management. Saxagliptin, in its stand-alone form, was available in the market at around ₹ 41 to ₹ 45 per tablet. Other comparable leptin drugs were also available in the market in the same price range, and generic alternatives for these leptin drugs were available in the market at a much lower rate.

In June, 2015, Care and Cure Limited filed an application for a compulsory licence with the Controller of Patents for manufacturing Saxagliptin. In its application, it presented several charges against AZ's business functioning and practices in India, including the following:

- (i) Inventions that went against public morality, which included inventions dangerous to human, animal, or plant life or detrimental to the environment.
- (ii) Medical methods used for the treatment of humans or animals; and
- (iii) Plants and animals (other than micro-organisms and biological processes) used for reproduction.

#### **INDIAN PHARMACEUTICAL INDUSTRY: PERFORMANCE, PRICING POLICY, AND PATENT REGIME.**

The India Pharma Market (IPM) was among the world's top three pharmaceutical markets in terms of volume and 14th largest in terms of value. It was projected to grow to 55 billion US dollars by 2020 due to India's rising population, improved affordability, accessibility and acceptability of modern medicines and new therapies. Generic drugs dominated the IPM, possessing a 70% market share in terms of revenue. Over-the-Counter (OTC) medicines contributed 21% of the total revenue, and the remaining 9% came from the patented drugs. India was also among the top six global pharmaceutical products in the world. Due to the low cost of production, India was also a leading exporter of pharmaceuticals and the largest exporter of generic drugs globally, exporting medicines to more than 200 countries.

Indian medicines had a dominant presence in the US pharmaceutical market. In the past few years, the US Food and Drugs Administration (USFDA) and the UK's Medicines and Healthcare Products Regulatory Agency had raised some doubts about the quality of medicines manufactured in India. The

IPM was a highly fragmented market with around 24,000 registered companies, of which 330 operated in the organised sector. The top 10 companies accounted for more than 40 per cent of the market share in India.

### **PRICING POLICY:**

The National Pharmaceutical Pricing Authority (NPPA) in India regulated the prices of all essential medicines, with the objective of making essential medicines available at an affordable cost and with assured quality. The essential medicines were those that took care of the health needs of the general public. There were 348 medicines in the National List of essential medicines in 2011. It covered just 17 percent of the total pharmaceutical market in India and did not contain several diabetes drugs including Saxagliptin, as well as certain drugs used in the treatment of tuberculosis, human immunodeficiency virus (HIV), and cancer. The ceiling prices of the medicines listed on the NPPA were fixed at a simple average price of all the branded or generic versions of all such medicines that had a market share of more than or equal to 1 per cent of the total market revenues for that medicine. Additionally, the manufacturers of medicines that were not under price control were allowed to increase the maximum retail price of those medicines only up to 10 per cent annually.

### **PATENT REGIME: PROCESS PATENT TO PRODUCT PATENT**

The Patents Act, 1970 governs the patent system in the country. Prior to a 2005 amendment, the Act granted “process patents” that allowed the manufacturers to patent their manufacturing method for a given product. The other manufacturers could not produce the product using the patented process although they could produce it using a different process of their own design. In the context of food and medicine, a process patent implied that the patent could be granted only for the process of manufacturing the substance rather than for the substance itself.

The pharmaceutical industry in India thrived under the process patent regime, as many drug manufacturers in India copied the drugs patented in other countries by inventing new processes of producing the same product. The competition among drug manufacturers drove down the medicines prices thus benefiting the consumers. It also helped Indian drug manufacturers to carve out a place for themselves in the international market, especially in poor countries. The process patent regime discouraged the domestic manufacturers from investing enough in research and development and discovering altogether new products. The process patent regime also resulted in the “ever-greening” of pharmaceutical patents whereby patent owners tried to extend the life of their patented products by inventing a slightly different process and acquiring another patent for what was basically the same product. The system also went against multinational companies that had spent millions of dollars to develop new products, and it also deterred them from investing in Indian companies.

Although Indian pharmaceutical manufacturing industry was thriving under the process patent regime, in order to comply with the WTO’s TRIPS Agreement, India was forced to amend the Patents Act, 1970. The amendments for the Act in 2005 recognized patented original drugs as products irrespective of the process used for manufacturing the same, and prevented domestic pharmaceutical companies from copying new drugs developed in other countries by designing new processes for manufacturing these products.

Indian technology and innovation companies welcomed the move to a new regime expecting that the new, stronger level of patent protection would encourage many multinational companies to tap into India’s relatively inexpensive workforce for product design, medicine development and clinical testing and also to invest large amounts in R & D in the domestic market, which would help India become more competitive in the global market.

But stronger patent protection also sparked debate that the new patent regime would create tough competition among domestic pharmaceutical companies. Since inventing a new product was more expensive than inventing a new process for producing an existing patented product, the general public feared that the new patent regime would drive up the cost of medicines and make them unaffordable to the masses. Critics also feared that new patent regime would dry up the supply of generic drugs in the international market thereby affecting the interests of poor countries. The proponents of product patent



regime set aside these fears by indicating that the generic drugs that were already patented under India's process patent regime could be sold on the payment of licence fees to the original patent holder.

To mitigate the public's apprehensions and fears, the proponents also referred to that provision of compulsory licencing in the WTO's TRIPS Agreement.

### **COMPULSORY LICENCING IN INDIA:**

The WTO included a provision for compulsory licensing in its TRIPS Agreement to safeguard the interests of the general public in developing and least-developed countries. This provision enabled the governments of these countries to grant a licence to domestic manufacturers to produce a patented drug without seeking the patent holder's consent. Instead domestic manufacturers in these countries were required to make appropriate compensation to the patent holder, as decided by the government or through negotiations with the patent holder.

Under the following situations, a generic drug manufacturer in India could apply for a compulsory licence any time after the expiration of three years from the grant of patent (a condition was not required under the TRIPS Agreement) upon payment of a reasonable royalty.

- (i) The patent-holding company was not able to make the patented invention available to the public.
- (ii) The patented invention was not made available at a reasonable price.
- (iii) There was a lack of working of the patented product within the territory of India.

The Patents Act, 1970 envisioned that the companies seeking a grant of a compulsory licence would consider doing so only as a last resort. Prior to seeking such a licence, the companies were expected to attempt to obtain a voluntary licence from the patentee. Once these attempts failed over a six-month period from the date of the initial request, the company could request patent-office intervention for the grant of a compulsory licence.

Natco Pharma Ltd. (NATCO), a generic drug manufacturer in Hyderabad, received the first compulsory licence in India in 2012 to produce and market Nexavar, a patented drug of a major multinational pharmaceutical company, Bayer Corporation. The compulsory licence was granted to NATCO as Bayer had not made the drug available on a large scale or at an affordable price within the stipulated period. The compulsory licence stipulated that the company would pay a 6 per cent royalty to Bayer from the sale of the generic drug Nexavar. On Bayer's appeal, the royalty rate was modified to 7 per cent.

The decision to grant a compulsory licence to NATCO spurred some controversy and speculation in India as well as abroad. It was felt that in a country where almost 90% of all pharmaceutical patents were imported, the decision to grant a compulsory licence to NATCO would spur applications for grant of compulsory licences by local manufacturers for other essential patented drugs that were excessively priced by the patentee companies. Analysts also contemplated that the exercise of the compulsory licensing provision in developing countries would force multinational pharmaceutical companies to adopt a differential pricing scheme for essential drugs, charging significantly lower prices in developing countries for these drugs.

The compulsory licensing decision disappointed multinational pharmaceutical companies. Certain large multinational pharmaceutical corporations overtly articulated their disapproval with India's compulsory licencing process. It was said that in spite of being a member of the WTO, India

had failed to interpret and apply its intellectual property laws in a manner consistent with recognized global standards. Some other corporations stated that compulsory licensing should be used only in exceptional circumstances such as in the times of a national health crisis. If used arbitrarily, compulsory licences will serve to undermine the innovative pharmaceutical industry and will be to the long-term detriment of the patient.

The second application for compulsory licence for manufacturing BMS's cancer drug Dasatinib came from XYZ Ltd. The patent office rejected the application of XYZ Ltd. citing that it failed to establish a prima facie case for receiving compulsory licence. Care and Cure Limited was the third company to apply for a compulsory licence.

One Chief Executive of an American pharmaceutical manufacturing corporation stated that medicine is for the people. It is not for the profits. The Patent controller's grant of a compulsory licence to Care and Cure Limited for Saxagliptin would certainly address the public welfare concern in India and it would also break the monopoly of multinational giants and spur competition within the domestic market. Frequent use of compulsory licences, however, would surely result in retaliation by the developed world.

Alternatively, a rejection of Care and Cure Limited's compulsory licence application would show the world that India placed supreme importance in the intellectual property laws laid out by the WTO and that India was willing to provide sufficient protection to the rights of innovators.

How should the patent controllers proceed? Should the compulsory licence application of Care and Cure Limited be rejected emphasizing international relations and compliance with multilateral agreements, inventions and innovations, or should the licence be granted to provide vital support for human life? The patent office is faced with this dilemma.

Questions:

(a) What is the difference between a "product patent" and a "process patent"? How will developing countries be affected if they adopt a product patent regime?

(b) What is compulsory licence? What is the economic rationale behind compulsory licensing? On what grounds has Care and Cure Limited applied for compulsory licence for Saxagliptin ?

(c) Should the patent office grant a compulsory licence to Care and Cure Limited? Justify your stand using an economic rationale.

(d) What strategic changes can multinational pharmaceutical companies make to their business processes in order to avoid the issue of compulsory licences for their patented drugs in developing countries?

(10 marks each)

### **Answer 1(a)**

A lot of investment and R&D is required for the creation of a new product. It is often possible to identify ingredients or elements used in the newly-created product by dismantling it. Once these elements are known, it is much less expensive to design or discover new processes to replicate the original product. The product patent provides protection to the inventor of the new product, whereas the process patent provides protection to the new process only. Product patents provide monopoly power to the inventor and limit competition. If developing countries implement a product patent regime, they can expect both negative and positive aspects.

#### *Negative Impact*

- i. A large proportion of the population in developing countries lives below poverty line. An exorbitant price for the patented products puts them out of reach.
- ii. Product patent requires affect the interest of local manufacturers ling units which replicate patented products by using different processes.
- iii. Developing countries lack financial resources to overcome resource constraint, they adopt a lax approach towards protecting intellectual capital.

#### *Positive Impact*

- i. Product patent regime encourages resources-rich MNCs to move their production base into developing countries where the cost of production is cheap.
- ii. Stronger protection regime and cheaper cost of production alone encourages MNC to investing R&D activities in the developing countries they enter.
- iii. Every availability of goods and services improves the level of expenditure.

- iv. Developing countries benefit from the larger variety of goods and services, a natural outcome of R&D.
- v. Developing countries can expect to receive higher amounts of investment if they implement a product patent system.

A product patent is an exclusive right awarded to the product's original developer. This implies that no other creator can make the same product using the same or any other similar process. The inference being that the maker will not face competition since the product is patented. As a result, there will be no other patent holders. And hence, the Product Patent system offers a greater amount of protection to the innovator.

*The patent is issued to the product's original creator under this system. A Product Patent has the following characteristics:*

1. When a product patent is granted, it means that no one other than the inventor may make the same product using the same or a similar technique.
2. A product patent gives the creator a "True Monopoly" right.
3. When compared to process patents, product patents are thought to provide a better level of protection.

A process patent, as the name suggests, is given to a specific method rather than the final product that is created as a consequence of that process. A process patent is issued for a specific manufacturing method rather than for the product itself. Any other creator can create the exact thing but by employing some other process by adjusting various parameters. Because of the potential of alternative production processes, we can infer that several producers for the same product can exist.

- The safeguarding is seen as a limited patent. This prohibits any other manufacturer from developing the same thing.
- A process patent offers the inventor a limited amount of protection. As a result, there's a good probability that competitors may reverse engineer the product.
- A single product might also have many method patents.

### **Answer 1(b)**

A compulsory license is a license granted by the government to a person or company for the manufacture or sale of a patented product without obtaining the consent of the patentee. Compulsory licensing under the Indian Patent Act is well codified and is in line with international agreements. The purpose behind granting a compulsory license is to maintain the working of patented inventions on a commercial scale in India so that the interest of any person working or developing an invention is not prejudiced.

Section 84 (1) of the Indian Patents Act, 1970, provides the objective behind compulsory licenses and requires that when granting the same, the general considerations enunciated in this section be focused upon. The Indian Patent Act imposes a duty on the patentee to work the patent in India. Under the Indian Patent Act, compulsory license can be granted after the expiration of a period of three years from the date on which the patent has been granted. The grounds include:

- The reasonable requirements of the public with respect to the patented invention have not been satisfied; or
- The patented invention is not available to the public at a reasonably affordable price; or
- Patented invention is not worked in the territory of India.

The provision of compulsory licensing must be used judiciously as it is an exception and flexibility to the general rule of patent. The provision falls mid-way; neither full patent protection is granted, nor is it denied altogether it directly affects innovation funding and unfettered use of this provision may result in global pharmaceutical companies being hesitant to introduce new medicines in other countries. Hence the companies have to fix the cost of their patented module according to the economic status of the country if they want to protect their product from compulsory licensing. Compulsory licensing has now become

the hope for financially challenged patients in underdeveloped countries. India needs this provision owing to the economic condition of the majority population. But the challenge is that on one hand, it has to comply with the international standards of patent protection and on the other, it has to safeguard public health.

#### *Economic Rationale*

A patent provides legal protection or exclusive rights to the patentee for the use, manufacture and sale of patented invention for a limited period of time. Compulsory licensing is a framework that contrasts monopoly strategies that damage public interest at large. Compulsory licensing infuses competition into the market and thereby reduces prices and monopoly profits. To protect the interests of the general public and the overall welfare of society, many governments.

*Care and Cure Ltd. applied for the compulsory licensing on the following grounds:*

- i. The product owner AZ is not able to make patented inventors accountable to Indian public as a whole.
- ii. AZ cannot make the patented drug Saxagliptin available at a reasonable price.
- iii. There is a lack of working or absence of production of Saxagliptin within the territory of India.

*The following points Care & Cure Ltd's claims for the compulsory license:*

- i) It has capacity to manufacture a million tablets a day.
- ii) It can apply the drug at around Rs 30- per tablet at Rs 11 less than the price charged by AZ.
- iii) It would manufacture the drug within the country.

*Points Against Care & Cure Ltd:*

- (i) generic substitutes are available in the Indian market for the Saxagliptin
- (ii) Price of Rs 30 per tablet for which Care & Cure Ltd is willing to supply the tablet is also unaffordable for the general public in India.
- (iii) manufacturing the patented drug in the Indian market is not essential for the grant of a compulsory license.

#### **Answer 1(c)**

*Arguments in favour of granting a compulsory license to Care & Cure Ltd by the patent office:*

- i) **Competition Argument** - It will enhance competition in the diabetes market which is likely to reduce the price of the essential drug.
- ii) **Welfare argument** - To make essential drugs available at an affordable price to the wider public living below poverty line is a welfare measure.
- iii) **Employment Argument** - Care & Cure Ltd will manufacture the drug rather than importing it. It will enhance employment opportunities in India.
- iv) **Balance of Payment Argument**- Manufacture of the drug in India will reduce the burden on Balance of Payments.
- v) **Policy Signal Argument**- The grant of compulsory license signal to the outside world that India cannot be exploited to achieve Capitalist pursuits of expansion and higher profit. The MNCs that are exploiting the Indian market should cater to the needs of the country apart from seeking their own profit-oriented pursuits.

*Points Against Grant of Compulsory License:*

- i) Diabetes is not a national emergency. Sugar levels in diabetic patients can even be brought under control through simple lifestyle change.

ii) Availability of generic substitutes which are sometimes cheaper than what Care & Cure Ltd is willing to charge.

iii) Setting a poor precedent as the company's claim is not very strong and it will encourage other companies to seek compulsory license on equally weak grounds.

iv) Putting India under the scanner of developed world for its anti-competitive practices.

After granting compulsory license to NATCO for Nexavor, India comes under priority watch list of the USA.

v) Weakening of patent protection requires feasting on no protection for the outcomes of their R&D efforts, MNCs would be discouraged from investing in R&D activities in India.

vi) Creation of a conducive environment for foreign investment.

Denying compulsory regime would give a signal to MNCs that India promotes an environment that is conducive to the inflow of foreign direct investment and portfolio investment in pharmaceutical companies.

vii) Compelling Care & Cure Ltd and other local manufacturers to invest in R&D of new drugs

Domestic manufacturers would be compelled to invest in R&D to create new drugs to achieve a competitive advantage in a fragmented drug market.

#### **Answer 1(d)**

*Strategies changes by MNCs (Multi-National Corporations) in their sourcing distributions, and pricing strategies:*

i) Assessment of Economic Environment before venturing into developing countries.

ii) Differential pricing in developing countries since they cannot afford expensive medicines.

To make their products affordable in developing markets, they could supply their drugs at cheaper rates. At the same time to cover their production costs, they could charge a higher price for the same drug in developed countries.

iii) Dynamic Pricing- A patents can charge higher prices for the patentee drug from a few years after the receipt of the patent but could reduce the price of the patented drug as soon as the threat of compulsory license surfaces.

iv) Domestic production of patented drugs usually production costs are cheaper in developing countries. After inventing new drugs in the developed market MNCs can shift their manufacturing base for patented drugs to developing countries.

v) Corporate Social Responsibility- MNCs operating in developing countries can use a portion of their income for carry out CSR initiatives. Doing so will create improvements in the social environment in which they are operating as also create goodwill in favour of the company itself.

vi) Strategic partnership in developing countries- While expanding their business in developing countries, MNCs, can look for collaborations, partnerships and mergers and amalgamations and acquisitions. They can acquire or merge with domestic companies that have the expertise to replicate their medicines through reverse engineering or inventing new projects or one that have capability MNC's summer.

vii) R&D in developing countries

viii) Utilisation of economies of scale since a large market exists in developing countries.

ix) Voluntary license before applying for a compulsory license

x) Continuous inventions & innovations of new drugs

## Question 2

ABC Ltd. is a global automobile manufacturing company having headquarters in Japan. In 1990, it launched a hybrid model car with the name PRIUS which got trademark registrations in various countries. It started selling in USA and Europe in 2001 and 2002.

M/s Pious Auto Industries Ltd. used to manufacture spare parts and accessories for cars in India since 2001 and got the trademark registered in 2002.

In 2009 ABC Ltd. started promoting its PRIUS vehicle in India and launched the PRIUS in the year 2010.

When ABC Ltd. discovered the fact that M/s Pious Auto Industries Ltd. has been using the mark "PRIUS" for autoparts and accessories, it approached the Trade Marks Registry for cancellation of the trademark and also brought a suit for infringement against the company, on the ground of claiming of passing off of its famous mark which led to an unfair advantage of their reputation and goodwill in the market.

ABC Ltd. contended that various advertisements and news reports about the trademark in India and across the globe have made PRIUS a well-known trademark. These promotional tools are sufficient to establish reputation and goodwill within a particular geographical area. Since 1997, 'PRIUS' was widely publicised and advertised in leading newspapers.

It added that the mark PRIUS was a well-known mark under section 2(1) (zg) read with sections 11(6) and 11(a) of the Trade Marks Act, 1999 as the mark PRIUS had acquired a great deal of goodwill in several other jurisdictions in the world much prior to Prius Auto's use and registration in India.

M/s Pious Auto Industries highlighted the principle of territorial jurisdiction over universality principle. It also referred to the judgement of Starbucks vs. British Sky Broadcasting, wherein the court had held.

"No trader can complain of passing off as against him in any territory ..... in which he has no customers, nobody who is in trade relation with him."

M/s Pious Auto further contended that to establish goodwill and reputation in a particular jurisdiction, one has to show adequate evidence that he has acquired a substantial goodwill in India for its mark. Further, prior use of trade mark in one jurisdiction would not ipso facto entitle its owner or user to claim exclusive rights to the said trade mark in other jurisdiction.

Questions :

(a) Whether, using the mark PRIUS by M/s Pious Auto Industries Ltd. to market automobile parts manufactured by it amounts to infringement of reputation of ABC Ltd. in the market ?

(b) Whether M/s Pious Auto Industries Ltd. is guilty of passing off its products as those of ABC Ltd.? Give reasons and case law, if any in support of your answer.

(6+6=12 marks)

## Answer 2(a)

In *Toyota Jidosha Kabushiki Kaisha v M/S Prius Auto Industries Ltd. SC Civil Appeals No. 5375-7707 2017 of 2017*, Supreme Court observed that trademarks that have created a reputation in India in relation to any promotional instruments may be protected under trademark law but substantial evidence is required to show that the claimant has done so. Advertisements and articles in print media alone would not be enough to establish a trans-border reputation if they did not have an impact on the Indian population at large.

The advertisements, even if accepted, will not be a safe barn to hold the existence of the necessary goodwill and reputation in India in 2001. There is no advertisement of the product in India prior to April, 2001. The brand name of the car Prius had not acquired the degree of goodwill, reputation and the market or popularity in the Indian market. So as lost in the company the necessary attributes of the right of a prior user so as to successfully maintain an action for passing off even against the registered user.

Toyota's delayed approach to the courts has remained unexplained. Such delay cannot be allowed to work to the Prejudice of Prius Auto Industries Ltd who had kept using the trademark (registered) to market its goods during the Inadvertently long period of silence maintained by Toyota.

It held that there has been no infringement of reputation by Prius Auto Industries Ltd.

### **Answer 2(b)**

The principle of passing off, i.e., “Nobody has the right to represent his goods as the goods of somebody else” was decided in the case of *Perry v Truefitt (1842)*. The passing off law has changed over time. Previously it was restricted to depicting one person’s goods as another. Later it was extended to trade and services. This was later expanded to business and non-business activities. Now, it applies to many forms of unfair trade and unfair competition where one person’s activities harm the goodwill associated with the activities of another person or group of individuals.

The problem is based on Supreme Court judgement in *Toyota Jidosha Kabushoki Kaisha vs M/S Prius Auto Industries Ltd Civil Appeal No. 5375-7707 of 2017*. The Supreme Court accepted Prius Auto Industries Ltd’s arguments on Territorial Principle and stated that there needs to be substantial evidence to show that a mark has acquired a huge goodwill in India even if it already has acquired a huge goodwill in the jurisdictions. Also, the importance of having customers within a particular jurisdiction from a brand specific perspective was a key factor for establishing goodwill within that jurisdiction. The Supreme Court held in order successfully continue action for passing off, there must be a spillover of worldwide reputation and goodwill into Indian markets.

Prius has undoubtedly acquired a great deal of goodwill in other jurisdictions and that too much earlier than by Toyota. The Supreme Court held that there has not been any passing off by Prius Auto Industries Ltd.

### **Question 3**

(a) “Over the past fifteen years, intellectual property rights have grown to a stature from where it plays a major role in the development of global economy.” In the light of this statement, prepare a brief note on recent developments that have taken place in the regulatory regime of intellectual property in India.

(b) “Patent information is more than just technological or legal information.” In the light of this statement, enumerate the practical applications of patent information.

(6 marks each)

### **Answer 3 (a)**

Following the conclusion of the TRIPS Agreement, much has been written on the potential costs and benefits of stronger Intellectual Property Rights (IPRs) protection in terms of growth and technology transfer, particularly for developing countries. It is to be noted that the countries operating at different stages of development must use the flexibilities in the TRIPS Agreement to maximize its net benefits for their development. While stronger IPR protection in the poorest countries is not likely to lead to substantial benefits in terms of innovation or technology diffusion, the administrative cost of developing a patent system and the enforcement of TRIPS, along with the potential abuses of market power in small closed markets suggests that such countries could lose out from TRIPS.

Stronger IPR protection in the poorest countries may also inhibit or lengthen the imitative stage of development that seems to be necessary in order to develop innovative capacity in many industries. Policies aimed at improving the business environment and encouraging imports of technology embodied in goods could potentially reduce such costs, though their impact on other development-related goals needs to be carefully weighed.

However, there are other key developments which has taken place in the IPR regime over the period of time mentioned below:

(i) The Design Act, 2000 now has been enacted specially to protect individual designs and to encourage design activity to promote the design element in the article of production.

(ii) In after to comprehensive legislation in registration and for providing adequate protection for geographical indications, Geographical Indications of Goods (Registration and Protection) Act, 1999 has been passed.

(iii) Trade secrets are protected without registration. It can be protected for any period of time but a substantial element of secrecy must exist.

There are various enactments which seeks to protect trade secrets.

(iv) In order to provide for the establishment of an effective legal system of the protection of plant varieties, the rights of farmers and plant breeders and to encourage the developments of new varieties of plants, the protection of plants varieties and Farmer's rights Act 2001 has been enacted

(v) With the advancement of information technology, Semi-Conductor Integrated Circuits, Layout Design Act has been passed.

(vi) Copyright Act, 1957 has been amended in 2012 which contains

- a) Amendments to rights in artistic works, cinematograph films and sound recordings.
- b) WCT and WPPT related amendment to rights.
- c) Author friendly amendments on mode of assignments and Licences.
- d) Amendments facilitating access to work
- e) Strengthening enforcement and protecting against Internet piracy
- f) Restore of Copyright Board.

vii) Trade Mark Act, 1999 has been enacted replacing the Trade Mark Act, 1958 to make it harmonies with the Paris Convention for Protection of Industrial property and TRIPS Agreement.

viii) The patents act 1970 has been amended in 2002 pursuant to TRIPS Agreement.

### **Answer 3(b)**

A patent is an exclusive right granted for an invention, which is a product or a process that provides, in general, a new way of doing something, or offers a new technical solution to a problem. To get a patent, technical information about the invention must be disclosed to the public in a patent application. Patents are not just abstract concepts; they play an invaluable, practical role in everyday life. By rewarding ideas, patents encourage the development of innovations and new technologies in every field.

Patent information is the name we give to the technical information you find in patent documents, plus legal and business-relevant information about them. Patent documents consist of

- **a first page** comprising basic information, such as the title of the invention and the name of the inventor
- **a detailed description of the invention** indicating how it is constructed, how it is used and what benefits it offers compared with what already exists
- **drawings**
- **claims** containing a clear and concise definition of what the patent legally protects

Patent documents contain information which can be vital to a broad variety of professions. These range from technical developers and researchers to legal advisers and business strategy managers.

It is rightly states that Patent information is more than first technological or legal information. It includes not only the content of published patent documents but also bibliographic and that information concerning patents for inventions, investor certificates, utility certificates and utility models.

*Some practical applications of patents information include:*

i) Tool for creative thinking

Patent information provides a source of technological information that can be used by researchers and inventors to find new solutions to technical problems.

ii) Input for licensing strategy



Analysis of patent information provides valuable technical and business information regarding target or key technology.

iii) Supporting mergers and acquisitions

Once one or more potential target technologies/companies are identified, then the company can undertake additional patent analysis to narrow down its choices to decide which of the companies the best merger or acquisition target is .

iv) Guiding management of research and development

Knowing the life cycle of a technology makes it possible to judge the timing of development policy and focus on certain development themes.

v) Human Resource Management

Brain maps can identify star inventions within a company and key inventors in the companies.

vi) Well organized information for easier search and retrieval of patent documents, they are classified in accordance with an internationally accepted classification system called the International Patent Classification (IPC).

#### **Question 4**

(a) Ushodaya Enterprises Ltd. is engaged in the business of publishing a newspaper in Telugu called Eenadu. The company is in the business of publishing a newspaper, broadcasting, financing and developing a film city. Its products and services are corelated, identified and associated with the word Eenadu in the entire State of Andhra Pradesh. Its trade mark Eenadu has acquired reputation and goodwill in the entire state.

S.V. Venugopal is the sole proprietor of a firm carrying on business inter alia as manufacturers of and dealers in incense sticks in the name and style of ASHIKA Incense Incorporated at Bangalore and adopted the mark ASHIKA's Eenadu. S.V. Venugopal states that the word Eenadu in Kannada language means 'this land'. In Malayalam and Tamil language, it conveys the same meaning. In Telugu, it means 'today'. In consonance with the above meaning, he has devised an artistic label comprising

a rectangular carton in bottle green background with sky blue border and in the centre in an oval tricolour, the word 'Eenadu' is written. He started using the name 'Eenadu' for his incense sticks and used the same artistic script, font and method of writing as that of Ushodaya Enterprises Ltd.

Ushodaya Enterprises Ltd. has instituted a suit for infringement of copyrights and passing off trade mark against S.V. Venugopal. Will the company succeed? Give cogent reasons in support of your answer.

*(6 marks)*

(b) In Sept. 1990, XYZ Pvt. Ltd. started manufacture of Cetadine Microbicidal solution consisting of a Providone Iodine combination which is being marketed in pack sizes of 100 ml and 500 ml bottles under the trademark CETADINE. It has been extensively advertised by the company.

The bottles bear distinctive labels having distinct colour combination, layout and get up which qualify as original artistic work within section 2(c) of Copyright Act, 1957 and is registered with the Registrar.

R. Pharma Works manufactures microbicidal solutions in bottles with a label having an identical and/or substantially similar get up, layout and colour scheme as that of XYZ Pvt. Ltd. Its bottles contain the name Povidone Iodine Solution.

XYZ Pvt. Ltd. instituted a suit against R. Pharma Works for infringement and consequent damages. What are the defences that R. Pharma Works can plead in his favour? Will XYZ Pvt. Ltd. succeed?

*(6 marks)*

#### **Answer 4(a)**

In the case of *S.V Venugopal vs Ushodaya Enterprises Ltd. and another SC Appeal No. 6314-15, 2001*. Supreme Court held that:

- i) Ushodaya Enterprises Ltd. mark "Eenadu" had acquired extraordinary reputation and goodwill in the State of Andhra Pradesh.
- ii) S.V Venugopal cannot be referred or termed as an honest concurrent user of the mark "Eenadu".
- iii) S.V Venugopal has clearly wanted to ride on the reputation and goodwill of Ushodaya Enterprises Ltd.
- iv) Permitting S.V Venugopal to sell his product in Andhra Pradesh would amount to encouraging him to practice fraud on the consumers.
- v) S.V Venugopal's deliberate misrepresentation has the potentiality of creating serious confusion and deception for the public at large and the consumers here to be saved from such fraudulent and deceitful conduct.
- vi) Permitting him to sell his product with the mark Eenadu would be encroaching on the reputation and goodwill of Ushodaya Enterprises Ltd and this would constitute invasion of proprietary rights vested with the company.

As can be clearly seen from the judgment, the Court has clearly ruled on the basis of dilution of the trademark "Eenadu" registered to the respondent. A trademark is diluted when its uniqueness is lost owing to its unauthorised use in relation to products that are not identical or similar to the product of the trademark owner.

In this context it must be noted that dilution was not pleaded by the respondent in the first place. Dilution was incorporated (which was previously dominated the likelihood of confusion test) into the Trade Mark Act, 1999 via Sections 11(4) and 29(4).

The present case is clearly under the Trade Mark Act 1958 as the 1999 Act came into force with effect from 2003. This was also contended by the Respondents. Dilution of trademark essentially happens in relation to an extremely well-known mark. In relation to lesser known yet identifiable brands, the test of likelihood of confusion applies. The decision demonstrates that third parties will not be allowed to take undue advantage of trademarks that enjoy a high degree of goodwill and reputation in a particular region. The Supreme Court's ruling will enable the owner of such trademarks to prevent others from using similar marks for different of goods or services to obtain an unfair economic advantage.

#### **Answer 4(b)**

Section 2(c) of the Copyright Act defines "artistic work" as,

- a painting, a sculpture, a drawing (including a diagram, map, chart or plan), an engraving or a photograph, whether or not any such work possesses artistic quality;
- a work of architecture; and"
- any other work of artistic craftsmanship;

Therefore, to qualify as an artistic work, the work need not possess high quality of art. A work can be artistic even with *de minimus* artistic quality. However, the work must be an original expression of thought i.e. the work must have "originality" to qualify as an artistic work under the Copyright Act. The expression in the work should be the result of application of skill and judgement on the part of the artist creating the work, that is, the artist must have applied more than some mere mechanical exercise in order to create the work.

Delhi High Court in the case of, *Marico Ltd vs. Mrs. Jagit Kaur*, has allowed the rectification application of Marico Ltd (hereinafter referred to as the "Appellant") holding that the artistic work for the label of Mrs. Jagit Kaur (hereinafter referred to as the "Respondent") "NIHAL UTTAM" is not an original work under section 13 of The Copyrights Act, 1957. It was held that the Respondent's said label is a substantial reproduction and a colorable imitation of the Appellant's "NIHAR COCONUT OIL".

Adoption of identical and/or substantially similar setup, layout and color combination on its Providone Iodine Solution by K. Pharma works on its bottles would amount to infringement and consequent damages.

In the present case, it amounts the infringement of copyright which vests with XYZ Pvt. Ltd. The act and conduct of R.Pharma works would amount to passing off.

### Question 5

(a) Discuss the nature and scope of infringement of a copyright in the judicial pronouncements of the Apex Court in the matters of Copyright Act, 1957.

(6 marks)

(b) For a design to be called new or original under the Designs Act, 2000.

(i) There should be some original mental application involved; and

(ii) The design must be significantly distinguishable from known designs or combination of designs. Discuss and refer to decided case law, if any.

(3+3=6 marks)

### Answer 5(a)

The fabrication of a form of intellectual property work without the authorization of the copyright holders is known as a copyright infringement cases. Copyright violation occurs when a 3rd party violates the copyright owner's rights, like individual ownership of work for a specific period. Music and films are well-known entertainment products subject to severe copyright infringement. Violation lawsuits might result in future liabilities or funds set aside in the event of a lawsuit. Thus, copyright infringement means the unauthorised use of someone's copyrighted work for a profit. It results in the infringement of certain rights of the copyright holder, such as the right to distribute, reproduce, perform or display the protected work.

Primary infringement occurs when there is an actual act of copying, while secondary infringement occurs when unauthorised dealings take place, such as selling or importing pirated books, etc. In the case of secondary infringement, the infringer will know about infringement, while in the case of primary infringement, the infringer may or may not know about infringement.

The following elements should be present for copyright infringement:

- The copyrighted work is the original creation of the author
- The copyright infringement work is actually copied from the work of the author

The judicial pronouncements of the Apex Court would be in the public domain and its reproduction and publication would not infringe the copyright. The principle where there is common source, the person relying on it must prove that he actually went to the common source from where he borrowed the material employing his own skill, labour and brain and he didn't copy, would not apply to the judgments of the courts because there is no copyright in the judgments of the court, unless so made by the Court itself.

To secure a copyright for the judgments delivered by the Court, it is necessary that the labour, skill and capital invested should be sufficient to communicate or impart to the judgment printed in Supreme Court Cases some quality or character which the original judgment does not possess and which differentiates the original judgment from the printed one.

### Answer 5 (b)(i)

The Designs Act, 2000 incorporates the concept of '*absolute novelty*'. In simple language, absolute novelty means that an invention is new if it has not been used or published anywhere in the world. The concept of absolute novelty aids in judging a novelty on the basis of prior publications of any article.

For a design to be called new or original, there should be some original mental application involved. The novelty or originality of even a particular part of the article may be sufficient to call the design "novel or

original”, but this part must be a significant one and it must be potent enough to impart to the whole design a distinct identity.

In *Pental Kabushiki Kaisha & Anr. V. M/s Arora Stationers & Others*, the Court held that a mere superficial difference in the design will not make the article new or original.

It is pertinent to point out that only a unique design which is novel and original can be registered. However, a combination of two or more previously published designs can be registered only if the combination produces new visuals or designs. In *Hello Mineral Water Pvt. Ltd. vs Thermoking California Pure (1999)*, the dispute was concerning a water dispenser which was designed in a cylindrical shape. Delhi High Court held that mere form or shape is not sufficient for the purpose of novelty. The ultimate test is to consider the design with an instructed eye to locate the difference between the design previously published and the registered design. In *B.Chawla & Sons vs Bright Auto Industries (1980)*, the Delhi High Court observed that only slight differences existed between the two impugned designs presented before it. The Court further held that minor addition or alteration in shape which is a well-recognized shape of another product that exists in the market cannot provide such design the status of a new and novel design.

### **Answer 5(b)(ii)**

The design must be significantly distinguishing from known designs, or combination of designs. What constitutes as “substantial novelty or substantial originality” is left to the interpretation of the design’s office/courts.

In the case of *Simmons v Mathieson & Cold*, the court held that there must be a mental conception expressed in a physical form which has not existed before, but has originated in the constructive brain of its proprietor and that must not be in a trivial or infinitesimal degree, but in a substantial degree.

### **Question 6**

(a) India is among first countries in the world to have passed legislation granting farmers’ rights. Write an exhaustive note on the provisions contained in The Protection of Plant Varieties and Farmers’ Rights Act, 2001 regarding farmers’ rights.

(6 marks)

(b) There is no substantive authoritative separate statute to deal with trade secrets. How are, then, trade secrets (a form of intellectual property) sought to be protected in India?

(6 marks)

### **Answer 6(a)**

In order to provide for the establishment of an effective system for the protection of plant varieties, the rights of farmers and plant breeders and to encourage the development of new varieties of plants it has been considered necessary to recognize and to protect the rights of the farmers in respect of their contributions made at any time in conserving, improving and making available plant genetic resources for the development of new plant varieties, the Govt. of India enacted “The Protection of Plant Varieties and Farmers’ Rights (PPV&FR) Act, 2001” adopting sui generis system. Indian legislation is not only in conformity with International Union for the Protection of New Varieties of Plants (UPOV), 1978, but also have sufficient provisions to protect the interests of public sector breeding institutions and the farmers. The legislation recognizes the contributions of both commercial plant breeders and farmers in plant breeding activity and also provides to implement TRIPs in a way that supports the specific socio-economic interests of all the stakeholders including private, public sectors and research institutions, as well as resource-constrained farmers. India is among the first countries in the world to have passed legislation granting farmers’ rights.

Section 39 deal with farmers’ rights. It states that:

(1) - A farmer who has bred or developed a new variety shall be entitled for registration and other protection in like manner as a breeder of a variety.

(2) Farmers' variety shall be applied for registration if application contains declaration as Specifically in clause (A) of sub-section (1) of Section 18. A;

(3) A farmer who is engaged in the conservation of genetic resources of land and races wild relatives of economic plants and other improvements through selection and preservation shall be entitled for registration and reward from the gene fund.

(4) A farmer shall be deemed to be entitled to save, use, sow and re-sow exchange, share or sell his farm produce including seed of a variety.

Section 42 - Protection of innocent infringement

Section 43 - Authorisation of farmer's variety

The Protection of Plant Varieties and Farmers' Rights Act is a successful sui generis framework creating harmony between plant reproducers' privileges alongside ranchers' privileges and specialists' privileges. The act of little, minimal ranchers to trade the gathered material with others is fundamental for their work and rehearsals to a vast extent both in India and the major part of Asia-Pacific's creative nations. All endeavors are being made by The Protection of Plant Varieties and Farmers' Rights Act, Authority to actualize various arrangements of The Protection of Plant Varieties and Farmers' Rights Act and furthermore to make the accessibility of value seeds of enlisted assortments yet, in addition, to help ranch families for preservation and reasonable utilization of hereditary assets remembering for situ and ex-situ assortments and for reinforcing the ability of the partners in completing such protection and feasible use.

### **Answer 6(b)**

Trade secret law safeguards technological and commercial information that is not commonly recognized in the trade and prevents others from commercially exploiting it without authorization. The purpose of trade secrets protection is to promote research and development by protecting the source of business information and to uphold proper business ethics. A trade secret, or confidential information in the trade, must contain secret information that no one else knows about, it must have commercial value, and reasonable measures must be taken to safeguard the secret. A formula, pattern, compilation programme device, method, or technique that derives independent economic value from not being known can be recognised as a trade secret. Hence, trade secrets can be understood as Intellectual Property rights on confidential information which may be sold or licensed.

These are the following legislation which have a connection with trade secret:

- i. The Indian Contract Act, 1872
- ii. The Indian Penal Code

The Indian non-disclosure agreement (NDA) or Confidentiality Agreement (CA) - such agreement is signed first before signing of any commercial agreement of substance involving critical business relations for development of design of products, or for mass production on contract basis.

These basic agreements for protection of trade secrets are covered under the

- i. Indian Contract Act, 1872 (Sections 27)
- ii. The Indian Penal Code (Sections 408, 415)
- iii. The Copyright Act, 1957 (Section 51, 55, 63)
- iv. The Design Act, 2000
- v. The Information Technology Act, 2000 (Section 65-72)
- vi. The Competition Act, 2002 (Section 3)
- vii. The Civil Procedure Code, 1973

Misappropriation of trade secret can be understood as discovery of trade secret by improper methods, which is not covered by any specific law. Therefore, the common cause of action against misappropriation or unauthorized disclosure of trade secrets includes civil action for breach of contract and wrongdoing due to misappropriation; and criminal action for theft and breach of trust.

In India, there is no uniform legislation protecting trade secrets and confidential information. It is protected by numerous, disparate provisions of various statutes. Indian courts have recognized trade secret protection based on equity principles and common law remedies for breach of confidence and breach of contract such as Section 27 of the Contract Act, 1872, which states that, covenants shall be structured in such a way that they protect the firm's confidentiality while also allowing the employee to work in his preferred profession. Businesses have trade secrets that must be protected, which is why it is necessary to include a restrictive clause in service contracts to ensure that the firm's trade secrets are adequately secured.

In the case of *Richard Brady v. Chemical Process Equipment Pvt. Ltd.* , the Delhi High Court went farther by invoking a broader equitable jurisdiction and awarding an injunction in the absence of a contract. Non-compete covenants, non-solicitation covenants, non-poaching covenants, and confidentiality covenants are all examples of restrictive covenants. The courts have recognized client information kept in databases as copyrightable material under the Copyright Act, 1957, implying indirectly to protection of trade secrets and confidential information from disclosure/infringement.

India also requires formal legislation along the lines of the UTSA (Union Trade Secret Act) to deter the illegal transfer of trade secrets by individuals who has access to them as part of their employment responsibilities. These steps, in conjunction with provisions relating to breach of contract or Non-Disclosure Agreements, can help promote a culture of respect in industrial circles for trade secrets and undisclosed information as proprietary assets belonging to their owners. Without specific legislation, this is likely an area in which India falls short in its defence of intellectual property rights.

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## LABOUR LAWS & PRACTICE

### (Elective Paper 9.4)

Time allowed : 3 hours

Maximum marks : 100

**NOTE :** Answer **ALL** Questions

#### Question 1.

##### Case Study:

Twelve respondents instituted a civil suit before the Senior Sub-Judge against the employer's action of their termination and retrenchment from service. The reliefs they claimed in the suit consists in the:

(a) Declaration to the effect that the orders of their termination or retrenchment from service were illegal, and

(b) Entitlement against the retrenchment with back wages. It was pleaded that the plaintiffs-respondents were skilled workers working in a hydel project in Alandpur in various capacities such as T. Mate, Mixer Operator, Beldar etc. for more than 5 years and therefore as per the standing orders and the rules, they were regular employees of the defendants. It was alleged that the defendant- appellants did not maintain any seniority list of the workers and different categories of services on the said project and they arbitrarily removed the plaintiffs-respondents from service by obtaining their signatures on papers under coercion and force and also forcing them to accept payments.

It was further alleged that the defendant-appellants while removing plaintiffs-respondents did not comply with seniority criteria. As a result, juniors were retained in service and seniors were retrenched. It was alleged that the action was discriminatory and contrary to law resulting in victimization. This claim of the plaintiffs-respondents was contested by the defendant-appellants on the grounds that common suit could not have been filed since the cause of action of each defendant was distinct and separate; the plaintiffs-respondents were appointed on purely temporary basis and after the completion of the project, their services were validly terminated. On the contrary, the plaintiffs-respondents claimed injunction and reinstatement. On the diligent perusal of the above case, answer the following questions referring to legal provisions and decided case law, if any:

(a) Whether the orders of termination by the way of retrenchment of the plaintiffs-respondents are illegal and ineffective?

(b) Do you agree that the suit is bad for misjoinder of parties? State reasons.

(c) Whether plaintiffs-respondents are entitled to declaration and injunction? (d) The retrenchment should be bona fide and there should not be victimisation or unfair labour practice on the part of employer. Explain what acts of the employer would not constitute retrenchment under the Industrial Disputes Act, 1947.

(e) In case retrenchment is proved to be illegal or ultra vires, explain reliefs available to the plaintiffs-respondents under the Industrial Disputes Act, 1947.

(8 marks each)

#### Answer 1(a)

According to Section 25G of the Industrial Dispute Act, 1947, where any workman in an industrial establishment, who is a citizen of India, is to be retrenched and he belongs to a particular category of workmen in that establishment, in the absence of any agreement between the employer and the workman in this behalf, the employer shall ordinarily retrench the workman who was the last person to be employed

in that category, unless for reasons to be recorded the employer retrenches any other workman. It is clear that the retrenchment must be based on the principle last come first go. Further, as per Rule 77 of the Industrial Dispute (Central) Rules, 1957, it is the obligation of the employer to prepare the list of all workmen in the particular category from which the retrenchment is contemplated. The seniority list must be pasted on the notice board at least 7 days before the date of actual retrenchment.

The facts of the case are similar to ***Chief Engineer, Hydel Project vs. Ravinder Nath & Ors. held on 24 January, 2008***. The defendant-appellants while terminating the service of 12 respondents did not observe the principle (procedure) for retrenchment of workmen as per Section 25G of Industrial Dispute Act, 1947. In an industrial establishment, there may be different categories of workmen depending upon the duration and nature of their service. These may be category of persons who have completed 1 year of continuous service or might be another category not having completed continuous service of one year.

The defendant-appellants did not observe the aforesaid principle while terminating their services and hence conditions precedent for valid retrenchment have not been complied with the termination of 12 plaintiffs-respondents, were held illegal and ineffective.

#### **Answer 1(b)**

Regarding the issue of misjoinder of parties, where in a suit, there are two or more defendants and two or more cause of action, the suit will be bad for misjoinder of parties. In the given case, the defendant-appellants firstly urged that the common suit was bad since the cause of action of each of them was distinct and separate. It was urged that the plaintiffs-respondents were appointed on purely temporary basis as work-charged employees and after the completion of the project, their services were validly terminated.

But plaintiffs-respondents pleaded that they were skilled workers and working in the various capacities in a hydel project in Alandpur for more than 5 years and therefore as per the standing orders and the rules, they were regular employees of the defendants. Nature of work or the skill level may vary but the cause of action remains the same and not at all separate. As a result, on the ground of misjoinder of parties, the suit cannot be held to be bad.

Though, it may be bad since mechanism for adjunction of disputes have been provided under the Industrial Disputes Act, 1947 and jurisdiction of civil courts is barred but not bad because of misjoinder of parties.

#### **Answer 1(c)**

According to Section 2A of the Industrial Disputes, Act, 1947, where any employer retrenches, or otherwise terminates the services of an individual workman, any dispute or difference between that workman and his employer connected with, or arising out of, such discharge, dismissal, retrenchment or termination shall be deemed to be an industrial dispute notwithstanding that no other workman nor any union of workmen is a party to the dispute.

In the case of ***The Premier Automobiles Ltd. & Ors. vs. Kamlekar Shantaram Wadke of Bombay & Ors. [(1976) 1 SCC 496]***, the court culled out following four principles:

1. If the dispute is neither an individual dispute, nor it relates to enforcement of any other right under the Industrial Disputes, Act, 1947, the remedy lies only in the civil court.



2. If the dispute is an industrial dispute arising out of a right or liability under the general or common law and not under the Act, the jurisdiction of the civil court is alternative, leaving it to the election of the senior concerned to choose his remedy for the relief which is competent to be granted in a particular remedy.
3. If the industrial dispute relates to the enforcement of a right or an obligation created under the Industrial Disputes, Act, 1947 then the only remedy available to the suiter is to get the adjudication under the Industrial Disputes, Act, 1947.
4. If the right which is sought to be enforced is a right created under the Act such as Chapter VA then the remedy for its enforcement is either Section 33C or the raising of an industrial dispute, as the case may be

Since the relief claimed for reinstatement with back wages hence, this could only be available to plaintiffs-respondents under the Industrial Dispute Act, 1947. The civil courts jurisdiction was barred and therefore they are not entitled to declaration and injunction.

#### **Answer 1(d)**

In the case of ***Workmen of Subong Tea Estate vs. The Outgoing Management of Subong Tea Estate, (1964) 5 S.C.R. 602; A.I.R. 1967 S.C. 420***, the Court laid down that the management can retrench its employees only for proper reasons, which means that it must not be actuated by any motive of victimisation or any unfair labour practice.

The employer has to execute retrenchment in accordance with Section 25F of the Industrial Disputes Act, 1947. This section states that a workman employed in any industry working continuously for at least 1 year cannot be retrenched unless the following conditions are fulfilled:

- The workman has been served a notice of 1 month in writing that states the reasons for retrenchment or the workman has been paid in lieu of such notice, wages for the notice period.
- The workman is paid compensation equivalent to the average pay of 15 days' for every completed year of continuous service. The period of 6 months or more is considered equivalent to a year for calculation of retrenchment compensation.
- Notice in the prescribed manner is served on the appropriate Government.

According to Section 25N of the Industrial Disputes Act, 1947, an industrial establishment which employs 100 employees or more, has to fulfill certain additional conditions for retrenchment of the workman. The section states that a workman employed in any industry working continuously for at least 1 year cannot be retrenched unless the following conditions are fulfilled: -

- The workman has been served a notice of 3 months in writing that states the reasons for retrenchment or the workman employee has been paid in lieu of such notice, wages for the notice period.
- The prior permission of the appropriate Government or such authority as may be specified by that Government by notification in the Official Gazette has been obtained on an application made in this behalf.

Section 25G of the Industrial Disputes Act lays down the procedure of retrenchment, which states that an employer can terminate the employment of the last workman hired, by way of retrenchment. If any other employee is retrenched, then the employer has to specify the reason for doing so. For this, the employer is required to maintain a seniority list of its employees.

In absence of any of the abovementioned acts of the employer, the retrenchment would not be constituted under the Industrial Dispute Act, 1947.

### Answer 1(e)

In the case of '*Bharat Sanchar Nigam Limited v. Bhuruma*', the Court held that the ordinary principle of grant of reinstatement with full back wages, when the termination is found to be illegal is not applied mechanically in all cases. While that may be a position where services of a regular/permanent workman are terminated illegally and/or mala fide and/or by way of victimisation, unfair labour practice, etc. However, when it comes to the case of termination of a daily-wage worker and where the termination is found illegal because of a procedural defect, namely, in violation of Section 25F of the Industrial Disputes Act, this Court is consistent in taking the view that in such cases reinstatement with back wages is not automatic and instead the workman should be given monetary compensation which will meet the ends of justice.

The court also added the caveat here that there may be cases where termination of a daily-wage worker is found to be illegal on the ground that it was resorted to as unfair labour practice or in violation of the principle of last come first go viz. while retrenching such a worker daily wage juniors to him were retained. There may also be a situation that persons junior to him were regularised under some policy but the workman concerned terminated. In such circumstances, the terminated worker should not be denied reinstatement unless there are some other weighty reasons for adopting the course of grant of compensation instead of reinstatement. **In such cases, reinstatement should be the rule and only in exceptional cases for the reasons stated to be in writing, such a relief can be denied.**

Therefore, in case of illegal retrenchment, the workman is entitled to get the benefits of re-instatement with back wages. If the employer does not comply with the procedure and retrenchment is resorted to as unfair labour practice, then it's illegal and liable to pay penalty for committing unfair trade practices under Section 25U of the Industrial Disputes Act, 1947.

### Question 2

*(a) Bhuvesh, working as supervisor in Shantala Silks applied for leave for 8 days from 2nd March to 9th March. He reported for duty on 28th March and produced a medical certificate issued by the Civil Surgeon to the effect that he had been suffering from typhoid from 10th March till 27th March. The Manager of the factory referred him for the medical examination but the medical officer could not confirm the illness. The management under the rules of the standing orders refused to allow Bhuvesh to report back to duty as absence for the work without leave amounted to discharge from service. However, Bhuvesh was granted sick leave benefit by the ESI Corporation from 10th March till 27th March. Whether the act of the management is valid? State the relevant legal provisions.*

(6 marks)

*(b) Hari and Vishnu, employees in Kashinath Stone Crushing Factory, were engaged in loading a consignment to a truck. While doing the work, Vishnu sustained injuries due to the negligence of Hari. Vishnu claimed compensation from the management of the factory but the factory management told Vishnu to institute a suit against Hari only for the grant of relief. Decide the validity of the stand taken by the management.*

(6 marks)

### **Answer 2(a)**

The facts of the given case are very much similar to ***Venkatiah vs. Management of the Buckingham.***

In the instant case, the management is bound to accept any medical certificate that might be produced by the worker, in support of his case that he was too ill to attend to his work. It is always for the management to consider whether the certificate produced by the worker from a medical officer other than the company's medical officer should be accepted or not. Here, the company's doctor did not say definitely whether the worker was really ill or not. The management does not seem to have rejected the Civil Surgeon's certificate as untrustworthy. Under such circumstances it could not be held that the company had discharged their obligations under their Standing Orders or considering the explanation of the worker in regard to his absence.

Such a failure of duty on the part of the management particularly having regard to the terms of standing Order which oblige them to convert absence of a worker as one on leave in case they were satisfied with the explanation of the worker showed that there was an act on their part which brought about discharge or dismissal of the worker.

The action of the management amounted to a contravention of the provisions of Section 73 of the Employees State Insurance Act, 1948 which provides that the employer not to dismiss or punish employee during period of sickness and hence, such is invalid.

### **Answer 2(b)**

The objective of Employees Compensation Act, 1923 is to protect workman and their dependents from being deprived of economic security on account of accidents sustained by them arising out of employment and in the course of employment. Section 3 of the Employees Compensation Act, 1923 provides that if personal injury is caused to an employee by accident arising out of and in the course of his employment, his employer shall be liable to pay compensation in accordance with the provisions as prescribed under this Act.

The expression "in the course of employment" suggests the period of employment and the place of work. In other words, the workman, at the time of accident must have been employed in the performance of his duties and the accident took place at or about the place where he was performing his duties.

In a workplace, where the job is done by two or more employees then there is all the likelihood that one of the employees may sustain injury on account of the negligence of the other co-employee. In the given case, instead of instituting a case against Hari, it is the liability of the employer to pay compensation as per Employees Compensation Act, 1923.

### **Question 3**

*(a) Protection of the well-being of workers is more important than mere payment of wages with a view to increasing productivity. Substantiate the statement referring to relevant provisions of the Factories Act, 1948.*

*(b) Manoj & Co. Ltd. desired to start an Aluminium Electrical Fittings and Pipes factory in Vijayawada. They made an application to the appropriate authority with all necessary documents. Even after the expiry of 3 months, the appropriate authority did not intimate its order either sanctioning or declining the permission. Manoj & Co. Ltd. intend to pursue legal remedies. Will the action of the company be tenable or desirable? Discuss with reference to legal provisions.*

*(6 marks each)*

### **Answer 3(a)**

The main objective of the Factories Act, 1948 is to ensure adequate safety measures but also to promote health and welfare of the workers employed in factories as well as to prevent haphazard growth of factories. Factories Act, 1948 is legislated to lay guidelines on working conditions in factories including leaves, working hours, holidays, etc. It also ensures health, safety and welfare measures of workers in factories.

The welfare measures are defined under Section 42 to 50 of Factories Act, 1948, viz, washing facilities, facilities for storing & drying clothes, sitting facilities, first aid appliances, canteen, shelters, rest rooms & lunch rooms, crèches and welfare officers.

There are other provisions in the Act which deals with health measures including cleanliness, ventilation, lightning, drinking water, latrines & urinal, etc., safety measure includes fencing, lifting, casing of machinery, employment of young workers with dangerous machines, etc. This Act also focuses on hazardous process by industries and the level of chemical substances permissible in work environment. The Act contains provisions regarding hazardous process, constitution of Site Appraisal Committee, compulsory disclosure of Information, appointing competent person in handling hazardous substances, etc.

### **Answer 3(b)**

Section 6 of the Factories Act, 1948 states that if an application for permission to be obtained for the site on which the factory is to be situated and for the construction or extension of any factory or class or description of factories and no order is communicated to the applicant within three months from the date on which it is so sent, the permission applied for in the said application shall be deemed to have been granted but only when applicant had duly complied with all the license requirements.

Since the Manoj & Co. Ltd. complied with all requirements, it is presumed that permission is granted. Accordingly, Manoj & Co. Ltd. can go ahead with their establishment of factory.

### **Question 4.**

*(a) 'Articles 23 and 24 of the Constitution of India are wide enough to encompass various aspects of rights of labourers'. Elaborate and refer to decided case law, if any.*

*(b) 'Discipline, far from being enforced by the management, must be voluntarily observed by the employees'. Elaborate.*

*(6 marks each)*

### **Answer 4(a)**

The Laws in India prohibits slavery and any act which harms dignity and freedom of person. The Right against exploitation is enshrined in the Article 23 and 24 of the Indian Constitution which guarantees human dignity and protect people from any such exploitation.

Article 23 prohibits the trafficking of human beings, beggar or any similar form of forced labour. It also states that any contravention of this provision is punishable by the law. Article 23 has a very wide scope by ensuring that a person is not forced to do anything involuntarily. Bonded labour, prisoners made to work without even minimum remuneration, poor labours made to work free or forcing women or child into prostitution etc. are some of the instances which the law prohibits. Article 23 forbids all forms of exploitation and also makes bonded labour as well as human trafficking unconstitutional. Article 23 States that it ensures citizen protection both against the State and Private Individuals.

Withholding of pay of a government employee as a punishment has been held to be invalid in view of Article 23 which prohibits beggar. 'To ask a man to work and then not to pay him any salary or wages savours of beggar. It is a Fundamental Right of a citizen of India not to be compelled to work without wages.' (***Suraj vs. State of Madhya Pradesh, AIR 1960 MP 303***).

The Supreme Court has given an expansive significance to the term "forced labour" used in Article 23(1) in a series of cases beginning with the *Asiad* case in 1982. (***People's Union for Democratic Rights vs. Union of India, AIR 1982 SC 1473***). The Court has insisted that Article 23 is intended to abolish every form of forced labour even if it has origin in a contract. Article 23 strikes at forced labour in whatever form it may manifest itself, because it is in violation of human dignity and is contrary to the basic human values.

Article 24 states that any child under the age of 14 years cannot be employed as a worker in any factory or be engaged in any other hazardous employment. The purpose of this article is to protect children's welfare and to guarantee their safety and well-being.

In ***M.C.Mehta v. State of T.N.: (AIR 1997 SC 699)***, the Supreme Court directed that the employers of children below 14 years must comply with the provisions of the Child Labour (Prohibition and Regulation) Act, 1986 providing for compensation, employment of their parents / guardians and their education.

#### **Answer 4(b)**

Discipline means a state of order in an organisation. Observing discipline increases the efficiency and effectiveness. The rules of discipline instruct as to who should do the job, what kind of job, how it should be done, when and under whose guidance etc. Unless such procedure is observed the end result may not get accomplished.

Approaches to the rules of discipline may be positive or negative. A positive approach is voluntary and self-imposed. Employees are expected to comply with the rules not out of fear of punishment but because of their desire to abide by it for an orderly result. A positive discipline is a self-disciplined attitude of the employee in rendering the service.

Whereas negative approach warrants that someone should enforce rules of discipline. The fear of some sanction prevents him from being negligent or irresponsible in his work. Instances of indiscipline could be enumerated such as absenteeism, insubordination, negligence, threat, go slow tactics etc. The Standing Orders helped to maintain discipline in the industry.

To tackle discipline there is the need to train, educate, appraise, inform the employees about the need of rules and regulations and enlighten the employees that their livelihood is ultimately connected with the organisation's future. There are judicial human relations, human resource, leadership and group discipline approach to tackle indiscipline.

#### **Question 5.**

(a) *Tanuja Industries employed 200 workers in its establishment. Due to poor performance in one section of the establishment, workers employed therein were paid with reduced wages which were below the minimum wages. Whether the establishment is justified in its act? Discuss referring to decided case law, if any.*

(b) *Ramesh, an employee with more than one year of continuous service in an establishment was terminated from the job owing to his insubordination. He assured that he will not repeat his misbehaviour but the employer did not reinstate him. Ramesh challenged the dismissal and after a prolonged litigation, he was reinstated. Decide the rights of Ramesh regarding payment of bonus during the period of dismissal under the Payment of Bonus Act, 1965.*

(6 marks each)

### Answer 5(a)

According to Section 12 of Minimum Wages Act, 1948, the employer shall pay to every employee engaged in a scheduled employment under him wages at a rate not less than the minimum rate of wages fixed by such notification for that class of employees in that employment without any deductions except as may be authorised within such time and subject to such conditions as may be prescribed.

Therefore, it is binding obligation of every employer to pay the minimum of wages fixed under the Act from time to time. It must be paid without any deduction. In case of poor performance of workers, the employer may pay the reduced wages but it should not be below the minimum wages. Reducing the payment of minimum wages on the ground of less output or poor performance is illegal as was held in ***Bandhua Mukti Morcha Vs Union of India (1984 35 CC161)***. Instead, the employer may take disciplinary action against the workman.

### Answer to Question 5 (b)

According to Section 9 of the Payment of Bonus Act, 1965, an employee shall be disqualified from receiving bonus under this Act, if he is dismissed from service for--

- (a) fraud; or
- (b) riotous or violent behaviour while on the premises of the establishment; or
- (c) theft, misappropriation or sabotage of any property of the establishment.

'Ramesh' an employee was terminated from the service owing to his insubordination. He challenged the dismissal after his request for reinstatement was rejected by the employer. After a prolonged legal battle, the court found the termination order as bad and ordered his reinstatement.

The High Court held that the employee is eligible to claim bonus because the service of the employee was terminated only by the employer although the employee was prepared to work. Hence, the employee is eligible even for the days of suspension till reinstatement as per provisions of Section 9 of Payment of Bonus Act, 1965 (***Project Manager Ahmadabad ONGC vs Shyam Kumar Sehgal 1955 LLJ, 1863, Gujrat.***)

### Question 6.

*Explain how the Labour Codes on wages, industrial relations, social security and welfare, and occupational safety, health and working conditions pave the way for labour empowerment in the country.*

(12 marks)

### Answer 6.

With the objective of strengthening the safety, security, health, social security for every worker and to pave the way for labour empowerment in the country, the Government has amalgamated, simplified and rationalized the relevant provisions of the existing Central Labour Laws into four codes:

- The Code on Wages, 2019
- The Occupational Safety, Health and Working Conditions Code, 2020
- The Code on Social Security, 2020
- The Industrial Relations Code, 2020

### **Salient features of the Code on Wages, 2019**

- (a) It provides for all essential elements relating to wages, equal remuneration, its payment and bonus;
- (b) The provisions relating to wages shall be applicable to all employments covering both organised as well as un-organised sectors;
- (c) The power to fix minimum wages continues to be vested in the Central Government as well the State Government in their respective sphere;
- (d) It enables the appropriate Government to determine the factors by which the minimum wages shall be fixed for different category of employees. The factors shall be determined taking into account the skills required, the arduousness of the work assigned, geographical location of the workplace and other aspects which the appropriate Government considers necessary;
- (e) The provisions relating to timely payment of wages and authorised deductions from wages, which are presently applicable only in respect of employees drawing wages of twenty-four thousand rupees per month, shall be made applicable to all employees irrespective of wage ceiling. The appropriate Government may extend the coverage of such provisions to the Government establishments also;
- (f) It provides that the wages to employees may also be paid by cheque or through digital or electronic mode or by crediting it in the bank account of the employee. However, the appropriate Government may specify the industrial or other establishment, where the wages are to be paid only by cheque or through digital or electronic mode or by crediting the wages in the bank account of the employee;
- (g) It provides for floor wage for different geographical areas so as to ensure that no State Government fixes the minimum wage below the floor wage notified for that area by the Central Government;
- (h) In order to remove the arbitrariness and malpractices in inspection, it empowers the appropriate Government to appoint Inspectors-cum-Facilitators in the place of Inspectors, who would supply information and advice the employers and workers;
- (i) It empowers the appropriate Government to determine the ceiling of wage limit for the purpose of eligibility of bonus and calculation of bonus;
- (j) In the place of number of authorities at multiple levels, it empowers the appropriate Government to appoint one or more authorities to hear and decide the claims under the proposed legislation;
- (k) It enables the appropriate Government to establish an appellate authority to hear appeals for speedy, cheaper and efficient redressal of grievances and settlement of claims;
- (l) It provides for graded penalty for different types of contraventions of the provisions of the proposed legislation;
- (m) It provides that the Inspector-cum-Facilitator shall give an opportunity to the employer before initiation of prosecution proceedings in cases of contravention, so as to comply with the provisions of the proposed legislation. However, in case of repetition of the contravention within a period of five years such opportunity shall not be provided;
- (n) It provides for the appointment of officers not below the rank of Under Secretary to the Government of India or an officer of equivalent level in the State Government to dispose of cases punishable only with fine up to fifty thousand rupees, so as to reduce the burden on subordinate judiciary;
- (o) It provides for compounding of those offences which are not punishable with imprisonment;
- (p) It provides that where a claim has been filed for non-payment of remuneration or bonus or less payment of wages or bonus or on account of making deduction not authorised by the proposed

legislation, the burden shall be on the employer to prove that the said dues have been paid to the employee;

- (q) It enables the appropriate Government to constitute Advisory Boards at Central and State level to advice the Central Government and the State Governments, respectively, on matters relating to wages, women employment etc.
- (r) The period of limitation for filing of claims by a worker has been enhanced to three years, as against the existing time period varying from six months to two years, to provide a worker more time to settle his claims.

### **Salient features of the Occupational Safety, Health and Working Conditions Code, 2020**

- a) To impart flexibility in adapting dynamic factors and technological changes, in the matters relating to health, safety, welfare and working conditions of workers;
- b) To apply the provisions of the proposed Code for all establishments having ten or more workers, other than the establishments relating to mines and docks;
- c) To expand –
  - a. the ambit of the provisions relating to working conditions of cine and theatre workers to include them in the digital audio-visual workers encompassing all forms of electronic media;
  - b. the scope of journalists to include them in electronic media such as in e-paper establishment or in radio or in other media;
  - c. the scope of Inter-State migrant workers to include therein the workers recruited or engaged by an employer directly, from one State to another State for employment in his establishment;
  - d. the definition of “family” to include therein the dependent grandparents in order to take care of them in old age;
- d) To provide the concept of “one registration” for all establishments having ten or more employees;
- e) To constitute “the National Occupational Safety and Health Advisory Board” to give recommendations to the Central Government on policy matters, relating to occupational safety, health and working conditions of workers;
- f) To constitute “the State Occupational Safety and Health Advisory Board” at the State level to advice the State Government on such matters arising out of the administration of the proposed Code;
- g) To make a provision for the constitution of “Safety Committee” by the appropriate Government in any establishment or class of establishments;
- h) To allow the women employees to work at night, that is, beyond 7 PM and before 6AM subject to the conditions relating to safety, holiday, working hours and their consent;
- i) To make a provision of “common license” for factory, contract labour and beedi and cigar establishments and to introduce the concept of a single all India license for five years for engaging the contract labour;
- j) To enable the courts to give a portion of monetary penalties upto fifty per cent. to the worker who is a victim of accident or to the legal heirs of such victim in the case of his death; and



- k) To make a provision for adjudging the penalties imposed under the Code.

### **Salient features of the Code on Social Security, 2020**

- a) to extend the coverage of Employees' State Insurance to all establishments employing ten or more employees and to the employees working in establishments with less than ten employees on voluntary basis and also to plantations on option basis. It further seeks to empower the Central Government to notify the applicability of the said coverage to establishments which carries on the hazardous or life-threatening occupation irrespective of the number of workers employed therein;
- b) to extend the Employees' Provident Fund, Employees' Pension Scheme and Employees Deposit Linked Insurance Scheme to all industries or establishments employing twenty or more;
- c) to make provision for specifying differential rates of employees' contribution for class of employees for employees' provident fund as the Central Government may notify for a specified period;
- d) to provide that the money dues shall be the charge on the assets of the employer and shall be paid on priority basis in accordance with the Insolvency and Bankruptcy Code, 2016;
- e) to provide that in case of employer's failure to register the employee with Employees' State Insurance Corporation or failure to pay contribution and the Employees' State Insurance Corporation releasing the benefits to the workers, then, such benefits shall be recovered from the employer;
- f) to empower the Central Government to frame schemes for providing social security, to the gig workers and platform workers who do not fall under traditional employer-employee relation;
- g) to empower the Central Government, by notification, to constitute a Social Security Fund or funds for provision of social security for the unorganised workers, platform workers or gig workers or any such class of workers;
- h) to provide for payment of gratuity in case of Fixed Term Employment on pro-rata basis even if the period of fixed term contract is less than five years;
- i) to provide for maternity benefit to the woman employee;
- j) to provide for compensation to the employees in case of the accidents while commuting from residence to place of work and vice versa;
- k) to provide for levying and collecting the cess for the purposes of social security and welfare of building workers;
- l) to provide for limit limitation period of five years for institution of proceedings in respect of assessment and determination of money dues from employer;
- m) to expand the sources of the fund for schemes to include funds from corporate social responsibility or any other source as may be specified in the scheme and also contains enabling provision for constituting the special purpose vehicle for the purpose of implementation of schemes for unorganised workers;
- n) to provide for renaming the designation of Inspector as Inspector-cumFacilitator and to enhance his power to supply information and give advice to employers and workers concerning the most effective means of complying with the provisions of the proposed Code;
- o) to provide for filing of a single return electronically or otherwise by the employer;

- p) to provide that the interests charged on delayed payments under the provisions of the proposed Code be specified in the rules;
- q) to provide penalty for the different types of violations commensurate with the gravity of the violations;
- r) to make Aadhaar mandatory for seeding at the time of registration of member or beneficiary or any other person to register or for receiving benefit;
- s) to empower the appropriate Government to exempt certain establishments from all or any of the provisions of the proposed Code.

### **Salient features of the Industrial Relations Code, 2020**

- a) to define the expression “fixed term employment” to mean engagement of a worker on the basis of a written contract of employment for a fixed period. The fixed term employee will get all statutory benefits like social security, wages, etc., at par with the regular employee who is doing work of same or similar nature;
- b) to define the term “industry” with certain exceptions;
- c) the definition of “strike” is proposed to be modified to include mass casual leave within its ambit;
- d) to define the term “worker” to include persons in supervisory capacity getting wages up to fifteen thousand rupees within its ambit. At present, under the Industrial Disputes Act, 1947, definition of ‘worker’ includes person in supervisory capacity getting salary up to ten thousand rupees per month;
- e) to provide for the obligation on the part of the industrial establishment pertaining to mines, factories and plantation having one hundred or more workers to take prior permission of the appropriate Government before lay-off, retrenchment or closure. However, the appropriate Government is proposed to be empowered to modify such threshold number of workers by notification;
- f) to set up a re-skilling fund for training of retrenched employees, to which the employers will pay a contribution of fifteen days wages or such other days as may be notified by the Central Government in case of retrenchment of workers;
- g) to provide for a sole negotiating union in an industrial establishment for negotiating with the employer of the industrial establishment, on such matters as may be provided by rules. In case of more than one Trade Union of workers, a Trade Union would be designated as a sole negotiating union if it has support of seventy-five per cent. or more of the workers on the muster roll in an establishment and if no Trade Union has such support strength on the muster roll of an establishment, then a negotiating council will be constituted for negotiation;
- h) to provide for Industrial Tribunal to be the adjudicating body to decide appeals against the decision of the conciliation officer in place of multiple adjudicating bodies like Court of Inquiry, Board of Conciliation and Labour Courts;
- i) the maximum number of members in the Grievance Redressal Committee has been increased from six to ten;
- j) provisions are being made to have two-member Industrial Tribunals, with second member being from administrative side, in place of single member Labour Court and Industrial Tribunal at present. Further, the Tribunal will be empowered to execute the award as a decree of a civil court, which will facilitate speedy disposal of disputes;
- k) to provide for continuation of services of Presiding Officers of the existing adjudicating authorities;
- l) to provide that reference by the Government will not be required for Industrial Tribunal, except the National Industrial Tribunal;

- m) to prohibit strikes and lockouts in any industrial establishment without giving notice of fourteen days and also during the pendency of conciliation proceedings;
- n) to provide for penalties for different types of violations to rationalise with such offences and commensurate with the gravity of the violations;
- o) to empower the appropriate Government to appoint officers for holding enquiry and impose penalty in certain contraventions punishable with fine up to fifty thousand rupees;
- p) to provide for compounding of offences which are not punishable with imprisonment.

## INSOLVENCY - LAW AND PRACTICE

### (Elective Paper 9.5)

Time allowed : 3 hours

Maximum marks : 100

**NOTE** : Answer **ALL** Questions

#### Question 1.

Sober Ltd. (the Company) is engaged in the business of running hotel chains in India as well as outside India. Due to less demand faced during the pandemic, the Company was unable to meet its financial obligations. Financial creditors of the Company decided to file an application under section 7 of the Insolvency and Bankruptcy Code, 2016 (IBC). On 1 st January, 2022, Corporate Insolvency Resolution Process ('CIRP') of the Company started and Shyam was appointed as an Interim Resolution Professional. The Company was subjected to parallel insolvency proceedings in India as well as Netherlands (where it had registered office). In the Netherlands, the Company was declared bankrupt and the Dutch trustee had been appointed to manage the estate of the Company. During the 1st meeting of the Committee of Creditors (CoC), Shyam was confirmed to act as Resolution Professional (RP). Considering the future potential in the Company, many strategic and financial investors expressed their interest in buying the Company including one of the members of the CoC who also submitted Expression of Interest to the RP. Shyam after due verification, published the final list of the prospective resolution applicants. One of the investors, Simba Ltd. wrote an email to Shyam stating that they also want to participate in the process and submitted all the required documents to Shyam for their name to get included in the final list of the prospective resolution applicants. Shyam refused to include their name in the final list stating that no provision exist under the IBC to include name of any party, once the final list of the prospective resolution applicants is published by the RP.

During the CIRP process, Shyam had appointed two valuers to carry out valuation. The fair value given by Valuer 1 was ₹ 1,750 crore and Valuer 2 was ₹ 550 crore and liquidation value was ₹ 1,000 crore and ₹ 200 crore respectively. During the discussions with the valuers to understand the methodology adopted by them to carry out the valuation, Shyam realized that both the valuers have carried out valuation based on the internationally accepted valuation methods and have made certain assumptions while arriving at the final numbers. Lawyer of Shyam had suggested that since the valuation given by Valuer 1 is advantageous for the stakeholders, he can put the valuation report issued by Valuer 1 before the CoC. Shyam agreed and moved ahead accordingly. During one of the meetings of the CoC, the financial creditors were deliberating on how to maximize the value of the Company and fetch a best possible resolution plan. In response, one of the members of the CoC requested the entire CoC to explore possibility of 'Swiss Challenge' to improve value of the resolution plans. However, none of the other members agreed stating that there is no provision under the IBC for exercising a 'Swiss Challenge'. When the final resolution plans had come, the RP after due verification and completing required formalities, had put-up all the plans on voting. The outcome of voting was as under:

S. No.	Particulars	Voting result
1	Resolution Plan 1	56%
2	Resolution Plan 2	67%
3	Resolution Plan 3	67%
4	Resolution Plan 4	75%

One of the members of the CoC suggested to carry out the voting again since the voting percentage of Resolution Plan 2 and 3 is same. The RP denied stating that once the voting is done, re-voting on the plans cannot be done again in the present scenario. Accordingly, Resolution Plan 4 was filed with the adjudicating authority for approval.

The resolution applicant had mentioned in the Resolution Plan 4 to put ` 80 crore in the form of working capital as well as capital expenditure, once the company's handover formalities are completed. Even after 1 year of handover, the resolution applicant did not infuse the aforesaid amount. In fact, the resolution applicant requested the financial creditors to waive off the condition to infuse money for working capital and

capital expenditure. Shyam being part of the monitoring committee, overseeing implementation of the resolution plan, expressed his concern on the request made by the resolution applicant citing violation of the provisions under the IBC. Consider the above case and relevant provisions of the IBC, its rules and regulations made thereunder, answer the following questions:

(a) Whether the IBC has provisions in relation to cross border insolvency? If yes, elaborate based on decided case law how cross border insolvency in case of any cross-border cases can be achieved effectively.

(b) Whether the contention of Shyam is correct that once the final list of prospective resolution applicants is published, name of any other party cannot be included in the list of prospective resolution applicants? Suggest the plausible option if the name of any party has to be included after publication of the final list of the prospective resolution applicants.

(c) Whether the following contentions of the CoC are correct?

(i) In case two resolution plans receive the same votes, voting has to be done again.

(ii) There exists no provision to initiate 'Swiss Challenge'.

(d) Whether the following actions of Shyam are in accordance with the IBC? (i) Accepting the valuation report given by Valuer 1 and moving forward? If not, suggest an action plan to Shyam.

(ii) Expressing concerns on the request made by resolution applicant citing violation of the provisions under the IBC.

(10 marks each)

**Answer. 1. (a)**

Sections 234 and 235 of the Insolvency and Bankruptcy Code, 2016 contains provisions to deal with the cases involving cross border insolvency.

Section 234 empower the Central Government to enter into an agreement with other countries to resolve situations pertaining to cross border insolvency. Section 234 of the Code provides that:

(1) The Central Government may enter into an agreement with the Government of any country outside India for enforcing the provisions of this Code.

(2) The Central Government may, by notification in the Official Gazette, direct that the application of provisions of this Code in relation to assets or property of corporate debtor or debtor, including a personal guarantor of a corporate debtor, as the case may be, situated at any place in a country outside India with which reciprocal arrangements have been made, shall be subject to such conditions as may be specified.

Section 235 of the Code lays down that notwithstanding anything contained in this Code or any law for the time being in force if, in the course of insolvency resolution process, or liquidation or bankruptcy proceedings, as the case may be, under this Code, the resolution professional, liquidator or bankruptcy trustee, as the case may be, is of the opinion that assets of the corporate debtor or debtor, including a personal guarantor of a corporate debtor, are situated in a country outside India with which reciprocal arrangements have been made under section 234, he may make an application to the adjudicating authority that evidence or action relating to such assets is required in connection with such process or proceeding.

Considering the above provisions, the IBC has provisions in relation to cross border insolvency.

The case of *Jet Airways (India) Ltd. v. state Bank of India & Anr. Company Appeal (AT) (Insolvency) no. 707 of 2019* is the first case touching the realm of cross border insolvency in India.

In the instant case Jet Airways (India) Limited, ("Company") was subjected to parallel insolvency proceedings in India as well as in the Netherlands. In India, the Company has been admitted into a corporate insolvency resolution process under the insolvency and Bankruptcy Code, 2016 (the "Indian Proceedings"). Pursuant to the order of the National Company Law Tribunal (NCLT) and resolutions duly

passed at the meeting of the Committee of Creditors of the Company ("CoC") dated 16<sup>th</sup> July, 2019, the Resolution Professional (RP) had been appointed, resulting in the powers of the board of directors of the Company being vested with the RP.

In the Netherlands, the Company has been declared bankrupt and the Dutch trustee had been appointed to manage the estate of the Company (the "Dutch Proceedings").

On an application made by the Dutch trustee, appealing the 20<sup>th</sup> June, 2019 order of the NCLT before the Hon'ble National Company Law Appellate Tribunal, New Delhi ("NCLAT"), the NCLAT, by its orders dated 12<sup>th</sup> July, 2019 and 21<sup>st</sup> August, 2019 ("NCLAT Order"), inter alia, directed the RP, in consultation with the CoC, to consider the prospect of cooperating with the Dutch trustee so as to have joint "corporate insolvency resolution process of the Company" and further vide its order dated 4<sup>th</sup> September, 2019 directed the RP under the Indian proceedings to reach an arrangement/agreement with the Dutch trustee to extend such cooperation to each other, further allowing the CoC to guide the RP to enable him to prepare an agreement in reaching the terms of arrangement of cooperation with the Dutch trustee in the best interest of the Company and all its stakeholders ("Proposed Cooperation").

The NCLAT set aside the order dated 20<sup>th</sup> June, 2019 passed by the National Company law Tribunal, Mumbai Bench in so far it related to the observations that the 'Dutch Court' has no jurisdiction in the matter of 'corporate insolvency resolution process' of 'Jet Airways (India) Limited, (Offshore Regional Hub) and the consequential directions as given to the 'Resolution Professional' in respect of 'Offshore proceedings'. However, NCLAT did not interfere with the order of admission of application under Section 7 of the Code filed by the 'State Bank of India' against 'Jet Airways (India) Limited', therefore, joint 'Corporate Insolvency Resolution Process' will continue in accordance with the Code.

The Parties facilitated the Proposed Cooperation with formulation of a 'Cross Border Insolvency Protocol'. The key agreements under the said Protocol were as follows:

(i) This Protocol represents a statement of intentions and guidelines designed to minimize the costs and maximize value of assets/recoveries for all creditors of the Proceedings, by promoting the sharing of relevant information among the Parties and the international coordination of related activities in the Proceedings, while respecting the separate interests of creditors and other interested parties to the Proceeding, and the independence, sovereignty, and authority of the NCLT/NCLAT and Dutch Bankruptcy Court.

(ii) In recognition of the substantive differences among the Proceedings in both jurisdictions, this Protocol shall not impose on the RP or the Dutch trustee any duties or obligations (i) that may be inconsistent with or that may conflict with the duties or obligations to which the Parties are subject under applicable law, or (ii) that are not in the interests of the Company's estate represented by the Parties and/or its creditors. Furthermore, nothing in this Protocol should be interpreted in any way so as to interfere with (i) the proper discharge of any duty, obligation or function of the Parties, or (ii) the exercise of statutory or other powers otherwise available to a Party under applicable law.

(iii) The Parties should coordinate with each other and cooperate in all aspects of the Proceedings in terms of this Protocol. In doing so, the Parties acknowledge and agree that the Parties shall deal in good faith with each other in the interests of maximizing value of assets/recovery for all of the Company's creditors. The Parties recognised that the Company being an Indian company with its centre of main interest in India, the Indian Proceedings are the main insolvency proceedings and the Dutch Proceedings are the non-main insolvency proceedings to promote international cooperation and the coordination of activities in the Proceedings; and to promote communication among the Parties and the CoC.

(iv) In the spirit of cooperation, the Dutch trustee aims to not take any decision under the Dutch Proceedings that would adversely impact the interests of the Company or the creditors. In the event it becomes necessary for the Dutch trustee in compliance of the Dutch Bankruptcy Court or any other court, or under any applicable law, to take any decision that might adversely impact the interests of the Company or the creditors, the Dutch trustee shall give advance intimation of such decision to the RP.

(v) The Dutch trustee shall seek inputs, notify the RP and consult the RP, and will be mindful of the Indian Proceedings prior to any material decision being taken in the Dutch Proceedings.

(vi) The 'Committee of Creditors' have no role to play as the agreement reached between the 'Dutch administrator' and the 'Resolution Professional' of India is on the basis of the direction of this appellate tribunal. In spite of the same, unfortunately the 'Committee of Creditors' interfered with the matter and put its view to the 'Resolution Professional' resulting into difference of the suggestions.

(vii) The NCLAT clarified that the 'Dutch Trustee (Administrator)' will work in co-operation with the 'Resolution Professional of India' and, if any, suggestion is required to be given, he may give it to the 'Resolution Professional'. The draft of 'Cross Border Insolvency Protocol' clause is made final and should be treated as a direction of this appellate tribunal and it would be mandatory to comply with the order of this appellate tribunal subject to the other procedures which are to be followed in terms of the 'Insolvency and Bankruptcy Code, 2016'.

### **Answer 1 (b)**

As per Regulation 36A (6) of the IBBI (Resolution Process for Corporate Persons), Regulations, 2016, the expression of interest received after the time specified in the invitation under sub regulation 3(b) shall be rejected.

Further, Regulation 36A(12) provides that on considering the objections received under sub regulation 36A (11), the resolution professional shall issue the final list of prospective resolution applicants within 10 days of the last date of receipt of objections, to the committee.

Considering the above provisions, the contention of Shyam is correct that once the final list of the prospective resolution applicants is published, name of any party cannot be included in the list.

However, in many cases it has been observed that any party still intends to participate in the process for submission of the resolution plan, has been taken by the resolution professional before the committee of creditors for their consideration. If the committee of creditors agrees, the resolution professional may consider approaching the adjudicating authority for seeking direction to include the name of the party into the final list of prospective resolution applicants or to reissue the expression of interest subject to availability of time for completion of the corporate insolvency resolution process. On the contrary, even the party whose name has not been included can also approach the adjudicating authority for seeking directions to the resolution professional for including their name in the final list of prospective resolution applicants. On the merits of the case, the adjudicating authority for the purpose of value maximization and wider participation from the investors may allow the resolution professional to reissue the expression of interest. *Refer the case of M/s Riddhi Siddhi Gluco Biols Limited vs Sumit Binani & Ors [IA 325/2021 in CP (IB No. 492/07/HDB/2019)]*

Therefore, in the present case, Shyam, could have considered taking the matter before the committee of creditors for discussions and if approved by majority of the members of the committee he could have considered approaching adjudicating authority for necessary directions.

### **Answer 1(c)(i)**

As per Regulation 39(3B) of the IBBI (Resolution Process for Corporate Persons) Regulations, 2016, where two or more resolution plans are put to vote simultaneously, the resolution plan, which receives the highest votes, but not less than requisite votes, shall be considered as approved.

Provided that where two or more resolution plans receive equal votes, but not less than requisite votes, the committee shall approve any one of them, as per the tie-breaker formula announced before voting.

Provided further that where none of the resolution plans receives requisite votes, the committee shall again vote on the resolution plan that received the highest votes, subject to the timelines under the Code.

Considering the above provisions, since Resolution Plan 4 has received highest votes (and more than 66% required for approval of the resolution plan). The said Resolution Plan will be considered as approved. Therefore, the contention of CoC is not correct.

#### **Answer 1(c)(ii)**

As per Regulation 39(1A) of the IBBI (Resolution Process for Corporate Persons) Regulations, 2016, the Resolution Professional may, if envisaged in the request for resolution plan use a challenge mechanism to enable resolution applicants to improve their plans.

Considering the above provisions, contention of the CoC is not correct since the law gives opportunity to the CoC to use a challenge mechanism (Swiss Challenge, etc.) to improve the value of the resolution plans provided that the fact that challenge mechanism will be used is mentioned in the request for resolution plan.

#### **Answer 1 (d)(i)**

As per Regulation 35 of the IBBI (Resolution Process for Corporate Persons) Regulations, 2016, fair value and liquidation value shall be determined in the following manner:

- the two registered valuers appointed under regulation 27 shall submit to the resolution professional an estimate of the fair value and of the liquidation value computed in accordance with internationally accepted valuation standards, after physical verification of the inventory and fixed assets of the corporate debtor.
- if in the opinion of the resolution professional, the two estimates of a value are significantly different, he may appoint another registered valuer who shall submit an estimate of the value computed in the same manner; and
- the average of the two closest estimates of a value shall be considered the fair value or the liquidation value, as the case may be.

Considering the above provisions, in the present case, valuation given by Valuer 1 is Rs 1,750 crore as well as Rs 1,000 crore and Valuer 2 is Rs 550 crore as well as Rs 200 crore.

Since the difference in the valuation is significant (i.e. Rs 1200 crore and Rs 800 crore), action of Shyam to adopt valuation report given by Valuer 1 is not correct. He should have appointed a third valuer as per provisions of the Regulation 35.

#### **Answer 1(d)(ii)**

As per section 74(3) of the Insolvency and Bankruptcy Code, 2016, where the corporate debtor, any of its officers or creditors or any person on whom the approved resolution plan is binding under section 31, knowingly and wilfully contravenes any of the terms of such resolution plan or abets such contravention, such corporate debtor, officer, creditor or person shall be punishable with imprisonment of not less than one year, but may extend to five years, or with fine which shall not be less than one lakh rupees, but may extend to one crore rupees, or with both.

As per section 31, since the approved resolution plan will be binding on the resolution applicant as well, the present scenario will fall under the provisions of section 74(3) mentioned above. [*Liberty House Group v. Mr. Dinkar T Venkatasubramaniam and Another (NCLAT)*]

Accordingly, the contention of Shyam is correct and the request made by the resolution applicant is in violation of the terms of the approved resolution plan and falling under the provisions of section 74(3) mentioned above.



## Question 2.

(a) Neeraj is a practicing company secretary and is acting as a resolution professional in Bom Ltd. Before practising as a company secretary, he was working as a DGM in Bank of Surat. Bank of Surat contacted him to act as an Interim Resolution Professional (IRP) in the case of Bom Ltd. since he was known to the bank and his performance during the tenure with the bank was also satisfactory. Upon appointment as IRP in the case of Bom Ltd. he was informed by one of the members of the Committee of Creditors (CoC) that he has to disclose his details of the employment to the CoC to take informed decision as to whether he can continue to act in the capacity of the resolution professional in the case of Bom Ltd. During the 1st meeting of the CoC, he informed that the employment with Bank of Surat was 7 years ago and he is not under obligation to disclose now. Further, during the same meeting of the CoC, an agenda item for appointment of technical consultant was being discussed and deliberated among the members of the CoC. Candidature of many reputed persons were put before the members by Neeraj for the consideration and one amongst them was Suraj (son of Neeraj). He made a detailed presentation on the achievements of Suraj and mentioned that he is willing to work at a nominal cost. The appointment of Suraj will be advantageous for the process considering that is known to Neeraj and is willing to quote a nominal fee. In light of the above facts, discuss whether the conduct of Neeraj as resolution professional is proper?

(6 marks)

(b) Ghanshyam is a well known jeweler in Delhi. He is known for selling best antique jewelry at an affordable price. Due to dispute within the partners, the business started suffering losses and lost credibility amongst the customers. Ghanshyam filed an application for his bankruptcy. Raman's appointment was confirmed by the Adjudicating Authority to act as bankruptcy trustee in this case. Bankruptcy commencement date was 1st January, 2022. Consider the facts below :

S. No.	Event	Date
1	Notice sent by the Adjudicating Authority to creditors for inviting claims	9th January, 2022
2	List of creditors was prepared by Raman	15th January, 2022
3	Raman issued notice for calling meeting of creditors	20th January, 2022

Simba sent a letter to Raman expressing her wish to cast a vote in the meeting since her name was not appearing in the list of creditors prepared by Raman and accordingly notice of the meeting was not sent to her. Further, Pawan (father of Ghanshyam, whose name was included in the list of creditors) wished to cast his vote during the meeting. However, Raman refused stating he cannot cast vote during the meeting. Consider the above facts and answer the following questions:

(i) Whether the time lines mentioned above in the table are in accordance with the provisions of the Insolvency and Bankruptcy Code, 2016?

(ii) Whether Simba and Pawan eligible to vote during the meeting of the creditors?

(3 marks each)

### Answer 2 (a)

The IBBI (Insolvency Professionals) Regulations, 2016 makes provisions for the examination and registration of Insolvency Professionals with the Insolvency and Bankruptcy Board of India. These regulations also make provisions for the disciplinary proceedings against the insolvency professional as well as prescribes a code of conduct for insolvency professionals.

First Schedule to the aforesaid regulations prescribes a code of conduct for insolvency professionals. According to regulation 7(2)(h) the registration of an insolvency professional shall be subject to the condition that he shall abide by the Code of Conduct specified in the First Schedule to the Regulations:

-An insolvency professional shall disclose as to whether he was an employee of or has been in the panel of any financial creditor of the corporate debtor, to the committee of creditors and to the insolvency professional agency of which he is a professional member and the agency shall publish such disclosure on its website. (Regulation 8A of the First Schedule to the Regulations).

As per the above regulation, an insolvency professional shall disclose his employment details to the committee of creditors. Accordingly, Neeraj shall disclose the details of his employment to the committee of creditors irrespective of the fact that he was employed 7 years back.

-An insolvency professional shall not influence the decision or the work of the committee of creditors or debtor, or other stakeholders under the Code, so as to make any undue or unlawful gains for itself or its related parties, or cause any undue preference for any other persons for undue or unlawful gains and shall not adopt any illegal or improper means to achieve any mala fide objectives. (Regulation 9 of the First Schedule to the Regulations).

'As per the above regulation, an insolvency professional shall not influence the decision or the work of the committee of creditors so as to make any undue or unlawful gains for his related parties. Accordingly, conduct of Neeraj to solicit work for Suraj is not correct as per the code of conduct.

**Answer 2 (b) (i)**

Section 130 of the Insolvency and Bankruptcy Code, 2016 provides that the adjudicating authority shall send notices within ten days of the bankruptcy commencement date to the creditors mentioned in the statement of affairs submitted by the bankrupt under Section 129 of the Code; or the application for bankruptcy submitted by the bankrupt under Section 122 of the Code.

Section 132 of the Code provides that the bankruptcy trustee shall within fourteen days from the bankruptcy commencement date prepare a list of creditors of the bankrupt on the basis of the information disclosed by the bankrupt in the application for bankruptcy filed by the bankrupt under Section 118 of the Code and the statement of affairs filed under Section 125 of the Code, and claims received by the bankruptcy trustee under subsection (2) of Section 130 of the Code.

Section 133 of the Code provides that the bankruptcy trustee shall within twenty- one days from the bankruptcy commencement date, issue a notice for calling a meeting of the creditors, to every creditor of the bankrupt as mentioned in the list prepared under Section 132 of the Code.

Considering that the bankruptcy commencement date is 1<sup>st</sup> January, 2022, the correct answers are as under:

Sl.N	Event	Date	Correct Answer
1	Notice sent by the adjudicating authority to creditors for inviting claims	9th January, 2022	Yes, as per section 130
2	List of creditors was prepared by Raman	15th January, 2022	No, as per section 132
3	Raman issued notice for calling meeting of creditors	20th January, 2022	Yes, as per section 133

### Answer. 2 (b) (ii)

As per section 135 of the Insolvency and Bankruptcy Code, 2016, the following creditors shall not be entitled to vote under this Section:

(a) creditors who are not mentioned in the list of creditors under Section 132 of the Code, and those who have not been given a notice by the bankruptcy trustee;

(b) creditors who are associates of the bankrupt.

Considering the above provisions, the correct answers are as under:

Both Simba and Pawan cannot cast vote in the meeting since name of Simba was not included in the list of creditors prepared by Raman and Pawan is an associate of Ghanshyam.

### Question 3.

*Super Ltd. is engaged in the business of producing auto ancillary products and has a plant near Mumbai. As per the latest audited financial statements the turnover of Super Ltd. was ` 200 crore and investment in plant and machinery was ₹ 35 crore. Turnover and investment in plant and machinery never crossed ₹ 200 crore and ₹ 35 crore respectively. Due to reduction in the demand of the products by the auto companies, Super Ltd. started facing financial difficulties. It evaluated many options for rescuing the business and discussed on multiple occasions with the lenders. In one of the consortium meeting, lenders decided to take action under the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (SARFAESI). During the said meeting one of the lenders holding 30% share in the consortium suggested that in the present circumstances it would be apt to proceed under the provisions of the Insolvency and Bankruptcy Code, 2016 (the Code) since the Code is one of the effective tools for resolution of the debt. However, due to the difference in opinion amongst the lenders few of them decided to move ahead under the SARFAESI and others decided to file an application under the Code. Legal counsel of Super Ltd. intervened and informed that once proceedings are initiated under both the laws, SARFAESI being an old law will prevail and the lenders may be in a position to quickly recover their outstanding dues. Considering the circumstances, Rohan, promoter of Super Ltd. suggested to provide one last chance to Super Ltd. to submit a resolution plan for its revival and requested the lenders to consider the Pre-Packaged Insolvency Resolution Process. Rohan is now fully active in the business and making all possible attempts for revival of Super Ltd. and Duper Ltd. (wholly owned subsidiary of Super Ltd.) which is also classified as non-performing asset for last 5 years. On the option given by Rohan, one of the lenders informed that law relating to Pre-Packaged Insolvency Resolution Process is still at a nascent stage and may take years to complete. In response, Rohan clarified that it may not take years, since the process of filing an application is very simple and no documents are required to be attached to the application. Therefore, the adjudicating authority will be in a position to quickly consider and dispose off the case.*

Consider the above facts and answer the following questions:

- (i) *Whether the contention of legal counsel of Super Ltd. is correct? Discuss in light of the decided case laws(s).*
- (ii) *Whether Super Ltd. is eligible for getting resolved under the provisions of Pre-Packaged Insolvency Resolution Process?*
- (iii) *Considering the timelines provided under the Code, whether the contention of one of the lenders that the process may take years to complete legally correct ?*
- (iv) *Whether the contention of Rohan is correct that no document are required to be furnished along with the application?*

(3 marks each)

### Answer 3 (a)(i)

The contention of the legal counsel is not correct. In the case of *Canara Bank v. Sri Chandramoulisvar Spg. Mills (P) Ltd.*, the NCLAT while referring to Supreme Court's verdict in *Innoventive* case has ruled that when two proceedings are initiated, one under the Insolvency and Bankruptcy Code, 2016 (the Code) and the other under the SARFAESI Act, 2002, then the proceeding under the Code shall prevail. The appeal in

the case was preferred by the Financial Creditor i.e., Canara Bank against the NCLT's (National Company law Tribunal) order, whereby the application preferred by Operational Creditor under Section 9 of the Insolvency and Bankruptcy Code, 2016 (application for initiation of corporate insolvency resolution process by operational creditor) against the Corporate Debtor i.e. M/s. Sri Chandramoulisvar Spinning Mills Private Limited was admitted by the Tribunal. The Appellant's main grievance in the case was that he had already initiated proceedings under the SARFAESI Act, 2002 for recovery against the Corporate Debtor. The NCLAT in view of the issue involved in the case, made reference to Supreme Court's verdict in the case of *Innoventive Industries Ltd. v. ICICI Bank*, whereby the Apex Court was of the view that if the application under Section 9 is complete and there is no 'existence of dispute' and there is a 'debt' and 'default' then the Adjudicating Authority is bound to admit the application.

Thus, NCLAT upheld NCLT's decision and also noted that such action cannot continue as the Code will prevail over SARFAESI Act, 2002.

### Answer 3 (a)(ii)

As per section 54A of the Insolvency and Bankruptcy Code, 2016, an application for initiating pre-packaged insolvency resolution process may be made in respect of a corporate debtor classified as a micro, small or medium enterprise under subsection (1) of section 7 of the Micro, Small and Medium Enterprises Development Act, 2006. MSME thresholds are as under:

Class	Capital Investment in Plant and Machinery or Equipment (Crore)	Cap in Turnover (Crore)	Applicability of Pre-pack
Micro Enterprise	1	5	Yes
Small Enterprise	10	50	Yes
Medium Enterprise	50	250	Yes

Super Limited will be treated as medium enterprise since its turnover and capital investment in plant and machinery is less than Rs 250 crore and Rs 50 crore respectively.

Without prejudice to sub-section (1), an application for initiating pre-packaged insolvency resolution process may be made in respect of a corporate debtor, who commits a default referred to in section 4, subject to the following condition:

-it is eligible to submit a resolution plan under section 29A of the Insolvency and Bankruptcy Code, 2016.

Section 29A of the Insolvency and Bankruptcy Code, 2016 states that a person shall not be eligible to submit a resolution plan, if such person, or any other person acting jointly or in concert with such person:

-at the time of submission of the resolution plan has an account, or an account of a corporate debtor under the management or control of such person or of whom such person is a promoter, classified as non-performing asset in accordance with the guidelines of the Reserve Bank of India issued under the Banking Regulation Act, 1949 or the guidelines of a financial sector regulator issued under any other law for the time being in force, and at least a period of one year has lapsed from the date of such classification till the date of commencement of the corporate insolvency resolution process of the corporate debtor.

Since the account of Duper Limited which is wholly owned subsidiary of Super Limited and under the control of Rohan is also classified as non-performing asset, Super Limited will not be eligible for pre-packaged insolvency resolution process irrespective of the fact that Super Limited is a medium enterprise as per section 54A of the Insolvency and Bankruptcy Code, 2016.

### Answer 3 (a)(iii)

As per section 54D of the Insolvency and Bankruptcy Code, 2016:

-The pre-packaged insolvency resolution process shall be completed within a period of one hundred and twenty days from the pre-packaged insolvency commencement date.

-Without prejudice to sub-section (1), the resolution professional shall submit the resolution plan, as approved by the committee of creditors, to the Adjudicating Authority under sub-section (4) or sub-section (12), as the case may be, of section 54K, within a period of ninety days from the pre-packaged insolvency commencement date.

Considering the above, the contention of one of the lenders is legally not correct that it may take years to complete the process.

### Answer 3 (a)(iv)

As per section 54C of the Insolvency and Bankruptcy Code, 2016, the corporate applicant shall, along with the application, furnish:

a) the declaration, special resolution or resolution, as the case may be, and the approval of financial creditors for initiating pre-packaged insolvency resolution process in terms of section 54A;

b) the name and written consent, in such form as may be specified, of the insolvency professional proposed to be appointed as resolution professional, as approved under clause (e) of sub-section (2) of section 54A, and his report as referred to in clause (a) of sub-section (1) of section 54B;

c) a declaration regarding the existence of any transactions of the corporate debtor that may be within the scope of provisions in respect of avoidance of transactions under Chapter III or fraudulent or wrongful trading under Chapter VI, in such form as may be specified;

d) information relating to books of account of the corporate debtor and such other documents relating to such period as may be specified.

Accordingly, the contention of Rohan is not correct.

### Question 4.

(a) *Raghu owns a toy shop at the ground floor of his house in a remote village in the state of Chhattisgarh. He deals in selling toys for kids below 5 years. Due to short circuit in his house, all the toys were destroyed and he could not recover any of them and suffered a huge loss. He used to purchase the toys from his savings as well as the borrowings from the local lenders. His total outstanding borrowings from the lenders were ₹ 39,000 including a loan amounting to ₹ 7,000, he obtained for his elder daughter for her studies. His annual income never exceeded ₹ 50,000 and only owns a house which is worth ₹ 20,000. He is also liable to pay a fine to the local court because of the electricity theft he committed 2 years back. Given his financial condition he has still not paid the said fine amounting to ₹ 5,900. He is now contemplating filing an application before the relevant adjudicating authority for a fresh start process. His wife who is a teacher in a local school has suggested him to nominate her brother Karan, resident of Raipur, to act as a resolution professional and assist Raghu in filing an application for fresh start process. During the discussions between Raghu and Karan, Karan mentioned that in one of the large case, disciplinary committee of the Insolvency and Bankruptcy Board of India has initiated proceedings against him. However, since this is a small case within the family, he can act as resolution professional.*

*Considering the above facts, answer the following questions:*

*(i) Whether Raghu is eligible for making an application for a fresh start process?*

*(ii) Compute total eligible qualifying debt.*

*(iii) Whether the contention of Karan to act as resolution professional is correct?*

*(2 marks each)*

*(b) In respect of an order of the adjudicating authority regarding approval of the resolution plan it was informed by a practicing lawyer to Rinku that appeal before the National Company Law Appellate Tribunal (NCLAT) can only be filed within 30 days of the receipt of the order in case of matters other than approval of the resolution plan. Once the resolution plan is approved by the adjudicating authority, it cannot be challenged at all. Examine the correctness of the statement made by the practicing lawyer in light of the provisions of the Insolvency and Bankruptcy Code, 2016.*

(6 marks)

**Answer 4 (a)(i)**

As per section 80 of the Insolvency and Bankruptcy Code, 2016, a debtor may apply, either personally or through a resolution professional, for a fresh start under this Chapter in respect of his qualifying debts to the Adjudicating Authority if:

- (a) the gross annual income of the debtor does not exceed sixty thousand rupees;
- (b) the aggregate value of the assets of the debtor does not exceed twenty thousand rupees;
- (c) the aggregate value of the qualifying debts does not exceed thirty-five thousand rupees.

Considering the above, since Raghu's annual income, aggregate value of the assets and aggregate value of the qualifying debts doesn't cross the above limits, he is eligible to make an application under fresh start process.

**Answer 4 (a)(ii)**

As per section 79(19) of the Insolvency and Bankruptcy Code, 2016, "qualifying debt" means amount due, which includes interest or any other sum due in respect of the amounts owed under any contract, by the debtor for a liquidated sum either immediately or at certain future time and does not include excluded debt. As per section 79(15) of the Insolvency and Bankruptcy Code, 2016, excluded debt means:

- liability to pay fine imposed by a court or tribunal.
- liability in relation to a student loan.

Accordingly, as per the above provisions, the qualifying debt is as under:

Total debt: Rs 39,000

Less: student loan: (Rs 7,000)

**Qualifying debt: Rs 32,000**

**Answer 4 (a)(iii)**

Section 82 of the Insolvency and Bankruptcy Code, 2016, provides that where an application under Section 80 is filed by the debtor through a Resolution Professional, the Adjudicating Authority shall direct the Board within seven days of the date of receipt of the application and shall seek confirmation from the Board that there are no disciplinary proceedings against the Resolution Professional who has submitted such application.

The Board shall communicate to the adjudicating authority in writing either:

- Confirming the appointment of the Resolution Professional who filed an application or
- Rejecting the appointment of the Resolution Professional who filed an application and nominating a Resolution Professional suitable for the fresh start process

Considering the above provisions, contentions of Karan is not correct since disciplinary proceedings are already initiated against him by the Board.

#### Answer 4 (b)

Section 61 of the Insolvency and Bankruptcy Code, 2016 provides that notwithstanding anything to the contrary contained under the Companies Act 2013, any person aggrieved by the order of the adjudicating authority in the context of corporate insolvency resolution process or liquidation of corporate person may prefer an appeal to the National Company Law Appellate Tribunal (NCLAT).

Every appeal before NCLAT shall be filed within thirty days (30 days) from the date of receipt of such order. However, NCLAT may allow one time extension of fifteen days (15 days) to file an appeal after the expiry of 30 days if it is satisfied that there was sufficient cause for not filing the appeal within first 30 days

An appeal against an order approving a resolution plan under Section 31 of the Insolvency and Bankruptcy Code, 2016 may be filed on the following grounds:

- The approved resolution plan is in contravention of the provisions of any law for the time being in force;
- There has been material irregularity in exercise of the powers by the resolution professional during the corporate insolvency resolution period;
- The debts owed to operational creditors of the corporate debtor have not been provided for in the resolution plan in the manner specified by the Insolvency and Bankruptcy Board of India ("Board");
- The insolvency resolution process costs have not been provided for repayment in priority to all other debts;
- The resolution plan does not comply with any other criteria specified by the Board.

Accordingly, the statement made by the practicing lawyer is not correct.

#### Question 5.

(a) *Ram and Suman are 3rd year law students. During a joint discussion on the process of law making, both of them were debating and discussing on the Insolvency and Bankruptcy Code, 2016 (the Code). Ram said that finance minister is the sole authority to decide on what should form part of any law and approves the construct of the sections based on the suggestions given by the employees working in the Ministry of Finance. However, Suman had altogether a different perspective and said that law making is a structured process and, in many situations, proper committees are formed which are headed by an eminent person in the relevant field to give recommendations to the government. Provide any six suggestions made by the committee which was set up to study corporate bankruptcy legal framework in India and whose report formed a basis for promulgation of the Code.*

(6 marks)

<b>Scenario</b>	<b>Observations made by Rubin on eligibility to initiate corporate insolvency resolution process (CIRP)</b>
<i>A Ltd. who owes ₹ 5 crore from B Ltd. under a contract for supply of goods</i>	<i>A Ltd. is eligible</i>
<i>C Ltd., undergoing CIRP, intends to file an application under section 7 of the Insolvency and Bankruptcy Code, 2016 (the Code) against an outstanding amounting to ₹ 70 crore from a debto</i>	<i>C Ltd. is not eligible</i>
<i>B Pvt. Ltd. has lent money to Z Ltd. Total outstanding amount including interest is ₹ 95 lakh</i>	<i>B Pvt. Ltd. is eligible</i>

*Examine whether the observations are in accordance with the provisions of the Code?*

*(6 marks)*

**Answer 5 (a)**

Highlights of the Bankruptcy Law Reforms Committee (BLRC) Report are as under:

1. The objectives of the Committee were to resolve insolvency with: lesser time involved, lesser loss in recovery, and higher levels of debt financing across instruments.
2. The Committee had recommended a consolidation of the existing legal framework, by repealing two laws and amending six others. It had proposed to repeal the Presidency Towns Insolvency Act, 1909 and the Provincial Insolvency Act, 1920. In addition, it had proposed to amend: (i) Companies Act, 2013, (ii) Sick Industrial Companies (Special Provisions) Repeal Act, 2013, (iii) Limited Liability Partnership Act, 2008, (iv) Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002, (v) Recovery of Debts due to Banks and Financial Institutions Act, 1993 and (vi) Indian Partnership Act, 1932.
3. The Committee had proposed to establish a creditors committee, where the financial creditors will have votes in proportion to their magnitude of debt.
4. The creditors committee would undertake negotiations with the debtor, to come up with a revival or repayment plan.
5. The report outlined the procedure for insolvency resolution for companies and individuals. The process may be initiated by either the debtor or the creditors.
6. At that time, only secured financial creditors (creditors holding collateral against loans), could file an application for declaring a company sick. The Committee had proposed that operational creditors, such as employees whose salaries are due, be allowed to initiate the insolvency resolution process (IRP).
7. The entire IRP would be managed by a licensed insolvency professional. During the IRP, the professional would control and manage the assets of the debtor, to ensure that they are protected, while the negotiations take place.
8. The Committee had proposed to set up Insolvency Professional Agencies. The agencies would admit insolvency professionals as members and develop a code of conduct.
9. The report recommended speedy insolvency resolution and time bound negotiations between creditors and the debtors. To ensure this, a 180-day time period for completion of the IRP was recommended. For cases with high complexity, this time period could be extended by 90 days, if 75% of the creditors agree.
10. The Committee had proposed to establish information utilities which would maintain a range of information about firms, and thus avoid delays in the IRP, typically caused by a lack of data.
11. The Committee had proposed to establish the Insolvency and Bankruptcy Board of India as the regulator, to maintain oversight over insolvency resolution in the country. The Board would regulate the insolvency professional agencies and information utilities, in addition to making regulations for insolvency resolution in India.
12. The Committee proposed two Tribunals to adjudicate grievances under the law: (i) the National Company Law Tribunal would continue to have jurisdiction over insolvency resolution and liquidation of companies and limited liability partnerships; and (ii) the debt recovery tribunal would have jurisdiction over insolvency and bankruptcy resolution of individuals.

**Answer 5 (b)**

As per section 11 of the Insolvency and Bankruptcy Code, 2016, the following persons shall not be entitled to make an application to initiate corporate insolvency resolution process:

-a corporate debtor undergoing a corporate insolvency resolution process or a pre-packaged insolvency resolution process; or

-a financial creditor or an operational creditor of a corporate debtor undergoing a pre-packaged insolvency resolution process; or;

-a corporate debtor having completed corporate insolvency resolution process twelve months preceding the date of making of the application; or



-a corporate debtor in respect of whom a resolution plan has been approved under Chapter III-A, twelve months preceding the date of making of the application; or

-a corporate debtor or a financial creditor who has violated any of the terms of resolution plan which was approved twelve months before the date of making of an application under this Chapter; or

-a corporate debtor in respect of whom a liquidation order has been made.

Explanation [I]. - For the purposes of this section, a corporate debtor includes a corporate applicant in respect of such corporate debtor.

Explanation II.- For the purposes of this section, it is hereby clarified that nothing in this section shall prevent a corporate debtor referred to in clauses (a) to (d) from initiating corporate insolvency resolution process against another corporate debtor.

Further as per Section 4 read with Notification No. S.O. 12505 (E), dated 24th March, 2020, the Central Government has specified Rs 1 crore as the minimum amount of default for the purpose of section 4.

Considering the above provisions, the correct answers are as under:

<b>Scenario</b>	<b>Observations made by Rubin on eligibility to initiate corporate insolvency resolution process (CIRP)</b>	<b>Correct Answer</b>
A Limited who owes Rs 5 crore from B Limited under a contract for supply of goods	A Limited is eligible	Yes, the observation is correct
C Limited, undergoing CIRP, intends to file an application under section 9 of the Insolvency and Bankruptcy Code, 2016 (the Code) against an outstanding amounting to Rs 70 crore from a debtor	C Limited is not eligible	No, the observation is not correct
B Pvt. Ltd. has lent money to Z Ltd. Total outstanding amount including interest is Rs 95 lakh	B Pvt. Ltd. is eligible	No, the observation is not correct

### Question 6.

(a) Whether the application for initiating fast track insolvency resolution process can be made in respect of the following companies? Examine.

S. No.	Scenario
1.	A Ltd., an unlisted company having assets amounting to ₹ 99 lakh as per latest audited financial statements of the immediately preceding financial year.
2.	Network LLP which was incorporated in the year 2005 having peak turnover of ₹ 20 crore in the FY 2012-13. Network LLP's business is such that it generates very high employment. B Pvt. Ltd. was demerged in the year 2005 from Cable Ltd. B Pvt. Ltd. clocked peak turnover of ₹ 22 crore in FY 2011-12 and is engaged in the business which results in the improvement and development of products.
3.	A Ltd., a listed company having assets amounting to ₹ 55 lakh as per latest audited financial statements of the immediately preceding financial year.

4.	<i>Tom Pvt. Ltd. is having paid up capital of ₹ 35 lakh. It has turnover amounting to ₹ 1 crore as per the profit &amp; loss account for the immediately preceding financial year.</i>
5.	<i>Z Ltd., a dormant company is having assets amounting to ₹ 6.5 crore as per the last available financial statements.</i>
6.	

(b) *Legal consultant of Keval Ltd. has informed to the Board of directors that the company cannot evaluate voluntary liquidation just to save cost and time involved in ensuring compliances irrespective of the fact that presently the company does not have any business. Examine the contention of the legal consultant in light of the relevant case law.*

(6 marks)

**Answer 6 (a)**

According to Section 55 of the Insolvency and Bankruptcy Code, 2016, a corporate insolvency resolution process carried out in accordance with this Chapter IV of Part II of the Code shall be called as fast track corporate insolvency resolution process.

The Ministry of Corporate Affairs vide notification dated 14th June, 2017 notified the provisions of section 55 to section 58 of the Code. Moreover, it notified that an application for fast-track corporate insolvency resolution process may be made in respect of the following corporate debtors:

-a small company as defined under clause (85) of section 2 of Companies Act, 2013;

-a startup (other than the partnership firm) as defined in the notification of the Government of India in the Ministry of Commerce and Industry number G.S.R. 501(e), dated the 23rd May, 2017 published in the Gazette of India, extraordinary, Part II, Section 3, Subsection (i), dated the 23rd May, 2017; or

-an unlisted company with total assets, as reported in the financial statement of the immediately preceding financial year, not exceeding rupees one crore.

As per the notification by the Ministry of Commerce and Industry dated 23rd May, 2017, an entity shall be considered as a Startup:

-if it is incorporated as a private limited company (as defined in the Companies Act, 2013) or registered as a partnership firm (registered under section 59 of the Partnership Act, 1932) or a limited liability partnership (under the Limited Liability Partnership Act, 2008) in India; and -

-up to seven years from the date of its incorporation/ registration; however, in the case of Startups in the biotechnology sector, the period shall be up to ten years from the date of its incorporation/registration; and

-if its turnover for any of the financial years since incorporation/ registration has not exceeded Rupees 25 crores; and

-if it is working towards innovation, development or improvement of products or processes or services, or if it is a scalable business model with a high potential of employment generation or wealth creation.

Provided that any such entity formed by splitting up or reconstruction of a business already in existence shall not be considered a 'Startup'.

Section 2(85) of the Companies Act, 2013 small company means a company, other than a public company paid-up share capital of which does not exceed fifty lakh rupees or such higher amount as may be prescribed which shall not be more than ten crore rupees and turnover of which as per last profit and loss account for the immediately preceding financial year does not exceed two crore rupees or such higher amount as may be prescribed which shall not be more than one hundred crore rupees.

**According to the above provisions the correct answers are as under:**

S. No.	Scenario	Correct Answer
1	A Limited an unlisted company having total assets amounting to Rs 99 lakh as per latest audited financial statements of the immediately preceding financial year.	Yes
2	Network LLP which was incorporated in the year 2005 having peak turnover of Rs 20 crore in the FY 2012-13. Network LLP's business is such that it generates very high employment.	No
3	B Pvt. Ltd. was demerged in the year 2005 from Cable Ltd. B Pvt. Ltd. clocked peak turnover of Rs 22 crore in FY 11-12 and is engaged in the business which results in the improvement and development of products.	No
4	A Limited a listed company having assets amounting to Rs 55 lakh as per latest audited financial statements of the immediately preceding financial year.	No
5	Tom Pvt. Ltd. is having paid up capital of Rs 35 lakh. It has turnover amounting to Rs 1 crore as per the profit & loss account for the immediately preceding financial year.	Yes
6	Z Limited a dormant company having assets amounting to Rs 6.5 crore as per the last available financial statements.	No

**Answer 6 (b)**

Contention of the legal consultant that the company cannot evaluate voluntary liquidation just to save cost and time involved in ensuring compliances irrespective of the fact that presently the company doesn't have any business, is not correct. This can be explained through a decided case in the matter of Nippei Toyoma India Private limited.

The petition was filed by Nippei Toyoma India Private limited to initiate voluntary liquidation proceedings under Section 59 of Insolvency and Bankruptcy Code, 2016 (IBC) before NCLT, Mumbai Bench.

*The facts of the case are as under:*

The Company was incorporated under the provisions of Companies Act, 1956 on 27<sup>th</sup> April, 2007. It was engaged in the business of providing engineering services and trading of automotive components for automotive industries. The Company does not have any operations and not carrying on any business activities.

Considering the cost and time involved in ensuring compliances regarding the Company, the members of the Company in their Extra Ordinary General Meeting held on 28th September, 2017 resolved to voluntarily liquidate the Company. The directors of the Company declared on affidavit dated 27th September, 2017 that they have made full inquiry into the affairs of the Company, and are of the opinion that the Company has no debts/will be able to pay its debt in full from the proceeds of assets to be sold in the voluntary liquidation and that it is not being wound-up to defraud any person. The directors have appended to the aforesaid affidavit, audited financial statements and record of business operations of the company of previous two financial years viz. year ending on 31st March, 2016 and 31<sup>st</sup> March, 2017. The statement of payment to stakeholders, annexed to the petition, detailed the payment made to various stakeholders and Dividend Distribution Tax. Post the aforementioned payment, the accumulated profit of Rs.53,06,973/- as dividend and investment in share capital of Rs.1,00,00,000/- were paid to the members of the company thereby the assets of the company were fully liquidated. The Independent Auditor certified that during the liquidation period 28th September, 2017 to 23rd July, 2018 the proper books of accounts were kept and the said financial statements comply with the accounting standards under section 133 of Companies Act 2013.

Further, it certified that there is no pending litigation involving the Company, there are no long-term contracts with the Company for which there may be any foreseeable losses and there is no amount which is to be transferred to the Investor Education and Protection Fund by the Company. The copy of the final report of the Liquidator dated 12th September, 2018 was annexed to the petition, stating how the liquidation process has been conducted from 28th September, 2017 to 12<sup>th</sup> September, 2018, that all the assets of the Company have been discharged to the satisfaction of the creditors and that no litigation is pending against the company. The said Final report of the liquidator was submitted with the registrar of Companies vide Form GNL-2 dated 13th September, 2018. The Liquidator had filed this petition before the Tribunal under section 59(7) of the Code seeking order of dissolution of the Company. NCLT noted that on examining the submission made by the counsel appearing for the petitioner and the documents annexed to the petition, it appears that the affairs of the company have been completely wound- up, and its assets completely liquidated. NCLT in view of the above facts and circumstances and Final report of the liquidator directed that the Company shall be dissolved from the date of its order. The Petitioner was further directed to serve a copy of the order upon the registrar of Companies, with which the Company is registered, within fourteen days of receipt of the order.