



40th National Convention of Company Secretaries

Theme: Vision 2020 : Transform, Conform and Perform

Dates: October 4, 5 & 6, 2012

**Venue: Aamby Valley, Aamby Valley City, Ambavane, Dist. Pune
Maharashtra (Near Lonavala)**



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Theme Articles

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THEME

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EMERGING ROLE OF COMPANY SECRETARIES IN EMPLOYMENT : A STUDY

PROF. J P SHARMA* & SONIA THAKKAR VIJ**

Introduction

Over the years, the status and stature of the company secretaries have grown considerably. A company secretary is no more a clerk or record keeper but the principal officer of the company. There are many quantitative and qualitative changes in the job profile of a company secretary. The corporate sector in India has witnessed several developments since independence of the country. Modern business administration has become so complex and its procedures and practices so difficult that it became must for company management to have an executive head possessing professional skills so as to perform the statutory duties as well as numerous administrative responsibilities in conformity with overall corporate objectives. The Companies Act encompasses a voluminous set of rules, forms, sections, schedules, annexure, appendices and ministerial guidelines. Besides compliance with the provisions of the Companies Act, there are several other economic laws such as Competition Act, Foreign Exchange Management Act, Insurance (Development & Regulation) Act, Securities and Exchange Board of India Act, the provisions of which have to be complied with by the companies. A number of returns/ forms have to be filed, a number of statutory registers have to be maintained. Therefore, all these activities require a professional who has a good deal of professional skills acquired through specialized study, training and experience. Moreover, change in the position of company secretaries over the years is also the result of the liberalization and relaxation of controls policy adopted by the Government of India in the eighties with a view to opening up the economy. The Government began to rely on professionals so as to perpetuate its policy of control by exception. This attitude of the Government gave more responsibility to professionals in the governance of corporate sector. The company secretaries of today are expected to play the role as a compliance officer, as a coordinator, as an integrator, as a counselor, as a confidant of the Board of Directors and various other roles.

Purpose of the Study and Hypotheses

The present study is undertaken with a view to analyse the role(s) played by company secretaries in employment in India and to explore the emerging areas for company secretaries

* Professor of Corporate Governance & Law, Department of Commerce, Delhi School of Economics, University of Delhi.

** Assistant Professor, Dyal Singh College, University of Delhi.

in employment. For the purpose of the study, the following sets of hypotheses have been developed

Hypotheses for Company Secretaries in Employment

- H₀₁ : There is no significant difference among different segments in respect of functions performed by the company secretaries.
- H₀₂ : There is no significant difference on the basis of age in respect of functions performed by the company secretaries.
- H₀₃ : There is no significant difference on the basis of experience in respect of functions performed by the company secretaries.
- H₀₄ : There is no significant difference on the basis of qualification in respect of functions performed by the company secretaries.

Theoretical Background

The Profession of company secretaries owes its origin to the managing agency system in India. The managing agency system occupies an important place in the industrial development of the country. The origin of the managing agency system can be traced to the social and economic conditions that prevailed in India at the time when the monopoly of trade was lost by the East India Company. In the beginning of the nineteenth century, India had offered plenty of opportunities to the enterprising businessmen. However, there were certain obstacles in the way of exploitation of these business opportunities such as shortage of entrepreneurial ability; shortage of venture capital; and lack of technical and managerial know-how. The managing agency system was evolved to meet these challenges. The managing agents acted as the promoters, financiers and managers of the companies and thus contributed in a significant way in the industrial development of India. Important industries such as jute, cotton, textiles, tea, coal, iron and steel, sugar and cement owe their promotion and development to the managing agency system. However, later on the system was degenerated into a device for concentration and improper use of economic power. Due to several shortcomings and increasing malpractices in the system, it was finally abolished on April 3, 1970. The discontinuance of the system paved the way for the recognition and development of the profession of company secretaries in India,

Data Source and Methodology

The study seeks to trace the evolutionary process of the profession of company secretaries. It relies on the survey method to explore the various issues and generate empirical evidence on the basis of accepting or rejecting the hypotheses chosen for the study. Hence, the primary design of the present study is exploratory. The empirical edifice of the study rests on the researcher designed survey instrument targeted at the company secretaries in employment.

The study intended to cover nearly 250 company secretaries in employment. The questionnaire was administered to nearly 180 company secretaries in employment at the 37th National Convention of the Institute of Company secretaries of India at Hyderabad out

of which 96 questionnaires were received at the convention itself. Nearly 32 self-addressed stamped envelopes were also given to the company secretaries with a request to send them by post out of which 11 were received. The questionnaires were also sent by e-mail for the purpose of collecting necessary data. The questionnaires were mailed to nearly 115 respondents out of which 34 responded. Nearly 83 questionnaires were personally administered in Delhi out of which responses were received for 31 questionnaires. Data on 9 questionnaires could not be included in the final sample due to inadequacy of information provided by the respondents. Finally responses of 163 company secretaries in employment (65 percent) are included in the study. Besides this, discussions were also made with a number of company secretaries in employment to make the study a comprehensive one.

Major Findings

The study reveals the following facts and findings in respect of company secretaries in employment:

- (i) Classified on the basis of gender, the male respondents (85.3 percent) far exceeded their female counterpart (14.7 percent).
- (ii) The distribution of the sample on the basis of age-group shows that majority (39.9 percent) of the respondents are up to 45 years of age, only 24.5 percent respondents are in the age group of 45 to 55 years as against 35.6 percent above 55 years of age.
- (iii) The experience-wise distribution of respondents revealed that 41.1 percent respondents have more than 15 years of experience in the profession, 34.4 percent respondents have experience between 5 to 15 years and 24.5 percent respondents have up to 5 years of experience.
- (iv) The distribution of respondents by qualification indicates that more than half (58.9 percent) of the respondents are Bachelors of Law (LLB) besides being qualified company secretaries and the rest (41.10 percent) possess other qualifications such as CA, CWA, MBA, PGDBA etc. but do not possess LLB qualification.
- (v) Company secretaries working in different organizations are dealing with a wide variety of areas. Majority of the respondents (72.4 percent) are dealing with Corporate Governance issues. More than half (68.1 percent and 54.6 percent) of the respondents are dealing with Corporate and Securities Laws and Corporate Affairs. Less than half (42.9 percent) of the respondents are rendering services in Finance, Accounts and Taxation. 33.7 percent respondents are dealing with Mergers and Takeover issues and Monitoring Code of Conduct and Ethics in the organization where they are working. 20.9 percent, 21.5 percent and 28.2 percent respondents deal with IPR protection issues, Labour Laws matters and Corporate Social Responsibility matters respectively. Very few are dealing with areas such as International Trade laws (9.2 percent), IT and Cyber Laws (7.4 percent), Compensation Plans (7.4 percent) and Project Management (8 percent).
- (vi) In order to analyse the functions performed by the respondents working in different

segments, they have been grouped into four groups on the basis of frequency distribution. The groups are as follows:

- (a) Group I comprises of industries such as Banking, Insurance, Tourism and Hotel, Consulting, Stock broking, Financial Services and FMCG;
- (b) Group II comprises of industries such as Manufacturing, Engineering and Trading;
- (c) Group III comprises of Real Estate, Telecommunications, IT and Pharmaceuticals industries; and
- (d) Group IV comprises of Power, Sugar, Cement and other industries.

In order to see if significant difference exists across the four groups with respect to the functions performed by the company secretaries, chi-square test has been resorted to and the results are shown in the succeeding tables.

It is amply clear from Table 1 that there is no significant difference among the four groups in performing of Due Diligence, Representation, Advisory and Secretarial Administration functions. Hence, the null hypothesis that, “there is no significant difference among different segments in respect of functions performed by the company secretaries” fails to be rejected. Thus, it can be inferred that the company secretaries are performing all these functions in all the sectors where they are employed.

Table 1
Functions Performed by the Respondents: Segment-wise Analysis

<i>Function</i>	<i>Groups</i>				<i>Total (N= 163)</i>	<i>Chi-Square</i>
	<i>Group I (N= 30)</i>	<i>Group II (N= 51)</i>	<i>Group III (N= 47)</i>	<i>Group IV (N= 35)</i>		
Compliance	27 (90.0)	47 (92.2)	41 (87.2)	30 (85.7)	145 (89.0)	@
Due Diligence	16 (53.3)	30 (58.8)	25 (53.2)	18 (51.4)	89 (54.6)	0.57NS
Representation	12 (40.0)	30 (58.8)	18 (38.3)	14 (40.0)	74 (45.4)	5.43NS
Advisory	12 (40.0)	26 (51.0)	24 (51.1)	20 (57.1)	82 (50.3)	1.95NS
Secretarial Administration	23 (76.7)	40 (78.4)	31 (66.0)	27 (77.1)	121 (74.2)	2.40NS
Any Other	2 (6.7)	3 (5.9)	4 (8.5)	4 (11.4)	13 (8.0)	@

NS : Not Significant

@ : Chi-Square cannot be computed as in some cells the expected frequency is less than 5.

Note: Figures in parenthesis are the percentages.

(vii) As is evident from Table 2 significant differences on the basis of age exists in performing of Representation, Advisory and Secretarial Administration Functions. It may be observed from the table below that the number of company secretaries performing Representation and Advisory function is more in the age group of 45 years and above than those below 45 years of age. Further, the number of company secretaries performing Secretarial Administration function is more below 55 years of age as compared to those above 55 years of age. This may be because of the reason that company secretaries in higher age groups are more experienced to perform important functions such as advisory functions in the organization and are therefore given the responsibility of advising on matters of strategic importance whereas comparatively younger and less experienced company secretaries are assigned the responsibility of performing the routine administrative functions in the organisation. However, there is no significant difference on the basis of age in performing of Due Diligence Function. Hence, the findings documented in Table 2 may be seen as an affirmation of the partial acceptance of the null hypothesis that, “there is no significant difference on the basis of age in respect of functions performed by the company secretaries”.

Table 2
Functions Performed by the Respondents : Age-wise Analysis

<i>Function</i>	<i>Age</i>			<i>Total (N= 163)</i>	<i>Chi-Square</i>
	<i>Upto 45yrs (N= 65)</i>	<i>45-55yrs (N= 40)</i>	<i>Above 55yrs (N= 58)</i>		
Compliance	58 (89.2)	38 (95.0)	49 (84.5)	145 (89.0)	@
Due Diligence	29 (44.6)	27 (67.5)	33 (56.9)	89 (54.6)	5.42NS
Representation	22 (33.8)	25 (62.5)	27 (46.6)	74 (45.4)	8.25*
Advisory	24 (36.9)	24 (60.0)	34 (58.6)	82 (50.3)	7.76*
Secretarial Administration	48 (73.8)	35 (87.5)	38 (65.5)	121 (74.2)	5.99*
Any Other	5 (7.7)	2 (5.0)	6 (10.3)	13 (8.0)	@

* : Significant at .05 level. NS : Not Significant.

@ : Chi-Square cannot be computed as in some cells, the expected frequency is less than 5.

Note : Figures in parenthesis are the percentages.

- (viii) Different compliance functions performed by the respondents on the basis of age are shown in Table 3. From the table, it may be observed that significant difference on the basis of age exists in performing of Compliance Functions such as establishing internal policies/ procedures, monitoring activities within the firm, providing training to employees/ management on compliance. This may be because all these functions require requisite experience and that is why company secretaries in higher age groups are preferred for such functions. However, no significant difference on the basis of age exists in respect of reporting on non-compliance to concerned authorities.

Table 3

Compliance Functions Performed by the Respondents : Age-wise Analysis

Compliance Function	Age			Total (N= 163)	Chi-Square
	Upto 45yrs (N= 65)	45-55yrs (N= 40)	Above 55yrs (N= 58)		
Regulatory Filing	59 (90.8)	36 (90.0)	49 (84.5)	144 (88.3)	@
Establishing Internal Policies/ Procedures	19 (29.2)	21 (52.5)	40 (69.0)	80 (49.1)	19.61**
Monitoring Activities within the Firm	18 (27.7)	19 (47.5)	33 (56.9)	70 (42.9)	11.12**
Providing Training to Employees/ Management on Compliance	5 (7.7)	12 (30.0)	21 (36.2)	38 (23.3)	15.27**
Report on Non-compliance to Concerned Authorities	22 (33.8)	15 (37.5)	23 (39.7)	60 (36.8)	0.46NS
Any Other	1 (1.5)	–	1 (1.7)	2 (1.2)	@

** : Significant at .01level. NS : Not Significant.

@ : Chi-Square cannot be computed as in some cells, the expected frequency is less than 5.

Note : Figures in parenthesis are the percentages.

- (ix) It can be noticed from Table 4 that significant difference on the basis of age exists in performing of Advisory functions such as advisory on mergers & acquisitions, advisory

on new business initiatives and advisory on public offerings. However, no significant difference on the basis of age exists in respect of all other Advisory functions such as advisory on amendment in laws, advisory on settlement of disputes, advisory on business agreements, advisory on compliance issues, advisory on day-to-day management issues, advisory on corporate borrowings and advisory on international trade.

Table 4
Advisory Functions Performed by the Respondents: Age-wise Analysis

<i>Advisory Function</i>	<i>Age</i>			<i>Total (N= 163)</i>	<i>Chi-Square</i>
	<i>Upto 45yrs (N= 65)</i>	<i>45-55yrs (N= 40)</i>	<i>Above 55yrs (N= 58)</i>		
Advisory on Mergers & Acquisitions	12 (18.5)	17 (42.5)	22 (37.9)	51 (31.3)	8.50**
Advisory on Amendment in Laws	37 (56.9)	25 (62.5)	36 (62.1)	98 (60.1)	0.46NS
Advisory on Settlement of Disputes	14 (21.5)	12 (30.0)	17 (29.3)	43 (26.4)	1.31NS
Advisory on New Business Initiatives	16 (24.6)	8 (20.0)	26 (44.8)	50 (30.7)	8.73**
Advisory on Business Agreements	24 (36.9)	19 (47.5)	30 (51.7)	73 (44.8)	2.87NS
Advisory on Compliance Issues	37 (56.9)	31 (77.5)	41 (70.7)	109 (66.9)	5.33NS
Advisory on Public Offerings	5 (7.7)	19 (47.5)	20 (34.5)	44 (27.0)	22.47**
Advisory on Day-to-Day Management Issues	25 (38.5)	17 (42.5)	29 (50.0)	71 (43.6)	1.68NS
Advisory on Corporate Borrowings	17 (26.2)	14 (35.0)	26 (44.8)	57 (35.0)	4.70NS
Advisory on International Trade Agreements	7 (10.8)	6 (15.0)	12 (20.7)	25 (15.3)	2.33NS
Any Other	2 (3.1)	1 (2.5)	2 (3.4)	5 (3.1)	@

** : Significant at .01level. NS : Not Significant.

@ : Chi-Square cannot be computed as in some cells, the expected frequency is less than 5.

Note : Figures in parenthesis are the percentages.

- (x) Table 5 shows the different representation functions performed by the respondents in the three age groups. Significant difference on the basis of age is there in respect of the two Representation Functions such as representing employer before judicial/ quasi-judicial bodies and representing employer before regulatory authorities. It may be observed that the number of company secretaries representing employer before judicial/ quasi-judicial bodies and before regulatory authorities are more in the age group of 45 years and above. Thus, it can be inferred that the companies assign the responsibilities of representing employers before various regulatory authorities to the senior company secretaries who are more experienced.

Table 5

Representation Functions Performed by the Respondents: Age-wise Analysis

Representation Function	Age			Total (N= 163)	Chi-Square
	Upto 45yrs (N= 65)	45-55yrs (N= 40)	Above 55yrs (N= 58)		
Represent Employer before Judicial/ Quasi-judicial Bodies	22 (33.8)	21 (52.5)	32 (55.2)	75 (46.0)	6.51*
Represent Employer before Regulatory Authorities	34 (52.3)	28 (70.0)	43 (74.1)	105 (64.4)	7.09*
Liaison with Shareholders, Employees, Customers etc.	42 (64.6)	31 (77.5)	40 (69.0)	113 (69.3)	1.94NS
Represent Employer before Foreign Regulators	7 (10.8)	5 (12.5)	4 (6.9)	16 (9.8)	@
Any Other	1 (1.5)	–	1 (1.7)	2 (1.2)	@

* : Significant at .05 level.

NS : Not Significant.

@ : Chi-Square cannot be computed as in some cells, the expected frequency is less than 5.

Note : Figures in parenthesis are the percentages.

- (xi) From Table 6 it may be observed that there is no significant difference on the basis of age in performing of Secretarial functions such as convene meetings, drafting and sending notices of meetings, drafting minutes of meetings, maintaining registers and filing returns. However, difference on the basis of age is found to be significant in respect of counting resolutions. It is clear from the table below that the number of respondents performing this function is more up to 55 years of age than those above 55 years of age. This may be because it is a routine administrative function and does not require higher experience and expertise.

Table 6

Secretarial Functions Performed by the Respondents: Age-wise Analysis

<i>Secretarial Function</i>	<i>Age</i>			<i>Total (N= 163)</i>	<i>Chi-Square</i>
	<i>Upto 45yrs (N= 65)</i>	<i>45-55yrs (N= 40)</i>	<i>Above 55yrs (N= 58)</i>		
Convene Meetings	58 (89.2)	35 (87.5)	48 (82.8)	141 (86.5)	1.14NS
Drafting & Sending Notices of Meetings	57 (87.7)	35 (87.5)	47 (81.0)	139 (85.3)	1.30NS
Drafting Minutes of Meetings	57 (87.7)	36 (90.0)	47 (81.0)	140 (85.9)	1.86NS
Maintaining Registers	54 (83.1)	34 (85.0)	42 (72.4)	130 (79.8)	3.06NS
Filing Returns	56 (86.2)	33 (82.5)	43 (74.1)	132 (81.0)	2.95NS
Counting Resolutions	44 (67.7)	27 (67.5)	26 (44.8)	97 (59.5)	8.05*
Any Other	2 (3.1)	–	3 (5.2)	5 (3.0)	@

* : Significant at .05 level.

NS : Not Significant.

@ : Chi-Square cannot be computed as in some cells, the expected frequency is less than 5.

Note : Figures in parenthesis are the percentages.

- (xii) As shown in Table 7, there is no significant difference on the basis of experience in respect of Due Diligence and Secretarial Administration functions. However, difference on the basis of experience is found to be significant in performing of Representation and Advisory functions. It is amply clear from the table that the

number of company secretaries performing these functions is more with higher experience than those with lesser experience. On the basis of the above empirical evidence, the null hypothesis that, “there is no significant difference on the basis of experience in respect of functions performed by the company secretaries”, is partially accepted. Thus, it can be inferred from the table below that job of performing important functions such as Representation and Advisory functions are assigned to senior and more experienced company secretaries working in the companies.

Table 7

Functions Performed by the Respondents: Experience-wise Analysis

<i>Function</i>	<i>Experience</i>			<i>Total (N= 163)</i>	<i>Chi-Square</i>
	<i>Upto 5 yrs (N= 40)</i>	<i>5-15yrs (N= 56)</i>	<i>Above 15yrs (N= 67)</i>		
Compliance	34 (85.0)	52 (92.9)	59 (88.1)	145 (89.0)	@
Due Diligence	21 (52.5)	26 (46.4)	42 (62.7)	89 (54.6)	3.35NS
Representation	13 (32.5)	23 (41.1)	38 (56.7)	74 (45.4)	6.57*
Advisory	15 (37.5)	22 (39.3)	45 (67.2)	82 (50.3)	12.96**
Secretarial Administration	31 (77.5)	43 (76.8)	47 (70.1)	121 (74.2)	0.99NS
Any Other	3 (7.5)	5 (8.9)	5 (7.5)	13 (8.0)	@

* : Significant at .05 level.

** : Significant at .01level.

NS : Not Significant.

@ : Chi-Square cannot be computed as in some cells, the expected frequency is less than 5.

Note : Figures in parenthesis are the percentages.

- (xiii) It may be observed from Table 8 that there is a significant difference on the basis of experience in performing of Compliance Functions such as establishing internal policies/ procedures, monitoring activities within the firm, providing training to employees/ management on compliance. The number of company secretaries performing these functions is more with experience of more than 15 years. This may be because of the reason that performance of these functions requires seniority, intellect as well as experience and that is why these function are assigned to the senior and more experienced company secretaries in the companies.

Table 8

Compliance Functions Performed by the Respondents:
Experience-wise Analysis

<i>Compliance Function</i>	<i>Experience</i>			<i>Total (N= 163)</i>	<i>Chi-Square</i>
	<i>Upto 5 yrs (N= 40)</i>	<i>5-15yrs (N= 56)</i>	<i>Above 15yrs (N= 67)</i>		
Regulatory Filing	35 (87.5)	51 (91.1)	58 (86.6)	144 (88.3)	@
Establishing Internal Policies/ Procedures	11 (27.5)	27 (48.2)	42 (62.7)	80 (49.1)	12.43**
Monitoring Activities within the Firm	11 (27.5)	22 (39.3)	37 (55.2)	70 (42.9)	8.32*
Providing Training to Employees/ Management on Compliance	3 (7.5)	10 (17.9)	25 (37.3)	38 (23.3)	13.87**
Report on Non-Compliance to Concerned Authorities	14 (35.0)	22 (39.3)	24 (35.8)	60 (36.8)	0.23NS
Any Other	1 (2.5)	–	1 (1.5)	2 (1.2)	@

* : Significant at .05 level.

** : Significant at .01level.

NS : Not Significant.

@ : Chi-Square cannot be computed as in some cells, the expected frequency is less than 5.

Note : Figures in parenthesis are the percentages.

- (xiv) It is noticeable from Table 9 that there is no significant difference on the basis of experience in respect of two Advisory Functions such as advisory on day-to-day management issues, and advisory on corporate borrowings. However, difference on the basis of experience is found to be significant in respect of all other functions such as advisory on mergers and acquisitions, advisory on amendment in laws, advisory on settlement of disputes, advisory on new business initiatives, advisory on business agreements, advisory on compliance issues.

Table 9
Advisory Functions Performed by the Respondents: Experience-wise Analysis

<i>Advisory Function</i>	<i>Experience</i>			<i>Total (N= 163)</i>	<i>Chi-Square</i>
	<i>Upto 5 yrs (N= 40)</i>	<i>5-15yrs (N= 56)</i>	<i>Above 15yrs (N= 67)</i>		
Advisory on Mergers & Acquisitions	5 (12.5)	16 (28.6)	30 (44.8)	51 (31.3)	12.43**
Advisory on Amendment in Laws	20 (50.0)	30 (53.6)	48 (71.6)	98 (60.1)	6.42*
Advisory on Settlement of Disputes	4 (10.0)	14 (25.0)	25 (37.3)	43 (26.4)	9.70**
Advisory on New Business Initiatives	6 (15.0)	17 (30.4)	27 (40.3)	50 (30.7)	7.54*
Advisory on Business Agreements	11 (27.5)	23 (41.1)	39 (58.2)	73 (44.8)	10.03**
Advisory on Compliance Issues	19 (47.5)	39 (69.6)	51 (76.1)	109 (66.9)	9.56**
Advisory on Public Offerings	3 (7.5)	11 (19.6)	30 (44.8)	44 (27.0)	19.99**
Advisory on Day-to-Day Management issues	14 (35.0)	25 (44.6)	32 (47.8)	71 (43.6)	1.70NS
Advisory on Corporate Borrowings	10 (25.0)	19 (33.9)	28 (41.8)	57 (35.0)	3.15NS
Advisory on International Trade Agreements	1 (2.5)	10 (17.9)	14 (20.9)	25 (15.3)	6.94*
Any Other	2 (5.0)	1 (1.8)	2 (3.0)	5 (3.1)	@

* : Significant at .05 level. ** : Significant at .01level.

NS : Not Significant.

@ : Chi-Square cannot be computed as in some cells, the expected frequency is less than 5.

Note : Figures in parenthesis are the percentages.

- (xv) From Table 10, it may be observed that experience is an important factor in performing Representation Functions such as representing employer before judicial/quasi-judicial bodies and regulatory authorities. Thus, it can be inferred from the table that experience does matter in performing of important Representation functions and company secretaries with higher experience are preferred for these functions

Table 10
Representation Functions Performed by the Respondents:
Experience-wise Analysis

<i>Representation Function</i>	<i>Experience</i>			<i>Total (N= 163)</i>	<i>Chi-Square</i>
	<i>Upto 5 yrs (N= 40)</i>	<i>5-15yrs (N= 56)</i>	<i>Above 15yrs (N= 67)</i>		
Represent Employer before Judicial/ Quasi-judicial Bodies	11 (27.5)	21 (37.5)	43 (64.2)	75 (46.0)	16.05**
Represent Employer before Regulatory Authorities	19 (47.5)	33 (58.9)	53 (79.1)	105 (64.4)	12.03**
Liaison with Shareholders, Employees, Customers etc.	24 (60.0)	41 (73.2)	48 (71.6)	111 (69.3)	2.20NS
Represent Employer before Foreign Regulators	2 (5.0)	9 (16.1)	5 (7.5)	16 (9.8)	@
Any other	–	1 (1.8)	1 (1.5)	2 (1.2)	@

** : Significant at .01level.

NS : Not Significant.

@ : Chi-Square cannot be computed as in some cells, the expected frequency is less than 5.

Note: Figures in parenthesis are the percentages.

- (xvi) It is amply clear from Table 11, that there is no significant difference on the basis of experience in performing of Secretarial Functions such as drafting minutes of meetings, maintaining registers, filing returns and counting resolutions. Thus, it can be inferred that experience does not matter in performing of different Secretarial functions as these are routine administrative functions and do not require much experience.

Table 11
Secretarial Functions Performed by the Respondents:
Experience-wise Analysis

<i>Secretarial Function</i>	<i>Experience</i>			<i>Total (N= 163)</i>	<i>Chi-Square</i>
	<i>Upto 5 yrs (N= 40)</i>	<i>5-15yrs (N= 56)</i>	<i>Above 15yrs (N= 67)</i>		
Convene Meetings	35 (87.5)	47 (83.9)	59 (88.1)	141 (86.5)	0.49NS
Drafting & Sending Notices of Meetings	34 (85.0)	48 (85.7)	57 (85.1)	139 (85.3)	0.01NS
Drafting Minutes of Meetings	34 (85.0)	48 (85.7)	58 (86.6)	140 (85.9)	0.05NS
Maintaining Registers	33 (82.5)	46 (82.1)	51 (76.1)	130 (79.8)	0.93NS
Filing Returns	33 (82.5)	48 (85.7)	51 (76.1)	132 (81.0)	1.90NS
Counting Resolutions	24 (60.0)	39 (69.6)	34 (50.7)	97 (59.5)	4.53NS
Any Other	2 (5.0)	1 (1.8)	2 (3.0)	5 (3.1)	@

NS : Not Significant.

@ : Chi-Square cannot be computed as in some cells, the expected frequency is less than 5.

Note : Figures in parenthesis are the percentages.

(xvii) Table 12 shows that no significant difference on the basis of qualification exists in performing of different functions by the respondents. In accordance with the table, the null hypothesis that, “there is no significant difference on the basis of qualification in respect of functions performed by the company secretaries” fails to be rejected. It is evident from the table below that qualification does not matter in performing of different functions by the respondents.

Table 12
Functions Performed by the Respondents: Qualification-wise Analysis

<i>Function</i>	<i>Qualification</i>		<i>Total (N= 163)</i>	<i>Chi-Square</i>
	<i>CS+ LLB (N= 96)</i>	<i>CS+ Others (N= 67)</i>		
Compliance	85 (88.5)	60 (89.6)	145 (89.0)	0.04NS
Due Diligence	52 (54.2)	37 (55.2)	89 (54.6)	0.02NS
Representation	46 (47.9)	28 (41.8)	74 (45.4)	0.60NS
Advisory	52 (54.2)	30 (44.8)	80 (50.3)	1.39NS
Secretarial Administration	70 (72.9)	51 (76.1)	121 (74.2)	0.21NS
Any Other	9 (9.4)	4 (6.0)	13 (8.0)	0.62NS

NS : Not Significant.

Note : Figures in parenthesis are the percentages.

(xviii) It may be observed from Table 13 that only in case of reporting non-compliance to concerned authorities, the number of company secretaries is more with other qualifications whereas in case of all other Compliance functions, there is no significant difference on the basis of qualification.

Table 13
Compliance Functions Performed by the Respondents : Qualification-wise Analysis

<i>Function</i>	<i>Qualification</i>		<i>Total (N= 163)</i>	<i>Chi-Square</i>
	<i>CS+ LLB (N= 96)</i>	<i>CS+ Others (N= 67)</i>		
Regulatory Filing	84 (87.5)	60 (89.6)	144 (88.3)	0.16NS
Establishing Internal Policies/Procedures	48 (50.0)	32 (47.8)	80 (49.1)	0.08NS
Monitoring Activities within the Firm	45 (46.9)	25 (37.3)	70 (42.9)	1.47NS
Providing Training to Employees/Management on Compliance	26 (27.1)	12 (17.9)	38 (23.3)	1.86NS
Report on Non-compliance to Concerned Authorities	28 (29.2)	32 (47.8)	60 (36.8)	5.87*
Any Other	1 (1.0)	1 (1.5)	2 (1.2)	0.000NS

* : Significant at .05 level. NS : Not Significant.

Note: Figures in parenthesis are the percentages.

- (xix) As shown in Table 14, there is no significant difference on the basis of qualification in performing of Advisory Functions such as advisory on amendments in laws, advisory on new business initiatives, advisory on compliance issues, advisory on public offerings, advisory on day-to-day management issues, advisory on corporate borrowings and advisory on international trade agreements. Further, it may be observed from the table that the number of company secretaries acting as advisory on mergers and acquisitions, settlement of disputes, and business agreements is more with LLB qualification. This may be because of the reason that these functions require in-depth knowledge of various civil as well as criminal laws and company secretaries having LLB qualification are better equipped to advise on such matters.

Table 14

Advisory Functions Performed by the Respondents : Qualification-wise Analysis

Advisory Function	Qualification		Total (N= 163)	Chi-Square
	CS+ LLB (N= 96)	CS+ Others (N= 67)		
Advisory on Mergers & Acquisitions	36 (37.5)	15 (22.4)	51 (31.3)	4.19*
Advisory on Amendment in Laws	63 (65.6)	35 (52.5)	98 (60.1)	2.95NS
Advisory on Settlement of Disputes	32 (33.3)	11 (16.4)	43 (26.4)	5.81*
Advisory on New Business Initiatives	35 (36.5)	15 (22.4)	50 (30.7)	3.67NS
Advisory on Business Agreements	51 (53.1)	22 (32.8)	73 (44.8)	6.57**
Advisory on Compliance Issues	67 (69.8)	42 (62.7)	109 (66.9)	0.90NS
Advisory on Public Offerings	29 (30.2)	15 (22.4)	44 (27.0)	1.22NS
Advisory on Day-to-Day Management Issues	47 (49.0)	24 (35.8)	71 (43.6)	2.77NS
Advisory on Corporate Borrowings	35 (36.5)	22 (32.8)	57 (35.0)	0.23NS
Advisory on International Trade Agreements	19 (19.8)	6 (9.0)	25 (15.3)	3.57NS
Any Other	4 (4.2)	1 (1.5)	5 (3.1)	0.26NS

* : Significant at .05 level. ** : Significant at .01level. NS : Not Significant.

Note : Figures in parenthesis are the percentages.

(xx) From Table 15, it may be observed that there is no significant difference on the basis of qualification in performing of Representation Functions such as liaison with shareholders, employees, customers etc. and representing employer before foreign regulators. Further, it is clear from the table that the number of company secretaries representing employer before judicial/ quasi-judicial bodies and regulatory authorities is more with LLB qualification. This may be possibly because LLB qualification gives them an edge over those who do not have LLB qualification and that is why Company secretaries with LLB qualification are preferred for representing employers before various regulatory authorities.

Table 15
Representation Functions Performed by the Respondents:

<i>Representation Function</i>	<i>Qualification</i>		<i>Total (N= 163)</i>	<i>Chi-Square</i>
	<i>CS+ LLB (N= 96)</i>	<i>CS+ Others (N= 67)</i>		
Represent Employer before Judicial/ Quasi-judicial Bodies	54 (56.3)	21 (31.3)	75 (46.0)	9.85**
Represent Employer before Regulatory Authorities	69 (71.9)	36 (53.7)	105 (64.4)	5.67*
Liaison with Shareholders, Employees, Customers etc.	64 (66.7)	49 (73.1)	113 (69.3)	0.78NS
Represent Employer before Foreign Regulators	11 (11.5)	5 (7.5)	16 (9.8)	0.71NS
Any Other	2 (2.1)	–	2 (1.2)	0.22NS

* : Significant at .05 level.

** : Significant at .01level.

NS : Not Significant.

Note : Figures in parenthesis are the percentages.

(xxi) It is amply clear from Table 16 that there is no significant difference on the basis of qualification of the respondents in performing of different Secretarial functions such as convening meetings, drafting and sending notices of meetings, drafting minutes of meetings, maintaining registers, filing returns and counting resolutions. Thus, it can be inferred from the table that qualification does not matter in performing of the secretarial functions in the organization as these are routine administrative functions and do not require any additional knowledge.

Table 16
Secretarial Functions Performed by the Respondents : Qualification-wise Analysis

<i>Secretarial Function</i>	<i>Qualification</i>		<i>Total (N= 163)</i>	<i>Chi-Square</i>
	<i>CS+ LLB (N= 96)</i>	<i>CS+ Others (N= 67)</i>		
Convene Meetings	86 (89.6)	55 (82.1)	141 (86.5)	1.90NS
Drafting & Sending Notices of Meetings	82 (85.4)	57 (85.1)	139 (85.3)	0.004NS
Drafting Minutes of Meetings	83 (86.5)	57 (85.1)	140 (85.9)	0.06NS
Maintaining Registers	77 (80.2)	53 (79.1)	130 (79.8)	0.03NS
Filing Returns	77 (80.2)	55 (82.1)	132 (81.0)	0.09NS
Counting Resolutions	57 (59.4)	40 (59.7)	97 (59.5)	0.002NS
Any Other	3 (3.1)	2 (3.0)	5 (3.1)	.000NS

NS : Not Significant.

Note : Figures in parenthesis are the percentages.

- (xxii) Nearly half (50.3 percent) of the respondents feel that the Government Authorities duly support the profession of company secretaries. Compulsory appointment of a company secretary in every company with paid-up capital of more than Rs. 5 Crore and CS being prescribed as a qualification for appearing before many authorities as well as to practice in areas such as custom/ excise, FEMA, NCLT etc. shows the supportive attitude of the Government towards the profession. Moreover, CS being designated as the “Key Managerial Personnel” in the Companies Bill, 2011 also depicts the positive attitude of the Government. Whereas, 25.2 percent respondents feel that the profession is not getting the desired support from the Government Authorities. They believe that the Company Secretaries are not treated as specialist in their own field and are not treated at par with the Chartered Accountants.
- (xxiii) 25.8 percent respondents view Company Secretary (CS) as a complete qualification in itself and feel it does not need to be supplemented by other qualifications. They believe that the course curriculum of CS course has a vast coverage that imbibe the members with expert knowledge of each subject with which he/she can deal with the overall functioning of the corporate with confidence

and provide value addition inputs to all the departments of the company. Whereas majority (67.5 percent) of the respondents feel that multiple (related) qualifications is desirable as it provides an easy entry in employment and helps in discharging one's duties better with a multi-pronged approach.

- (xxiv) Majority (64.4 percent) of the respondents are satisfied with the role played by the Institute in the promotion and development of the profession, 20.9 percent respondents find the role played by the Institute as adequate while 14.7 percent are not satisfied with the role played by the Institute and are of the view that more efforts need to be done on part of the Institute for the growth of the profession.
- (xxv) 79.1 percent respondents feel that the Institute has no role to play in cases of harassment. All the members of the Institute are bound by the code of conduct laid down by the Institute. The institute can take an action against a member in case of violation of the code of conduct. Moreover, employment of a company secretary in a company is on the basis of a contract between the company secretary and the company. However, 20.9 percent respondents feel that the Institute should play a role in cases of harassment. The Institute must come forward to protect their members if they have not done any thing wrong.

Emerging Areas for Company Secretaries in Employment

The following areas have been highlighted by the company secretaries as the emerging areas in employment:

- Corporate Governance
- Corporate Social Responsibility and Business Ethics
- HR and Administration
- Due Diligence
- International Laws, WTO, Global Environmental Issues
- IT and Cyber Laws
- Corporate Restructuring
- Mergers & Amalgamations, Takeovers, joint Ventures
- IPRs
- Internal Control System/ SOX Compliances
- Finance and Taxation (Direct & Indirect)
- Merchant Banking
- Risk Management
- Competition Law

- Investor Relations
- Arbitration
- Management Planning

Qualities/ Skills Required to Excel in Employment

Company secretaries feel that certain qualities are necessary to excel in the fast changing international business environment. They are as follows:

- Well versed with the amendments and the corporate laws/ affairs and timely compliances.
- Intelligence, presence of mind, analytical mind, eagerness to learn new things.
- Thorough knowledge of domain area, practical application of theoretical knowledge, excellent communication skills (oral & written) especially in English, fearless, dependable, confident, disciplined, presentable, fast grasper, decisive, determined in intention but flexible in approach, thirst to excel and compete within your own self.
- Articulate, sensitive to the needs of various stakeholders, ability to align different interests, manage conflict and work under pressure.
- Visionary, ability to guide and make value addition to the company through constant involvement in the company matters.
- Positive attitude and a proactive approach.
- Mastering management skills.
- To establish as an indispensable service center for not only Board of Directors but also at levels higher and down below.
- Leadership skills.
- Excellent drafting skills.
- Presentation skills.

Conclusions & Recommendations

Company secretaries in employment are no longer dealing with only company law matters and performing only routine administrative and compliance functions in the companies where they are working. In fact, they are dealing with a wide variety of areas and are performing important functions such as Advisory and Representation functions in their respective companies. However, different functions performed and areas dealt with by the company secretaries depend on the age, experience and qualification of the company secretaries

The recommendations emanating from the study are as follows:

The scope of the company secretaries' work is very vast and has enlarged with changing times. Apart from the company law, he should have the knowledge of various general laws and procedures, industrial laws and procedures, direct tax laws and tax planning, indirect

tax laws and various economic legislations. He should also be familiar with finance, accounts, management accounting, and management information system. Therefore, he should develop his skills and abilities not only with respect to every aspect of legal functions but also administrative and management functions.

A Company secretary should stay updated with the latest Laws, Legislations, Regulations, Government notifications and various amendments done to the existing laws. He should constantly upgrade his professional knowledge and expertise by reading, attending the seminars, discussions with co-professionals and qualify in the new and emerging areas.

The fast changing scenario emerging in the corporate world requires innovative ideas and expert handling. A company secretary must use his talents to transform the challenges facing the corporate world into working opportunity. In order to keep the profession alive, vibrant and dynamic, it is necessary to be actively involved as catalyst of all economic activity in the corporate hierarchy along side of management. Since, a company secretary is closely involved in the decision making process at the highest level of the corporate hierarchy, it is very much essential for him to develop new perception and priorities in the fast changing environment.

The protection of consumers' and investors' interest in the changing economic scenario is of utmost importance. The modern day company secretary should act as a custodian of public interest and therefore, should rise to the occasion to play his true role between the company and various stakeholders.

The Institute should try to create awareness among the bright students in the country about the profession and encourage them to join the course. It should enlighten them about the secured future that the profession has and the contributions they can make within and outside the country as a member of the profession.

The future of any profession depends on the quality of the professionals churned out by the Institute. Therefore, the institute must make special efforts in developing good communication and effective presentation skills among company secretaries that is vital for the profession. Moreover, a periodic review of the syllabus is essential to incorporate the changes emerging in today's globalised economy so as to keep pace with the changes and imparting necessary skills to the members to survive in this competitive environment.

The institute needs to establish good lobbying capacity by networking with the various regulatory authorities and the Government on a regular basis to place its point of view, suggestions and recommendations and get them accepted to protect and safeguard the rights and interests of its members.

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ECONOMIC VOLATILITY AND RISK MANAGEMENT

EXPLORING THE INDIAN CONTEXT

PROF. GOPAL KRISHNA AGARWAL*

Introduction

Economic Volatility triggers upheavals in the economy of the country, adding to global business risks and uncertain performance of the corporate sector. The investors become quite reserve to invest further, the investors' confidence is shaken and sometimes invested funds are withdrawn from the system and the economy feels the heat of cash crunch further leading to vicious circle for a disaster.

The economic slowdown of 2008 has witnessed several organizations going into red, leaving thousands of people jobless across the globe and hundreds of banks, especially in USA, bankrupt; resulting into billions of dollars losses to investors. It pushed several organizations into so much dismay and despair that their wounds were not even healed and another slowdown of 2011 surfaced.

The global economic activity in the year 2011-12 has slowed down across the world resulting into the socio economic turbulence in the Middle East and North America, tsunami in Japan, the Sovereign debt crisis in the Euro zone and dismal growth in US. The downturn in the economic activity has impacted the commodity prices across the globe and the uncertainty in Middle East region has caused oil prices to remain firm. In mature markets, debt crisis and slow recovery remain unresolved while emerging markets are grappling with persistent inflation and high energy prices seemingly entering a new phase with continued uncertainty.

Against the backdrop of an extremely turbulent world, the Indian economy is facing its own share of pain in the form of unabated inflation, ballooning fiscal deficit, weakening rupee, the worsening industrial performance, sluggish exports and spiraling fuel prices. The Reserve bank of India was prompted to hike the interest rate 13 times since 2010 to curb inflation, except only recently trying to reverse the trend by 50 basis points reduction to give a breather to economic growth but this too could not make any impact on lowering the inflation or smoothening other economic indicators. Combined effect of this turbulence can be seen in GDP numbers which has slumped to 6.5% in 2011-12 from 8.4% in 2010-11, lowest in 9 years. The manufacturing, services and agriculture sector growth declined to 2.5%, 8.9% and 2.8% from the levels of 7.6%, 9.3% and 7%, respectively in the previous fiscal which the Government is optimistic to slightly improve in 2012-13 fiscal but the Reserve

* FCA, FCS, ACMA. Professor and Area Chair (Finance) Jaypee Business School, IIIT University, NOIDA.

Bank of India has dwindled all hopes by lowering the GDP estimates to 6.5% this fiscal further supplementing this fear by planning commission by lowering this growth estimate to 6 percent due to drought.

There is no sign of reversal of despair and dejection amongst the masses and the heat of this cry can be heard and felt in mass movements against the governments, social unrest, fall in the income and consequent expense of the people leading to cascading effects of slowdown all around. Corporate wheels are getting slower and jobs opportunities are getting reduced.

This paper deals with the concept of economic volatility, its causes, consequent effects of economic volatility and risks mitigation and management at all levels with a special focus on risk management by corporate sector. It also focuses on extremely meticulous management of risks by corporate sector so that it may withstand the shocks of volatility lest its constituents may not wipe out of the economic scene leaving millions of people financially wounded without healing touch. While at the national level the paper touches upon the wide spectrum of measures to be adopted by the government, risk management at the corporate level has been dealt with in some greater detail.

What is Economic Volatility ?

Economic Volatility pertains to frequent acceleration and deceleration in economic indicators i.e. currency exchange rates, interest rates, inflation index, GDP, industrial production index, agriculture production index etc. When there is frequent change in economic indicators, there is bound to be clouds of uncertainty of economic development of the nations with cascading ill effects on economic resources of the nations and general living standards of the people.

Causes of Economic Volatility

a. *Fiscal Deficit*

Unchecked Fiscal deficit leads to high government borrowings, higher interest payments, rise in interest rates, higher taxes and inflation resulting into lower demand and lower production, retrenchment of workers lowering income and savings leading to further reduction in demand and so on.

b. *Political Uncertainty & Political Greed*

Immature, self centered and coalition political power does not really work in the interest of the country and causes economic destabilization. Political parties remain busy in pursuing their personal political interest at a great cost of the nation. After coming to the power they are mostly busy in saving their chair and their coalition partners from the clutches of the criminal law for their own benefits or remain engaged in preparing for the next general election to grab the chair perpetually. In the process very little time is left to focus on the economics of the country and they fail to take proper decision in time causing loss of enormous economic resources.

Matter gets worse when these parties connive amongst themselves as well as with the corporate world, causing heavy drain on the rich economic national resources to the benefit of few pockets. Getting/ granting a license unreasonably and selling it at high price, grabbing land, mines and other valuable resources at throw away price, influencing law making authorities to frame laws for the benefit of few very resourceful persons/entities at the cost of nation at large, legally looting the exchequer in the guise of spending at enormously inflated rates (oil touching \$200 per barrel in 2008, the US election time and again rising currently at the time of US election) on highly scarce natural required resources i.e. oil; dragging for years to simplify regulations to fill the demand supply gap of much needed scarce infrastructure like power, roads etc which are very essential for economic development and all round prosperity; using ways and means to keep the generations of the nation locked only into earning throughout life for their food, cloth and shelter and having no time to look, analyze and act for the wrong actions of the political parties, are some examples of political scams and unhealthy practices which can be revisited in last few decades across the globe. Scams in India since 1990 are estimated over Rs. 100 lac crores. Some Indian Scams include Harshad Mehta Scam 1991 worth Rs. 4000 crores. There were 600 cases registered against him but hardly anything came out of this. The fodder scam of Bihar worth Rs. 1000 crores drained Bihar's treasury for upkeep of holy cows, cases still in courts. Telgi stamp paper scam cost nation Rs. 30000 crores. 2G spectrum scam worth Rs. 1.76 lac crores, coal scam worth Rs. 1.86 lac crores, Common Wealth scam, Bofors scam, Hawala scandal, IPL scam, Ketan parekh scam, Adarsh Complex scam, Housing loan scam involving LIC Housing Finance and some Nationalized banks, certain land and mining scams etc. are some further known examples through which Indian economy lost/ migrated its substantial resources.

Since majority of high profile and mighty people are party to these scams, it loses its sheen in legal battle with no consequences except to leave majority of the countrymen poor, weak and uneducated as also the nation's economy shattered and it is a shame for us that political pundits do not, in the first place, agree for the reported scams unless these are proved through lengthy legal fight with the help of Hon'ble courts.

This political attitude has led to downgraded rating of some nation's world over by international rating agencies and it is a pity that even this downgrade is protected by the advisors of the political parties on one pretext or the other showing true color of their misdeeds to the world.

c. *Natural Calamity*

Fast and vast unregulated urban development, making environment highly polluted, destruction of green belts on large scale, waste of natural resources or non protection of scarce natural resources, lack to will to refill the decaying natural resources have brought national stress and distress time and again- may be tsunami of Japan, earthquake of Gujarat, drought, floods- causing drain to national economic resources to bring back human life in order and this results into economic disorders for decades to come.

d. *Outbreak of War*

Several outbreaks of war-internal or external proved to be heavy dent on economic condition of the nations. There is a race to dominate other at any cost resulting into earmarking heavy amounts for defense expenditure which could have been used for the development of the economies. The issues across the nations emerging out of wars or causes of wars remain open for settlement for decades without any outcome except political statements. All this contribute to unhealthy economic development as well as economic instability. The exorbitant budget of countries for defense causes great strain on economic resources of the countries. A very large manpower remains idle for decades waiting for wars to break.

e. *Outbreak of Diseases*

Unhealthy environment created by polluted minds has brought us pains frequently during last several decades in the form of incurable diseases in spite of so much revolution in healthcare sciences. Stress levels of human being have gone up considerably and life has become very fast. All this is happening in the name of, 'fast developing prosperity' which ultimately is bringing pains to the people. Unhealthy mind and unhealthy body-how these can bring economic prosperity? On the surface it looks good in GDP numbers but at what cost? Diabetes, heart attacks, neurological outbreaks, cancer are some of the examples which are eating ultimately the economic resources through diminishing potential productive strength of the countrymen. Corporate world desires the work to be performed on yesterday's date; young people are employed at a very high compensation to be returned in the form of work for 16-18 hours a day leaving them stressed after a very short time and it pushes them into the hands of either of devils-diseases described hereto above and this reduces their future potential for productive performance-an ultimate loss to the national economy.

f. *Corporate' Greed*

An open secret known to all. Be it inflated cost of projects or use of national resources dirt cheap or taking unfair advantage of demand supply gap of human resource or no/ low spend on pollution control measures or adopting unfair accounting practices for their personal benefit at the cost of the general investors/ exchequer are all such examples which transfers the economic resources from the national use to private benefit of few. Ongoing practice since ages to highly inflate the cost of project, getting it funded through public financial institutions and banks or through public issue brings huge financial resources to few hands without its righteous defined use and sometimes this money is diverted under full legal protection for other projects- by passing shareholders' resolution (Satyam scam worth Rs. 14000 crores and Bernard Madoff scam of US worth 60 billion US dollars are good examples which ultimately got caught under the clutches of law). But many such Satyam and Bernard Madoff are roaming free because they are still at large and out of the clutches of law. Such economic resources many a times do not remain in the national economic system and funds are parked in tax heaven countries. One can visualize the cascading effects of national economic resources leaving the boundaries of

the nation-low government revenue collection, NPAs of Financial Institutions and Banks, loss of productive use of these resources for ever, increasing disparity of income and wealth resulting into social unrest. This brings high fiscal deficit and imposing high taxes by the government to meet the end with a suffering to masses for the benefits to few.

g. Unhealthy and Unethical Practices of Financial and Commodities Markets

Let me discuss first the financial markets. Under the umbrella of liberalization, public issues are priced at a phenomenally high price. I am talking of the Indian scene. Earlier when price of public issue was fixed, there was a check by Controller of Capital Issue and this highly risk bearing security used to give good returns to the public at large. Instead of bringing further relief to the investors, the promoters are largely benefitted now in free price regime at the cost of public at large. Few groups get richer by several billion rupees and they enjoy this kitty leaving general investor high and dry. There is a long list of such promoters and such public issues and it is going on unabated. Economic turmoil happens and is bound to happen due to such issues. This results into concentration of economic power in few hands.

Commodities market is another feather in the cap of economic upheavals. In a country where majority of population only survives on poor quality nutrition, how can these speculative commodities markets be beneficial to economic uplift of the people? Forward contracts allow indirect hoarding of commodities leading to spiraling prices of commodities day by day again leaving majority of countrymen economically poor with health hazards.

h. Untapped Sources of Revenue in the Guise of Protecting Illegal Income of the High and the Mighty

In an agriculture dominated country (India), there is no income tax on agricultural income. As claimed by the government, this is in clear view of the uncertain income source and sector earmarked for the poor farmers of the country. In the name of the farmers' benefits this remains untapped source, while the true story hugely differs. Majority of the farmers earning from agriculture are well below the exemption limit of income tax and they may be further allowed for another some exemption for uncertain nature of income. But those who have amassed land and earning huge agricultural income or converting other illegal income in to agriculture income without paying tax, why their agriculture income is exempt, is anybody's guess. There is an urgent need to revisit this source of income to strengthen and balance economic resources of the country and to avoid colossal loss to the exchequer.

i. Environment destabilized

Air and water are two very essential life supports on this earth. Both of these are being polluted by so called civilized humanity. In fact, we are sowing the seeds ourselves for low value human life on this earth in times to come. Current benefits to the present society will outweigh the massive losses to future generations. Lot of hue and cry is made by various concerned segments of the society but it is lost in the deaf ears of the decision makers as if they will not have their future generations. Massive loss of green belts has added further woes to the environment.

It is a misery that corporate citizens of developing country loudly sing a song of earning “CARBON CREDITS’ and show its positive effect on their balance sheets but it is hardly realized that these credits are paid by those who commit the sin to whole world’s environment by emitting pollutant gases in the atmosphere and this happens in developed world. It is a tragedy for the total human race that inhabitants of developed world do not want to compromise with their comforts which they enjoy at the cost of polluting environment and those who buys these sins in the name of Carbon Credits forget that when environment is polluted it does not remain within the boundaries of developed nations or real culprits, it also affects heavily the developing world. How much economic resources are needed and would be needed to correct this environment imbalance cannot even be measured because it may so happen that some loss becomes irreparable. Economies of developing world are heavily burdened to deal with the menace of environment pollution.

j. *Great Loss of Human Conscience*

Majority of the issues discussed above are a testimony to the fact that there has been great erosion in human values across the world! We are concerned for self at the cost of others. In fact, this is at the cost of ours only. Unless wholesome welfare is considered, it will be very difficult to reverse the trend and economic volcano will continue with a great suffering to human race at large.

Risk Management

As said at the outset of this paper that economic volatility causes great risk to financial health at the macro as well as micro level of nation’s economy. It may lead to dent or scarcity of economic resources, uncertain future growth, pains to the countrymen, concentration of economic power and social unrest.

While the macro level risk is to be managed at state level, micro level risk will be addressed by the corporate sector and others. Risk Management has been classified in to two parts for discussion in this paper-Risk Management by the State and Risk Management by the Corporate World. State level risk management is very wide and complex issue and has been broadly covered to identify the vehicle which may be useful to minimize ill effects of economic volatility, the corporate risk control measures have been discussed in greater detail for survival during the highly volatile times.

I. *Risk Management by State*

This needs total restructuring and reshuffling at political/ governance level. Whether ruling the country/ states or sitting in the opposition, all political parties have to ensure the eradication of corruption from the system. This will require rock like ‘will’ to implement clean governance at all levels of the government as well as society. There will be lot of pains to all those who have been eating the resources like white ants, but in the long run this will be good for the nation as a whole where all citizens will have privilege to enjoy food, shelter and cloth and have economic freedom and

fearless existence. Various measures which may be adopted by the State are summarized as under:

a. *State Governance Overhauled- “An Honest Beginning to Emerge”*

Things travel from the top. To say that bottom should improve first and it should filter up to the top is unseen and impossible. The political system and bureaucracy have to send strong signal down the line that they mean business and no theft of economic resources would be tolerated/ accepted. Good state governance has to replace the rotten one. Unless wholesome view is taken by the state governance, it is impossible to deal with the consequences of economic volatility. Good governance would ensure the minimization of economic upheavals and deal with it successfully if at all we are confronted with the same due to reasons beyond our control with the additional economic resources made so available.

b. *Strong Legal System*

Law and legal machinery to be strengthened so much that law breaker thinks thousand times before committing economic frauds. Law should take recourse with everyone without his/ her size. This would send very strong signal to countrymen to be sincere and honest. Economic resources are bound to be saved from slippages if law is strong in application. In fact, there are hundreds of laws in existence. It is needed that its implementation should be ensured in right earnest.

c. *Honest Collection of Taxes by the State*

Year after year there has been sharp increase in number of direct and indirect taxes as well as its percentile for collecting revenue for plan and non plan expenditure of the government. In the name of law people are being looted and cheated by the State. People have been made totally slave in hands of State. Enormous taxes leave the countrymen poor. Majority of them are not able to meet their ends comfortably through out life. When there is no check on state expenditure or on productive usage of State revenue, how is it justified to keep increasing the tax burden on the masses? In this process, poor gets poorer year after year. State must recognize and realize that a minimum income is required by any individual or unit of a family for a healthy living and keeping that in view resources should be mobilized through taxes (direct and indirect both). This will happen only when there is honest spend by state machinery on the administrative expenditure as well as on development planned expenditure. The whole thing revolves round the same one thing i.e. practicing “Honesty” at all levels by the State. The countrymen would never mind to support the cause of national development by contributing more towards taxes provided they are also comfortable for the welfare initiatives of the State.

The area of Agriculture (in case of India) has got to be revisited and detailed analysis is required to ensure that only the farmers (in true spirit) are only exempted from tax on agriculture income by providing extra exemption due to its very nature

of uncertainty and all black sheep should be brought under tax net as early as possible.

d. *Check on Corporate*

There should be strong check on economic offenders who are committing fraud either through capital markets or through commodity markets or otherwise. Commodities which are essential for daily needs of the people and are in short supply as compared to their demand should be brought out of the purview of commodity market as the forward trading in those commodities escalates indirect hoarding by wealthy traders causing undue spiraling in prices of those commodities. Capital market frauds also need great attention of State authorities. In fact, the fast and stringent prosecution in capital market frauds will be immensely helpful to prevent its occurrence. Judiciary was highly praiseworthy in US Bernard Madoff 60 billions US Dollars fraud case in which Bernard Madoff, aged 75 years, was sentenced to 75 years imprisonment in less than one year of the case was filed in the court.

Economic offenders should be debarred legally from taking any positions in corporate world may be for ever depending upon the severity of their crime and their properties confiscated. Economic fraud should be listed in the category of heinous crime as it deprives millions of people of their due share in the economic prosperity of the country. Fraud by corporate is ultimately funded by public at large either through more taxes imposed by government to meet revenue shortfall, as it is not made good by corporate due to frauds, or due to losing their investments made with such corporate in the form of share capital or loans.

e. *Environment Protection*

Several global initiatives have been taken. Regular meetings are held at global platform without any concrete resolutions. Billions of dollars are spent on such meetings alone without any favorable outcome except to meet next. Developing world will have to take centre stage and pressurize the developed world to honestly support for the cause of environment protection. Selling and buying carbon credits must be banned as this supports the environment crime inflicted by the seller of such credits. There would definitely be revenue loss to environment protector but this would also offset the ill effects on economic resources of the nation due to environment pollution and would also sideline the group of Corporate/ State committing such heinous crime by polluting the environment so sacrosanct for the survival of human race.

f. *Education and Health for All*

At world level effort are being done for the good causes of education and health. But it needs sincere approach at national level as well. The funds allocated for these two sectors by the government are siphoned to a large extent and whatever

is spent does not provide the desired results leaving mass population with health hazards and low education both of which are detrimental to the happy, healthy and economically sound society. Healthy and educated society would greatly contribute towards gross domestic products and help the government to meet its required revenue.

II. *Risk Management by Corporate*

High economic volatility storms the corporate balance sheets and leaves them red faced if risk due to volatility not addressed timely in effective manner. High fluctuations in economic and financial variables destabilize corporate strategies and affect performance. It is of utmost importance that based on the past parameters, these changes are suitably forecasted and action plan initiated well in advance to avoid negative impact on corporate balance sheet. Derivatives—forwards, futures, options and swaps have come to the rescue under such situations. There has been tremendous growth especially in early nineties in using derivatives as instrument to hedge the risk of volatility. Till now it has been found that business managers are confused as to how this instrument is used most effectively because there is no single set of principles guiding for hedging programme. Hence, risk management goals should be clearly demarcated without which using hedge instruments could be very dangerous. This is established due to the fact that in last few years numerous cases of derivative trades have backfired. A latest example of such failure is of exchange risk hedge on a large scale by Indian corporate that lost enormous money in spite of hedging their foreign exchange risks.

A guided framework is presented here for senior business managers to develop comprehensive risk management strategy and make a sensible use of risk management financial derivatives. In the first instance these managers must understand that risk management strategy should be integrated with overall corporate strategy. While understanding this integration, corporate managers have to answer one important question as to why hedging is at all required. The corporations are owned by several small shareholders and risk of the corporations is distributed amongst the small shareholders and they can hedge their risk themselves. For example, if cement prices are declining, the shareholders of cement companies can offset their risk of low stock price of Cement Company through investment in those companies' shares which are users of cement like infrastructure companies. Corporations may sometime make money through hedging and sometime they may lose. Overall they break even. So the risk-reward relationship for hedging/ not hedging the risks have to be ascertained before taking the decision that which risk should be subject to hedging and which can be left unheeded.

A more important risk management in case of economic volatility may be to ensure that loss due to economic volatility can be more than offset by consolidation of the existing operations as well as exploiting any emerging opportunities for further investments in times of slowdown.

A. In Perspective:

a. *“Consolidation for Existing Operations”*

Taking the example of consolidation, suppose economic slowdown has started. One organization is into manufacturing of passenger cars. Interest rates have become very high. There is high inflation, slower growth, overall low demand with a steep fall in demand of high value capital goods specially passenger cars. Now the risk of lower business by this corporation could result into lower revenue and profits. The multi dimensional strategy may be adopted by this corporation to meet this risk, survive well during this period of slowdown and also explore opportunities to expand horizontally/ vertically or through conglomerate merger.

During the period of slowdown, all flab on avoidable expenditure should be cut to size. All existing projects nearing completion must be completed on a war footing level to avoid any slippage and overshoot in expenses, projects just started for expansion may be slowed down to minimize interest cost on projects and these projects may be taken up on faster pace once there are signs of rebound of economy. Redundant assets may be identified for disposal and/ or productive use strengthening economic resources of corporation, human resource development may be prioritized, customer satisfaction index may be reviewed and steps taken to take it to higher level because this is the time when the corporation has to ensure that retention of customers is of highest priority. Customer’s preferences may be reviewed during this period more aggressively. All this will carry message to the company customers about company’s focus on the customers care. After sales service may be relooked and all loopholes which lower the customer service may be plugged.

b. *Expansion through Mergers and Acquisitions*

The corporation should look for opportunities of mergers and acquisitions whether horizontal/ vertical or conglomerate. This is the time when many organizations which are not capable to withstand the storm of economic slowdown do want to get out of the business and look for support from the sound corporate. This is good opportunity to cash by investing in expansion/ diversification at lowest cost. Sometimes the units are available at throw away price. Hence, cash rich corporate can use this opportunity for setting up further facilities at cheapest cost for reaping the benefits through them when economy rebounds. This way losing money in slowdown can be made good handsomely in better times.

c. *Having Internal Cash Aligned with Demand for Satisfactory Risk Management*

The above discussion significantly highlights that the role of risk management by corporate is to ensure that the company has the cash available to make value-enhancing investments and/ or to meet the requirement of consolidation

of existing operations in times of economic slowdown. Further, availability of this cash must be ensured internally, reason being that during economic volatility, interest rates become very high and many a times economy feels the heat of dried resources. Hence, cost of debt becomes very high and equity resources are also very hard to be harnessed due to gloomy atmosphere all around. Adequate internal generation of cash and its retention for value investment also depends upon whether revenue generation is subject to exchange risk. In this situation it will be worthwhile for managers to hedge such risk to ensure the availability of desired cash in case of wide exchange risk fluctuations.

B. Added Dimensions for Risk Management by Corporate Sector (*David Hillson (2004), Risk Management : Best Practice and Future Developments, ICAI J Projects & Profits., 11-15*)

The value of a proactive formal structured approach to managing uncertainty has been widely recognized, and many organizations are seeking to introduce risk processes in order to gain the promised benefits. But it is important that overall direction of risk management is maintained otherwise risk management could dissipate and lose coherence. There are three areas where active development is needed if risk management is to fulfill its promise as a significant contributor to business success. These are:

- * *Integration of Risk management* : Risk Management is often perceived as a special activity undertaken by experts using dedicated tools and techniques. In order to take full benefits from implementing the risk process, it is important that risk management should be fully integrated at both operational and strategic levels in an organization. Without such integration, there is a danger that the results of risk management may not be used appropriately or at all and that the business strategy may not take proper account of any risk assessment.

True integration requires number of changes, including recognition of the existence of uncertainty (especially in such highly volatile economic environment) as an inherent part of being in business, together with proper interfaces to business processes and tools. In addition, there is a need to develop strategic risk-based thinking within organization culture. The denial of risk is common at senior management levels, and much of the value of implementing risk management can be diluted or lost if decision makers do not properly take account of risk. Risk management must be seen as an integral part of doing business, and must become “built-in not bolt-on”, a natural feature of all business processes, rather than being conducted as an optional additional activity.

- * *Increased Depth and Breadth* : Further development is always required to improve the effectiveness of risk management both in functionality and scope.

These two dimensions of improvement are termed “depth of analysis” and “breadth of application”. The depth of analysis could be improved by-

- Development of better tools and techniques, with improved functionality, better attention to the user interface and improved integration with other parts of the toolset.
- Use of advanced information technology capabilities to enable effective knowledge management and learning from experience, for example using artificial intelligence, expert systems or knowledge based systems to permit new types of analysis.
- Development of existing techniques from other disciplines for application within the risk arena, for example from value management, system dynamics, safety and hazard analysis, financial trading etc.

The current scope of risk management is fairly limited, tending to concentrate on timescales and cost targets. While these are undeniably important, there are number of areas, which should be covered by the risk process. The breadth of application could be enhanced by-

- Inclusion of opportunity within the definition of risk and ensuring that the risk process covers both threats and opportunities.
- Measurement of impact against all types of objectives, including performance, quality, compliance, environmental or regulatory, soft objectives such as human factors issues etc.

- * *Behavioral Aspects* : There is a general agreement on the importance of human behavior in determining performance (Old Field A & O’ clock M1997). Future development in risk management must take more account of these issues, both in generating input data for the risk process, and in interpreting outputs. It should also consider risk attitudes and their effect on the validity of the risk process. A reliable means of measuring risk attitudes needs to be developed, to identify and counter potential bias among participants (for example, Greenwood 1997). This would also permit building of risk-balanced teams, including people who are comfortable with taking risks, balanced by others who are more conservative and safety conscious, in order to ensure that risks are only taken where appropriate.

Although risk management has matured into a recognized discipline, it has not yet reached its peak and could still develop further. There are several areas where progress is required. Development in these areas would have a significant effect on risk management, by producing-

- (i) A set of risk management tools techniques, which are fully integrated with projects and business processes, with the existence of uncertainty being recognized and accepted at all levels (via integration of risk management).

- (ii) Improved analysis of the effects of risks on project and business performance, addressing its impact on issues wider than time and cost (via increased depth of analysis and breadth of application), and covering both threats and opportunities.
- (iii) Proper account being taken of human factors in the risk process using assessment of risk attitudes to counter systematic bias and build risk-balanced teams (via behavioral aspects).

Attention to these areas will ensure that risk management continues to develop. Risk management must not remain static, if it is to fulfill its potential as a significant contributor to business success, and if it is to take its place as an indispensable and effective management tool.

Conclusion

Risk Management is a very complex field and several statistical and mathematical modules have been developed to contain the macro and micro level risks. But the moot point is that the causes of risk due to economic volatility are so deep and varied in nature that these modules have proved to be of little help. The testimony of this fact is already in place and recorded that in spite of hedging done and devised by so qualified management experts, heavy losses to the Corporate as well as State could not be avoided in recent past due to high exchange rate fluctuations. The solution of risk management not only lies in statistical and mathematical modules but greatly imbibed in high level serious thinking to eradicate deep rooted corruption, environment protection and welfare of all by ensuring food, shelter, health and economic protection. These value based suggestions may be of great help in this regard.

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RISK MANAGEMENT IN TIMES OF ECONOMIC VOLATILITY

RISHIKESH GAGAN VYAS*

Preface

The subject of Economic Volatility and Risk Management is very beguiling in nature. The recent slowdown of the Advanced Economy is both a cause and an effect of the sovereign debt crises in the Eurozone and the associated fiscal problems. The sovereign debt crisis in the Eurozone has not only aggravated the macroeconomic conditions of the countries of the Eurozone but also, in turn, has deeply affected the balance sheets of global banks having exposures to these countries. The political measures and announcements, co-ordinated initiatives of the Governments, and prolonged easing policies backed by unconventional measures of the central banks to provide a solution to the problems arising out of this crisis have not been able to evoke sustainable confidence in the financial markets. The European Union and the US form the two largest economies in the world and are deeply inter-twined with each other even in such adversities. There is, thus, a felt need for concerted actions by the policy-makers across the Advanced Economies to save the global economy from falling into a downward spiral, rejuvenate the employment led recovery and pave the way for structural reforms required for sustainable and balanced growth not only in these economies but also in other economies including India.

Economic Volatility

We are still recovering from the bursting of the internet bubble in 2001, stock market crash of 2008 and sovereign crisis of the year gone by, the image most immediately conjured up by the word “volatile” might be that of an unstable stock market; or, in view of the balance-of-payments crises of the late 1990s, of unpredictable capital flows driven by fickle market sentiment to emerging market countries. But the adjective could equally be applied to the weather. In India, for example, even though the share of agriculture in national output has dropped from one-half in the 1960s to one-quarter today, a good monsoon can still make a significant difference to GDP growth. “Volatile” can also be used to describe a political climate, such as that prevailing in Middle East or Some African Countries; or the procyclical response of fiscal policy to fluctuations in the price of oil for an oil exporter such as Nigeria; or even the behavior of a crowd in downtown London.

Depending upon how one looks at it, volatility in conventional economics has either been around for a long time or else is of more recent vintage. The first view would assert that

* Compliance and Governance Personnel, Mumbai.

volatility dates to the time that the study of business cycles began, although it might be more correct to say that the concern there was more with decomposing economic growth into a cyclical and trend component than with volatility per se. The second view is that volatility began to develop into an independent field of inquiry in macroeconomics only over the last decade. Up to then, it was regarded as an oscillation around an independent growth trend, a second-order issue of interest mainly to industrial economies concerned about smoothing the fluctuations of the business cycle. It is now beginning to occupy a central position in development of economics.

Risk Management

Risk management is the identification, assessment, and prioritization of risks followed by co-ordinated and economical application of resources to minimize, monitor, and control the probability and/or impact of unfortunate events or to maximize the realization of opportunities. Risks can come from uncertainty in financial markets, project failures legal liabilities, credit risk, accidents, natural causes and disasters as well as deliberate attack from an adversary, or events of uncertain or unpredictable root-cause. Several risk management standards have been developed. Methods, definitions and goals vary widely according to whether the risk management method is in the context of project management, security, engineering, industrial processes, financial portfolios, actuarial assessments, or public health and safety.

Sovereign Debt

Sovereign debt is the debt owed by the government of a country and it is usually denominated in the national currency (domestic debt), and international currencies (external debt) like the USD, Euro, Yen, Pound Sterling or even the local currency. The government needs to borrow money when its spending is more than its revenues (known as fiscal deficit). When the government borrows it can borrow in its own currency or in a foreign currency. A government that needs to pay for foreign goods and one that doesn't have enough foreign currency will have to borrow in a foreign currency. For example, India imports oil from Iran, and Iran demands that India pays for it in US Dollars. India uses a Turkish bank to facilitate this transaction and due to the recent sanctions by the US and EU – the Turkish bank is likely to refuse being the intermediary, and force India to look for another channel. If Iran accepted Rupee payments for its oil then there will be no problem because India could settle with them directly, but since they don't, India will have to find a way to settle this transaction in dollars. Thus, debt will be created.

Sovereign Downgrade

A sovereign credit rating is the credit rating given by a recognized international rating agency to a sovereign entity. Just like any other credit rating, which indicates the level of risk associated with investing in a particular security/debt instrument of a company, sovereign credit rating indicates the level of risk associated with investing in a country's economy. Since sovereign rating is determined by various factors associated with any economy, it gives an insight into the prevailing economic environment of a country. Thus, it is an indicator

used by various investors looking to invest abroad. Sovereign credit ratings are assigned to countries on a relative basis. Since the Sovereign Credit Rating indicates the state of health of an economy on various fronts, including political scenario, it becomes a strong reference point for investors wanting to invest in other countries. From a country's point of view, it is important to have a healthy credit rating in order to attract much needed foreign capital inflows in to the economy, especially in case of developing countries. Generally, when a recognized international rating agency downgrades the credit rating of a country, it is negative for the country. A downgrade would generally mean that, of the various important factors determining the credit worthiness of a country, some or several factors have become unfavorable, which can potentially lead to a risk on investments done in that country. This can lead to an outflow of foreign capital from that country, which in turn impacts the capital markets of the country i.e. equity and debt markets. Similarly, in case of an upgrade, the FIIs would be more willing to invest in that country, considering the economic prospects of that country has improved.

Factors Determining Sovereign Rating

Sovereign Rating of a country is determined on the basis of various quantitative as well as qualitative factors on the economic, social and political front. Some of the critical factors are –

- (a) Per capita income
- (b) Gross domestic product (GDP)
- (c) Government income
- (d) Exchange rate
- (e) Inflation rate
- (f) Default history
- (g) Fiscal deficit
- (h) Governance of a country
- (i) High inflation
- (j) High fiscal deficit
- (k) Political uncertainty
- (l) Social unrest
- (m) Low levels of corruption etc.

Risk Moderation

(a) *Conserve Cash and Control Costs*

Corporations need to preserve every bit of cash they can. There are some obvious places to look, such as discretionary spending and corporate travel. What non-core functions can be outsourced or moved offshore? Is this the time to launch a large-scale, enterprise-wide cost reduction initiative? Everybody's looking for the quick, easy wins but many companies will also need to implement more comprehensive, far-reaching cost reduction efforts to get the results they're looking for.

(b) *Diversify capital sources & establish new credit lines*

Plan for deeper relationships with a wider variety of credit providers and banks and develop a better understanding of the risk exposure those entities may be facing themselves. Also, companies seeking capital from banks will need to work closely with them to make sure they have the information they need to extend revolving credit facilities. The days of “covenant light” loans are over. Expect to operate in an environment of tighter debt-to-equity ratio, heightened restrictions in the use of capital and investments, and more extensive reporting requirements to providers of capital.

(c) *Lower Working Capital Requirements*

For the most part, the current set of operational processes that drive inventory, accounts receivable and accounts payable levels required to run business today have all been designed for an environment in which cash has essentially been ‘free’. The result is a gold mine of cash tied up in working capital that can be rapidly released by taking the ‘blocking and tackling’ measures to improve these operational processes. Improving demand forecasting and inventory planning processes to lower inventory requirements, tracking accounts payable performance by commodity and extending terms to industry benchmarks, and eliminating errors in the order to delivery process to reduce disputes and improve accounts receivable performance are just a few of the operational improvements that can dramatically reduce working capital requirements.

(d) *Seek out Strategic Assets*

There will be many opportunities to pick up strategic assets, not to mention entire companies, in the coming months. But only companies with strong balance sheets will be able to take advantage of this environment. There are recent examples of companies making moves today to bolster their competitive advantage in the future. Expect to see many more mergers and acquisitions over the next two years and if a company has the financing and cash on hand to support it, start looking for strategic assets today, and be prepared to move quickly but carefully. As one negotiates this slippery terrain, don’t lose sight of the fact that the company may already be considered a strategic acquisition target by someone else.

(e) *Consider a New Capital Mix*

In the long term, Corporations will likely need to develop a new mix of capital to finance their companies. That may mean bank loans and private equity investments, for starters. In the near term, the differences between companies with high credit ratings and those without are likely to be stark, in terms of both cost and availability of capital. This is a time to improve company’s credit ratings if possible to take advantage of more favorable conditions. They should also consider innovative new ways of pricing capital.

(f) *Strategy C, D & even E*

Scenario planning can be an extremely valuable tool at a moment marked by such uncertainty. Cash flow and demand forecasting are good places to start. But for many

companies, traditional budgeting cycles are no longer applicable or particularly useful. Focused, short-term 30- and 60-day forecasts may provide a much more practical option for allowing finance to respond to unpredictable changes in their business. What will receivables and payables look like next month? In six months? What if demand falls off, where does that leave the company? When will one know it's time to take another look at selling off assets? Seriously considering scenarios like this can help one establish not just Plan B, but Plan C.

(g) Perfect and Perpetual Communication

Everyone's on edge these days - the board, suppliers, lenders and employees. And while one may feel that it's more important to hunker down and focus on the tremendous challenges at hand, it's important to stay in constant communication with most important stakeholders, with a strong focus on those closely involved with finance. Even if one is not planning something major let them know how things are going. If they hear nothing, they will assume the worst. If it really is that bad, it's better for them to know sooner rather than later. This is the time for transparency, start by clearly defining which stakeholders need which information, and commit to regular reviews and communications with them for the foreseeable future.

(h) Talent Lock

In tough times, it's a given that companies will shed underperformers. But many find their best talent also heading for the door during tough times, picked away by competitors looking to consolidate power during the downturn so that they can come out fighting when the economy starts warming up again. That's why it's important to have a strategy for identifying and retaining best talent during the downturn.

Conclusion

Like in Life, in Economic situation is like hands of clock, when it is up at 12 Clock be prepared for downturn at Six and Vice Versa. Situation and Occasion's will come and go but the one who will triumph, is one who is prepared for the vilest and faces it with insight. Economic Volatility should not be seen as a disease requiring antibiotic but as an opportunity, but in order to encash this opportunity preparation with foresightness is required. Thus, as part of any prudent Governance Policy, Risk Management should be one of the ethos and Risk Management should not be looked as a shelter measure but more as an opportunity measure.

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ECONOMIC VOLATILITY AND RISK MANAGEMENT

CS DIVYA SAXENA*

Introduction

Companies are characterized by complex operating environment and rapid product innovation, so it is not surprising to see them evolving their risk management capabilities to fit for such a demanding environment. Today's more complex, interconnected World calls for more sophisticated approaches such as scenario modeling, which can show the impact of external shocks or new assumptions, calculate the accelerating change and magnitude of impact and identify the catalytic effects. In a world that is tied together ever more closely by trade, finance, and digital communications, risks are arising more quickly and unexpectedly than ever before, with significant potential impacts on companies' operations, reputations and even survival. To survive in a fittest way in the long run, the companies must adopt a new and more robust approach to defining, communicating and managing their global risk profile. Going forward, the only predictable thing about risk will be that it is always changing. The challenge for companies is to craft a risk management approach that is defined by its readiness—for anything. It must be noted that globalization is also one of the core factors behind changing economic conditions and the impact of globalization on a Country is closely linked to how well it manages idiosyncratic risk. Constant change requires unprecedented agility and flexibility. As such, the business pressures are creating volatility, variability and variety at every stage to increase their ability to operate efficiently even as conditions change. The global economy faces acute uncertainties and volatility, which present serious concern for survival and growth. In order to better understand the structural or systemic challenges of the current global economic and financial order and to explore adequate policy responses on the current economic and financial situation, an effective management of price volatility and risks is urgently needed to ensure balanced economic growth. Economic progress in the region will continue to be highly dependent on the overall political climate. Financial market uncertainty and fiscal consolidation associated with the high deficits and debt levels of high-income countries are likely to be recurring sources of volatility for several years to come.

Definition of 'Volatility'

'Volatility' refers to the amount of uncertainty or risk about the size of changes in a Security's Value. A higher volatility means that a security's value can potentially be spread out over a larger range of values. This means that the price of the security can change

* M.Com., FCS, MBA, LL.B. Executive Partner, M/s S K Gupta & Co., Company Secretaries, Kanpur.

dramatically over a short time period in either direction. In other words, 'volatility' refers to the degree to which financial prices fluctuate. The rise and the fall of shares are linked to a number of conditions such as political climate, economic cycle, economic growth, international trends, budget, general business conditions, company profits, product demand etc. Changes in local or global economic and political environment influence the share price movements and show the state of stock market to the general public. The issues of return and volatility have become increasingly important in recent times to the Indian investors, regulators, brokers, policy makers, dealers and researchers with the increase in the FIIs investment.

Meaning and Nature of 'Economic Volatility'

The term 'Economic Volatility' implies a situation in which a Country's economy experiences a sudden variation commonly in the form of a downturn or recession. It is characterized with the following indicators:-

- Sharp decline in GDP rate;
- Liquidity crunch;
- Rampant movements in prices;
- Inflationary / deflationary conditions;
- Economic crises in the form of recession / depression
- Uncertainty in economy;
- Fragility in Financial Markets;
- Distortion to productivity cycle;
- Large dispersion of productivity/profitability across businesses;
- Ongoing reallocation of outputs and inputs across businesses;
- Economic crises resulting in increasing inflation, decrease in the foreign currency reserves, increase in the fiscal deficit, increasing the negative balance of payment, decreasing the value of Indian currency and increasing the dollar, lack of liquidity markets etc.

Driving Factors of 'Economic Volatility'

In fact, the underlying factors contribute to economic volatility across the globe:-

1. *Country-specific factors* which involve events specifically affecting output growth in a particular Country--including stability of macroeconomic policies, institutional capacity and structural changes, political leadership/change, adverse publicity, new corporate competition, structural economic change, proliferating technology, increasing regulations, industrial products which includes the automotive and energy sectors, as well as utilities.
2. *Regional factors* which involve events that grip the entire region such as armed

conflicts, natural disasters and the recurrence of droughts spilling into neighbouring countries, as well as disturbances in intra-regional trade, corruption, changing market needs.

3. *External factors* which involve events that influence output growth across all countries- such as steep rises in international interest rates and commodity price changes, notably crude oil, Technology, information and communications.

The pace of 'economic volatility' has indeed gathered momentum and consequently there has been a long phase of foreign exchange fluctuations, depreciation of Indian Rupee in terms of U.S. Dollars. As such, an effective implementation of flexible exchange rate regime, full convertibility of rupee in current account and a gradual move towards full capital account convertibility would raise the volatility of exchange rate. Thus, the issue of Exchange rate exposure has become quite important in present times for the corporate world. The volatility of the exchange rate of Indian Rupee in respect to US Dollar during recent periods has caused anxiety in many quarters of the economy, particularly Export-Oriented Sectors such as IT and Business Process Outsourcing (BPO).

The market forces that lead to depreciation of Indian Rupee are:-

- Increase of imports into India;
- RBI buying dollars to absorb forex inflow;
- Foreign Institutional investors pulling money out of Indian economy; and
- Rise in Global Commodity prices.

The market forces that lead to appreciation of Indian rupee are:-

- Increase in Exports;
- RBI selling dollars as forex intervention;
- Positive Trade Balance; and
- Increase in Non-Resident Indian forex remittance into India.

Causes of Economic Crises

One of the direct effect of economic volatility is the generation of economic crises. In recent years, the pace of economic crises has aggravated, some of the causes of economic crises in India can be cited below:-

I. *Internal causes* which includes-

- Failures in Policy implementation;
- Huge quantum of Government Subsidies;
- Increasing interest rates announced by Reserve Bank owing to rising prices / inflation;
- Low Investments in Core Sectors of the Economy;

- Corruption and red tapism at various Government and Non-Government Organisations.

II. External causes which includes-

- Ever increasing Imports of crude oil viz; Petroleum and oil;
- Depreciation of Indian Rupee in terms of Dollar;
- Impact of Euro-zone crises;
- Lesser investment by Foreign Institutional Investors or repatriation / repayments of funds back to Foreign Countries;
- Foreign Economies crisis directly affecting the economic climate.

Global Challenges of Economic Volatility

The rise of the digital economy is adding to the competitive pressures. With the Internet entering a second phase dominated by mobile devices, the barriers to market entry have fallen in many industries and business models and customer loyalties are changing swiftly. In this new climate, risk functions need to be agile with regard to how they identify and respond to risks. These Organizations may have a competitive edge in accessing these fast-growth markets, through digital technology, better business practices and effective marketing strategies. Data privacy and security risk is gaining further prominence as a strategic threat and has gained attention from Executives and Risk Managers. In present times, the global economy found itself at a dangerous crossroads evidencing sharp deterioration in financial conditions in the Euro-zone, slow growth in the market economies.

Changes in long-accepted paradigms and perceptions about regions and risk, together with an increasingly globalized world where technology and capital move across borders at rapid rates, the companies that do business overseas must give priority to monitoring regional risks. Every country must be monitored as its own unique operating environment with different resources, labour market qualities, regulations, political stability and security considerations. In 2012, increasing pressures from Board of Directors and Senior Management will impel management leaders to take stronger measures to assess and prepare for external risks. How will Organizations change their risk management approaches in 2012 and how well prepared are they for the challenging times ahead? Accordingly, the companies would be putting greater emphasis on effective communication and data sharing techniques. Infact, times of increasing turmoil require increasing vigilance on the part of managers of risks. For this purpose, the investment team has to be in frequent communication with the pricing, sales and actuarial groups.

There is a direct relation between the economic volatility and risk. It is known that risks is inherent in volatility. The World Economies in today's context are volatile and probability of risks are high which lead to variation / fluctuation in market conditions. An effective management of economic volatility requires proper implementation of risk management tools/ strategies.

Classification of Risks

<i>Risk type</i>	<i>Risk</i>		
Financial	<ul style="list-style-type: none"> — Reporting integrity — Financial statements/disclosures are misstated according to accounting/industry standards — Insufficient liquidity — Lack of reliability in the systems reporting key financial data 	<ul style="list-style-type: none"> — System security vulnerabilities — Inadequate recording/oversight of financial information — Estimates are not adequate — Interest rate/ market risk — Foreign currency exchange — Credit risk 	<ul style="list-style-type: none"> — Balance sheet risk — Product-liability risk tax rate risk — Transactions are not properly approved — Inability to raise capital — Asset/ liability risk — Investment risk
Compliance	<ul style="list-style-type: none"> — Non-compliance with employment Practices (FMLA, EEO, etc.) — Environment contamination — Record retention policy — Regulatory noncompliance — Inability to meet contractual obligations 	<ul style="list-style-type: none"> — Breaching existing capital requirements — Non-adherence to debt covenants — Data used support compliance is unreliable — Fraud 	<ul style="list-style-type: none"> — Adherence to 401k/benefit plan requirements — Insider trading
Strategic	<ul style="list-style-type: none"> — Acquisitions and strategic alliances — Strategic planning does not consider external impacts — New products and services — Customer demands shortfall — Disruptive technologies 	<ul style="list-style-type: none"> — Competitive pressure — loss of key customers — Misaligned products — Counterparty failures — Customer pricing pressure — Business concentration 	<ul style="list-style-type: none"> — Distribution strategy — Litigious trends and judicial uncertainty — Research and development — Reputation risk — Insufficient governance structure and practices
Operational	<ul style="list-style-type: none"> — Loss of key personnel — Supply chain failures — Obsolete technology — Insufficient information, Technology governance 	<ul style="list-style-type: none"> — Natural disasters — Acts of terror — Third-party outsourcing — Security breaches — Lack of business continuity/disaster recovery planning 	<ul style="list-style-type: none"> — Service quality project/change management — Business disruption/ system failures — Lack of sufficient contractual oversight — Process control risk

Figure 1: Classification of Risks

Risk Management Strategies

Risk is active, and therefore, constantly evolving due to ongoing changes in external and internal factors. Whether there are modifications in business systems or processes, or events in the industry, a company with a strong ERM Strategy will periodically review its program and risk profile, allowing management in charge to respond to these changes as needed. It is true that risk exposes us to potential losses but risk also provides us with opportunities. A simple vision of successful risk taking is that we should expand our exposure to upside risk while reducing the potential for downside risk. Some of the common strategies of Risk Management are as under:-

Enterprise Risk Management (ERM) is the leading approach to managing and optimizing risks, enabling a company to determine how much uncertainty and risk are acceptable to an organization. Enterprise Risk Management can contribute to successful, compliant and effective governance, enabling companies to better understand and measure those risks that threaten strategic objectives. Moreover, ERM provides information that helps quantify business performance, narrow the focus of controls and streamline compliance efforts. ERM serves as a strategic analysis of risk throughout an organization, cutting across business units and departments and considering end-to-end processes. In adopting an ERM approach, companies gain the ability to align their risk appetite and tolerance with business strategy by identifying events that could have an adverse effect on their organizations and then developing an action plan to manage them. By applying ERM in conjunction with other operational elements in the current business environment, companies can also accomplish many of their governance-related tasks. Specifically, ERM can help organizations to:-

- Identify strategic risk opportunities that, if undertaken, can facilitate achieving organizational goals.
- Provide Senior Management with the most up-to-date information regarding risk that may be used in the decision-making process.
- Use the Sarbanes-Oxley compliance process to assist in identifying key financial risks.
- Establish co-dependency between the ERM initiative and considerations for Securities/Market Regulator reporting disclosures and other laws and regulations.
- Align annual performance goals with risk identification and management.
- Encourage and reward upstream reporting of business-risk opportunities and challenges.
- Risk diversification, costs.
- Effective and more efficient factors of production and expectation of global dominance in the world wide market place.

ERM frameworks

There are various ERM frameworks that a Company could potentially follow – all of which should define the essential components, suggest a common language and provide clear guidance for Enterprise Risk Management. In addition, each framework that is implemented should also describe an approach for identifying, analyzing, responding to and monitoring risks and opportunities facing the Enterprise.

‘GRC Framework’ for Risk Management

The integration of governance, risk management, compliance and ethics can also help an organization more effectively and efficiently to drive performance. ‘Governance’ establishes objectives and at a high level, the boundaries inside of which an entity must operate. Risk Management helps a company identify and address potential obstacles to achieving objectives. Compliance Management ensures that the boundaries are well set and that the organization does indeed conduct business within those boundaries. Finally, a strong culture provides a safety net when formal controls and structures are weak or non-existent while, at the same time, providing an environment that helps the workforce reach its highest level of productivity. High-performing organizations master and integrate these disciplines for maximum effectiveness and responsiveness, allowing their companies to leverage innovation in one area across the entire enterprise to address all set requirements.

An effective ‘GRC Framework’ enhances a company’s governance structure in that the “tone at the top” message is promulgated as one where compliance with laws, regulations and internal policies and procedures is mandatory and non-compliance is unacceptable. This assists in motivating desired conduct and provides assurance to management that they are operating within legal, contractual, internal, social and ethical boundaries. Moreover, it further assists in establishing the fundamentals of a good governance environment and structure, promoting a common risk language and collaboration on risk management issues throughout the organization (e.g., sharing of any risk issues identified by internal audit, compliance officer and others). As such, it is a forward-looking, process-oriented approach that provides business intelligence to companies to help better plot the future and make more informed decisions. When implemented correctly, it can provide organizations with a means of leveraging risks for greater performance, building a foundation for competitive advantage and ultimately establishing themselves as market leaders.

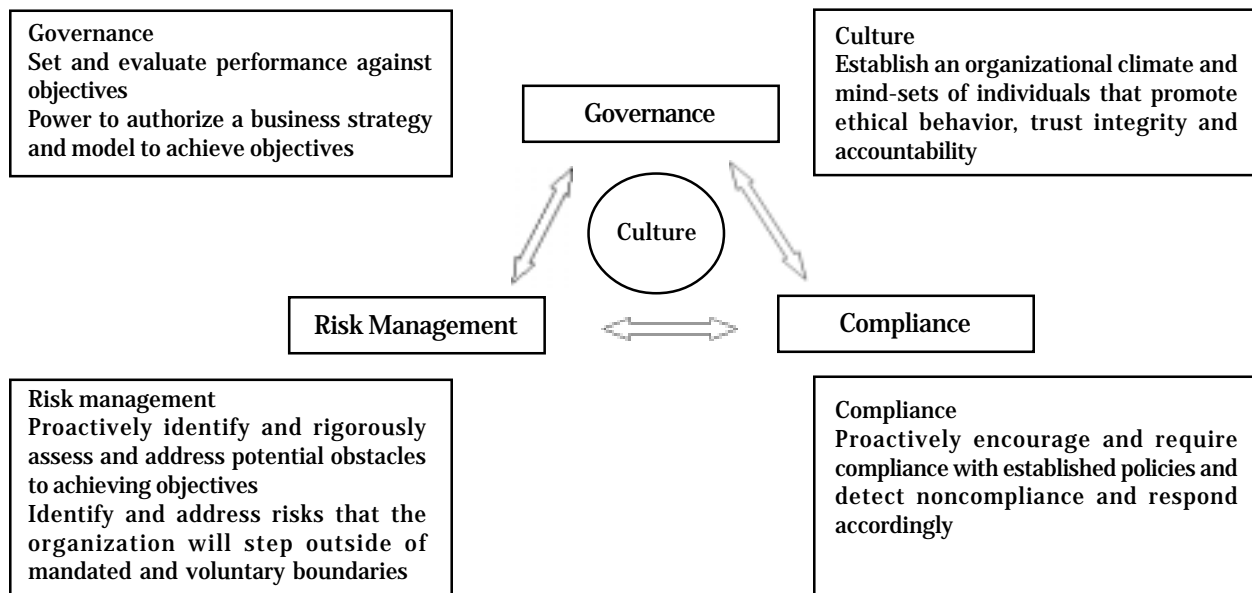


Figure 2: A GRC Framework of Risk Management

Responsibility Centres for Risk Management

Board / Board Risk Management Committee

- Sets the requirements for superior risk management measurement, monitoring and reporting, as well as the organization's appetite for risk.
- Ultimate strategic oversight of risk within the organization and recommends risk policy and guidelines to Chief Executive Officer and monitors risks.

Board Audit Committee

- Responsible for oversight of the internal controls of an organization including appropriate risk management processes.

Chief Risk Officer (CRO)

- Recommends Risk Management Policy and tolerance for approval by Chief Executive Officer.
- Ensures that the risks are identified in the organisation.
- Develops risk measurement methodologies and tools to quantify risk and assures that they are effectively utilized.
- Conducts overall risk coordination.
- Analyzes and reports on risk exposures.
- Provides ongoing risk training.
- In some organizations, he takes an active role in assisting line management in developing risk strategies.

Chief Executive Officer (CEO) with assistance from Chief Financial Officer (CFO)

- Approves risk policy and tolerance (initially suggested by CRO then reviewed by Internal Risk Committee).
- Manages overall risk.
- Approves risk tolerance.
- Takes action to mitigate risks.
- Assures proper control environment is restored in the Organisation.

Business Unit CRO

- Assures that each Unit's stated Risk Management tolerance is baked into each business unit's planning and budgeting processes.

Business Unit Personnel along with CEO/CFO

- Follows Organization's risk policy.
- Identifies and reports all risk exposures to CRO and CEO.
- Assures risk information is reported to CRO and CEO.

Internal Audit

- Assures the Board and Audit Committee that each Business Unit's activities effectively manage risk according to the organization's risk tolerance.

- In some Organizations, assists in leading the implementation of an enterprise-wide management risk assessment process.

Risk management culture dealing with the following aspects of organization:-

- Risk management organizational and governance structures.
- Roles, capabilities and accountabilities of risk management staff.
- Risk management communication and transparency.
- Risk management policies and metrics.
- Influence of risk management on budgeting and management compensation.
- Frequency with which top risks are identified and how often the identification is examined and updated.
- Influence of risk sensitivity on liability management and financing decisions.
- Role of risk management in strategic decision-making.

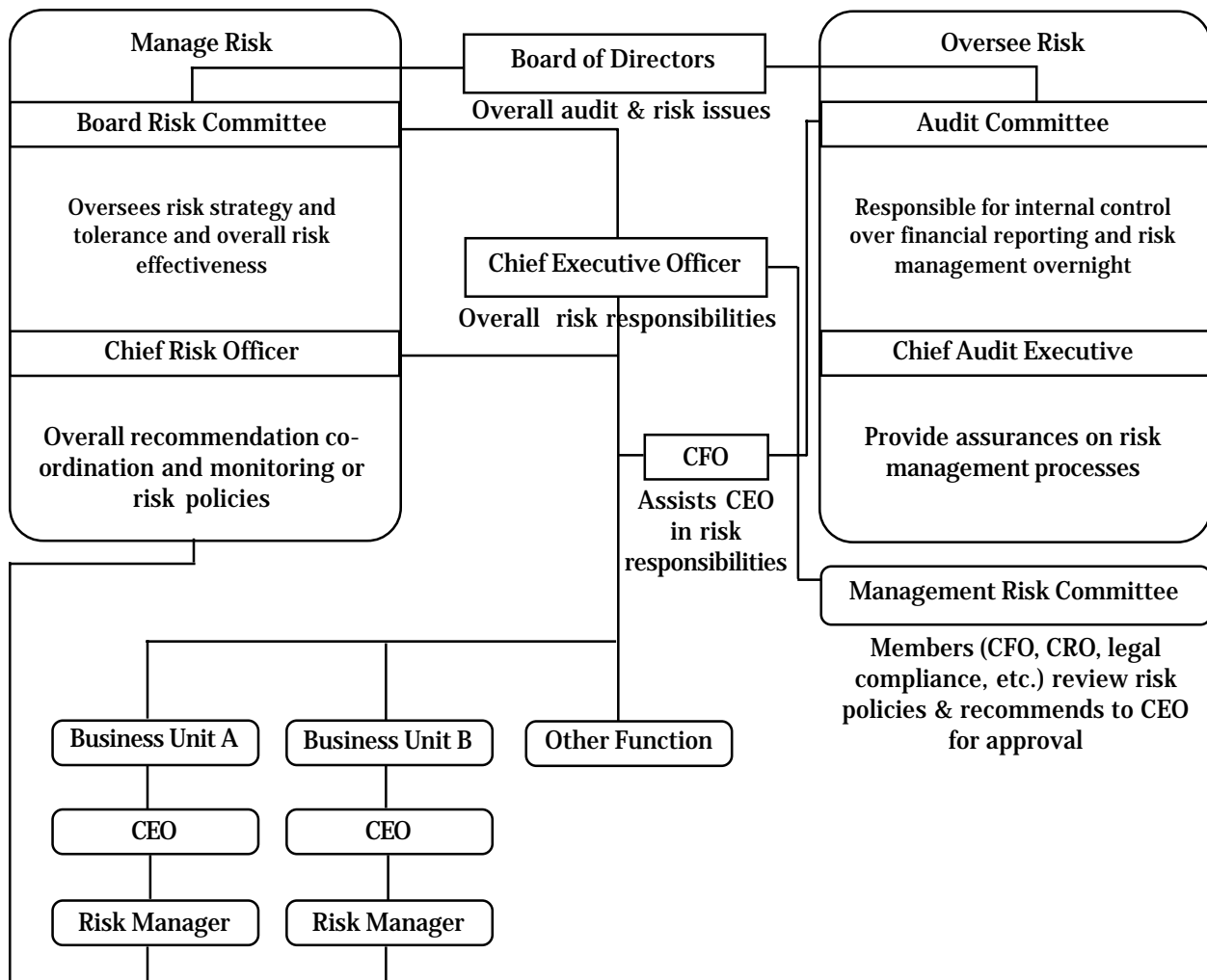


Figure 3: Business Unit Risk Management roles and responsibilities

Steps for Effective Management of 'Economic Volatility'

- Labour markets need to be sufficiently flexible to permit reallocating workers from less-productive to more-productive establishments without intervening long spells of unemployment.
- The infrastructure needs to be of sufficiently high quality to ensure that the existing and starting-up businesses that seek to grow are not thwarted by factors such as poor transportation and communication.
- Product Markets need to be sufficiently competitive that firms are not large for reasons of market power (or having obtained favourable treatment from the Government).
- Financial Markets need to be sufficiently developed to provide funding to starting-up and expanding businesses and to be able to deal with the inevitable failure of young and small businesses.
- Regulation has to provide appropriate oversight without imposing onerous time and resource costs on starting up a business or shutting down a business.
- The legal system has to work sufficiently well so that property rights are well established and bankruptcy and business failure can be accommodated.
- The rule of law and the role of the Government need to be such that graft, corruption and other forms of criminal activity do not thwart private sector businesses from starting and growing.
- With all of the above components in place, opening up the markets and competing in world markets is much more likely to enhance productivity without the costs of reallocation being too high for businesses and workers.
- Another challenge is how to handle crises. In crises, even in otherwise healthy economies, reallocation dynamics get distorted. In crises there is a lot of job destruction but not much job creation, with accompanying high unemployment. In crises, especially like the recent financial crisis, financial markets are not facilitating reallocating resources away from less-productive to more-productive businesses. A well functioning financial markets play a critical role in facilitating static and dynamic allocative efficiency. A feature of healthy advanced market economies is that they are constantly reinventing themselves as businesses and households adapt and adjust to changing economic conditions and market opportunities.

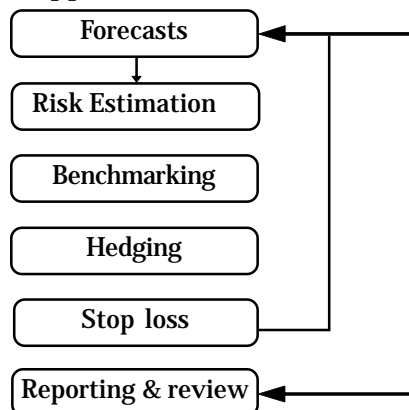


Figure 4 : Effective Steps for Risk Management

Global Risk Landscape and Corporate Planning for Economic Volatility

In 2011, economic turmoil, political upheavals and ripple effects from natural disasters converged with advancing globalization and rapid technological advances to create a riskier marketplace of complexity, unpredictable events and sudden change. Globalization and technology had created more intricate linkages that could cause risks to arise more suddenly and reverberate around the World. Over the course of 2011, Corporate Leaders grew to accept these new market realities, and realized that this new era of global uncertainty and complexity called for a fresh approach to risk management. To respond to this new era of risk, forward-looking Companies in 2011 continued to shift their risk management focus in several fundamental ways i.e from internal to external, from operational to strategic and from bottom-up to top-down. As Corporate leaders began to recognize the far-reaching impact of these risks on their businesses, they installed new risk management organizational structures and processes that leveraged corporate resources and vital information and integrated risk management across corporate functions. Some put in place a new breed of more strategic, collaborative, and business-savvy risk management leaders. Discouraged by the failure of traditional risk and forecasting approaches, a bevy of Companies also adopted innovative techniques such as scenario analysis, predictive indicators and reverse stress-testing to challenge conventional thinking and better prepare themselves to deal with unexpected events.

In 2012 and the years that follow, creating an effective approach to managing the ever-widening risk landscape remains a work in progress. Many Organizations are still struggling to improve their overall management of risk, whether that means identifying the risks that matter most or finding effective ways to link their strategy with the day-to-day handling of business risks. Companies are scrambling to fix weak links in their system, often stemming from non-traditional risks that have risen to the forefront in today's new marketplace— for example, risks from new social media and digital technology, competition from emerging markets and the supply and demand of global talent. In this new risk era, Corporate Boards and Senior Management have a crucial role to play.

At present, the India's exchange rate policy essentially focuses on managing volatility with no fixed rate target while allowing the underlying demand and supply conditions to determine the exchange rate movements over a period in an orderly way. The Reserve Bank continues to follow the approach of watchfulness, caution and flexibility in regard to foreign exchange market. It co-ordinates its market operations carefully, particularly in regard to the foreign exchange market with appropriate monetary, regulatory and other measures as considered necessary from time to time. The conduct of exchange rate policy in India is currently guided by three major purposes. First, to maintain orderly conditions in the foreign exchange market by providing foreign exchange as considered necessary from time to time and to prevent the emergence of destabilizing and self-fulfilling speculative activities. Second, to help maintain an adequate level of foreign exchange reserves. Third, to help eliminate market constraints with a view to facilitating the development of a healthy foreign exchange market. The risks emanating from exchange rate movements should be borne by the parties concerned and they should be encouraged to use hedging products for their risk-management.

Recent World events, for example, highlight the fact that economic surprises can subject Governments to enormous pressures to relax or repeal taxes or other policies perceived to impede economic growth. For a climate policy to survive future shocks, therefore, it must have dynamic consistency and be optimal for each Government to continue to enforce the policy even when confronted with sharp departures from the conditions expected when the Governments undertook the commitments. Thus, a climate regime that exacerbates downward macroeconomic shocks or depresses the benefits of positive macroeconomic shocks would be more costly and less stable than a system that better handles global business cycles and other volatility.

The challenge is to move from an essentially reactive risk management philosophy to a proactive mindset that anticipates coming risks and helps position an organization for new threats and opportunities. Reassigned the risk owners and moved the governance of risk from the Audit Committee to the Board discussing about the risk management related issues.

The Boards of Directors have become more engaged with risk issues and have been seeking to improve their ability to define and communicate a clear, organization wide risk appetite. The shift from an operational to a strategic risk perspective and the elevation of the Chief Risk Officers role, which in previous years had largely been found at financial services firms. This new C-suite role requires a new kind of risk manager, who is strategic, collaborative and business-focused. New CROs are being given the ability to have a real impact on both business decisions and operations and are responsible for expanding the Company's comprehensive Risk Management practices to establish a more integrated, enterprise-wide approach. CRO is required to report to the CEO and to integrate risk management systems across corporate departments and functions.

Large Global Organizations tend to have developed more complex management and operational structures, leaving them vulnerable to breakdowns in internal communication and understanding. The risk function is only one element of this, but it is often the one that is perceived as inadequate, vulnerable or blameworthy when things go wrong. Risk Managers and other Senior Executives are wrestling with this issue in both its external and internal dimensions.

Organizations are turning to more sophisticated tools such as early warning systems and contingency plans as they reconfigure their approaches to managing risk to improve analytics and risk modeling through scenario analysis and other risk management techniques that map out, monitor, readjust and respond to alternative scenarios.

The Organisations would in future times, continue to adopt the integrated risk management processes viz; Enterprise risk management (ERM), ORM (operational risk management), and BCM (business continuity management).

Some Organizations, however, are taking the lead in allocating Internal Audit, a role that enhances overall risk management. For instance at Microsoft, internal audit has earned a seat at the table and demonstrates how it can create business value.

Efforts to manage risk more holistically or in a more integrated fashion can be hampered by the difficulty of finding Risk Professionals from a sufficiently diverse set of background.

Companies continue to integrate risk management into decision-making processes relating to “traditional” functions such as strategic planning.), investment/divestment, budgeting/forecasting and performance measures.

Corporate Governance and Risk Management

If there is a key to successful risk taking, it is to ensure that those who expose a business to risk or respond to risk make their decisions with a common purpose in mind – to increase the value of their businesses. If the interests of the decision makers are not aligned with those who own the business, it is inevitable that the business will be exposed to some risks that it should be not be exposed to and not exposed to other risks that it should exploit.

In recent years, we have seen a spirited debate about Corporate Governance and why it is important for the future of business. In particular, proponents of strong Corporate Governance argued that strengthening the oversight that Stakeholders and Directors have over Managers allows for change in badly managed firms and thus performs a social good. The link between Corporate Governance and risk taking is not only intuitive but is backed up by the evidence. A study of 5452 firms across 38 Countries looked at the link between risk taking and corporate governance by defining risk in terms of standard deviation in EBITDA over time, as a percent of total assets and relating this number to measures in corporate governance were better protected – i.e., high in corporate governance – tend to take more risk in operations. The appropriate corporate governance structure for the risk taking firm would, therefore, require decision makers to be invested in the equity of the firm but to be diversified at the same time, which is a tough balance to maintain since one often precludes the other. Once you have aligned the interests of decision makers with those of claimholders in the firm and hired good risk takers, the reward and punishment mechanism has to be calibrated to reward good risk taking behavior and punish bad risk taking behavior. The culture of a firm can also act as an engine for or as a brake on sensible risk taking. Some firms are clearly much more open to risk taking and its consequences, positive as well as negative. One key factor in risk taking is how the firm deals with failure rather than success, after all, risk takers are seldom punished for succeeding. Good risk taking organizations treat failure and success not as opposites but as complements since one cannot exist without the other.

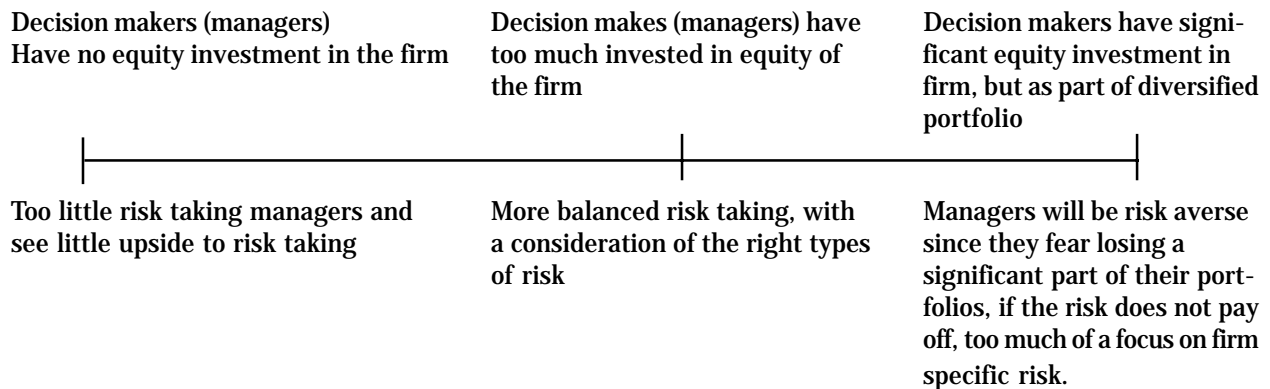


Figure 5 : Corporate Planning for Risk Management

Hedge Accounting

Hedge Accounting is a complex process involving numerous and technical requirements with the objective to avoid temporary undesired volatility in Profit and Loss Account. This volatility is the result of valuation and or timing mismatch between the hedged item and the hedge instrument.

International Accounting Standard 39 (IAS 39) for Hedge Accounting

It establishes uniform hedge accounting criteria for all financial assets, financial liabilities and derivatives and recognizes symmetrically the offsetting effects on net income of changes in fair value of the hedging instrument and the hedged item in order to reduce volatility in the Income Statement. For this purpose, the Enterprise must formally designate a hedging instrument to a related item or to a group of similar items being hedged and to assess and document the effectiveness of transactions that receive hedge accounting. By increasing the use of fair values in accounting for financial instruments and implementing provisions for certain embedded derivatives, as well as consistent accounting standards for the use of hedge accounting, IAS 39 will affect many companies. Its compliance will have major, widespread impact on users of financial instruments. Volatility in the Income Statement and in equity require significant changes in financial risk management strategies and to business processes and systems. Infact, it is a forward looking approach to measure expected hedge effectiveness at inception and a backward looking approach to measure realized hedge effectiveness throughout the life of the hedge. It requires additional disclosures in the Financial Statements relating to accounting policies, hedging and financial instruments and further requires a multi-disciplinary effort which demands treasury, operations, risk management and accounting expertise.

Effective steps for risk management in uncertain times

- Increased integration of risk.
- Management with decision-making.
- IT infrastructure.
- Quality of Board level/Senior Professionals.
- Management governance.
- Better analytics and risk modeling.
- Improved data quality and reporting system.
- Better cross-functional/departmental communication.
- The Role of Internal Audit in assuring data security and privacy.
- Knowledge Management for understanding the growing and volatile markets as a competitive advantage.
- Corporate Financial hedging through derivatives viz; forwards, currency and interest rate swaps.

Benefits of Risk Analysis and Management

There are five ways in which you can make use of risk to gain an advantage over your competitors. The first is access to better and more timely information about events as they occur and their consequences, allowing you to tailor a superior response to the situation. The second is the speed with which you respond to the changed circumstances in terms of modifying how and where you do business; by acting faster than your competitors, you may be able to turn a threat into an opportunity. The third advantage derives from your past experience with similar crises in the past and your knowledge of how the market was affected by those crises, enabling you to respond better than other firms in the business. The fourth derives from having resources – financial and personnel – that allow you to ride out the rough periods that follow a crisis better than the rest of the sector. The final factor is financial and operating flexibility, being able to change your technological base, operations or financial structure in response to a changed environment can provide a firm with a significant advantage in an uncertain environment.

Conclusion

In the overall analysis, it can be stated that the World Economies are under continuous pressure of economic crises, uncertainty, rising prices, cut throat competition evidenced by high volatility in market place. As such, the survival and growth of the countries across the globe requires a forward looking approach with high flexibility and adaptability to cope up with the pace of 'change in economies' coupled with effective Risk Management Strategies, Government controls and Regulations, Scenario analysis. Infact, it requires an effective planning, having more timely and reliable information when confronted with a crisis and allowing to map out a superior plan of action in response to risks to meet the challenges of economic uncertainty. In such an environment, perhaps the optimal strategy is to follow a steadier course, keeping policy instruments focused on the domestic forces that policy can expect to influence, while allowing automatic stabilizers such as exchange rates and the tax system to deal with the constant changes of a still febrile international environment.

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COMPLIANCE EFFORTS TO MITIGATE COMPETITION RISK IN VOLATILE BUSINESS ENVIRONMENT

VINAY KUMAR SANDUJA*

Introduction

Competition/Antitrust issues in India are now governed by the Competition Act, 2002 (“the Act”). In today’s volatile business environment, it is important for the business operating in India to assess the impact of competition/antitrust rules on its business operations from competition perspective. In this context, businesses should identify the conduct that exposes them to a serious risk of substantial fines for breaching the rules of competition law. Generally speaking, it is easy to identify the most serious anti-competitive behavior such as price fixing, bid rigging and market sharing etc. and to proscribe such behavior as part of compliance and risk management strategy. However, in today’s complex business environment where commercial strategies are interdependent, it often becomes difficult to distinguish the lawful business behavior from the unlawful. For instance, the line between accepted and forbidden practices is very thin particularly on issues like abuse of dominant position by market player or definition of product and geographic markets. Aforesaid, in turn, may give rise to unintended competition law risks of violating the competition law rules which may be serious for any business in terms of significant financial penalties; agreements being declared void including directions by the competition authority; and loss of reputation and goodwill.

How the New Competition Regime in India may affect Businesses ?

The Act applies to businesses of all sizes, including government undertakings covering activities both within and outside India across all sectors. Further, the Act is applicable to activities, agreements and conduct of all departments of Government, statutory bodies and excludes only those activities of the Government which are relatable to the sovereign functions of the Government including all activities carried on by the departments of the Central Government dealing with atomic energy, currency, defense and space.

Although the Act was passed in 2002, the prohibitions against anti-competitive

* Dua Associates, Advocates, New Delhi

agreements¹ and abuse of dominant position² came into effect on May 20, 2009 whilst the provisions pertaining to regulation of combinations³ which includes M&As that are above relevant thresholds in terms of assets or turnover to be pre-cleared by the Competition Commission of India (“CCI”) before the transaction can be closed entered into force on June 01, 2011.

Anti-competitive conduct, whether in the form of anti-competitive agreements or abuse of dominant position is prohibited under the Act, exposing the businesses involved to very significant penalties for infringement of the Act. Further, M&A transactions which qualify as combination under the Act will be reviewed by the CCI to assess whether the transaction is anti-competitive. When the Act came into effect, there was considerable uncertainty as to how it would be applied in practice by the CCI. After three years, the basic contours of enforcement under the Act are beginning to emerge and perhaps the most important lesson to date is that the CCI is committed to aggressive enforcement of the new law and it appears that vigorous enforcement of the Act is here to stay. That said, it may be noted that, following the enforcement of the Act, it appears that there is greater opportunity for the CCI to obtain information with regard to anti-competitive activities in Indian markets.

It is noteworthy that the Act will prohibit many practices that have been previously common in India. CCI, tasked to enforce the Act, has substantial enforcement powers including substantial discretion to collect and evaluate evidence on the manner in which a particular arrangement affects the consumer or the relevant market, as the Act leaves it substantially

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- 1 Section 3 of the Act provides that anti-competitive agreements are void and prohibits businesses from entering into any agreement in respect of production, supply, distribution, storage, acquisition, or control of goods or services that causes or is likely to cause an appreciable adverse effect on competition within India. As in other jurisdictions, the definition of ‘agreement’ is very broad and encompasses not only written but also oral arrangements and understandings and even implicit agreements. Further, it may be noted that the Act applies to horizontal agreements (e.g. cartels) and vertical commercial agreements, such as distribution and supply agreements.
 - 2 Section 4 of the Act prohibits any conduct on the part of enterprise or group, which is an abuse of dominant position, in a relevant market in India. Importantly, the Act does not prohibit a business from being dominant but prohibits a dominant enterprise from abusing its dominant position. Examples of abusive behavior by a dominant enterprise or group include imposition of unfair or discriminatory condition in purchase or sale; or price in purchase or sale of goods or services (including predatory price) of goods or service.
 - 3 Section 5 of the Act, which sets out the various types of “combinations” contemplated by the Act is very widely and comprehensively worded and both domestic and cross border transactions will be affected if the acquirer’s and the target’s asset values or turnover is in excess of the prescribed threshold. In such cases the transaction will have to be examined to ascertain whether they are within the footprint of Section 5, or within any special exemptions provided in the Act or procedural regulations issued by CCI or any notification by the Government of India, and unless exempted, the proposed transaction will have to be notified to the CCI. Further, there is standstill obligation, i.e. the combination must not be implemented before its notification and until it has been cleared pursuant to the CCI decision or 210 days whichever is earlier. That said, it may be noted that Section 6 of the Act inter alia stipulates that if a ‘combination’ cause or is likely to cause an appreciable adverse effect on competition in the relevant market in India, such combination shall be void.
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to the CCI to decide the various parameters and yardsticks as provided in the Act that will ultimately determine whether an arrangement is anti-competitive.

Penalties for Infringement of the Act

The Act bestows substantial discretion on CCI to decide the penalty amount in case it comes to conclusion after inquiry that there has been violation of the Act. Before discussing various types of penalties for contravention of the provisions of the Act, let us briefly examine the Section 48 of the Act which provides that where a contravention of the provisions of the Act or order, direction etc. is committed by a company then every person who at the time of contravention was in charge of and was responsible to the company for the conduct of business of the company shall be deemed to be guilty of the contravention and shall be liable to be proceeded and punished accordingly. However, in such cases, a limited due diligence defense is provided by the Act in the sense that if person liable to any punishment proves that the contravention was committed without his knowledge or that he had exercised all due diligence to prevent the commission of such contravention. Having said that it is pertinent to note that where a contravention has been committed by a company and it is proved that the contravention has taken place with the consent or connivance of or is attributable to any neglect on the part of any director, manager, secretary or other officer of the company then aforesaid officers shall also be deemed to be of that contravention and shall be liable to be proceeded against and punished accordingly. From the aforesaid it appears that violation of the Act by companies will render officers of the company deemed to be guilty of the contravention in the circumstances discussed above.

Penalty for anti-competitive agreements and abuse of dominant position

In case of violation of section 3 relating to anti-competitive agreements or section 4 relating to abuse of dominant position, the CCI can impose such penalty as it may deem fit which shall be not more than 10% of the average of the turnover for the last three preceding financial years upon each of such person or enterprise which are party to such agreement or abuse. In case of cartels, a penalty of up to three times of its profits for each year of the continuance of such agreement or 10% of its turnover for each year of the continuance of such agreement whichever is higher. That said, it may be noted that various orders can be passed by CCI including cease and desist order; directions to modify agreement; directions to abide by such other orders as it may pass and comply with the directions including payment of costs (if any). In relation to aforesaid, it is noteworthy that if CCI comes to finding that an enterprise in contravention of section 3 or 4 of the Act is a member of a group and other members of such group are also responsible for or have contributed to such contravention then it may pass aforesaid orders against such members of the group. CCI can also order division of enterprise enjoying dominant position to ensure that such enterprise does not abuse its dominant position.

Penalty in case of regulation of combinations

Failure to give notice to CCI in relation to combination attracts penalty which may extend to 1% of the total turnover or the assets whichever is higher of such combination. Further,

the Act provides for penalty of not less than Rs. 50 Lakh but which may extend up to Rs. 1 crore for making false statement or omission to furnish material information in relation to combination.

Contravention of orders of CCI

Contravention of orders of CCI without reasonable cause can attract fine which may extend to Rs. 1 Lakh for each day during which non-compliance occurs subject to a maximum of Rs. 10 crore. Further, any non-compliance with the aforesaid order is punishable with imprisonment for a term which may extend to 3 years or with fine which may extend to Rs. 25 crore or both by the Chief Metropolitan Magistrate upon a complaint filed by CCI.

Other Penalties

Failure to comply with directions of CCI and Director General (DG) without reasonable cause attracts penalty which may extend to Rs 1 Lakh for each day during which such failure continues subject to maximum of Rs. 1 crore. Further, any person who makes any statement or furnishes any document which he knows or has reason to believe to be false in any material particular; or omits to state any material fact knowing it to be material; or willfully alters, suppresses or destroys any document which is required to be furnished shall be punishable with fine which may extend to Rs. 1 crore.

Execution of orders of CCI imposing monetary penalty

Failure to pay any monetary penalty imposed by CCI will be recovered by CCI in the manner specified by The Competition Commission of India (Manner of Recovery of Monetary Penalty) Regulations, 2011. The said Regulations provide that to recover a penalty from an enterprise, the CCI shall issue "Demand Notice". Where an enterprise makes default, CCI issues "Recovery Certificate" to realize the amount of penalty imposed upon enterprise in default and authorizes its Recovery Officer to proceed for recovery of penalty imposed in accordance with various modes specified in the said Regulations including attachment and sale of movable and immovable property of the enterprise. CCI can also make reference to the Income Tax Authority for recovery of the penalty as "tax due" under the Income Tax Act, 1961.

Orders of CCI Imposing Penalties for Violation of Provisions of the Act

The prohibitions under the Act in relation to anti-competitive agreements and abuse of dominant position have been robustly enforced by the CCI. In this regard, we may now look at some of recent cases which came before CCI and in which penalties were imposed by CCI for contravention of provisions of the Act.

- In *FICCI-Multiplex Association v/s United Producers/Distributors Forum & Ors*, CCI imposed a penalty of Rs. 1 Lakh on each of 27 opposite parties.
- In *MCX Stock Exchange Ltd. v/s National Stock Exchange of India Ltd. & Ors*, CCI imposed a penalty of Rs. 55.5 crores being 5% of the average of 3 years annual turnover.

- In *Belaire Owner's Association v/s DLF Limited and HUDA*, CCI imposed a penalty of Rs. 630 crore @ 7% of the average of 3 years annual turnover.
- In *Uniglobe Mod Travels Private Limited v. Travel Agents Federation of India*, CCI has imposed a fine of Rs. 1 Lakh on each member of the travel agents associations.
- In *Kapoor Glass Private Limited v/s Schott Glass India Private Limited*, CCI levied a penalty of Rs 5.66 crore @ 4% of average turnover of preceding three years.
- In *Re : suo-motu case against LPG cylinder manufacturers*, CCI imposed aggregate penalty of Rs 169.59 crore @7% of the average turnover of the companies. However, in relation to Hyderabad Cylinders Ltd. a penalty @ 2.1 times of its net profit was imposed as details of turnover were not available.
- In *Explosive Manufacturers Welfare Association v/s Coal India Limited and its Officers*, CCI imposed penalties @ 3 % on average of three years turnover on the ten explosive suppliers aggregating to about Rs 58.83 crore.
- In *Varca Druggist & Chemist & Ors. v/s Chemists and Druggists Association, Goa*, CCI imposed penalty of Rs. 2 lakhs being 10% of average turnover for financial years 2008-09 and 2009-10.
- In *Re : Aluminium Phosphide Tablets Manufacturers*, CCI imposed penalty on three aluminium phosphide tablet manufacturers of more than Rs. 300 crore @ 9% of average turnover of three years.
- In *M/s Kasan News Pvt. Limited v/s Fastway Transmission Private Limited & Ors*, CCI imposed a penalty of more than Rs. 8 crores calculated @ 6% of average turnover of last three preceding financial years on Multi System Operators for violation of provisions of the Act.
- In *Builders Association of India v/s Cement Manufacturer's Association & Ors*, CCI has imposed penalty of more than Rs. 6000 crores on cement companies @ 0.5 times of net profit for 2009-2010 (effective May 20, 2009) and 2010-2011 on each cement company named as opposite party in the present case.⁴ As regards, Cement Manufacturers Association, a penalty of 10% of its average total receipts of two years has been imposed by CCI since it provided a platform to cement companies and facilitated cartelization in the aforesaid case.

Implications for Businesses

As regards implications for businesses is concerned, it may be noted that in case competition law violations are found, businesses may not only suffer financial losses as a result of imposition of fines and penalties (as discussed above) but also damage to their reputation established over the years. Furthermore, an infringement of the provisions of the Act may expose the infringing party to significant claims for compensation before the Competition Appellate Tribunal ("COMPAT"). Aforesaid may raise serious implications for businesses. For instance, formerly acceptable behavior may, in many cases, no longer go

⁴ For the purposes of calculation of penalty on cement companies, period from 1/04/2009 to 19/05/2009 has not been considered by CCI and amount of penalty has been calculated accordingly for 2009-10.

unchallenged. It is in this context, businesses operating in India may carry out self assessment of their business practices by taking steps to ensure that their practices, business contracts and dealings comply with the provisions of the Act.

Self Assessment of Competition Risk by Businesses to Achieve Compliance

Indian competition law operates on a “self-assessment” basis, meaning that businesses must determine for themselves whether its agreement, conduct, M&A transaction will be lawful or could breach the provisions of the Act particularly in view of the fact that there are no block exemptions, market share based test to evaluate anti-competitive conduct as prevalent in other matured jurisdictions such as EU.

Anti-competitive agreements

It is advisable that businesses carry out a self-assessment of the possible consequences of their commercial agreements. The issue is to judge whether an agreement has appreciable adverse effect on competition in terms of section 3 of the Act. Analysis of commercial agreement to determine whether it is caught by section 3 of the Act can only be made on a case-by-case basis. That said, it may be noted that certain horizontal agreements like price fixing, allocation of markets, bid rigging etc. are presumed to have appreciable adverse effect on competition. Further, the Act expressly recognizes that the provisions relating to anti-competitive agreements shall not restrict the right of any person to restrain any infringement of, or to impose reasonable conditions, as may be necessary for protecting any of his rights which have been or may be conferred upon him under various intellectual property rights (IPR) statutes mentioned under the Act. Having said that it may be noted that as with other provisions of the Act, aforesaid analysis often involves complex economic reasoning. Once an agreement is found to be restrictive of competition under the provisions of the Act relating to anti-competitive agreements, it also becomes necessary to determine the pro-competitive benefits produced by that agreement (if any) and to assess whether these pro- competitive effects outweigh the anti-competitive effects. Scheme of the Act provides that pro-competitive effects may include accrual of benefits to consumers; improvements in production or distribution of goods or provision of services; promotion of technical, scientific and economic development by means of production or distribution of goods or provision of services. Whereas anti-competitive effects may be in the form of creation of barriers to new entrants in the market; driving existing competitors out of the market; foreclosure of competition by hindering entry into the market.

In the aforesaid context, it is submitted that businesses should be alert to the possibility of competition issues that may arise depending upon the nature of commercial agreement and particularly while entering into horizontal agreements including Joint Ventures as these are generally viewed as high risk category from competition law perspective.

Abuse of dominant position

Since a dominant firm is not exposed to efficient competitive constraints, it is “subject to a special responsibility not to allow its conduct to impair genuine competition in market” as observed in Michelin I, Case 322/81[1983] ECR 3461 para 57. Similarly, it may be noted that

the actions of dominant enterprises may also be looked into by the CCI if it results in abuse of dominant position as per the provisions of the Act, businesses should carry out self assessment whether their conduct can be viewed as abuse of dominant position by CCI. For the purposes of self assessment, business should first ask themselves whether it is dominant in a relevant market. This must be done taking into account the factors outlined in the Act including market share; size and resources; size and importance of the competitors; economic power of the enterprise including commercial advantages over competitors; vertical integration of the enterprises or sale or service network of such enterprises; dependence of consumers on the enterprise; monopoly or dominant position whether acquired as a result of any statute or by virtue of being a Government company or a public sector undertaking or otherwise; entry barriers including barriers such as regulatory barriers, financial risk, high capital cost of entry, marketing entry barriers, technical entry barriers, economies of scale, high cost of substitutable goods or service for consumers; countervailing buying power; market structure and size of market; social obligations and social costs; relative advantage, by way of the contribution to the economic development, by the enterprise enjoying a dominant position having or likely to have an appreciable adverse effect on competition. However, it may be noted that any other factor which the CCI may consider relevant for the inquiry can also be taken into account for determining dominant position of an enterprise.

Under the Act, merely being dominant is in itself not an issue. Therefore, having determined that business is in dominant position, it should assess whether the business has abused its dominant position in terms of section 4 (2) of the Act which include imposition of unfair or discriminatory condition in purchase or sale; or price in purchase or sale of goods or services (including predatory price) of goods or service; or indulging in practice or practices resulting in denial of market access in any manner; or making conclusion of contracts subject to acceptance by other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts; or using its dominant position in one relevant market to enter into, or protect, other relevant market.

Mergers & Acquisitions (M&As)

Merger and acquisition (M&A) transactions which are above certain prescribed threshold limits in terms of assets or turnover as laid down in the Act are subject to combination review in accordance with the provisions of the Act. In the aforesaid context, it may be noted that for the purposes of compliance with the provisions relating to regulation of combinations under the Act, it is advisable parties to M&As develop strategies to mitigate competition risk and in turn protect business interest in the event of a challenge to transaction by CCI. In other words, businesses must carry out self assessment of (a) Inquiry risk i.e. the risk that the legality of the transaction will be put in issue; (b) Substantive risk i.e. the risk that the transaction will be found to be anti-competitive and hence void; (c) remedies risk i.e. the risk that the transaction will be prohibited or restructured by way of modification by the CCI. For the aforesaid purposes, it needs to be first assessed as to whether the mandatory notification is required or any exemption is available under the Act or procedural regulations framed by CCI or any notification by the Government. If the notification is required then parties to

M&A needs to determine in which Form (i.e. Form I or II) transaction must be notified including preparation of duly filled in Form which often requires economic data gathering and analysis. Thereafter, if a transaction looks likely to become subject to detailed investigation by CCI parties to M&A must make the best case to the CCI by providing the evidence that the benefits of the combination outweigh the adverse impact of the combination, if any. A case can also be made out before CCI that the transaction under review is relatively advantageous by way of the contribution to the economic development. In case, CCI still views transaction to have or likely to have appreciable adverse effect on competition, then parties to M&A need to negotiate remedies (if possible) by way of modification to the transaction which may include restructuring the transaction itself to remove the competition concerns of CCI. For getting the deal through, businesses will have to comply with rigorous and strict compliance of the timelines as provided in the Act and procedural regulations made by CCI.

To sum up, parties to M&A deal must at the earliest of deal negotiation process should self assess the following:

- Whether the transaction trigger pre-combination filing notifications, which result in waiting periods, suspending closing as well as potential extensive information requests;
- Whether the transaction involves any substantive competition/antitrust risk and how such risk should be allocated; and
- How to avoid “gun jumping”, i.e., premature pre-closing activity involving sharing of competitively sensitive information or joint marketing, production, or premature completion of a deal.

Competition Compliance Program to Mitigate Competition Risk

It may be reiterated that all businesses operating in India should carry out self assessment of their business practices by taking steps to ensure that their practices, business contracts and dealings comply with the provisions of the Act. In this regard, businesses should think of compliance with competition law as an important management tool and good business practice that can lead to success and profitability. Traditional competition compliance programs are typically broad in scope and often standardized. Corporations are generally advised to have competition compliance program in place taking into account the market in which it operates, its position in the said market etc. which may consist of training on competition related issues for its employees; devising competition compliance manual; preparation of competition compliance checklists in order to ensure compliance with the rules of competition law. Compliance programs like those described above are designed for ensuring compliance with the competition rules, to disseminate knowledge of what constitutes violation of the aforesaid rules and to create culture of compliance.

However, apart from aforesaid, businesses should also use current enforcement efforts of competition authority to target compliance efforts and mitigate their exposure which often require timely information and prompt assessment of business that may become subject to competition law investigation. In other words, by keeping abreast of enforcement efforts

of competition authority, a business can augment its compliance efforts (as discussed above) and increase the likelihood of avoiding severe penalties. In this regard, it may be noted that, a business that is not involved in any existing investigation but is looking to protect itself from being subject to such investigations may adopt risk based compliance approach by learning about new competition law developments including investigations and devising a system to navigate whether the business has any competition law exposure and assess the results of such navigation and quickly determine how to proceed. That said, it may be noted that failing to monitor and assess risks created by competition law investigations by competition authority may increase the likelihood that a business will fail to detect competition law violation.

Best Practices in Relation to Competition Compliance Program

The competition authorities the world over provide businesses an elaborate guidance to put in place the competition compliance program. Towards this end, the authorities publish guidelines on various aspects of competition law. Several competition authorities such as Australia, Canada, and Japan provide “template” or framework for competition compliance program. In this context, it may be noted that CCI’s advocacy booklet “COMPETITION COMPLIANCE PROGRAMME FOR ENTERPRISES (A Suggested Framework for compliance of the Competition Act, 2002 by Enterprises)” is a timely reminder to all businesses, large and small, that no one can afford to ignore the consequences of breaking competition rules. Taking clue from the practices being followed in other jurisdictions and those discussed in CCI advocacy booklet, businesses in India will also be able to protect themselves and their employees from adverse consequences of violations of competition law and also from being victim of anti-competitive behavior of other enterprises by adopting competition compliance program.

Role of Professionals

Professionals such as Lawyers, Company Secretaries, Chartered Accountants, and Cost Accountants have been statutorily recognized under the Act to represent businesses before CCI and COMPAT. In the aforesaid context, professionals apart from representing businesses before CCI and COMPAT can also seize the opportunity to provide competition law risk management services as discussed above including carrying out self assessment of competition risk on behalf of businesses to achieve compliance and assist businesses in establishing effective Competition Compliance Program to mitigate competition risk. In this regard, Company Secretary acting as Compliance Officer in an enterprise can become focal point while designing a competition compliance program, motivating officers and employees, preparing compliance manual etc.

Conclusion

Businesses with operations in India need to take into account the competition rules as provided in the Act in managing their business. In this context, it is vital for businesses to establish a competition law compliance regime, having examined the risks associated with competition law violations in the Act particularly in view of the fact that no business can

afford to ignore the consequences of breaking competition rules. Aforesaid call for specific, risk-based advice from competition/antitrust professionals including Lawyers, Company Secretaries, Chartered Accountants, and Cost Accountants. Further, each business should conduct its own risk identification and assessment and identify the risk mitigation activities taking into account enforcement efforts of CCI.

WORLD TRADE ORGANIZATION AND INDIA : A CRITICAL ANALYSIS

LALIT MOHAN SHARMA*

Introduction

The General Agreement on Tariffs and Trade (GATT) was originated in January 1948 to achieve harmonious trade relations at global level on the basis of multilateralism, globalization and international economics. The GATT was founded in Geneva to enlarge international trade. International trade deals with transactions between countries and is beneficial not only to the member countries but also the world at large. The GATT is a contractual agreement; the members are not bound by any structures of the forum. Its draft was a reflection of the direction taken by reforms around the world. It is a means to make these reforms mutually supportive and mutually compatible.

The last and largest GATT round, was the Uruguay Round which lasted from 1986 to 1994 and led to the creation of WTO. The GATT mainly dealt with trade in goods whereas the WTO and its agreement now cover trade in services, and in traded inventions, creations and designs which is included under intellectual property.

The World Trade Organization (WTO) is the only international organization dealing with global rules of trade between nations. The open trading system is based upon multilaterally agreed rules between the nations at a global or near-global level. Its main function is to ensure that trade flows as smoothly, predictably and freely as possible. World Trade Organization (WTO), a successor of the General Agreement on Tariffs and Trade (GATT), was established on 1st January 1995 which marked the biggest reforms of international trade since the second war. At present the WTO has 155 Member Countries of world trade including approx 100 developing countries representing more than 90% of world trade. The WTO began life on 1st January 1995, but its trading system is half a century older. The second WTO ministerial meeting, held in Geneva in May 1998, included a celebration of the 50th anniversary of the system. Over the years GATT evolved through several rounds of negotiations.

The WTO headquarter is based at Geneva (Switzerland) and is headed by Mr. Pascal Lamy appointed as fifth Director General w.e.f. 1 September 2005 for a four-year term. In appreciation to their contribution in the world trade, WTO members reappointed Mr Pascal Lamy for a second successive four-year term, commencing from September 1, 2009.

* ACS, LL.M.(Topper), M.Sc.(Chem.), ADPMIR, PGDIPR.

Development in any field of law provides new avenues in order to cater the needs and to fulfill the aspirations of any civilized society at any given point of time. The WTO provide a legal and institutional base for international trade where member countries governments can formulate their own domestic trade policy and provide the platform upon which trading relations among countries could evolve through collective debate, negotiation and adjudication.

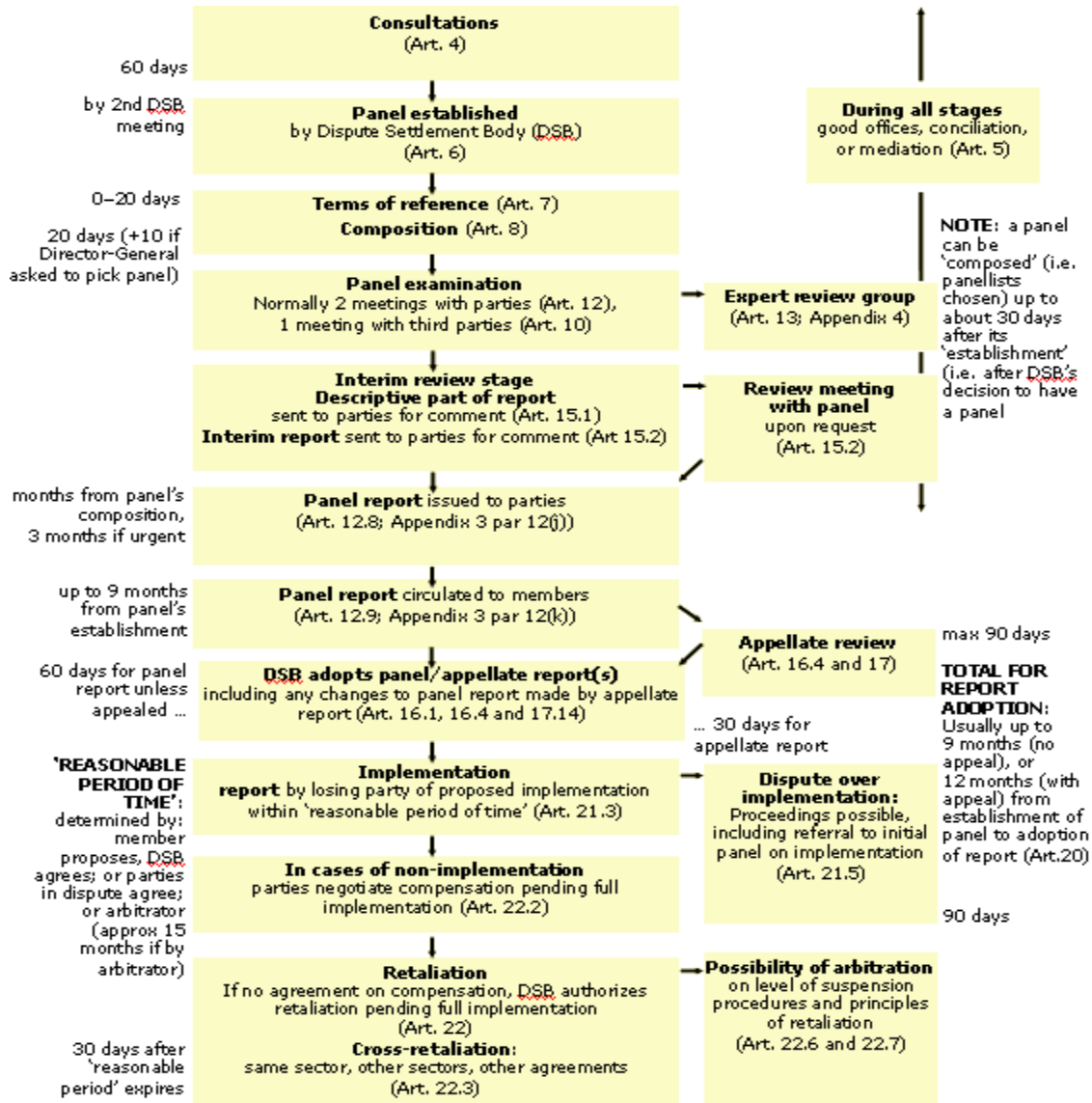
The WTO was created so that there could be an international organization with a firm legal basis covering full range of trade issues. The GATT continues to Exist as one of the WTO agreements. The GATT deals with trade in services and the agreement on trade aspects of intellectual property such as copyright, trademarks, patents, industrial designs and trade secrets.

The WTO replaced GATT as an international organization, but the General Agreement still exists as the WTO's umbrella treaty for trade in goods, updated as a result of the Uruguay round negotiations. Trade lawyers distinguish between GATT 1994, the updated part of GATT and GATT 1947, the original agreement which is still the heart of GATT 1994. The main goal is to improve the welfare of the peoples of the member countries.

The Uruguay Round took nearly eight years, almost twice the original schedule. By the time the Uruguay round comes to an end, 123 countries were taking part in it. It covers almost all trade from toothbrushes to pleasure boats, from the genes of wild rice to AIDS(Acquired Immune Deficiency Syndrome) treatments, from banking to telecommunication. It was quite simply the largest trade negotiations ever and most probably the largest negotiations of any kind in history of global trade.

There were various stages in which disputes were settled in WTO. At all stages, countries in disputes are encouraged to consult each other in order to settle "out of court". At all stages, the WTO director-general is available to offer his good offices, to mediate or to help achieve a conciliation. All the stages of the dispute settlement process under WTO can be shown diagrammatically as:

DISPUTE SETTLEMENT PANEL*



* Source: http://www.wto.org/english/thewto_e/whatis_e/tif_e/disp2_e.htm

Note : some specified times are maximums, some are minimums, some binding, some not.

The main principles on which WTO works is as follows:

1. **No-Discrimination** : A country should not discriminate between its trading partners and they are all equally granted MFN(Most Favoured Nations) Status. It should not

discriminate between its own and foreign products, services or nationals i.e. they are given National Treatment.

2. *Competition* : It creates more competitive environment by discouraging “unfair” practices such as export subsidies and dumping products at below cost to gain market share.
3. *Freedom* : WTO provides full freedom with barriers coming down through negotiations.
4. *Prediction* : Foreign Companies, investors and governments should be confident that trade barriers including tariffs, non-tariff barriers and other measures should not be raised arbitrarily. More and more tariff rates and market opening commitments are bound in the WTO.
5. *Benefits* : WTO is more beneficial for less developed countries by giving the more time to adjust, greater flexibility and special privileges.

WTO : An Open Debate

Financial and economic turmoil has shaken much of the world in the last few months, affecting most of Asia and Russia in particular, and presenting new challenges for many other countries. This crisis calls for a sense of collective responsibility, as urgently as at any other time in the post-war period. From the perspective of the global trading system, this means three things.

First, it requires a clear and continuing commitment by governments to the multilateral trading system and a firm resolution to resist protectionism.

Second, a fresh impetus toward trade liberalization would contribute to the resolution of the crisis and would send a positive signal to the markets.

Third, renewed efforts to bring the countries outside the system, including Russia and China, into the World Trade Organization would help to complete the global economic architecture for which the need has been so strongly demonstrated.

History tells us that this has been a major mistake. The growing economic crisis of the late 1920s became a full-blown recession when governments closed their borders to trade, making the pain more severe and the recovery slower. Today, with national economies ever more connected, and with 25 per cent of global output now being exported, resort to protectionism would be more costly still. Developing countries, with a trade/GDP ratio of 38 per cent, depend even more than advanced economies on trade to sustain growth.

Nations cannot hope that their exports will be freely accepted in foreign markets or that capital and technology will flow freely across borders, unless they accept their own share of responsibility in addressing the current global economic difficulties. This applies to developed and developing countries alike.

It is fortunate in this context that the WTO already has an impressive agenda, combining implementation, further negotiations and the preparation of key decisions about the future

development of the system, which are to be taken at next year's third Ministerial Conference in the United States. As they prepare for that meeting, a top priority for WTO Members will be to consider whether to extend this negotiating agenda and in what direction – whether, for example, to launch negotiations on trade and investment, trade and competition and transparency in government procurement. A number of Members want to see industrial goods included as well, and other issues such as the interface between trade and the environment have also been promoted as possible elements of a broader negotiating agenda.

The process of working towards agreement on these and other related issues should help to focus attention on the contribution the trading system can make to renewing confidence and growth. However, it will not do so automatically. The commitments already undertaken offer both reassurance in our present problems and a launching pad for future progress, but only if we can maintain the vision and the resolve to act on them fully and energetically. The need is greater than ever for governments to maintain their adherence to the rules of the system and to work constructively within it.

The evolution of the WTO over the past years provides encouraging evidence that its Members recognize and are willing to act on this need. The outstanding example is the commemoration of the 50th anniversary of the multilateral trading system in May 1998 – an event which brought together world leaders and ministers from every region, every background and every stage of development. This was far more than a ceremonial occasion.

It demonstrated how far the world has come towards constructing a truly global economic system. Even during this period of significant change and uncertainty, not a single speaker at the 50th anniversary meeting questioned the validity of multilateral trade or of the WTO. Even if each one had a different perspective, reflecting different backgrounds and historical experiences, all the leaders present saw the multilateral trading system as indispensable to growth and stability in our interdependent world.

The past year has also seen increased emphasis on the importance of thorough, timely implementation of existing commitments. This was a major theme of the second Ministerial Conference, and of the Ministerial Declaration it produced. It is accompanied by a general recognition that more needs to be done to assist Members – especially developing and transition economies. The WTO's technical cooperation programmes are being expanded, thanks to the contribution of a few Members who have voluntarily provided significant extra funds to augment the limited resources available in the WTO's regular budget. It is now necessary to increase significantly the resources available for these activities under the WTO's regular budget, which now cover only 20 per cent of the programme, while maintaining these additional contributions will remain essential to improving our efforts in this key area.

Whereas improvements and adjustments are constantly introduced, other approaches and ways of providing technical cooperation need to be explored. One idea is “outsourcing” them, that is subcontracting to outside services. What is needed is an approach that would facilitate an increased and improved WTO response to ever-growing demands for technical cooperation.

Significant action has also been taken during the past year to improve the participation of least-developed countries in the trading system and their access to its opportunities. One striking way in which the integration of least-developed countries into the trading system can be advanced is to ensure they have immediate access, through the new information technologies, to knowledge and advice about it. This is why over the past year the WTO, with assistance from the World Bank and financial contributions from a number of Members, has been working to provide computer equipment and skills and put in place the necessary infrastructure so that least-developed countries can have inter-active contact with the WTO in Geneva and with many other resource centres around the world. Such centres have been established in around 30 trade ministries of least-developed and developing countries in Africa and Asia. The centres are actively using their internet access for regular communications through electronic mail and to download working documents from WTO database resources.

WTO Contributions

As we begin to address the growing gap between the rules of international trade and the rules needed to manage the many other facets of global integration, the WTO can contribute to the international architecture in several important ways:

- (1) The WTO provides a powerful bulwark against protectionist pressures.
- (2) The WTO can help to advance and anchor necessary economic reforms in the affected economies.
- (3) Continuing the momentum towards universal membership of the system would obviously enhance the WTO's ability to provide a stable foundation for the global trading system, particularly during times of economic stress. The current crisis makes no distinction between WTO Members and others, and we cannot afford to maintain a situation where millions of people and their governments are outside the benefits and responsibilities of the trading system.
- (4) Finally – perhaps most importantly – the WTO can help provide the response to the central governance challenge of our new global age: the fact that governments answer mainly to national constituencies, while increasingly the economic system must answer to global needs. The experience of the WTO, and the way it works through binding commitments reached by consensus, gives some guidance as to how these systemic gaps might be bridged. Building upon this experience – and expanding it to other policy areas which now transcend borders – will of course not be easy. Yet if Asia's current turmoil is any indication of the risks of inaction, then the challenge of building a more stable international system is clearly well worth the effort.

The situation in Asia has contributed to falling commodity prices and the reversal of capital flows between emerging markets and industrial countries, and these factors have had a beneficial effect on growth in North America and Western Europe. Oil-importing countries have benefited from lower energy prices. The deterioration of global trade and output growth is therefore the result of a much steeper than predicted slowdown in Asia,

only partly offset by stronger than predicted internal demand growth in the United States and continental Europe. In considering these forecasts for trade and output growth for 1998, it is important to note that considerable uncertainty prevails in regard to world economic developments in the coming months.

A broad range of empirical studies conclude that open trade policies are conducive to growth. The conclusion appears to hold regardless of the level of development of the 6 countries concerned, challenging the notion that a certain level of development is required before the benefits from trade can be fully realized. One study, for example, finds that greater openness to trade was associated with more than two percentage points in annual GDP growth over several years for a sample of developing countries, as compared with the growth performance of countries that have maintained closed economies. Several factors account for this relationship. Most notably, trade allows countries to specialize at what they do best, it facilitates the dissemination of productivity-enhancing technology, and it creates an environment in which foreign direct investment can make a strong contribution to growth. The positive impact of foreign investment on growth appears greater in outward oriented countries than inward-oriented ones.

The Doha Ministerial in November 2001 intended to raise new issues such as investment, competitions policy and transparency in Government procurement. It was agreed that developing countries need not source their essential medicines and drugs at high cost from western multinational companies, which hold patents. Hence India, Brazil and China possess the capacity and technology to manufacture these drugs, they will be entitled to export these medicines/drugs without having to secure compulsory licence from the licence-holders.

For poor countries, food security concern is the main priority which would become possible through negotiations on reduction of domestic support and elimination of export subsidies being provided by the US and European Union to the farmers. With regard to services and the related removal of restriction on the natural movement of people, developed countries are going to be tied down for negotiations. Reduction and elimination of tariffs in non-agricultural goods and other barriers, particularly on products that are important to developing countries, is another major gain for India. It is hoped that India would gain by increasing access for banking, insurance and other companies and increasing opportunities for people to work in another countries. The Doha Development Round of WTO and Cancun Ministerial meet collapsed but as a victory for world's poor. It was important to tell the Western world that unless there was a time-bound commitment to end farm subsidies once and for all, there was simply no way forward.

The gains on account of tariff reductions on goods may also not materialize as the number of goods of export interest to India is very small. Not only that "there will be erosion of the preferences enjoyed by India and India will most probably graduated out of the generalized system of preferences (GSP). The most serious disadvantages to India are likely on account of Agreements pertaining to the TRIPs, TRIMs and Services. The Indian Patents Act provides for a general term of 14 years for both product and process patents, whereas the TRIPs Agreement provide for 20 years. Thus, to meet the requirements of TRIPs, the Indian Patents

act will have to be changed. The extension of intellectual property rights to agriculture has serious consequences for India. In India, plant breeding and seed production are largely in the public domain. Plant breeding is undertaken by agricultural universities and units of ICAR whereas seed multiplication is in the hands of the National and State Seed Corporations. Patenting of plant varieties will transfer all the gains to the MNCs. As regards services like banking, insurance, telecommunications and shipping as between developed and developing countries are concerned the inclusion of trade in services is bound to benefit the developed countries much more than the developing countries like India.

WTO : Its Impact on Economy

The proposition that countries can benefit from trading with one another is less contentious than virtually any other idea in economics. But easy agreement ends there. Questions such as how quickly to open up markets to foreign competition, what sectors to focus upon and what sequence of policies to follow all generate important differences of opinion. These differences arise from a variety of factors, some political and social, others economic. One major reason for competing views and interests is that the reduction of barriers to trade will benefit some and hurt others, although sound policy should be able to reduce the latter costs. The redistributive consequences of changes in trade policy can be justified if the economy as a whole is better off as a result of more open trade, but this is small comfort to those adversely affected by change.

In November 2001 a new round of trade negotiations was launched at Doha, Qatar. An important aim of these negotiations is further to reduce barriers to trade. Many studies over the years conclude that further trade liberalization will lead to increases in income, especially in developing countries. The World Bank, for instance, estimated that abolishing all trade barriers could increase global income by US\$ 2.8 trillion and lift 320 million people out of poverty by 2015.

While supporters of a more open trading system point to these positive economic effects of trade liberalization, others emphasize its costs. In the United States, for instance, 45,000 steelworkers have lost their jobs since 1997 and thirty per cent of the country's steel making capacity has filed for bankruptcy since 1998, while steel imports were on the rise.³ In Mozambique liberalization of trade in cashew nuts resulted in 8,500 of 10,000 cashew processing workers losing their jobs.

These examples highlight losses suffered by particular sectors of the economy. Under standard assumptions about the efficiency gains from trade, these losses will be offset by gains in other sectors. Sometimes, however, the question is asked whether trade liberalization is worthwhile in light of the associated adjustment costs. In the first five years following the implementation of the Free Trade Agreement (FTA) with the United States, for example, Canada lost a staggering 390,600 jobs in the tradable sector (Gaston and Trefler, 1997). As a consequence, calls for the re-negotiation and even abandonment of the agreement enjoyed popular political support in Canada. It turned out, however, that other economic factors were responsible for the largest part of these job losses. Even if arguments against the FTA were based on a mis-perception, this episode brought into sharp relief the tension between

future gains from trade and likely losses suffered by the economy during the adjustment phase.

While economists emphasize the long-run gains from trade, policy makers are in many cases worried about the short-run costs. Not much evidence is available about the size of these costs, in particular when it comes to developing countries. Nor is the adjustment process following trade liberalization very well understood. Yet policy makers need to have an understanding of this process if they are to win support for trade reform and if they are to intervene effectively as necessary to mitigate the costs of adjustment.

Technological progress is a more important source of structural change with in manufacturing than is trade

Changes within manufacturing do not seem to be a direct reflection of changes in trade flows. It is evident that the importance of textiles and clothing and basic metal industries in manufacturing has declined substantially in the US and Japan. Both industries are relatively labor intensive and would be expected to be among those facing difficulties in remaining competitive when faced with increased competition from developing countries. In both the US and Japan, in contrast, the share of machinery and equipment in manufacturing output has increased, with both countries being major exporters of products in this category. In the US the same thing is true of the chemical industry.

The share of textiles and clothing in Japan's manufactured imports increased from 3 per cent to 14 per cent between 1963 and 1995, while the share in exports declined from 23 per cent to 2 per cent in the same period. The share of machinery and transport equipment in exports rose from 32 to 74 per cent, while imports showed a decline from 53 to 43 per cent. Changes in Japan's trade pattern thus show certain similarities with changes in the composition of production across branches within manufacturing.

The same cannot be said for the US, where the share of textiles and clothing in total manufacturing exports decreased from 4 to 3 per cent, while the share of machinery and transport equipment rose from 58 to 63 per cent. In general the composition of manufacturing exports remained fairly stable in the US over this period. Major shifts took place, however, in US manufacturing imports, with the share in imports of machinery and transport increasing from 27 to 59 per cent and those of textile and clothing and of semi-manufactured goods (includes leather and wood) decreasing from 15 to 9 per cent and 27 to 9 per cent, respectively.

Of the two countries, only Japan do changes in the composition of manufacturing. Output show some parallels with changes in the country's trade flows. But shows that in both countries, the weight of each manufacturing branch in the country's total GDP has declined. In other words, the increased importance of certain branches within manufacturing merely reflects the fact that they declined less (in absolute terms) than other branches. In other words, the expanding service sector attracted production factors from all branches in the manufacturing sector.

WTO and Agriculture

- As required by the Uruguay Round Agreement on Agriculture, all agricultural tariffs are bound, but in many cases these bindings are at very high rates and offer limited market access opportunities.
- Agricultural bindings are not always transparent. Transparency and comparability of agricultural tariffs is impaired by the use of specific or mixed tariff rates—that is, by non-ad valorem tariffs. Twenty five Members, both developing and developed, have non ad valorem bindings on more than 50% of their agricultural tariff lines.
- The share of tariff lines with duties above 100% reaches 45% for India and 69% for Bangladesh, but it also reaches 45% for Norway, 8% for Iceland and almost 7% for Switzerland. Large traders among the developed Members also have tariff peaks. More than one third of the European Union's agricultural tariff lines, for instance, carry duties above 15%.
- Agricultural bindings are sometimes far above applied tariff levels. Evidence suggests that the level of tariffs applied by developing countries is often far below the level of their bindings.
- Tariffs tend to increase with the level of processing. There are signs of escalation in most countries' tariff structures.
- Tariff rate quotas were introduced to establish minimum access opportunities where there had been no significant imports before the tariffication process or to maintain current access opportunities where the tariffication would otherwise have reduced market access conditions. The “fill rate” of tariff quotas, however, has been disappointingly low. Between 1995 and 1998, the simple average fill rate for all quotas for which information was available fell from 66% to 62%. One factor explaining the low fill rates might be the high level of certain in-quota tariff rates. Administration methods might also play a role, although this role is difficult to ascertain from available information.
- The special agricultural safeguard that was put in place to help countries cope with the effect of tariffication has been moderately used in the last five years. Of the 38 Members who have reserved the right to apply the special safeguard, only 8 have used it between 1995 and 1999. The total number of actions reached a peak of almost 180 in 1996 before dropping to 132 in 1999. However, this decline in the total number of actions should not mask the steady increase in the use of the price — based special agricultural safeguard, from 42 actions in 1995 to 128 or more in 1999. So far this trend has been more than offset by the decrease in the number of volume—based special agricultural safeguard actions. Also, observers have noted that the special agricultural safeguard has been triggered where only minimal import quantities are taking place.
- Of the 136 Members of the WTO (July 2000), 30 had commitments to reduce domestic support to agriculture, the so-called total Aggregate Measurement of Support (AMS) reduction commitments. Between 1995 and 1997, total AMS reduction commitments

have generally not been binding, as total current AMS has been kept far below commitment level. For only half (10) of the 21 committed Members for which sufficient information is available, has the current AMS decreased between 1995 and 1997. For the others, total current AMS either increased (8 Members) or remained constant (3 Members) during this same period.

- Based on information for the period 1995-1997, the three years for which sufficient data are available, the evolution of total domestic support (more distortive or less distortive) does not show any clear trend. The composition of some Members' domestic support has however changed away from the most trade restrictive measures towards less trade restrictive ones. Most of the Members who reduced their total current AMS between 1995 and 1997 simultaneously increased their so called Green Box support, i.e. support with no or only minimal distortive impact on trade.
- Data suggest that the potential impact of export subsidies on agricultural markets is still significant. Also, between 1995 and 1998, the average use of export subsidy commitments has increased for 10 of the 25 countries with reduction commitments, while it declined only for 5 of them.
- When considering the evolution of domestic support and export subsidies over the period 1995-1997, it is important to bear in mind that the level of support is influenced by commodity prices. Recent information from the OECD (2000) suggests that farm subsidies in OECD countries reached a low of 31% of gross farm receipts in 1997 after a decade of steady decline, but that since then, low commodity prices have prompted OECD countries to increase subsidies to 40% in 1999.

The Agreement on Agriculture's origins

The Agreement on Agriculture (AoA) is one of the most controversial agreements under the World Trade Organization (WTO) regime. The objective of the AoA, is to reduce barriers to trade such as tariffs, quotas and subsidies, thereby making domestic and global agricultural sectors more market-oriented.

The volume of world agricultural exports has expanded substantially over recent decades, with an increasing diversification of products and markets. As in most other sectors of world merchandise trade, the rate of growth of agricultural trade continues to outstrip growth in world agricultural production with the result that an increasing proportion of world agricultural production is now traded. This phenomenon/trend is less pronounced in the agriculture sector reflecting, amongst other factors, the lower rate of growth of world agricultural trade relative to that of more price-elastic traded products.

This has resulted in a steady decline in agriculture's share in world merchandise trade which, in 1998, accounted for 10.1% of total merchandise trade compared to 14.5% at the beginning of the 1980's. Nevertheless, agriculture's current share of world merchandise trade is not far behind that of office and telecommunications equipment (12.9%), and ahead of sectors such as automotive products (10%), chemicals (9.5%), textiles and clothing (6.3%), and iron and steel (2.7%).

Among the agricultural goods traded internationally, food products make up almost 80% of the total. The other main category of agricultural products is raw materials.

The share of the traditional bulk agricultural products in world agricultural trade—such as cereals, oilseeds, cotton and unprocessed tropical products—has continued to decline from about 35% in the early 1980's to about 22% in 1997; with the share of semi-processed intermediate agricultural products, such as vegetable oils, flour and refined sugar, having remained steady at about 25%.

Since the mid-1980's there has been a rather dramatic acceleration in the growth of world exports of high value and processed agricultural products. The share of this dynamic product category in world agricultural trade has increased from 39% in the early 1980's to 52% on average in 1995-1997.

Agricultural trade remains, in many countries, an important part of overall economic activity. It continues to play a major role in domestic agricultural production and employment, particularly in the developing countries. Trade also plays a fundamentally important role in global food security, for example by ensuring that temporary, or protracted, food deficits arising from adverse climatic and other conditions in one country or region can be met from world markets.

Although agriculture has always been covered by the GATT, prior to the WTO the rules that applied to agricultural primary products deviated from the general rules.

The GATT 1947 allowed countries to use export subsidies on agricultural primary products, whereas the use of export subsidies by developed countries on industrial products was prohibited. The only conditions were that agricultural export subsidies should not be used to capture more than an "equitable share" of world exports of the product concerned. The GATT rules also allowed countries to resort to non-tariff import restrictions (e.g. quantitative import restrictions) under certain conditions, notably when these restrictions were necessary to enforce measures to effectively limit domestic production. This exception was also conditional on the maintenance of a minimum proportion of imports relative to domestic production.

In actual practice, many non-tariff border restrictions were applied to imports without any effective counterpart limitations on domestic production, and without maintaining minimum import access. In some cases this was achieved through the use of measures not specifically provided for under Article XI. In other cases this reflected exceptions and country-specific derogation's such as grandfather clauses, waivers and protocols of accession. In still other cases non-tariff import restrictions were maintained without any apparent justification.

The result of all this was a proliferation of impediments to agricultural trade including, by means of import bans, quotas setting the maximum level of imports, variable import levies, minimum import prices and non-tariff measures maintained by state trading enterprises. Major agricultural products—such as cereals, meat, dairy products, sugar and a range of fruits and vegetables—have faced barriers to trade on a scale uncommon in other merchandise sectors.

In part, this insulation of domestic markets was the result of measures originally introduced following the collapse of commodity prices in the 1930s Depression. Furthermore, in the aftermath of the Second World War, many governments were concerned with increasing domestic agricultural production so as to feed their growing populations. With this objective in mind, and in order to maintain a certain balance between the development of rural and urban incomes, many countries, particularly in the developed world, resorted to market price support: farm prices were administratively raised; while import access barriers ensured that domestic production could continue to be sold. In response to these measures, and as a result of productivity gains, self-sufficiency rates rapidly increased.

In a number of cases, expanding domestic production of certain agricultural products not only replaced imports completely but resulted in structural surpluses. Export subsidies were increasingly used to dump surpluses onto the world market, thus depressing world market prices.

This factor—plus the effects of overvalued exchange rates, low food price policies in favour of urban consumers and certain other domestic measures—reduced the incentive for farmers in a number of developing countries to increase, or even maintain, their agricultural production levels.

Trade policies under the Agriculture Agreement

It became increasingly evident in the lead-up to the Uruguay Round negotiations, that the causes of disarray in world agriculture went beyond import access problems, the traditional focus of GATT negotiations. To get to the root of the problem, disciplines with regard to all measures affecting trade in agriculture, including domestic agricultural policies and the subsidization of agricultural exports, were considered to be essential. The Uruguay Round reform program comprised specific commitments to reduce support and protection in the areas of domestic support, export subsidies and market access. It also strengthened, and made more operationally effective, rules and disciplines in each of these areas, including export prohibitions and restrictions. Clearer rules for sanitary and phyto-sanitary measures were also considered to be required, both in their own right and to prevent circumvention of stricter rules on import access through unjustified, protectionist use of food safety, as well as animal and plant health measures. This section provides a description of the post-Uruguay Round landscape.

Market access

The Uruguay Round resulted in a key systemic change on the market access side: the switch from a situation where a myriad of non-tariff measures impeded agricultural trade flows to a regime of bound tariff-only protection plus reduction commitments. The effects of this fundamental change have been to stimulate investment, production and trade in agriculture by:

- (i) Making agricultural market access conditions more transparent, predictable and competitive;

- (ii) Establishing or strengthening the link between national and international agricultural markets, and thus;
- (iii) Relying more prominently on the market for guiding scarce resources into their most productive uses, both within the agricultural sector and economy wide.

In many cases, tariffs were the only form of protection for agricultural products before the Uruguay Round—which led to the “binding” in the WTO of a maximum level for these tariffs. For many other products, however, market-access restrictions involved non-tariff barriers. This was frequently, though not only, the case for major temperate zone agricultural products. The Uruguay Round negotiations aimed to remove such barriers.

For this purpose, a “tariffication” package was agreed which, amongst other things, provided for the replacement of agriculture-specific non-tariff measures with a tariff which afforded an equivalent level of protection.

The tariffs resulting from the tariffication process account, on average for developed country “Members” (WTO member countries), for around one fifth of the total number of agricultural tariff lines. For developing country Members, this share is considerably smaller. Following the entry into force of the Agreement on Agriculture, there is now a prohibition on agriculture-specific non-tariff measures, and the tariffs on virtually all agricultural products traded internationally are bound in the WTO.

Tariffs

The tariff schedules negotiated during the Uruguay Round list the base rate of duty in relation to which reductions in the first and subsequent years of the 1995-2000 implementation period are calculated, as well as the final bound rate of duty valid at the end of the six year implementation period. The base rates were established in different ways depending on the situation prevailing before the Uruguay Round.

Developing countries were able to offer “ceiling bindings” for all previously unbound tariffs, and many developing countries availed themselves of this option. Where non-tariff measures had to be converted into tariffs, the base rate is the result of the tariffication exercise. In this case, the base rate was calculated by the countries themselves—in accordance with the tariffication modalities—as the difference between the internal and the external price for the product concerned in the reference period (1986-1990). The agreement required a reduction by an un-weighted average of 36%, with the only constraint being that reduction rates needed to be at least 15%. Where developing countries had to reduce their tariff rates, they were required to reduce them by an un-weighted average of 24%, subject to a minimum cut of 10% per product, with flexibility to implement their reductions over a period of 10 years instead of six years.

The analysis of agricultural tariff statistics is complicated by the prevalence of non-ad valorem tariffs. Some Members have bound all their agricultural tariffs in ad valorem terms, but others have bound many of their agricultural tariffs in other forms including specific, mixed (ad valorem or specific), compound (ad valorem plus specific), or technical tariff rates (for example based on alcohol or sugar content).

Non-ad valorem tariffs do not only have protective effects which differ from the effect of ad valorem tariffs, they are also far less transparent. To conduct our analysis of post-Uruguay Round bound tariff rates, tariffs must be aggregated and averages need to be calculated. Non ad valorem tariffs however cannot be aggregated and ad valorem equivalents (AVE) need to be calculated. AVEs of specific and other non-ad valorem tariffs are usually calculated either by comparing collected custom revenue to the value of imports or by comparing unit values of traded products with the applied non-ad valorem tariff. Only few sources for AVEs of WTO bound tariff rates are available.

Because the availability of AVEs from WTO sources is currently limited, we present agricultural tariff statistics calculated by the OECD Secretariat and we compare them to those established by the World Bank. It is important to keep in mind that estimates of AVEs of specific rates must be interpreted with caution. AVEs depend on prices which tend to fluctuate. Moreover, there are many cases where the price information needed to calculate AVEs is simply not available. This is the case, in particular, for the wide range of high value and processed agricultural products which now account for more than half of world trade in agricultural products.

The tariff statistics for industrial products are provided for the sake of comparison. The proportion of agricultural tariff lines that are bound duty free varies significantly between countries. Developing countries in the OECD sample generally have only very few lines bound duty free.

Among OECD countries, the share ranges between zero per cent for Turkey and 50% for New Zealand. One group of countries, which includes the EU and Canada, has a higher share of duty-free lines for agricultural products than for industrial products while another group, which includes the United States and Japan, exhibits the opposite situation. Despite differences, which are mainly accounted for by differences in the techniques used to calculate the ad valorem equivalents, the two series are relatively well correlated. For most industrial countries, as well as for some developing countries, average bound tariff levels on agricultural products are a multiple of those on industrial products. The OECD average is 36% which compares with 14% for industrial products. Among the Quad countries, the EU has the highest average at 20% and Canada has the lowest at 5%, followed by the United States at 6%.

The dispersion of tariffs is another important dimension of a country's tariff schedule. The higher the dispersion of tariffs, the higher will be the cost of tariff protection in terms of economic welfare.

As can be seen, the standard deviation is much higher for agricultural products than for industrial products, indicating that the differences between the tariffs on different agricultural products are significantly higher than the differences between the tariffs on different industrial products.

It is interesting to note that the four WTO members with the highest standard deviation in the sample of countries reviewed by the OECD, i.e. Norway, Republic of Korea, Switzerland,

and Iceland, are all OECD countries. Another related problem is the very high tariffs, the so-called tariff “peaks” or tariff “spikes”, on many basic agricultural products. It has been shown that the share of agricultural tariff lines at tariff rates bound above 15% is larger than 10%. Bangladesh, India, Tunisia and Norway, for instance, have more than 40% of their agricultural tariff lines at peak rates above 100%. Among the products most affected by tariffs higher than 15% are dairy products, meat, cereal flour and sugar. Many tariff equivalents that emerged from the tariffication process are among the very high tariffs. Some of these tariffs are so high that they discourage the importation of even minimum quantities

Conclusion and Suggestions

- The WTO provides a permanent institutional framework for the multilateral trading system, with its own Secretariat. The WTO not only covers trade in goods, but also covers trade in services and trade-related aspects of intellectual property rights. The dispute settlement mechanism has been considerably strengthened in the WTO. International trade in services has expanded exponentially over the past three decades covering both conventional and emerging areas like Finance, Professional Services, IT related services, Environmental and Educational services. The New era has provided professionals including Company Secretaries to play a major role in the development of the economy. Intellect/Knowledge is the strength by which we as professionals like Company Secretaries can acquire more and more business and help the society at large. Under WTO, lots of opportunities are available for Professionals in the field of International Trade Laws and WTO aides in providing opportunities for professionals including Company Secretaries in International Trade Laws.
- WTO covers Trade in Goods, Trade in Services, Trade Related Investment Measures (TRIMs), Trade Related Intellectual Property Rights (TRIPs), Dispute Settlement Mechanism, and Dumping and Anti-Dumping Rules, etc. Undoubtedly, global markets offer unlimited opportunities for professionals like Company Secretaries.
- The professional services exports have been occupying the center stage of ongoing thrust for increasing India's share in Global Trade. The thrust of the successive governments have been on targeting export of services as instrumentality to cause an upsurge in the Opportunities for the Professionals like Company Secretaries. India is pushing the reforms in WTO because it has the requisite soft power to intervene and make a turnaround. It will change the world and the way the corporate governance is managed.
- There is lot of emphasis on sustainability reporting which is major leap and will open many windows for the professionals. Countless opportunities are opening up as the world markets are desperately trying to adopt transparency and ethical practices with emphasis on sustainability.
- Trade liberalization is an agent of economic change, but evidence shows that it does not lead to drastic changes in a country’s overall production structure.
- Adjustment costs are typically smaller, sometimes much smaller, than the gains from trade.

- Governments can identify individuals and groups that may suffer from the adjustment process and they can also develop policies to alleviate the burden falling on those adversely affected. Governments can adopt policies that influence the size of adjustment costs faced by the economy.
- Adjustment costs can be reduced if trade policy reforms are underpinned by international commitments.
- The pace of trade reforms can have a beneficial impact on adjustment costs.
- The implementation of trade reforms at a gradual pace may lessen political opposition to change, but the risk of undermining reforms by adopting them too slowly must also be borne in mind.
- In many cases effective adjustment to trade liberalization will require the expansion of a country's export sector and this may be an argument for pro-export policies.
- WTO agreements seek to provide space for governments to tackle adjustment problems.

In the WTO regime, reservations may have to be withdrawn, preferential purchase and other support measures may not be available and thus Small Scale Industries (SSIs) have to compete not only with the large units within the country, but also with cheap imported products. SSIs are thus losing their markets to cheap imported products. Dumping of Chinese goods has seriously affected SSI sector. It is imperative that wide ranging changes in infrastructure, capital markets, governance and privatization are a must for India to be able to meet the challenges thrown forward by the WTO. Although there are many stumbling blocks that are preventing the government from satisfying all the demands, it is imperative that reforms must be pushed through with an iron hand.

Hence it can be said that the Developing countries cannot be a silent spectator. Globalization has to be on equal terms, based on the principles of equity and justice and not on economic superiority. Instead of succumbing to pressure tactics, a collective stand based on the following two planks appear to be the only way forward to protect agriculture, the mainstay of the developing economies:

- "Zero-tolerance" on agricultural subsidies: Developing countries should make its stand clear that the negotiations will move ahead only when the subsidies are removed. The Agreement on Agriculture should wait till the subsidies in the west are grounded. Any agreement without the subsidies being removed will play havoc with developing country agriculture.
- "Agriculture shield" for developing countries: Following Mexico's announcement of an "agriculture shield" program aimed at ensuring that the country's farmers are not harmed by unfair competition from the United States, developing countries need to unilaterally adopt the shield programme. The agricultural shield program includes compensatory tariffs on some food products that would enter Mexico duty free as of January 1 under the North American Free Trade Agreement. Such tariff complies

with World Trade Organization policies allowing nations to take protective action when the viability of agricultural sectors is threatened by foreign competition.

Under the Agriculture Agreement, WTO members have to reduce their subsidized exports. But some importing countries depend on supplies of cheap, subsidized food from the major industrialized nations. They include some of the poorest countries, and although their farming sectors might receive a boost from higher prices caused by reduced export subsidies, they might need temporary assistance to make the necessary adjustments to deal with higher priced imports, and eventually to export. A special ministerial decision sets out objectives, and certain measures, for the provision of food aid and aid for agricultural development. It also refers to the possibility of assistance from the International Monetary Fund and the World Bank to finance commercial food imports.

For the 2005 WTO ministerial in Hong Kong, negotiations have stalled even before the ministerial has begun. The developed countries will be putting enormous pressure on the developing countries to break through the deadlock. But it is a broken model, and for the developing world, no deal is better than a bad deal.

While concluding it is stated that it is not entirely true that the WTO is a tool used by developed countries to exploit undeveloped ones further. The gains made by India at Doha are definitely an indication of what is possible. we can state that the WTO is a conditional gift for India. It is now up to us to face the challenges or to shy away and be exploited by developed countries. It is only depend on us how we take the challenges and face the competitions to survive in the competitive world.

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XBRL

VIVEK BAID*

With the issue of General Circular No. 16/2012 dated July 6, 2012, the Ministry of Corporate Affairs (MCA) has kick-started the second phase of XBRL Implementation wherein it has marginally increased the scope by including those companies also who were required to file their financials in XBRL format last year. It implies that companies who had filed in XBRL voluntarily last year, they are not covered under the mandate of XBRL this year as well. After the successful completion of first phase of XBRL Implementation last year, the MCA has also covered Cost Audit Report and Cost Compliance Report into the ambit of XBRL filings from this year vide General Circular No. 18/2012 dated July 26, 2012.

eXtensible Business Reporting Language (XBRL) is, now, not a new concept. We all are aware that instead of treating financial information as a block of text, XBRL provides a computer-readable tag to identify each individual item of data. By attaching identifying tags to individual pieces of data, a business reporting document becomes “intelligent” data, allowing the exchange of business reporting data by encoding the information in a meaningful way. For assigning an appropriate “tag” to the data, taxonomy (dictionary of all financial and non-financial reporting requirements) is required.

Background

While XBRL is being adopted by other regulators in India, the Ministry of Corporate Affairs has taken a lead in its implementation by extending the mandate of XBRL filings to around 30,000 companies in its first year of XBRL Implementation and discontinuing the pdf filings for those companies. Banking Companies, Power Companies and NBFCs were exempt from XBRL filing owing to non-availability of taxonomies specific to their reporting requirements.

C & I Taxonomy

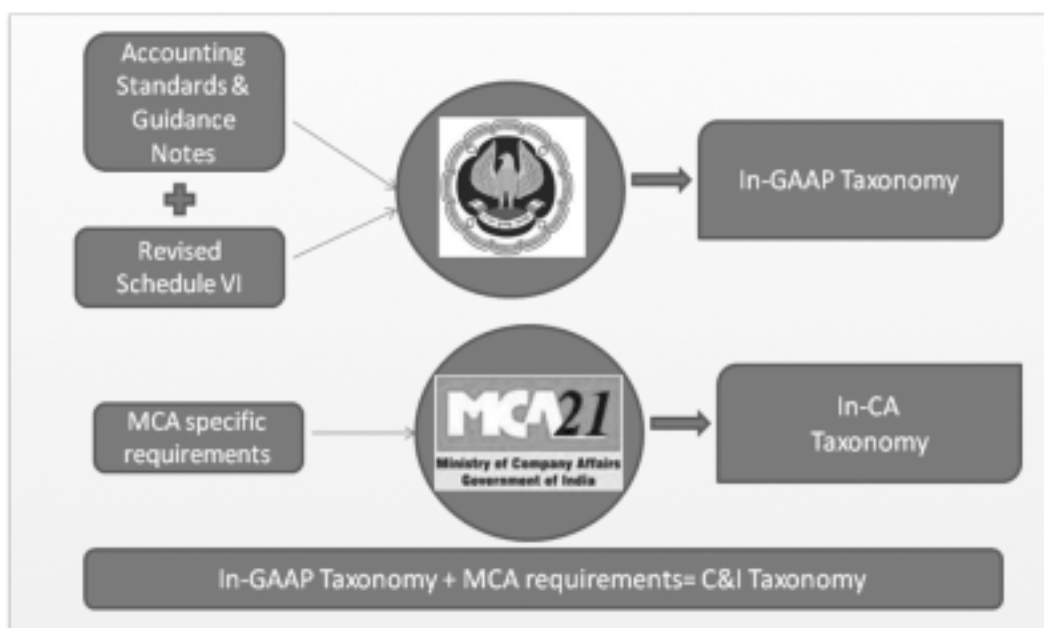
With the change in the presentation format of Financial Statements under the Companies Act, 1956 viz. Revised Schedule VI, the taxonomy was also required to undergo a change to be aligned with the new presentation format. In view of the taxonomy being prepared afresh, architecture of the taxonomy was also considered for a change to the latest IFRS Taxonomy Architecture 2011 as against earlier architecture viz. IFRS Taxonomy Architecture 2006.

* Managing Director, AAA Professional Services Pvt. Ltd.

The C&I Taxonomy had been prepared as per the requirements of the Revised Schedule VI to the Companies Act, 1956 and disclosure requirements under the Accounting Standards and Guidance Notes. Being general purpose taxonomy, it does not contain industry specific elements except for those for which the ICAI had issued a Guidance Note w.r.t. their accounting aspects viz. Guidance Notes on Oil & Gas and Real Estate. It also includes MCA specific regulatory elements and a few common reporting elements to the extent they are not contrary to the accounting framework. Common reporting elements were introduced in the taxonomy to make it more comprehensive, considering the fact that the taxonomy is not extendible for this year as well i.e. filer cannot create an element in the taxonomy as per their specific requirements.

The taxonomy basically has two types of elements.

- o The “in-gaap” elements - These refer to the requirements of the Revised Schedule VI to the Companies Act, 1956, Accounting Standards and the Guidance Notes;
- o The “in-ca” elements - These refer to the requirements of the Ministry of Corporate Affairs (MCA).



Taxonomy contains linkbases which defines relationships among the taxonomy elements. There are six internationally prevalent linkbases:

- a. *Presentation Linkbase* - Defines hierarchical relationship amongst the elements. It defines how concepts should be presented and displayed.
- b. *Calculation Linkbase* - Defines calculation relationship amongst the elements. These

calculations include simple addition and subtraction only. Weight assigned to any element shows its calculation relationship with its parent element. For eg. element with “+ 1” weight would be added to its parent element.

- c. *Label Linkbase* - Provides human readable label names to every element
- d. *Reference Linkbase* - Provides an authoritative reference to the elements.
- e. *Definition Linkbase* - Defines the dimensional relationship among the elements in the taxonomy.
- f. *Formula Linkbase* - Defines advanced and user defined calculations among the elements. Eg. calculation of ratios, etc.

In the C&I Taxonomy, first five out of the above-mentioned six linkbases are present as advanced calculations are catered through the validation tool of the Ministry of Corporate Affairs (MCA).

The major changes in the new C&I Taxonomy *vis-à-vis* earlier C&I Taxonomy are as follows:

1. The C&I Taxonomy 2012 is based on the requirements of Revised Schedule VI to the Companies Act, 1956 whereas the earlier taxonomy was based on the then prevailing Schedule VI.
2. The new taxonomy has been developed as per the latest architecture viz. IFRS architecture 2011, whereas the earlier taxonomy was based on IFRS architecture 2006.
3. Addition of Definition Linkbase and Reference Linkbase.
4. The concept of ‘dimensions’ has been introduced in the taxonomy as against ‘tuples’. Dimensional concept was not supported by earlier architecture. Dimensions are used to capture the tabular data which was earlier captured line by line which made the analyses of data difficult.
5. Requirements of Industry-specific Guidance Notes viz. Guidance Note on Real Estate and Oil & Gas, and SEBI Employee Stock Option Scheme and Employee Stock Purchase Scheme guidelines, 1999 have been included in the new taxonomy which were not present in the earlier taxonomy.

Dimensions v/s. Tuples

With the use of tuples, a filer could use the elements as many times as required. Tuples were used in the taxonomy where there could be multiple information w.r.t the elements viz. in case of details of signatories to the Board Report, etc. In the figure 1.1 below, it can be

seen that the highlighted element is tuple, and accordingly elements underneath the tuple can be selected as many times as the number of signatories.

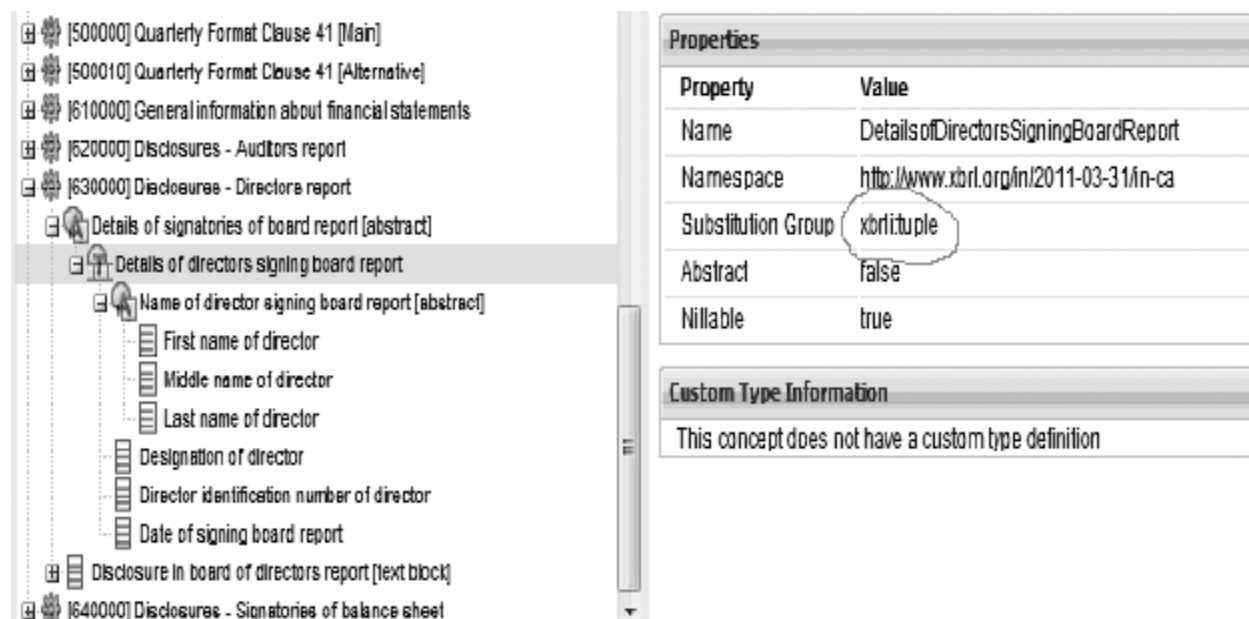


Fig 1.1 : Taxonomy View of Tuples in earlier taxonomy

Now, in the new C & I Taxonomy, tuples have been replaced by typed dimensions (explained in detail under “Types of Dimensions”) which are used to capture such information.

Dimensions are used to capture the tabular data in a presentable manner as against earlier taxonomy which used to capture such data line by line. Dimensions were not supported by the earlier architecture of the taxonomy viz. IFRS Taxonomy Architecture 2006. To understand dimensions, you must be familiar with the following terms:

Table (also called as Hypercube) is the collection of dimensions together with the tagged values. Table is the highest level of grouping item in Dimensions. It must contain at least one “Axis” and at least one “Line Item”. It is used to capture the tabular data.

Axis is used to create columnar axis in the table with the help of “members”. Each table must contain at least one “Axis”. However, table can contain more than one “Axis”. For e.g. in the table of “Borrowings”, 3 axes have been used.

Members are the description arranged on the horizontal axis of the table.

Line Items are group of the regular elements which appear in the vertical axis of the table. The values are tagged to the line item alongwith the applicable members from the table.

Classification of long-term trade receivables [Table]	Classification of assets based on security [Axis]		
	Classification of assets based on security [Member]		
	Secured considered good [Member]	Unsecured considered good [Member]	Doubtful [Member]
Long-term trade receivables [Abstract]			
Long-term trade receivables [Line Items]			
Breakup of long-term trade			
Long-term trade receivables, gross			
Allowances for bad and doubtful debts			
Long-term trade receivables			

Fig 1.2 Tabular view of Long term trade receivables

Types of Dimensions

1. **Explicit Dimensions:** In this type of dimensions, members are explicitly defined under an axis. For e.g. in “Notes-Share Capital”, members are explicitly defined under the “Classes of share capital [Axis]”. Filer can use only the given number of members.
2. **Typed Dimensions:** In this type of dimensions, members are not defined under the axis. It has been left on the part of filers to create any number of members under the axis as per their specific requirement. For e.g. in the case of signatories to the Board Report, no members have been defined under the “Directors signing board report [Axis]” thereby enabling the filer to create any number of members as per their requirement.

▼ Details of signatories of board report [Abstract]	19.0
▼ Details of directors signing board report [Table]	1.0
Directors signing board report [Axis]	1.0
▼ Details of directors signing board report [Line Items]	2.0
▼ Name of director signing board report [Abstract]	1.0
1 First name of director	1.0
1 Middle name of director	2.0
1 Last name of director	3.0
1 Designation of director	2.0
1 Director identification number of director	3.0
1 Date of signing board report	4.0

Fig: 1.3 : Taxonomy View of Typed Dimensions in the new Taxonomy

In the dimensions, “Members” are defined as columns and the corresponding line items would appear in the row side to present it in tabular format. Every line item can be linked with a member and be tagged with the value.

For instance, there is a figure of Rs. 15,000/- (say) for depreciation on owned vehicles in the note of tangible assets. For XBRL tagging purposes, the line item “DepreciationTangibleAssets” need to be tagged with Rs. 15,000/- alongwith the following members:

- a. Vehicles Member
- b. Owned Assets Member
- c. Accumulated Depreciation and Impairment Member

Accordingly, this would be presented as below

Disclosure of tangible assets	Vehicles member					
	assets held under lease member			Owned assets member		
	Carrying amount member			Carrying amount member		
	Gross carrying amount member	Accumulated depreciation member		Gross carrying amount member	Accumulated depreciation member	
Changes in tangible assets abstract						
Additions other than through business combinations tangible assets						
Acquisitions through business combinations tangible assets						
Depreciation tangible assets					15,000.00	
Impairment loss recognised in profit or loss tangible assets						
Reversal of impairment loss recognised in profit or loss tangible assets						
Revaluation increase decrease tangible assets						

Fig. 1.4 : Tabular view of the tagged data

In furtherance to this, it was observed that certain “members” would not be applicable to some of the line items, thus there arises a need to freeze those “members” for such line items. Accordingly, a new concept called as “not All hypercubes” has been introduced in the taxonomy through which certain “members” would become disable for some of the line items of that table. For eg. In the table “Classification of borrowings [Table]”, the line item “Nature of security” has been frozen for the member “Unsecured borrowings [Member]” as there cannot be any security for the unsecured borrowings.

Business Rules

Business Rules are built as validation checks in the “Validation Tool” released by the MCA. The Business Rules mainly comprises of the following sheets:

1. *Specific Rules* : All the elements are listed in the sheet and any rule if applicable on

any element is mentioned against the element. For instance, “Reserves and Surplus” appearing on the face of Balance Sheet is a mandatory element. Thus a filer has to enter a value against this element.

The following broad rules are made in this category:

- (a) This is a mandatory field- It means the value against the element have to be tagged. In case, the company does not have such element in its Financial Statements, it need to fill “0” (in case of monetary element) or N.A. (in case of text element) against those elements.
 - (b) Should be greater than or equal to zero- It does not mean that the element is mandatory to be entered. It means that in case the value is entered, it cannot be a negative value.
 - (c) The detailed table is mandatory in case “Yes” is selected for any corresponding element- It means that in case any element for eg. “Whether CARO is applicable” is tagged as Yes, the CARO Report has to be tagged in detail in the tabular format. Similar is the case with “Related Party Transactions”, etc.
2. *Generic Rules* : These are the general business rules to be complied with while creating the instance documents (XBRL financial statements). These are not element specific. For e.g. there is one generic rule which states that “It should be mandatory to enter at least one child element if parent element is entered and vice-versa”. It implies that this rule has to be followed throughout the complete tagging process.
 3. *Applicable ELR (Extended Link Role)* : This sheet explains the applicability of all ELRs to the applicable instance documents viz. ELR [200100] Notes - Share capital is applicable to the instance document of “Balance Sheet” only and ELR [100200] Statement of profit and loss is applicable to the instance document of “Profit and Loss” only. In case of ceratin ELRs, applicable instance document is not mentioned. Thus, such ELRs may be tagged in both the instance documents viz. Balance Sheet and Profit & Loss. [Refer the para “Filings with MCA”]
 4. *Mandatory line items* : This sheet enlists the line items which are mandatory only in case the applicable dimension table is used. For eg. in case filer uses “Details Of Noncurrent Investments Table”, the following line items under this table would become mandatory for the members:
 - a. Type of Noncurrent Investments
 - b. Class of Noncurrent Investments
 - c. Noncurrent Investments
 - d. Name of Body Corporate in whom Investment has been made
 5. *Exempt Parent and Child members- Dimensions* : There is a generic business rule which states that “parent member of an axis shall be mandatory to enter in case value has been entered in any of its child members and vice versa”. This sheet enlists
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the exemption from the stated generic business rule. And on similar footings, there is one sheet “Parent child exempt-calculation” for the line items/ elements which are not covered under dimensions.

All the Business Rules must be complied with while creating the valid instance documents in order to file with the MCA. Only valid instance documents would get validated through the Validation Tool of the MCA. After the successful validation, filer needs to pre-scrutinize the instance documents through the same validation tool wherein the data is validated online from the information available on the MCA portal viz. CIN, PAN, etc.

Scope and Level of Tagging

This document explains the level of tagging whether any information is required to be tagged in detail or only block-text tagging is required. For eg. in previous year, related party transaction were required to be tagged in detail whereas Auditors Report and Directors Report were required as block-text tagging.

For the current year tagging, the scope or level of tagging would not be changed besides some minor changes like Auditors Report is now also required to be tagged in detail and certain elements of Directors Report would also be tagged in detail.

Certification of XBRL Financial Statements

The XBRL Financial Statements were required to be certified by a practicing professional viz. CA/CS/CMA vide General Circular No: 57/2011 issued by the MCA on 28th July, 2011. Practicing Professional needs to ensure the correctness, completeness and accuracy of the XBRL Financials vis-a-vis the financial statements which had been adopted at the Annual General Meeting of the company.

The certification language has been reproduced below :

“It is hereby certified that I have verified the above particulars (including attachment(s)) from the audited financial statements of the Company and that all required attachment(s) have been completely attached to this form. It is further certified that the attached XBRL document(s) fairly present, in all material respects, the audited financial statements of the company, in accordance with the XBRL taxonomy as notified under Companies (Filing of documents and forms in eXtensible Business Reporting Language) Rules, 2011.

It is confirmed that the attached XBRL document(s) are the XBRL converted copy(s) of the duly signed Balance Sheet and all other documents which are required to be annexed or attached to the Balance Sheet as required under Section 220 of the Companies Act, 1956.”

Practitioner may refer Guidance Note on Certification of XBRL Financial Statements/ Referencer on XBRL issued by the Professional Institute for the better understanding of the task of certification and to ensure a correct certification.

Filings with MCA

As already mentioned, Cost Audit and Cost Compliance Reports would also be filed with the MCA this year alongwith the Annual Financial Statements in XBRL mode.

As per MCA mandate the companies are required to prepare two separate Instance documents for the filing purposes:

1. Balance Sheet Instance Document
2. Profit & Loss A/c Instance Document

And in case the company is also preparing the consolidated financial statements then it is required to prepare four instance documents for filing with the MCA:

1. Balance Sheet Instance Document Standalone
2. Profit & Loss A/c Instance Document Standalone
3. Balance Sheet Instance Document Consolidated
4. Profit & Loss A/c Instance Document Consolidated

Similar to previous year, extensions have not been allowed by the MCA for this year as well. Thus, filer would not be allowed to create/add any element in the core C&I Taxonomy to meet its own specific reporting requirements.

Conclusion

The XBRL Regulatory Tool was employed for conducting technical scrutiny on XBRL filings made by companies. Three or more alerts were generated for 738 companies, which have been referred to RD/ROC for examination. [Refer MCA Monthly Newsletter May 2012]. Now, the focus of the Ministry of Corporate Affairs would be more on the quality aspects of the XBRL Financial Statements. It is hoped that professionals are now poised to welcome the second phase of XBRL Implementation with the hands wide open.

CONCEPT OF WHISTLE BLOWING AND THE ROLE OF THE COMPANY SECRETARY

CS SUDHEENDHRA PUTTY*

Introduction

Much like control is to planning in the managerial context, whistle blowing is to conscience keeping in the compliance realm. For the application of the best management practices, compliance of the applicable laws in true letter and spirit and adherence to ethical standards for the effective management and distribution of wealth, it is absolutely essential that there exists an institutional mechanism that gauges performance and adherence, helps detect fraud and errors and effectively flags them for remedial or corrective action at the appropriate time.

It becomes imperative to institutionalize the concept of a whistle blower in the corporate milieu. An important component of the corporate governance regime as envisaged the world over is the concept of a whistle blower.

Whistle Blower - Meaning of

Whistle blowing primarily means making a protected disclosure. According to the Oxford *Advanced Learner's Dictionary*¹, a whistle blower is a person who informs people in authority or the public that the company he/she works for is doing something wrong or illegal. A whistle blower mechanism may be understood as an internal policy for employees to report to the management any concerns about the unethical behaviour, actual or suspected frauds or violations of the company's code of conduct or ethics. (However, for a whistle blower to blow the whistle, it is not necessary that the company must first have in place a code of conduct). The whistle may be blown for any fraudulent or inappropriate or unethical management practice; furthermore, such practice need not necessarily amount to a violation of any law. A whistle blower policy is a mechanism that enables any employee of the company to report concerns about the company to the top management/audit committee, without necessarily informing his (immediate) superiors.

An essential feature of the Whistle Blower Policy (WBP), indeed its hallmark, is that it provides adequate safeguards against victimization of the employee who avails of the mechanism. Without these safeguards, a whistle blower policy would be a damp squib.

* B.Com., MA., LL.B., FCS, Company Secretary, Infotech Enterprises Limited, Hyderabad.

1. 8th Edition; 2010

Whistle blowing occurs when an employee raises a concern about dangerous or illegal activity that he is aware of through his work. If it has a good policy and culture, the concern will be raised with the employer in the first instance. As the *Committee on Standards in public life in the UK*² has explained:

“The essence of a whistle blowing system is that staff should be able to by-pass the direct management line because that may well be the area about which their concerns arise, and that they should be able to go outside the organization if they feel the overall management is engaged in an improper course.”

Need for a Whistle Blower Policy

The immediate trigger for implementing a WBP arose after a spate of corporate collapses in the Western world in the last decade of the 20th century. It is pertinent to note that these major corporate collapses and frauds came to light, courtesy the whistle blowers. Thus, the WBP has come to act as a catalyst in the corporate governance process. A WBP is a must where a company intends to transact its business in an open, fair, transparent and honest manner with integrity being the cornerstone of working.

The need for a WBP has been very succinctly summarized by the Committee on Standards in Public Life in its 2nd Report published in May 1996. The Committee noted :

“All organizations face the risks of things going wrong or of unknowingly harbouring malpractice. Part of the duty of identifying such a situation and taking remedial action may lie with the regulatory or funding body. But the regulator is usually in the role of detective, determining responsibility after the crime has been discovered. Encouraging a culture of openness within an organization will help: prevention is better than cure [Emphasis supplied]. Yet it is striking that in the few cases where things have gone badly wrong in local public spending bodies, it has frequently been the tip-off to the press or the local Member of Parliament - sometimes anonymous, sometimes not - which has prompted the regulators into action. Placing staff in a position where they feel driven to approach the media to ventilate concerns is unsatisfactory both for the staff members and the organization.”

During the debate on the Public Interest Disclosure Act, 1998, in the Parliament in the UK, Lord Nolan stated that his Committee had been persuaded of the urgent need for protection for public interest whistle blowers and he commended those behind the Bill ‘for so skilfully achieving the essential but delicate balance in this measure between the public interest and the interests of employers’.

The fundamental need for a WBP arises from the fact that elimination of unethical and improper practices is the responsibility of the respective corporate promoters and managements for which they have to put in place systems for efficient administration and transparent transaction.

2. The Committee on Standards in Public Life is an independent public body which advises government on ethical standards across the whole of public life in the UK.

Position in the UK

The Public Interest Disclosure Act was passed in 1998 in the UK. The Act came into force on 2 July, 1999. It encourages people to raise concerns about malpractice in the workplace and helps to ensure that organizations respond by

- * addressing the message rather than the messenger; and
- * resisting the temptation to cover up serious malpractice.

Through protecting whistle blowers from dismissal and victimization, the Act promotes public interest. The Act provides that the employees may report malpractices, raise genuine concerns about crime, civil offences (including negligence, breach of contract, breach of administrative law), miscarriage of justice, danger to health and safety or the environment and the cover up of any of these. The Act confirms that workers may safely seek legal advice on any concerns they have about malpractice. This includes seeking advice from public concern at work, which is designated a legal advice centre by the Bar Council. Wider disclosures are also enabled in case of more serious concerns. Complete protection is available to the employees reporting any concerns under this Act. Where the whistle blower is victimized in breach of the Act, he can bring a claim to an Employment Tribunal and seek for compensation. Awards will be uncapped and based on the losses suffered. Additionally, where an employee is sacked, he may apply for an interim order to keep his job. Gagging clauses in employment contracts and severance agreements are void in so far as they conflict with the Act's protection. The English Act is an exemplary and comprehensive piece of legislation and worthy of emulation in India.

In addition, the Financial Services Authority, the capital market regulator in the UK, has also strongly encouraged firms to set up their own internal procedures for processing whistle blowers concerns.

Position in the US

The Corporate Criminal Fraud and Accountability Act, 2002, (a fall out of the Sarbanes Oxley Act) deals with the WBP in the US. Section 806 of the Act provides for protection to employees of publicly traded companies who provide evidence of fraud. This protection includes, civil action to protect against retaliation in fraud cases and claiming compensatory damages. As a system, the WBP is well entrenched in the US.

Position in India

The revised clause 49 of the listing agreement as initially introduced in August, 2003 based on the recommendations of the Narayanamurthy Committee had provided for the mandatory setting up of a WBP. The Committee made two mandatory recommendations as follows :

- Personnel who observe an unethical or improper practice (not necessarily a violation of law) should be able to approach the audit committee without necessarily informing their supervisors. Companies shall take measures to ensure that the right of access is communicated to all employees through means of internal circulars, etc. The

employment and other personnel policies of the company shall contain provisions protecting 'whistle blowers' from unfair termination and other unfair prejudicial employment practices. (Para 3.11.1.3)

- Companies shall annually affirm that they have not denied any personnel access to the audit committee of the company (in respect of matters involving alleged misconduct) and that they have provided protection to whistle blowers from unfair termination and other unfair or prejudicial employment practices. Such affirmation shall form part of the Board report on corporate governance that is required to be prepared and submitted together with the annual report. (Para 3.11.1.4)

India Inc. was, however, clearly unhappy with these recommendations and opposed them intensely. Bowing to pressure, the SEBI, when it notified the revised clause 49 in October 2004, decided to make the WBP recommendation optional/recommendatory in nature.

Para 7 of Annexure ID to clause 49 dealing with non-mandatory requirements now reads as follows:

“The Company may establish a mechanism for employees to report to management concerns about unethical behaviour, actual or suspected fraud or violation of the company’s code of conduct or ethics policy. This mechanism should also provide for adequate safeguards against victimization of employees who avail of the mechanism and also provide for direct access to the Chairman of the Audit Committee in exceptional cases. Once established, the existence of the mechanism may be appropriately communicated within the organization.”

Further, the role of the Audit Committee would also include reviewing the functioning of the WBP in case the same is existing.

Benefits of a WBP

An effective WBP enables and empowers the employees to report violations and frauds to the management without fear of any persecution. Having a sound WBP can help a firm to nip problems in the bud, preventing or limiting any harm to the firm or its varied stakeholders. And, in responding constructively to public interest whistle blowers, firms reduce the likelihood that they will face litigation in the Courts and also enhance their corporate governance practices.

To put it very candidly, every organization faces the risk that something might go seriously wrong. Whenever such a risk arises, the first people to know about it will usually be those who work in or with the organization. Yet, while employees are the people best placed to raise the concern and so enable the risk to be removed or reduced, they are also the people who have the most to lose if they do. It is vital for effective risk management that employees are confident that they can raise their concerns with their employer without suffering any detriment. Without this confidence, employees may stay silent where there is a threat, even a grave one, to the employer or its stakeholders. Such silence denies organizations a fail-safe opportunity to deal with a serious problem before it causes real damage. The cost of such a missed opportunity can be huge - fines, compensation, higher insurance premiums, damaged

reputation, regulatory investigation, lost jobs, and even lost lives. Other advantages of a WBP are as follows. It,

- detects and deters wrongdoing;
- gets to managers the information they need to make decisions and control risk;
- demonstrates to stakeholders and regulators that the company is serious about good governance;
- reduces the chance of anonymous or malicious leaks (including to the media);
- reduces the chance of legal claims against the organization; and
- helps promote a free, honest and corruption free work environment.

Besides, it assists the company

- To identify risks that the company may not know about
- To remind employees that they may speak out as and when they have concerns
- To highlight to the employees that there are other routes of redressal if they cannot speak up internally.

Role of the Company Secretary

As an officer of the company at the centre of the decision making process, the company secretary is in a powerful position of influence. The company secretary should assist and guide the directors in their pursuit of profit and growth but should also act with *integrity and independence to protect the interests of the company, its shareholders and its employees*. Today's company secretary should play a pro-active and central role in the governance of the company. This requires excellent communication skills, a thorough knowledge of the company's business and applicable regulations, *strength of character, integrity, and above all a professional approach*.

The role of the company secretary concerns varied stakeholders – the board, the company, the shareholder, the employees, the regulators, the society and the *inter-se* relationships between and among them. He is at once a conscience keeper who needs to judiciously combine the seemingly juxtaposing elements of business – commercial viability and robust compliance. The company secretary's role can be delineated as

1. The generator and administrator of the whistle blowing mechanism and
2. The whistle blower

Generating and administering a whistle blower policy

The Institute of Chartered Secretary and Administrators (ICSA) best practice guide on 'Establishing a Whistle blowing procedure' states, "the company secretary will often have an important role in establishing an internal whistle blowing policy. They need to ensure

that there are trained people to operate the procedure so that any matters that are raised are dealt with effectively.”

Designing and implementing a whistle blower policy

The company secretary is best equipped to design and implement the WBP. It is he who can effectively synchronize the legal requirements with the practical considerations. While doing so, the company secretary must factor in the following components in any WBP:

Introduction : This part must talk about the rationale of having the WBP in the company and the need for introduction of the WBP. It is essential that the introduction emphasizes the importance of transparency and accountability in the management and administration of the company.

Definitions : Key words used in the WBP such as employee, whistle blower, protected disclosure, code of conduct or ethics, audit committee, nodal officer and ombudsperson and the like must be clearly indicated in the definitions part.

Scope and applicability : The applicability of the WBP to the employees, trainees and contract staff and the broad framework of the WBP must be indicated here.

Policy : The WBP must state that the company encourages employees to report to the immediate supervisors/management or audit committee (where the whistle blower feels that the management is itself involved in the wrong doings) any instances of fraud, inappropriate or unethical behaviour, questionable accounting or auditing practices and other serious concerns about the management and administration of the company. The above list is merely illustrative and by no means exhaustive. Other matters like the violation of the company’s code of conduct and ethics may also be reported as part of the WBP. Suggested instances of fraud or inappropriate conduct may also be included in the policy. All protected disclosures must be made in good faith and without mala fide intention.

Procedure : The company may appoint a senior official to act as the nodal point/ombudsperson for dealing with complaints under the WBP. The complaints must be in writing and may also be in e-mail. Anonymous complaints may not be encouraged. The complaint must be self-contained and convey all relevant details of the alleged misconduct or fraudulent practice. Vague indications, wild allegations and rumour and gossip mongering should not be encouraged in the WBP. The disclosures must be factual and clear and not speculative or conclusory.

Investigation : The WBP must have a normal procedure that thoroughly inquires into every protected disclosure and investigates the matter to its logical denouement. Such investigation must essentially be a neutral and fact-finding process and the principles of natural justice must at all costs be followed. If the complaint is not resolved within 30 days³ or is not resolved to the satisfaction of the complainant whistle blower, then he may prefer the complaint to the Chairman of the Audit Committee of the Company for resolution.

3. Illustrative

Protection to the Whistle blower: A key feature of the WBP is that it must protect the WB from any kind of persecution - direct, indirect, perceived, monetary or otherwise. In the absence of such protection, the WBP will serve little purpose. The WBP must explicitly prohibit any discrimination, harassment or retaliation against any whistle blower. Any complaint of such harassment, persecution or retaliation shall be independently reported and investigated. In other words, there shall be no victimization of the whistle blowers. However, adequate safeguards must be put in place to ensure that no frivolous and vexatious disclosures are made.

Communication to the employees: The WBP must be communicated to all the employees and others who can make protected disclosures under the policy. An acknowledgement from the employees must also be obtained from them at the time of joining employment. Wide publicity to the WBP must be provided in the company through internal circulars, intranet and as part of induction and personnel policies. Any amendments made to the WBP must also be indicated and communicated to reach all concerned.

The existence of a WBP must be disclosed on the website of the company and also disclosed in the Annual Report of the company. Needless to say, there must be widest possible dissemination of the same within the company.

The flip side

While the WBP helps bring to the fore fraudulent practices and curb them, it can also be misused by mischievous employees. Care must be taken to ensure that employees do not use it to grind personal axes, to settle personal scores or to nurse grudges against other employees. A proper and fine balance between the two is essential. Perhaps, it is for this reason that companies are wary of implementing a WBP. Time will tell which way India plc goes.

Company Secretary as Whistle blower

A spiritual guru often remarks, and rightly so, that in all good and positive aspects in life, it is never a case of “this” or “that”; instead it is always a case of “this” and “that”. Translating the same into the corporate milieu in the context of the working of the company secretary, his role is not “conscience keeper” or “whistle blower”; instead, it is always a case of “conscience keeper” and “whistle blower”. In fact, both the concepts – conscience keeping and whistle blowing are inter-linked and have an empirical relationship where one supplements and complements the other. For a corporate to function such that it operates its business in a commercially viable manner and simultaneously complies with the rules and principles of corporate governance is the litmus test of its being a good corporate citizen. The multi-faceted role that the company secretary plays epitomizes this seemingly juxtaposed scenario where a fine balance is struck between sound commerce and robust compliance. So, the conscience keeping role deals with ensuring the right thing every time. In a corporate context, it refers to compliance, adherence and fulfillment of laws, policies, procedures and covenants. Holistically, conscience keeping would be predicated and bulwarked in corporate governance. In many ways – corporate governance practised would be synonymous with conscience keeping.

While on the one hand the company secretary plays the role of a catalyst in devising, implementing and administering the WBP in a company, there is a more important role that he may be called upon to play in the days to come. As a conscience keeper, the company secretary already has the onerous responsibility to ensure that the company complies, adheres and fulfills its obligations under the laws, policies and procedures and other applicable covenants.

Be that as it may, where the board and senior management disregard the sage advice and cautionary words of the company secretary, it is incumbent upon him to personally assume the role of the whistle blower. His proximity to the highest executive body, awareness of the minutiae in the company, his frequent liaison within and outside the company – all cast on him the responsibility of discharging the role of the whistle blower.

It is settled law that the company secretary's duties are to a large extent fiduciary in nature. This entails upon him the fundamental duties to

- act in good faith in the interests of the company⁴;
- not to act for any collateral purpose;
- to avoid conflicts of interest; and
- not to make secret profits from dealings for or on behalf of the company.

In fact, the role is very delicate and calls for more than a modicum of courage, commitment and conviction. It is predicated on the fiduciary duty owed by the company secretary that he promptly brings to light any wrong doing. By virtue of his being an ex-officio board member and the position he occupies in the hierarchy, he is eminently best suited to be among the first whistle blowers. Besides board interaction and ensuring compliances, the company secretary invariably has responsibility for:

- Stock exchange requirements
- Finance and accounting matters/reporting
- Share registry
- Shareholder communication and monitoring
- Capital issues and restructuring
- Mergers, acquisitions and disposals
- Personnel related matters
- General commercial legal matters – contract negotiation/vetting and drafting
- IP, data protection, property and conveyancing
- Fiscal matters

4. An unofficial charter to act as whistle blower.

- Stock option administration and
- Price sensitive information

The above throws up a wide array of tasks dealt with by the company secretary and related exposure that could make him the right person to be the whistle blower, expose him as it does to every single aspect of the company's functioning.

Given the employer-employee relationship that exists in case of a whole time secretary, the later is more prone to be a conscience keeper. The practising company secretary, the secretarial auditor is perhaps better well suited to be act as the whistle blower. The Companies Bill, 2011, too seeks to provide impetus to this line of thought.

Conclusion

The pursuit of excellence is perennial. There is no room for compromise. In the discharge of our roles as company secretaries, whether in industry or in practice, we need to be constantly cognizant of our responsibility – to the economy, the company, the stakeholders and the profession. The beacon - we are partners in nation building; a cog in the wheel that is the Indian economy. Nation/Economy first, profession next, self last. This alone will do justice to the faith reposed in us by one and all.

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WHISTLE BLOWING — ARE WE HEADING IN THE RIGHT DIRECTION ?

VIVEK SADHALE* & VIKAS AGARWAL**

Introduction

In today's age of globalisation, it is not out of place to make an observation. Ethos, values in all spheres including in corporate is taking a back seat over the economic motives. The wind is blowing fast, and people seem to be changing fast too. India is hit with scams be it Satyam, allegations of fraud in OnMobile, Reebok has left investor confidence shattered.

After 9/11, we thought the global landscape would change. Change has come, but do we feel secure? If at all we felt secure for a while, the 26/11 Mumbai terror attacks changed life for the worse, once again. Some of these instances have a parallel to the corporate world.

With 9/11, US economy was hit with corporate scandals involving giants like Enron, Tyco, WorldCom to name a few. Post 26/11, India witnessed its first large scam, when Mr. Ramalinga Raju "confessed" to a large "fraud" in the books of Satyam, the then 4th largest Indian IT Company.

Did we not get a hint of these events before? Do people in charge of governance, really care for inside information or signals? Sometimes we wonder if Sherron Watkins (Ex VP at Enron) or Cynthia Cooper (Ex VP of Internal Audit at WorldCom) were heard at the right time, many such instances could have been controlled, if not completely avoided. In the hindsight, is it correct to assume that efforts of these whistle-blowers could have helped save life earnings, pensions of several innocent employees and other stakeholders ?

While it is true that public stakes are high in listed entities, governance issues are all pervasive. The magnitude may differ but the effect on stakeholders is the same. Governance issues haunt government as well as NGOs apart from corporate entities.

Corruption exists all over the world. Corruption has crippled the entire economy and resulted in widening of the gap between the various segments of the society. There are valiant few, who think that corruption can be eradicated and blew the whistle exposing the corruption, corrupt elements and their corrupt practices but they had to pay heavy price for their bravery.

* Company Secretary & Head – Legal and Investor Relations, Persistent Systems Ltd., Pune.

** Associate General Manager – Corporate Secretarial, Persistent Systems Ltd., Pune.

The views expressed in this article are strictly the personal views of the author(s).

KPMG India Fraud Survey Report 2008 highlighted some alarming facts. Over 80% of the respondents recognized that potential fraud was a big issue for most corporates and that the risk was perceived to be prevalent across all sectors. The respondents of the survey expressed concern that the “enemy”, both internal employees as well as suppliers, were perceived to pose the highest risk of fraud. Over 3/4th of the respondents stated that they were not fully geared to handle frauds in their companies. In a survey conducted by the Association of Certified Fraud Examiners in 2004, it was revealed that about 40% of the frauds were discovered through information provided by an “insider”. All these reports and surveys send a strong message to corporates for implementing a well-defined whistleblower policy.

What is Whistleblowing ?

While term ‘whistleblowing’ is a relatively recent entry into the vocabulary of public and corporate affairs and has gained significance in the recent past, the concept is an age old one. The concept of Whistleblower gained much recognition owing to two of the biggest known corporate scandals viz. Enron and Worldcom. Sheron Watkins and Cynthia Coopers came to be known as the two gutsiest women of the century who uncovered the fraud and misstatements in the accounts of these two well-known corporations in the United States.

Whistleblowing can be defined in a number of ways. Whistleblowing involves the act of reporting wrongdoing within an organization to internal or external parties. A whistleblower is defined as someone who exposes wrongdoing, fraud, corruption or mismanagement. Whistleblowing can also be defined which promote accountability by allowing for the disclosure by any person of information about misconduct while at the same time protecting the person against any action.

Whistleblowers may be an internal or an external person. Internal whistleblowers are employees who bring misdeeds of fellow employees or seniors to light. Whereas external whistleblowers would report misdeeds to other entities like regulatory agencies, investor protection agencies, etc.

Major Whistleblowing Legislations around the World

Most of the countries provide protection to whistle-blowers as a statutory right. Protection to whistleblowers is generally from dismissal or discrimination in employment or dealings. Many countries have devised and adopted a variety of laws and procedures for protecting whistleblower and to encourage whistleblowing.

The United States

The US has dozens of whistleblower laws at the state and federal level. The three principal Acts are the False Claims Act, the Whistleblower Protection Act and the Sarbanes-Oxley Act.

Whistleblowing arose almost a century ago in the False Claims Act, 1863, which was established to offer incentives to individuals who reported companies or individuals defrauding the government. Thereafter the Whistle Blower Protection Act, 1989 was enacted

under which federal employees are protected from workplace retaliation when disclosing waste and fraud. In 2007, Whistle Blower Enhanced Protection Act was enacted. Sarbanes-Oxley (SOX) Act, 2002 which was enacted thereafter introduced a series of corporate governance initiatives into the federal securities laws. For the first time, whistleblowing was included as a legislative precept of corporate governance norms. SOX which provided for substantive corporate governance provisions tried to change the attitude of corporation towards work place crimes. By mandating policies and protection for reporting wrongdoing, the SOX standards go beyond merely encouraging companies to be more responsive to employee whistleblowers.

The United Kingdom

In UK, legislation to protect whistleblowers was enacted in the wake of well-publicized scandals and disasters that occurred in 1980s and early 1990s. These included the collapse of Bank of Credit and Commerce International (BCCI), the drowning of four children at Lyme Bay, and the Clapham Rail crash.

The Public Interest Disclosure Act (PIDA) effective on July 2, 1999, covers both private and public employees (except police officers), and provides that "a worker has the right not to be subjected to any detriment by any act, or any deliberate failure to act, done on the ground that the worker has made a protected disclosure." Under the PIDA, whistleblowers must use prescribed channels for making disclosures in order to retain the Act's protection. The disclosure can be made to the employer itself or an appropriate authority, and forbids the disclosure to media. As is clearly apparent, the UK's scheme is materially different from that of the United States, which does not require employees to use any particular channel to raise their concerns.

Canada

Canada has very few laws which pertain directly to whistleblowing. The federal government enacted the Public Servants Disclosure Protection Act, 2007 to protect federal public service from reprisals for reporting wrongdoing. However, this Act has been extensively criticized as setting too many conditions on whistleblowers and for protecting wrongdoers.

Whistleblower legislation in India

The need of whistleblower legislation in India was on a rise in view of the glaring cases of corruption. A demand for suitable legislation for encouraging and protecting honest persons to expose corrupt practices on the part of public functionaries has been time and again raised. The Law Commission in its 179th Report had recommended that in order to eliminate corruption, a law to protect whistleblowers was essential.

Protection of Whistle Blowers gathered policy attention due the much controversial murder of Satyendra Dubey who tried to expose the corruption in the Golden Quadilateral Highway Construction Project by writing a letter to the Prime Minister. In 2004, in response to a petition filed after the murder of Satyendra Dubey, the Supreme Court directed that machinery be put in place for acting on complaints from whistleblowers till a law is enacted. The

government notified a resolution in 2004 that gave the Central Vigilance Commission (CVC) the power to act on complaints from whistleblowers.

Based on the 179th report of the Law Commission, the legislature drafted "The Public Interest Disclosure and Protection to Persons Making the Disclosures Bill, 2010 which was subsequently renamed as the Whistleblowers' Protection Bill, 2011.

Indian Scenario: Whistle Blower in Corporates and Legislative Efforts

The first step taken in regard to Whistleblower in corporate was in 1996, when the Confederation of Indian Industries (CII) took a special initiative with an objective to develop and promote a Code for Corporate Governance to be adopted and followed by Indian companies. The Code focused mainly on listed companies as these are financed largely by public money and hence, need to follow policies that make them more accountable to their investing public. The Code gave preference to the shareholders and the creditors instead of employees, suppliers and other stakeholders. While there was no material provision as regards the Whistleblowers Policy, Code in substance talked about the reporting of internal audit reports, including cases of theft and dishonesty of a material nature to the Board and an independent audit committee consisting of non-executive directors.

A major breakthrough on implementation of Whistleblower policy was achieved by an amendment to Clause 49 of the Listing Agreement to include the recommendations of the Narayan Murthy Committee Report on Corporate Governance, 2003. Owing to the controversy raised by the murder of Satyendra Dubey, the policy of Whistleblower was given as a mandatory recommendation. However, with the lobbying by the corporate world, many of the mandatory recommendations, including the Whistleblower policy, were made non-mandatory in the amendment to the Clause 49 of the Listing Agreement, which was enforced in April 2005.

Presently, clause 49 recommends the company to "establish a mechanism for employees to report to the management concerns about unethical behavior, actual or suspected fraud or violation of the company's code of conduct or ethics policy. This mechanism could provide for adequate safeguards against victimization of employees who avail of the mechanism and also provide for direct access to the Chairman of the Audit committee in exceptional cases. Once established, the existence of the mechanism may be appropriately communicated within the organization." This is a mere recommendation and not a mandatory provision which is to be complied with.

Whistleblowing and Good Governance

Whistleblower policy has been recognized as one of the basic features of Corporate Governance. Corporate Governance is a desired set of principles on which the corporate are expected to run their business diligently specially when there is separation of ownership and management and expects the timely compliance of other Acts and rules applicable to them. The concept of Corporate Governance has kept evolving to keep pace with the changing business environment. Corporate Governance is an all-pervasive term which touches all facets of the organizational operations. The best practices of Corporate Governance percolate right

from major financial decisions to every minute policy of the company. The major stakeholders of Corporate Governance are shareholders and the directors. The other stakeholders include employees, suppliers, customers, bankers, lenders, regulators and the community at large. The principles of Corporate Governance are same that are followed for ages together for running a disciplined business. However, the novel part is recognition of these principles by country specific laws.

Corporate governance is the system by which companies are directed and controlled. Directors are responsible for the governance of the companies on the Board which they sit. The shareholders' role in governance is to appoint the directors and the auditors and to satisfy themselves that an appropriate governance structure is in place. The very basic premise of corporate governance is accountability to shareholders as the directors always stand in a fiduciary relationship with the company and the shareholders, the welfare of the company is welfare of the shareholders.

Whistleblowing is a valuable tool in any organisation's corporate governance strategy as it empowers employees to act on incidences of misconduct and help maintain a safe workplace, while protecting profits and reputation of the Company. Whistleblowing can be a divisive topic and, while most would agree with the value of reporting wrongdoing and condone good organisational governance, external contexts can colour acceptance and perception. Even if an organisation has a whistleblowing hotline in place, they should not be complacent when it comes to its usage and communication. If a company doesn't receive many whistleblowing reports, they shouldn't assume that no news is good news.

Post Satyam scandal, there has been huge debate amongst corporate on deciding ways and means to strengthen the corporate governance framework for the listed companies. It has been opined by an international expert that a whistleblower policy is the best way to prevent corporate frauds from blowing up provided it is implemented in spirit, and not just in form. Whistleblower policy is the best way to check corporate frauds. In any organisation, where fraud develops with management collusion, there will be at least one good, solid whistle blower. There are large number of corporations that believe that there is a direct relationship between business governance and business valuation. To the extent this consideration is applied by drivers of corporate governance in the right spirit, this is a positive sign.

Corporate Involvement – Can Make or Mar the success of Whistleblower Policy

Attitudes toward whistleblowing have evolved considerably during the past 50 years. Time is changing from early days of the "organization man" ethos where loyalty to the company was the ruling norm, to the present time when public outrage about corporate misconduct has created a more auspicious climate for whistleblowing. Prior to the 1960s, corporations had broad autonomy in employee policies and could fire an employee at will, even for no reason. Employees were expected to be loyal to their organizations at all costs. Due to lack of protection for whistleblowers, problems were often concealed rather than solved. Even in cases where whistleblowing occurred, it was not always heeded. Over a period time, there have been successful cases of whistleblowing although even in these cases, the personal

and professional toll on the individuals has been heavy. Whistleblowers may well encounter difficulties when they appeal internally or go public with information that may damage their companies.

Corporate culture is an important ingredient for successful corporate governance. Complete buy-in from senior management is the most important factor for successful implementation of whistle blower policy. While it is granted that no risk can be eliminated, corporates must take proactive steps to counter internal and external threats. It is important that entities must initiate policies that encourage employees and external vendors / stakeholders to fearlessly report misdeeds that they come across.

Confidentiality and transparency are other ingredients for the success of the Whistleblower policy. Employees are concerned that they will be ill-treated or their complaints will not be heard. It is for this reason that most of the cases are never reported even-though co-workers are well aware of such instances. Companies must have courage to address all such cases. Employees must have confidence that they will be protected and will not have to face any personal deprivation on this account. It is important that the employees who are being investigated are given a fair chance to make their representation and the process of natural justice must be followed. Employees must see merit and should have confidence in the mechanism set up by the companies. The mechanism must be transparent, fair and must be motivating enough for employees to come forward with issues. Employees must be updated about the progress of the case from time to time.

Technology can help HR departments to achieve this. The Public Relation officer and HR managers have to work in tandem to do damage control as the rumor mill works overtime when an inquiry is being conducted. HR departments must make use of technology to set up open and transparent communication channels for employees to address their concerns. Once in a year, employees must be trained and informed about various policies that company has in place to deal with such crisis and situations. Employees must be made aware of whom to contact if they have to report any instance which is "wrong".

It is necessary for an organisation to implement best practices for encouraging employees to bring unethical or illegal practices to the forefront and addressing them before they become fatal to an organization. A whistleblower policy may be drafted and implemented by management, but it should then be submitted to the audit committee or board of directors. The foundation of any whistleblower policy is a clear and specific definition of whistleblowing.

It is important for the corporates to develop a whistleblower policy which is integrated and connected with organisation's code of conduct. Some companies set anonymous lines for reporting instances while some have an administrator responsible for such cases. It is not uncommon to see whistle-blowers being branded as "inside enemies" by fellow workers. Enron as well as WorldCom are live examples of how whistleblowers were publicly treated until law took its own course. It is in such a situation that all concerned stakeholders must be encouraged to play a constructive part in addressing the issue at hand. This brings out culture of a corporate.

Key Aspects of a Whistleblower Policy

1. A whistleblower policy should cover individuals within the organization as well as external parties, who conduct business with the organization.
2. Whistleblower policies should prevent discrimination or retaliation against employees who report problems. Policies should include methods to encourage employees, vendors, customers, and shareholders to report evidence of fraudulent activities in the organisation.
3. Protecting whistleblowers' confidentiality is an important part of any whistleblower policy because the goal is to create an atmosphere where employees feel comfortable to submit their names with claims to allow for further questioning and investigation. Allowing employees to file anonymous claims may increase the possibility of claims actually being reported.
4. Whistleblower policy needs to address the process employees should follow in filing their claims. The policy should explain how the claims will be investigated once received and whether the employee should expect to receive any feedback from the Whistleblower administrator.
5. Organizations may require whistleblowers to direct their claims to a certain person, such as a compliance officer, or, alternatively, to follow a ladder of reporting until they reach the top of management. Few organizations may also facilitate submission on anonymous complaints which can directly to the Chairman of the Audit Committee. Specific reporting mechanisms within the process could include telephone or e-mail hotlines, websites, or suggestion boxes.
6. Upon completion of the whistleblower policy, the organization should develop implementation and enforcement mechanisms consistent with the whistleblower policy.
7. Whistleblower policy cannot be effective unless it is communicated to employees, vendors, customers, and shareholders. Employees should be provided training about the whistleblower policy at human resources orientation process. Information can be posted throughout the company and on intranet sites. Customer service representatives can be trained to answer questions about the whistleblower policy.
8. To create a culture of openness and honesty, it is important that employees hear about the policy regularly. Top management should make every effort to talk about the commitment to ethical behavior in memos, newsletters and speeches to company personnel.
9. Publicly acknowledging and rewarding employees who pinpoint ethical issues is one way to send the message that management is serious about addressing issues before they become prevalent.
10. Managers should be required to investigate all allegations promptly and thoroughly, and report the origins and the results of the investigation to a higher authority.

11. Find out employees' opinions about the organization's culture vis-à-vis its commitment to ethics and values.

Are we headed in the right direction ?

Transparent and fearless communication within and outside organizations is important and proves to be a major deterrent of frauds. Whistleblowing is one such mechanism. If implemented well, it motivates employees to report misdeeds well in time and to take corrective action before it is too late. It is an important governance risk mitigating mechanism.

Whistleblowing is relevant and plays a critical role in corporate governance. There should be an effective regulatory framework which gives detailed thought on the protection to those who are prepared to blow the whistle. Those who help the system should get protection, regardless of the law being in place. We are loaded with examples where people exposing scams, faced wrath of those in power. If Sherron Watkins or Cynthia Cooper were heard at the right time, we would probably be in a different economic world. The corporate culture, its practices should indicate that individuals who raise a genuine concern against wrong doing will get adequate protection and they will not be subjected to risk victimisation, losing their job or damaging their career.

Whistleblower policy framed by a company should consider all the dimensions necessary not only to protect the Whistleblowers but also to inculcate among the employees a commitment to their work and fearlessness in conduct when exposing employees at higher pedestal. As it is always said, Norms of Corporate Governance are not merely to be complied with but have to be adopted as day-to-day practice of the Company. For this purpose, clear definition of Whistle-blowers, non-retaliation clauses, confidentiality and due process should be ensured.

The Companies Bill 2011 contains a provisions in respect of vigil mechanism (whistle blowing) proposed to enable a company to evolve a process to encourage ethical corporate behavior, while rewarding employees for their integrity and for providing valuable information to the Management on deviant practices. The vigil mechanism provides for an adequate safeguards against victimisation of persons who use such mechanism and make provision for direct access to the chairperson of the Audit Committee in appropriate or exceptional cases. The details of establishment of such mechanism need to be disclosed by the company on its Website and in the Board's report. Further, one of the duty of Independent Director has been prescribed to ascertain and ensure that the company has an adequate and functional vigil mechanism and to ensure that the interests of a person who uses such mechanism are not prejudicially affected on account of such use.

With Union Cabinet clearing "The Public Interest Disclosure and Protection to Persons Making the Disclosure Bill, 2010", we seem to have taken a right step, even though it is coming late in the hour. The Bill when passed by the Parliament will protect general public for reporting any improper working in corruption or willful misuse of power or willful misuse of discretion which causes demonstrable loss to the Government. The Bill is currently restricted to only government functioning and will not cover private sector in its ambit.

Needless to mention, the law needs to protect all whistleblowers, regardless of which stream of sector they cater to.

Corporates crib about the cost of compliance but time and again it is proved that cost of non-compliance is far greater and deeper. Investors will be more demanding. Those corporates, who have better governance and culture, will be winners in the long run. Investors will be happy to pay a premium for corporates with good conduct and governance. Corporate Governance is not about checking boxes.

Corporate should not shy away from investigating complaints made by the employees. The employees who are being investigated should be given a fair chance and the process of natural justice must be followed. Needless to mention, it is the duty of the Independent Directors to protect whistleblowers.

Finally, the question remains - can corporates be proactive and create a fair and simple whistleblowing mechanism. Of course, regulators need to educate one and all, but proactive organisations will help themselves and not create another potential ugly story for our next generation.

Only time will tell if we are heading in the right direction.

COMPANY SECRETARY – WHISTLE BLOWER OR CONSCIENCE KEEPER

KAUSHIK MUKHERJEE*

The topic was conceptualized some time back and was discussed threadbare in one of the seminars in Kuala Lumpur

Extracts are as follows

“KUALA LUMPUR, July 16 (Bernama) - Company Secretaries should raise the alarm when they detect wrongdoings in their organization to ensure that ethical business practices are in place as emphasized by the government.

Minister in the Prime Minister’s Department Detuk Seri Mohamed Nazri Aziz, in making the call, said the government was proposing the Companies Bill 2007 and amendments to the Securities Commission Act, 1993 to provide protection for “whistle blowers”.

Lauding MAICSA’s efforts to ensure good governance, Nazri said company secretaries, acting as the nexus between board members and stakeholders, should have a moral obligation to report misdeeds and act as gatekeepers for any wrongdoings.

He said although there are regulatory bodies such as the SC and Bursa Malaysia, nothing could be considered 100 percent foolproof.

MAICSA President Akbar Moidunny said although Company Secretaries should act as whistle blowers on corporate wrongdoings, this would not be possible if there was no guarantee in the aspect of job security.

They need confidence to do it. If they blew the whistle, they might lose their job. Protection can encourage them to curb these misdeeds,” he said.

Presently, about 4,700 Chartered Company Secretaries are operating in Malaysia.

MAICSA Council Member Mah Li Chen’s view that company secretaries should speak up when there was a proposal on directors’ remuneration which could be deemed excessive, sparked discussion on the benchmark amount that should be paid.

It should be a guideline for the whistle blower, who can be the Company’s secretary, chief executive officer, chief financial officer, among others.

* General Manager & Company Secretary, Phillips Carbon Black Limited, Kolkata.

“But, any report on breach of conduct should be substantiated by hard facts,” he said. Mah’s presentation also revisited other essential roles of a listed company’s company secretary on matters such as board composition and procedures, and ensuring relevant and sufficient information was given to board members so that they could make informed decisions at board or committee meetings.”

Indian Scenario

In India , the concept of whistle-blower is slowly gathering momentum and the Indian Cabinet has already approved Public Interest Disclosure (Protection of Informers) Bill 2009, popularly known as Whistle-blowers Protection Legislation. Though this proposed legislation is lacking in many areas, but at least, it makes a beginning in recognizing the role of the whistle blower in countering the menace of corruption which no instrumentality of the Government is able to contain. Public participation is the only effective method in curbing corruption, because it is the aggrieved class which alone can provide clue for proper diagnosis and treatment to contain, if not eliminate, the cancer of corruption.

Even the Hon’ble Supreme Court of India has made a beginning in the case of R.K. Jain [2010 (256) E.L.T. (641) (S.C.)] by recognizing the role of the whistle-blower and saddled CESTAT Bar Association, Bangalore with exemplary cost of Rs. 2 lakh as they tried to silence the whistle-blower from exposing the ongoing maladies in the CESTAT, through his writing in this very Law Journal.

The Supreme Court of India , explaining as to who is a whistle-blower, said that a whistle-blower is a person who raises a concern about wrongdoing occurring in an organization or body of people.

Enlarging the scope of whistle-blowers the Apex Court said “Usually this person would be from that same organization. The revealed misconduct may be classified in many ways; for example, a violation of a law, rule, regulation and/or a direct threat to public interest, such as fraud, health/safety violations and corruption. Whistleblowers may make their allegations internally (for example, to other people within the accused organization) or externally (to regulators, law enforcement agencies, to the media or to groups concerned with the issues). Most whistleblowers are internal whistleblowers, who report misconduct on a fellow employee or superior within their company.”

The Law Commission in its 179th Report submitted in December, 2001 formulated a draft Public Interest Disclosure (Protection of Informers) Bill, 2002. But the bill is still hanging fire after eight years. It was Mr. N. Vittal, then Chief Vigilance Commissioner who sought a law in 1999 to encourage disclosure of corrupt practices. While the bill under consideration now provides for penalization in case of false or frivolous complaints, a suitable reward mechanism is conspicuously absent. The National Anti-Corruption Strategy proposed by CVC calling for suggestions by 20-9-2010 also highlights protection angle to the exclusion of incentivising whistle-blowing activity.

It is high time that the Government of India takes a leaf out of S.C. judgement in R.K. Jain case by introducing provisions for providing compensation to whistle-blowers to assuage

their sufferings in the battle against corruption, particularly, in cases of economic offences and frauds against public revenue. Such provisions are presently available under the U.S. law and same pattern can be followed in India also.

A whistle-blower covers individuals within the organization as well as external parties who conduct business with the organization.

Examples of reportable activities include, but are not limited to:

- Questionable, accounting practices, breaches of internal controls, questionable matter relating to treasury and the financial statement;
- Bribery, receiving kick-backs or other forms of corruption, corporate fraud, and other unethical or illegal business conduct by NGCP Employees;
- Conduct which may result in a substantial mismanagement of Company resources or assets;
- Conduct which may result in a violation of applicable laws, rules or regulations; or
- Any other matter of concern that NGCP Employees, shareholders or other interested persons believe may adversely affect the NGCP Entities and/or NGCP Employees.

In evaluating materiality, the following may serve as guide:

- a. The matter is the result of a significant internal control or policy deficiency that is likely to exist at other units within the NGCP;
- b. The matter affects the integrity of the financial statement reporting;
- c. The matter is likely to receive media or other public attention;
- d. The matter involves the misuse of NGCP resources or creates exposure to a liability in potentially significant amounts;
- e. The matter involves allegations or events that have a significant possibility of being the result of a criminal act (e.g., disappearance of cash);
- f. The matter involves a significant threat to the health and safety of employees and/or the public; or
- g. The matter is judged to be significant or sensitive for other reasons.

Officers, employees, and representatives are expected to report violations of policies and procedures.

Employees are also encouraged to discuss ethical issues with their supervisors when in doubt about the best course of action to follow in a particular situation.

A Company Secretary is a Compliance Officer and a Conscience keeper. He has in his command all vital information as well as knowledge of the source of all such information. In many corporates, he is a part of the strategic management team. The position of a Company Secretary is that of utmost confidentiality, trust, good faith and credibility. In my view, he

cannot simple be a whistle blower in an organization because that would question his credibility.

Moreover, merely by whistle blowing, a Company Secretary cannot escape his responsibility. In the revised Companies Bill he is defined as a Key Managerial Personnel.

Parallely the following questions also come to the mind :

Can CFOs be Whistle Blowers ?

In this regard in US, draft legislation would exclude CFOs from collecting a whistleblower bounty created under the Dodd-Frank Act. The law passed in 2012 aimed to give witnesses to securities fraud a monetary incentive — starting at \$100,000 — to report wrongdoing to the Securities and Exchange Commission (SEC). Under an SEC proposal made in December 2010, informants would collect 10% to 30% of wrongdoers' payout to the commission for enforcement cases that involve penalties worth more than \$1 million.

However, the forthcoming bill, to be proposed by freshman congressman Michael Grimm (R-N.Y.), would make "any whistleblower who has legal, compliance, or similar responsibilities for . . . an entity and has a fiduciary or contractual obligation to investigate or respond to internal reports of misconduct" ineligible for the bounty.

Limiting the ability of a company's top executives to cash in on fraud that happened on their watch — even if they are not culpable — makes sense, says Luigi Zingales, a professor at the University of Chicago's Booth School of Business who has studied the issue of whistleblowers. "It would be reasonable to say that if you are the CFO and find something that doesn't work, you should resign," he says. "You shouldn't profit."

Can Auditors be Whistle Blowers ?

The Securities and Exchange Commission's new whistle-blower rules, issued in May 2011, received much attention for providing cash rewards to securities-fraud informants. CFOs should be aware of a potential outcome of the rules that was not well publicized: auditors can blow the whistle on their own audit clients and receive a substantial bonus for doing so.

Under the rules, the SEC may pay substantial monies to individuals whose tips lead to the collection of more than \$1 million in monetary sanctions. In fact, the awards will range from 10% to 30% of the government's financial recovery. To be eligible for a bounty, whistleblowers must report "original information" derived from their "independent knowledge or independent analysis." In an era of monetary sanctions from SEC enforcement actions totaling eight and sometimes nine figures, these rules obviously create enormous incentives for individuals to report suspected illegal activity.

Two aspects of the rules will allow auditors to collect a bounty from their own clients' misdeeds, by direct and indirect means. First, the rules say that information will be deemed "original," even if the provider of the information is affiliated with an audit firm, as long as the audit client's conduct is likely to cause substantial financial injury to investors. This provision could encourage auditors to report information on their own clients directly to the

SEC. It alone may render ineffective the other provision apparently designed to prevent auditors from reporting — and cashing in on — their own clients.

Second, auditors may blow the whistle on their own employers. Tellingly, if an auditor does so and the information reported ultimately leads the SEC to recover sanctions against the audit client, the reporting auditor is eligible for an award. To be sure, in adopting the rules the SEC stated it was "not excluding information that is received in breach of state-law confidentiality requirements, such as those imposed on auditors, because to do so could inhibit important federal-law enforcement interests." In other words, the commission wants to encourage auditors to come forward, even if an auditor breaches a duty of confidentiality to a client by doing so.

Because individual auditors now have ample opportunity to seek a substantial whistleblower bounty, the relationship between audit firms and their clients could become damaged by creating conflict and controversy that otherwise would not have occurred. At a minimum, the rules will likely create an atmosphere of suspicion and distrust when difficult audit issues arise and accounting judgments are made. Clients will naturally wonder whether an auditor who disagrees with an accounting judgment will report that issue to the SEC, causing the SEC to investigate.

Conclusion

In Indian context, need of the hour is therefore, not to have a whistleblower Company Secretary or a whistleblower Chief Financial Officer or an whistleblower Auditor but an independent Company Secretary, an independent Chief Financial Officer, a truly independent Auditor.

An independent Company Secretary can be both a whistleblower as well as a conscience keeper, but will be required to blow the whistle only in extreme cases when situation goes totally out of control and he needs to report to the shareholders per se i.e. the owners of the Company. He may have to put in his papers on his own without compulsion after blowing the final whistle. However an independent Company Secretary would be a far cry and perhaps can only happen if his appointment, appraisal (carrot as well as stick) and removal is in the hands of a independent body like the Audit Committee of the Board of Directors.

COMPANY SECRETARY – “CONSCIENCE KEEPER” OR “WHISTLE BLOWER”

ANIL K SEHGAL*

A Company Secretary is a senior position in a private sector company or public sector organisation, normally in the form of a managerial position or above. The duties and responsibilities of company secretaries vary depending on the size of the company and on the form of organisation adopted. Company Secretaries have the responsibility of setting up the contours for the deliberations of the Board and ensuring regulatory compliance with respect to all the decisions. They act as governance professionals.

Before dwelling upon Company Secretary’s role as “Conscience Keeper” or “Whistle Blower”, let us understand the terms “Conscience”, “Conscience Keeper” and “Whistle Blower”

Conscience

The Greek word for "conscience" literally means "co-knowledge, or knowledge with oneself." Commonly used metaphors for conscience include the "voice within" and the "inner light. As per Collins World Dictionary, conscience is the sense of right and wrong that governs a person's thoughts and actions.

Conscience is an aptitude, faculty, intuition or judgment of the intellect that distinguishes right from wrong. In psychological terms conscience is often described as leading to feelings of remorse when a human commits actions that go against his/her moral values and to feelings of rectitude or integrity when actions conform to such norms.

There have also been religious, secular and philosophical views about conscience. The secular approach to conscience includes psychological, physiological, sociological, humanitarian and authoritarian views. Contemporary scientists in ethology, neuroscience and evolutionary psychology seek to explain conscience as a function of the brain that evolved to facilitate reciprocal altruism within societies.

The idea of conscience involves some degree of sincerity with which one examines the moral credentials of his or her wants, omissions and commissions. Psychologists say feelings of remorse, shame, dismay, torment or guilt are major elements of a ‘functioning conscience’. Simply put, it is an individual’s system of moral values, the sense of right and wrong in his or her conduct.

* GM (Corporate)-cum-Company Secretary, WAPCOS Limited (A Government of India Undertaking).

Conscience Keeper

The dictionary meaning of “Keeper” is a person who manages or looks after something or someone, in particular. Synonyms of “Keeper” are custodian - guardian - guard - warden - caretaker etc. The term conscience-keeper refers to a person whom an individual listens to when in doubt about moral values but not necessarily agrees with. Conscience-keepers thus seek to guide but keep a respectful distance from the individuals or the systems involved in decision-making. They often think differently from the latter on the moral content of issues, and disagree with the individuals or the systems concerned either in public or in private, giving them the option to choose between two competing values.

In ancient times, kingdoms had a Rajguru, a conscience keeper who had no political power per se, but commanded a lot of authority nonetheless. Keeper of the King's conscience was a position in the English judiciary before the advent of parliamentary representative democracy. The person appointed as keeper of the King's Conscience was usually a bishop. He was responsible for overseeing the international affairs of the monarchy and for delivering justice on behalf of the king. Today this position has become the Lord Chancellor.

Whistle Blower

A whistleblower (whistle-blower or whistle blower) is an informant who exposes wrongdoing within an organization in the hope of stopping it. The wrong doing may be a violation of a law, rule, regulation and/or a direct threat to public interest, such as fraud, health/safety violations, and corruption. Whistle Blower tells the public or someone in authority about alleged dishonest or illegal activities (misconduct) occurring in a government department, a public or private organization, or a company. He blows the whistle on corruption, crime and other misconduct, including unethical conduct.

Whistleblowers may make their allegations internally (for example, to other people within the accused organization) or externally (to regulators, law enforcement agencies, to the media or to groups concerned with the issues). Most whistleblowers are internal whistleblowers, who report misconduct on a fellow employee or superior within their company.

Ideas about whistle blowing vary widely. Whistleblowers are commonly seen as selfless martyrs for public interest and organizational accountability; others view them as "tattle tales" or "snitches," solely pursuing personal glory and fame.

Legal protection for whistle blowing varies from country to country. In India, Whistleblowers' Protection Bill, 2011 was passed by the Lok Sabha on 28 December 2011.[37] The Bill is however currently pending in the upper house of Parliament, Rajya Sabha for discussion and further passage. The Bill was introduced in Rajya Sabha on 29 March 2012.

Company Secretary's Role

— *As a conscience Keeper*

There are a few questions in this context first of which is ‘Can a corporation have a conscience?’ when one of the arguments is that Corporations are not persons. They

are artificial legal constructions, machines for mobilizing economic investments towards the efficient production of goods and services. Let us answer this question first.

Conscience of a Corporation

Professors Kenneth E. Goodpaster and John B. Mathews, Jr., have mentioned in their article in the Harvard Business Review, “Can a Corporation Have a Conscience?”, in 1982 that “...the criticisms and counterarguments we have heard during hours of discussion with business executives and business school students. We believe that the replies to the objections about a corporation having a conscience are convincing.” The United States Supreme Court in January 2010 ruled in *Citizens United v. Federal Election Commission* that corporations were in fact human. However, Supreme Court Justice Stevens said “Corporations have no consciences, no beliefs, no feelings, no thoughts, no desire”. Efforts are on to have the position created by the United States Supreme Court amended.

As ‘conscience’ of an organization has been recognized, the next question comes ‘Who keeps conscience of a Corporation?. This question is simple to answer. As the identity of a Company as a ‘person’ is just a legal fiction thus it is only real people that might be said to have the capacity to respond to the still, quiet voice of conscience. Then, a further question arises ‘Is it the role of the Board, the Managing Director, Company Secretary, other members of senior management, the whole company (or all of the above)?

While others may also play their role as “Conscience Keepers”, the Company Secretary must contribute his best in this regard due to the position held by him. The Company Secretary is the pivot around which the whole corporate machinery revolves. He Commands high position in the value chain and acts as an interface between the company and its Board of Directors, shareholders, government and regulatory authorities. He/She ensures that Board procedures are both followed and regularly reviewed. Sir Roger Carr, President of The Confederation of British Industry argues that ‘Company secretaries are key players and have an important part to play in improving the overall perception of business.’

The crucial role that a Company Secretary plays in a company can be gauged by the fact that the Companies Bill, 2011 equates him to the Chief Executive Officer (CEO) and Chief Financial Officer (CFO) of the company by including him in the definition of Key Managerial Personnel thus placing heavy responsibility on his shoulders.

The corporate sector has recognized the role of the Company Secretaries, be it an entrepreneur, an industrialist, a management guru, an administrator or a politician.

On the basis of role played and responsibilities discharged, a Company Secretary, in effect, is organization’s ‘Corporate Conscience’. He is expected to uphold the highest standards of corporate governance and be “Conscience Keeper” of the organization he represents.

— As a Whistle Blower

Ernst and Young in a report based on India fraud survey 2012, “Fraud and corporate governance : Changing paradigm in India” have mentioned that Bribery and corruption continue to be a perpetual challenge for corporate India. As per the Report, Whistle-blowing is at a nascent stage in India, and most Indian companies do not use it as an effective tool against fraud. Some of the examples of business misconduct/malpractices are asset misappropriation, intentional misrepresentations directly or indirectly affecting financial statements, Suspicion of fraud or theft, serious non-professional or non-ethical behaviour, an abuse of authority, violation of any law or regulations environmental hazards like toxic leaks from the company’s plant, non-adherence to safety standards in respect of fire, flood, environment and public security.

The Company Secretary is in a powerful position of influence. He should try to ensure that affairs of the company and its constituents are conducted in a fair and transparent manner by adopting highest standards of professionalism, integrity, ethical behaviour and honesty. A culture needs to be developed where it is safe for all employees to raise concerns about any poor or unacceptable practice and any event of misconduct.

In case a Company Secretary feels that his all-out and sincere efforts notwithstanding, any dishonest or illegal activity, misconduct, malpractice, corruption or mismanagement in the organization does not stop, he should not hesitate in adopting the role of a Whistle blower in the interest of the organization.

Conclusion

There is no doubt that economic volatility, global competition, growing risk appetite demand the governance professionals like Company Secretaries to prioritise their role as a Conscience Keeper and as a Whistle Blower, the need of the hour is that a Company Secretary should pay more attention to his role as a ‘Conscience Keeper’. Also, on the other hand he should not fail to adopt pro-active and a positive role of a ‘Whistle Blower’ and act fearlessly, if need be.

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ROLE OF THE COMPANY SECRETARY WITH REFERENCE TO WHISTLE BLOWING POLICY OF AN ENTERPRISE

PROF. R BALAKRISHNAN*

Introduction

In line with best international governance practices, all enterprises, throughout the world, would like to put in place a system through which employees and its business associates may report unethical practices and infringements of the enterprise's business code of conduct and ethics without fear of reprisal. All enterprises, by and large, put in place a process by which the employees and its business associates have direct access to the chairman of audit committee, chief executive officer / managing director, chairman of the board and compliance officer who is generally the company secretary of the enterprise. The whistleblowing policy with proper documentation and the system in place could ultimately encourage employees and business associates to communicate their concerns / raise their voice and management would be in a position to listen them and at the end of the day, both employer and employee/ business associates could play their constructive role to bring about an effective risk management system within the organization. However, the crux point is that a whistleblowing policy can be successful only if the policy which is formulated by the enterprises guarantees the required protection which is one of the key components of a successful whistleblowing policy and procedure along with full commitment from top management and also guaranteeing the protection mechanism against victimization of the whistleblowers. Needless to mention, the regulatory protection has also to be in place.

Whistleblowing concept and the relevant laws

Whistleblowing

The organization is always interested to eliminate unethical and improper practices and in this perspective, management taking the responsibility to promote good corporate governance, formulate policy on whistleblowing and put in place an efficient administrative system thus bringing out the transparent transactions. Whistleblowing is an internal mechanism, which is formulated by organizations worldwide to help their employees to draw up a relevant whistleblowing mechanism through the established whistleblowing procedure, which provides a route of communication for individuals. The whistleblowing policy is put in place by organizations to ensure the safety of those individuals who blow the whistle. The organization formulates a policy on whistleblowing and this policy document spells out an

* CS - Pune (The first and only Indian to win the runner up award of Company Secretary of the year 2007 from the Institute of Chartered Secretaries and Administrators of London - UK).

internal policy to the employees of the organization and other stakeholders on the accessibility by them to the audit committee and the other responsible executives in the organization.

Whistleblower

A Whistleblower is an employee or ex-employee of an organization, who discloses information about serious malpractice by that organization, not otherwise known or visible, where the disclosure is made in the reasonable belief that there is malpractice and the disclosure is made in good faith, without malice and may in the public interest?.

Difficult Environment

Employees of an organisation are usually the first to become aware of conduct or activities taking place within an organisation, which could turn out to be cases of serious misconduct or malpractice. Unfortunately, due to fear that their concerns will not be taken seriously or that they will be victimised or dismissed or their loyalty to colleagues or their employer would be suspected, the employees with such knowledge often choose not to report their suspicions. By and large the vigilant employees must be able to come forward and report cases of malpractice, fraud, safety violations, etc., both for the public's sake and for the sake of the company wishing to maintain its public image and do the right thing. Small businesses are working in an increasingly competitive environment and may find themselves under increasing pressure to behave unethically or cut corners – in such companies, vigilant employees may find themselves highly vulnerable. The silence on the part of the employees is not in anyone's interests. The suspected malpractice is reported earlier, the same could be investigated immediately and quickly. In case, the same is, if proven, dealt with appropriately.

Relevant regulation on whistleblowing

The Market Regulator i.e., the Securities Exchange Board of India (SEBI) also recognises the above and through the clause 49 of the Listing Agreement the regulator had introduced the whistleblower policy to be in place which is one of the non-mandatory requirement as on date. The whistleblower requirement also categorically states that the employment and other personnel policies of the company shall contain provisions protecting "whistle blowers" from unfair termination and other unfair prejudicial employment practices. The regulator is definitely like to ensure that the protection against victimisation and dismissal employees who make certain disclosures of information in the public interest is protected.

Purpose for establishing whistleblowing policy

The intention of the Whistleblower Policy is that each organization's management establishes a mechanism for employees to report concerns about breach of any internal controls or company policy relating to financial malpractice or fraud, failure to comply with a legal obligation, criminal activity, improper conduct or unethical behaviour, corruption and mal-administration actual or suspected fraud or violation of the company's code of conduct or ethics policy. It would be a very good practice for all corporate organisations to reflect the principles of the act in creating internal procedures which could encourage employees to report their legitimate concerns and contain safeguards against misuse and also provide protection against victimisation / dismissal.

The exact details of such a mechanism should be left to each company, through its Board of Directors, to decide, but the existence and implementation must be reviewed by the audit committee. The mechanism must have adequate provisions to ensure there is no victimization of employees who avail of this procedure.

The prevalent Law on whistleblowing

The law of employment imposes on all the employee duties of confidentiality and fidelity to the employer during the currency of an employment relationship whilst they are in the employment of an organization. By and large this generally, prevents a disclosure, which could embarrass or harm the employer. The consequences of this are far-reaching for the whistleblower. As employees must not disclose their employer's confidential information, the disclosure of anything that the employer describes as "confidential", even if this is evidence of wrongdoing, then makes an employee in breach of this duty. Employees are also under a general duty not to act in a manner, which is calculated or likely to destroy the mutual trust and confidence on which the employment relationship is based.

At the same time, whistleblowers can also play a very important role in providing information about breach of any internal controls or company policy relating to financial malpractice or fraud, failure to comply with a legal obligation, criminal activity, improper conduct or unethical behaviour, corruption and mal-administration. Employees working in the same department of an organization know better as to who is corrupt in their department but unfortunately, they are not bold enough to convey the said information to the higher authorities of the organization due to their fear of reprisals by those officials against whom complaints are made. If adequate statutory protection and guarantee is granted, there could be no doubt that the company will be able to get adequate and more information regarding corruption, fraud, improper conducts or unethical behaviour, corruption and mal-administration.

Such provisions exist worldwide i.e., in England, Australia, New Zealand and in the United States of America. Good faith whistle blowers represent the highest ideals of public service and challenge abuses of power. Whistle-blower policy is an internal mechanism, which will dissuade employees disclosing fraud or corruption to the media. Encouraging a culture of openness within an organization helps. Placing employees in a position where they feel driven to approach the media to ventilate concerns is unsatisfactory both for the employee and the organization.

The UK Experience

Nolan Committee in the United Kingdom made various recommendations on the subject and the British Government accepted the same. This ultimately led to the passing of the United Kingdom Public Interest Disclosure Act, 1998 and this was subsequently amended in the year 1996.

The Public Interest Disclosure Act, 1998

The Public Interest Disclosure Act, 1998 amends the Employment Rights Act, 1996 to give protection from victimisation and dismissal to individuals who make certain disclosures

in the public interest. The Public Interest Disclosure Act, 1998 applies to virtually all employees in the public, private and voluntary sectors, irrespective of their period of employment, and protects them if they make “qualifying disclosures”. Thus in addition to employees, Public Interest Disclosure Act 1998 also covers agency staff, trainees, contractors and home workers. It does not, however, cover the genuinely self-employed (other than in the NHS), volunteers, the intelligence services, the armed forces and the police, and those who normally work overseas.

Qualifying and Protected Disclosures

In the normal circumstances a “qualifying disclosure” is one, which satisfies the following three criteria as given below:

The disclosure should have been made in good faith;

If the disclosure is made in the reasonable belief that the information disclosed tends to reveal one or more of the following:

- (i) that a criminal offence has been, is being or is likely to be, committed;
- (ii) that there has been, is or is likely to be, a failure to comply with a legal obligation (that is a statutory or contractual requirement or a common law Obligation);
- (iii) that the health or safety of any individual has been, is being or is likely to be endangered;
- (iv) that the environment has been, is being or is likely to be damaged;
- (v) that information that shows one of the above has been / is being or is likely to be concealed.

The disclosure is generally made to one of the following:

- To the employer or to the person specified by the employer under any internal whistleblowing procedure and policy;
- Where such disclosure concerns the actions of a person other than the employer, that person;
- If the disclosure is made in the course of obtaining legal advice, a legal adviser. In this case, the requirement for good faith may not apply here;
- Where the employee additionally believes that the allegation and any information contained in the allegation is substantially true.

The USA Experience

In the United States, the Whistleblowers Protection Act, 1989 is in force and it ensures the protection of the employees who blew the whistle. It may be noted that one of the purposes of the Whistleblowers Protection Act, 1989 is to strengthen and improve protection for the rights of the federal employees, to prevent reprisals and to help eliminate wrong doing within the government by mandating that employees should not suffer adverse consequences as a result of prohibited “personnel practices”.

The Australian Experience

In Australia the Public Interest Disclosure Protection Act, 1994 is in force with similar objective of protecting the employees who blow the whistle. The Fitzgerald's Report and the Gibbs Committee Report led to the passing of the Public Interest Disclosure Protection Act, 1994, in Australia.

The New Zealand Experience

In New Zealand, they have passed a statute which is known as "The Protected Disclosure Act, 2000" with the similar objectives.

SEBI Regulations in our country (India)

The Securities & Exchange Board of India amended the Listing Agreement vide its circular SEBI Circular No. CFD/DIL/CG/1/2006/13/1 dated 13th January 2006 and consequent to this the stock exchanges have given effect to this circular in the Listing Agreement of Clause 49 on corporate governance. The clause 49 of the Listing Agreement now provides for the formulation of an internal policy which extends to any level of employment. (Suggested (model) Whistleblower policy and the Code of Conduct and Ethics Policy are appearing at the appropriate place of this article). Pursuant to this introduction by the stock exchanges in the Listing Agreement, any personnel who observes breach of any internal controls or company policy relating to financial malpractice or fraud, failure to comply with a legal obligation, criminal activity, improper conduct or unethical behavior, corruption and mal-administration and such other things should be able to approach the audit committee directly without going through the routine channel of reporting hierarchy. Whistleblower policy would also give protection to the whistleblowers from reprisals, which could be loss of employment, harassment in the workplace and financial issues etc.

The Clause 49 further states that the companies need to issue an annual certification affirming that the board members and the senior management had followed the code of conduct and ethics, obviously, arising out of this is that no one is denied to access the audit committee in respect of matters involving alleged misconduct as per the whistleblower policy and the company had also provided required protection to the whistleblowers.

Annual Certification by the Board members and the Senior Management

At the end of each financial year of the company, the board members and as well the senior management confirms in writing to the board of directors that they have understood the Code of Conduct and Ethics policy of the company and the code is applicable to their activities and they have complied with the code during the year and their conduct in future also would be in compliance with the code.

Annual certification disclosed by board members & Senior Executives

By and large the Board members and the senior members of the companies make the following annual certification to the board of directors of the company. The certification format might vary from company to company and this is not a mandated format by the regulator.

Code of Conduct & Ethics

The Company's Code of Conduct & Ethics, enclosed in the Annual Report, provides guidelines to be followed by Directors and all employees to ensure the highest standards of professional conduct. Members of the Board and senior management have affirmed compliance with the Code of Conduct & Ethics for the yearon behalf of themselves and to the extent that they are aware, on behalf of all employees reporting to them.

In summary the whistleblower policy is essential to serve

- To identify risk that the company may not know about at times
- To provide an opportunity to employees to speak out if they have concerns and
- To highlight if the individuals feels they cannot speak up internally, there are other routes available for them to speak.

FORMULATING THE WHILSTLEBLOWING POLICY DOCUMENT

Internal Whistleblowing Policy & Procedure Document

Essential features

The internal whistleblowing procedure could only be effective if the whistleblowing procedure enjoys confidence of its intended users and beneficiaries i.e., the employer and as well the employees. In reality, it should be of utmost importance that the employees shall have to have the confidence in the whistleblowing policy for which there has to be commitment from the most senior management of an organization and the employees need to have the confidence for which the commitment of the top management is of utmost importance. Unless there is a genuine commitment from the top management of an organization the whistleblowing policy cannot secure the confidence of the employees and securing the confidence of the employees is very critical if the whistleblowing procedure to be successful.

Applicability of the whistleblowing policy

Whistleblowing policy and procedure should be applicable not only to the board of directors and senior management but throughout organization across the board.

Consistency of the policy

The whistleblowing policy should be in consistent with other relevant policies which are prevalent in the organization i.e., employment contracts, model standing orders, business code of conduct and ethics, rules regarding hospitality - say acceptance of gifts, internal complaints readressel procedure and such other relevant policies of the company.

Support from the employees

The whistleblowing policy necessarily needs to have the support of the employees (employee's representative) of an organization. It is very much essential that the employees should feel that they are co-owners of the whistleblowing policy and procedure and the

employees should not look at it that the whistleblowing policy and procedure is something forcibly imposed upon them by the management. Perhaps, it could be a good idea if the whistleblowing policy is drafted with the active involvement of the employee's representatives and implementation is also agreed upon to ensure the active working of the whistleblowing policy and its procedure.

The whistleblowing policy document

The whistleblowing policy document should contain a clear-cut statement spelling out various aspects such as (i) policy introduction, (ii) scope of policy, (iii) safeguards, (iv) protection, (v) confidentiality, (vi) anonymous allegations and untrue/malicious/vexatious allegations, (vii) procedure for making a disclosure, (viii) protection Against Retaliation and (ix) reporting and the relevancy Contacts.

Introduction to the policy

Under this head, the organization should spell out its firm commitment for conducting its business and working with all stakeholders including employees, customers, suppliers, shareholders and business associates in a manner that is lawful and ethically responsible and in a way that reflects the company's values at all times. The organization should also spell out that the organization would not tolerate attitudes or activities that constitute a breach of law or trust or infringe collective or individual liberties in any way. Ideally the organization should have its Code of Conduct & Ethics policy and the code of ethics policy should also describe company's approach to its business. The organization may further spell out that the Whistleblower policy formalizes the organization's commitment to enabling employees and business associates to make fair and prompt disclosure of circumstances where it is genuinely believed that a part of the organization's business is engaged in inappropriate practices and that the Code of Conduct & Ethics is being violated. Then the policy could set out arrangements that encourage individuals to disclose violations of the Code of Conduct & Ethics, knowing that in so doing, they are acting in the best interests of all the stakeholders of the organization. Finally, the policy could give assurance and ensures that the whistleblower will be protected from retaliation and reprisal. The policy may also spell out that in the normal circumstance that the employees could raise their concern about a workplace situation with the employee's immediate line manager or if identified by a business associate, rose with the appropriate member of the organization's management team.

Scope of Policy

The whistleblowing policy could spell out the scope by stating that the policy is intended to cover any concerns, which are in the public interest. They could be (i) Breach of any internal controls or company policy relating to financial malpractice or fraud, (ii) failure to comply with a legal obligation, (iii) dangers to health and safety or the environment criminal activity, (iv) miscarriage of justice, improper conduct or unethical behavior, (v) violation of the company's Code of Conduct & Ethics (vi) attempts to conceal any of the above. The above is not a complete list and it is only an illustrative one. The policy also could state that

any matter raised under this policy would be considered seriously and the policy may also spell out that any matters of a purely operational nature should not be raised under this policy and the concerned employees should raise such matters through the usual organizational channels.

Safeguards

The policy document may elaborately spell out the safeguards relating to (i) Protection to the whistleblowers (ii) Confidentiality maintenance (iii) Anonymous Allegations and (iv) Untrue/Malicious/Vexatious Allegations.

Protection

Under the head of Protection the policy may state that the policy is designed to offer protection to those employees or business associates who disclose such concerns provided the disclosure is made in: (i) accordance with the procedures laid down (ii) good faith, and in (iii) the reasonable belief of the individual making the disclosure that malpractice has taken place.

Confidentiality

Under the head of confidentiality, the policy may spell out that the organization would treat all such disclosures in a sensitive manner and will endeavor to keep the identity of an individual making an allegation confidential. The policy may also state that the investigation process may inevitably reveal the source of the information and the individual making the disclosure may need to provide a statement which cannot be kept confidential in case of legal proceedings if arise.

Anonymous Allegations

The policy may also state that the policy would encourage the individuals to put their name to any disclosures they make.

Untrue/Malicious/Vexatious Allegations

Under this head, the policy could state that if an individual makes an allegation, which is not confirmed by subsequent investigation, and the investigation shows that an individual has made malicious or vexatious allegations for personal leverage, and particularly if he or she persists with making them, disciplinary action may be taken against the individual concerned. This would keep a control over the malicious / vexatious allegations being made

Procedure for Making a Disclosure

Under this head, the policy could state that the employees are entitled to make their disclosure in the first instance through their line manager, or if they feel it would be more appropriate to approach directly the Company Secretary, Managing Director, Audit Committee Chairman or the Chairman of the Board. The policy may also state that the mode of contact could be by phone, e-mail or in writing and should include as much detail and evidence as possible. The policy may spell out that upon receipt of the disclosure the matter will be

investigated immediately to ascertain all the facts and a recommendation made to the Board and the recommendation would include a revision to company policies and procedures to reduce the risk of a reoccurrence.

Smith Guidance on this

The Smith guidance of UK on Guidance on audit committees, regarding the whistle blowing, states that the audit committee should review arrangements by which staff of the company may, in confidence, raise concerns about possible improprieties in matters of financial reporting or other concerns and the audit committee's objective should be to ensure that arrangements are in place for the proportionate and independent investigation of such matters and for appropriate follow-up action.

Protection against Retaliation

Under this head the organization could be in a position to commit it to ensure that no retaliatory action, of any sort, would take place against any employee or business associate making a disclosure in good faith and this is very essential and important without which the policy cannot see the light of its success.

Reporting

Under this head, the policy may state that the reporting could be done to the designated people such as the managing director of the company, the Chairman of the Audit Committee or the Chairman of the Board and the Company Secretary and the policy also could state that these executives would be responsible for reporting any whistle blowing disclosures to the Audit Committee.

Contacts

Under this head, the relevant contacts could be provided in the following format: -

Person	Position	e-mail address	Telephone number
Name	Chairman – Audit Committee		
Name	Managing Director		
Name	Chairman of the board		
Name	Compliance officer (Company Secretary)		

Code of Conduct and Ethics Policy

Whistle blower policy refers that the organization is firmly committed to conducting its business and working with all stakeholders including employees, customers, suppliers, shareholders and business associates in a manner that is lawful and ethically responsible and in a way that reflects the company's values at all times and the organization would not tolerate attitudes or activities that constitute a breach of law or trust or infringe collective or individual liberties in any way and by and large this approach is described in the organization's Code of Conduct & Ethics policy.

Audit Committee Vs day-to-day management

It should be well understood that the audit committee members are not involved in the day-to-day management of the organization and therefore the audit committee members would not be close enough on an ongoing basis to the details of matters related the conduct of business and especially on matters relating to fraud and unethical activities in the organization.

Audit committee role on monitoring the whistleblowing policy

Since audit committee is not involved on day-to-day management, the members of audit committee could focus their attention usefully on the need for proper policies and procedures are set in place in the organization and it can help them to prevent any unethical practices, fraud and such other activities which is not in the best interest of the organization. It may be also worth noting or mentioning here that the mal practices what we are talking about is not necessarily relating only to and restricted to financial and accounting matters and it can surpass across the company in all functions. For example, it may relate to quality of the product the organization is manufacturing, safety of the employees of the organization and even safety of the public who are dealing with the organization, protection to environmental matters and anything which is in the nature of causing damage to the reputation of the organization. The whistleblowing mechanism is one such method by which the people who have concern over the issue could inform the audit committee and it is definitely not the only method.

Objectives of audit committee

The audit committee's objective could include that there appropriate arrangements are in place to enable employees to report, in confidence, the possible breach of any internal controls or company policy relating to financial malpractice or fraud, failure to comply with a legal obligation, dangers to health and safety or the environment, criminal activity, miscarriage of justice, improper conduct or unethical behavior, violation of the company's Code of Conduct & Ethics and attempts to conceal any of the above or such other related matters.

Needless to mention that the audit committee should have the basic understanding of the relevant provisions of the Clause 49 of the Listing Agreement relating to corporate governance, especially on whistleblower policy according to which, the protection from victimization and dismissal to individuals who make certain disclosures in the public interest and the committee should ensure this guarantee to the whistleblowers.

The responsibility of the audit committee

The audit committee being the ensurer of the adequate and transparent disclosure requirement in the financial reporting of the company is specifically charged with ensuring that the company has the necessary arrangement and system in place for the proportionate and independent investigation of any concerns about possible improprieties raised and that

appropriate follow up action is taken. The guidance note of Smith Guidance in this respect reads as under: -

"The audit committee should review arrangements by which staff may raise concerns about possible improprieties in matters of financial reporting or other Matters"

Smith Guidance

In short, Smith Guidance emphasizes the audit committee should ensure that appropriate whistleblowing policies and procedures are in place.

Rights of employees

By going through the UK provisions (Public Interest Disclosure Act of 1998), it is seen that the employee has the following rights. The employees who make a qualifying disclosure have the right not to suffer any detriment, which could be straightforward dismissal, dismissal under a cover of redundancy, bullying, demotion or failure to receive promotion because the employee made such a disclosure. If the employees do suffer detriment, employees have the right to submit a complaint to an employment tribunal. It is ultimately the tribunal who could decide on the matter having regards to facts and circumstances of the case whether the qualifying disclosure has been made and any appropriate remedy available for the employee.

Indian legislation on this

Although in India, there is no such specific legislation, the employee's rights are protected under the various labour laws and there is a highest body known as the Labour Tribunal where the matter could be referred under the employment contract for a wrongful dismissal including the one covered above.

For successful implementation, the policy should specify

For the successful implementation of the whistleblower policy, the policy should address and spell out the parameters so that the purpose of this policy would be served in the best interest of the organization. The policy must provide the assurance to the employees and this assurance should come in the form of commitment from the top management i.e., the board of directors and Chief Executive of the company

In Summary

Unless and until the collaborative approach between the employer and employee is not taken, the whistleblower policy may not serve its purpose and it is absolutely essential that the top management should be committed and at the same time, there should be a guarantee of no action of victimization. The employees could then report their concerns fearlessly. If the collaborative approach is not taken, the policy may be only a paper document and no construction action would come through and it would not serve any purpose.

Role of the Company Secretary with reference to whistle blowing mechanism

Formulating the whistleblower policy

The board of directors of any company is required to formulate the whistleblowing policy

document which is being implemented by the organization. In this process, the company secretary could contribute and play his role in preparation of well documented policy and aid the management to bring out the same. The company secretary could add value to the policy documents spelling out some of the best global practices.

Periodical review of while blowing policy

The audit committee is expected to carry out the review of the whistle blowing procedure on an ongoing basis and while carrying out such review, various aspects needs consideration. In the review process of the whistle blowing policy, the company secretary could aid the audit committee in the following aspects so that the review procedure by audit committee is more effective

Communication of the policy across the organization

The policy document i.e. the whistleblower policy is required to be communicated to all across the organization.

The company secretary could ensure this is done and he could give a feedback to audit committee to this effect. Many companies they put their policies in their internal server at a designated place, say "Policies and Guidelines" or Policies and Procedures or "Company Policies" etc.

Publication of the whistleblower policy in the annual report of the company

It would be a good idea, to publish the whistleblower policy in the annual report so that all stakeholders are aware of the policy of the organization on Whistle blowing and the company secretary, invariably who is taking care of the annual report preparation (other than financial) could ensure that this is done.

Policy is welcomed by all employees and accepted by all

The company secretary being the Liasoning official between the board and the senior management team / core management team, he could run a check on this as to whether the whistle blowing policy and procedure make it clear that it is safe at one end and also acceptable for employees to raise their concerns about wrongdoing/unethical behavior happening in the organization and provide the feedback to the audit committee.

While doing the above exercise, the company secretary could run a check on the following aspects with the senior management team:-

- (a) Whether the whistleblower policy and its procedures were discussed between the management and the employees through a consultative process and the employees have agreed upon for the same i.e., the moot question is – do employees buy - in to the whistle blowing process?
- (b) While discussing, were there any concern raised by the employees and if so, whether they were responded to within a reasonable time frame and the concerns raised were addressed.

Protection against victimization

While it is the responsibility of the audit committee to ensure that the whistleblower policy provides and ensures that all reasonable steps are being taken to prevent the victimization of genuine whistleblowers, nevertheless, the company secretary could bring the awareness with the senior management on this and he could aid and encourage the whistleblower to raise the unethical issues without any fear.

Company secretary being the bridge between the audit committee and senior management team, this aspect could be well be handled by the company secretary.

Encouragement to individuals with reference to disclosure etc.

By and large the anonymous and making allegations. Is not encouraged in any organization and hence the whistleblower policy should and must encourage individuals to put their name to any disclosure they make rather than remaining anonymous due to fear of victimization. Here the role of the company secretary is vital since he is within the organization and he could communicate freely with the people and provide moral support and ensure that the whistleblower mechanism really works well in the organization. However, it is up to the audit committee, upon examination to see whether the whistleblower raised issues of true or /malicious/vexatious allegations and take the matter forward further.

Confidentiality clause(s) of the employment contract

The company secretary could also ensure that the employment contract or appointment letter or any other contract of employment has a clause to the effect of maintaining confidentiality clause(s) in order to protect employer and as well employee.

Disclosure of information by the whistleblower

At the drafting stage itself, the company secretary could ensure that the whistleblower policy spells out the senior person to whom the confidential concerns can be disclosed and obviously one of them could be company secretary besides chairman of audit committee, managing director and chairman of the board. The company secretary could provide the e-mail address / telephone / mobile number of these senior personnel in the policy itself and the policy is also published in the annual report as discussed elsewhere in this article.

Authority to act whenever concern is raised

In consultation with the board of directors and audit committee, the company secretary could put a framework and system in place to the effect that, whether the identified senior person have the necessary authority and determination to act whenever the concerns are raised with – properly dealt with by the immediate line management – a procedure could be made and circulated to all so that timely action taken and the senior person has the necessary authority to do so with the delegated authority by the board.

Publication of success story(ies)

Here the company secretary could collect the success stories on this subject and periodically get them published in the in-house magazine / share the same through the

intranet server of the organization or even share through the mail which would obviously boost the morale of all employees across the organization.

Bringing awareness with the managers

The company secretary could organize periodical meetings or get-together with the managers since it is most important consideration that the managers understand well as how to act if the employees raise a concern and also the managers are aware and understand that employees have the right to blow the whistle in the interest of the organization.

Independent advice where required

Of course, whenever and wherever required the company secretary could advise the board members / audit committee members to use of an independent advice center as part of the whistle blowing procedures so that the smooth working whistle blowing mechanism is on in the organization

Conclusion

All said and done, ultimately the company secretary need to take the initiatives, work with the team in the organization and bring about the awareness with the employees and also liaison officer between the senior management team and the top management. Company secretary being the only person who is acting as a connector between the top management and other senior management in the organization, he is the right person to do better things and ensure successful implementation of the whistle blowing mechanism and bring high morale in the organization.

KEEP CONSCIENCE AWAKEN : BLOW WHISTLE

AISHWARYA MOHAN GAHRANA*

Every academic book in common law countries generally describes Company Secretary as a focal point for all stake holders of the business organisation. This layman portray always attracts me more than all legal text running in volumes.

Law gives legal status to Company Secretary but not business feasibility for the appointment of a Company Secretary in employment of an organisation. Business feasibility could be measured in term of value addition to the organisation not legal addition to the organisation. The value addition may be in form of increased profitability, wealth creation or confidence building among its stakeholders. Majority of stakeholders are not financial literate or at least financial expert. These stakeholders measure success not in financial terms but through confidence towards an organisation amongst them. They relate their interests with various factors related to an organisation. From investors to debtor, everyone read annual report of many companies and a good number of them just read name of directors and auditors. Unfortunately, most of them never bother to read name of Company Secretary or Secretarial Auditors. Reason is obvious; they do not connect their interests with this focal point; company secretary.

To reach the desired heights we need consistent efforts to transform ourselves from a clerk attached to board room to conscience keeper of the corporate India. The profession is in transition period. We have completed many stages; clerk, manager, general manager, decision maker, managerial personal, Key managerial personnel and next step the conscience keeper. This journey may not be reflecting in career graph of every member of this profession but profession is surely achieving this height. Every height we gain always stands on a solid foundation of a concrete mix customised for individual need. So we need to look into basic foundation of our profession. The litmus test to judge strength of basic foundation of any profession is not its education, crowd of its student, number of its members, this and that legal recognition, written ethical value codes and International codifications but confidence put by its real paymaster, the stakeholders.

Let me explain. When a mediocre company approached a big name accounting firm for becoming its auditors, I asked managing director why we should feed this white elephant when we are already under pressure to cut cost to save us from declaring our accounts as non performing assets. The reply was simple; from creditors to dealers, all (stakeholders) have more faith in that big name. If they hire someone to gain confidence of stakeholders,

* B.Sc., LL.B., A.I.I., FCS, Practising Company Secretary.

these stakeholders are real paymasters. Stakeholders have confidence in a person who protect or can protect their interest more than interest of promoters or someone in management. This confidence among stakeholders may vary from person to person but we should concentrate to attain new heights day by day for profession. We must ask ourselves, why our stakeholders do not bother even to read our name. Why stakeholders never approach the management or the government asking for appointment to this important position i.e. Company Secretary whenever it become vacant. Why stakeholders never ask that Company Secretary be appointed after thorough discussion in general meeting.

After reading volumes of legal text, we may safely presume that company secretary is to be appointed as a consultant to the board for all legal and ethical matters. With increasing awareness towards corporate governance and ethical business practices, stakeholders eagerly look for someone who could come forward to grab this opportunity and transform themselves to conscience keeper of the organization. Presently, company secretary is a person who has mandate to analyse non-financial information and reporting it after coordinating with all financial information. When, corporate reporting is being shifted from merely financial data sheet to overall reporting by putting equal weight to non-financial reporting, it is a big responsibility. Non-financial reporting is an art of understanding all material information, their impacts, need and extends of reporting. All this depend not only on training and calibre of person handling this assignment but much upon conscience of corporate to decide why, what, when and where to report.

Conscience

The conscience is not easy to define.

Conscience is defined as the last practical "judgment of reason which at the appropriate moment enjoins [a person] to do well and to avoid evil".¹

*There is a higher court than courts of justice and that is the court of conscce.
It supersedes all other courts.*

—Mahatma Gandhi

Conscience is an aptitude, faculty, intuition or judgment of the intellect that distinguishes right from wrong. Buddha links the positive aspect of conscience to a pure heart and a calm, well-directed mind: "when the mind is face to face with the Truth, a self-luminous spark of thought is revealed at the inner core of us and, by analogy, all reality."² Conscience manifests as unselfish love for all living beings which gradually intensifies and awakens the mind to a purer awareness.³ Conscience is not a power of the soul like the mind or the will, or a habit

1 Catechism of the Catholic Church – English translation (U.S.A., 2nd edition) (English translation of the Catechism of the Catholic Church: Modifications from the Editio Typica, copyright 1997, United States Catholic Conference, Inc. — Libreria Editrice Vaticana) (Glossary and Index Analyticus, copyright 2000, U.S. Catholic Conference, Inc.). ISBN 1-57455-110-8 paragraph 1778

2 Edward Conze. Buddhism: Its Essence and Development. Harper Torchbooks. New York. 1959 p. 162.

3 Lama Anagarika Govinda in Jeffery Paine (ed) Adventures with the Buddha: A Buddhism Reader. WW Norton. London. pp. 92–93.

like prudence, but an act of the mind to direct personal action. As a practical judgment, conscience is the conclusion of a moral syllogism whose major premise is an objective norm and whose minor premise is a particular case or situation to which the norm is applied. The judgment that results is binding.

In light all available definition of conscience, we need to define conscience of Corporate and to find its nerve centre in a corporate body. "Corporate Conscience" is a term widely used for Corporate Social Responsibility but we use it here in different manner. Corporate conscience is more than corporate governance and corporate social responsibility. In light of Buddhist teaching, corporate conscience reflects in fair treatment and growth for all stakeholders and society without leaning toward profit for a particular interest group. Simply, corporate conscience is a gradually intensifying way of corporate life which guide corporate governance and lead it to do business responsibly.

Corporate conscience depends upon fair treatment of all stakeholders and empowering them for better decision making by providing timely and quality information. This information flow generate with understanding of legal provisions and intention of ethical treatment to stakeholders. The company secretary has dual responsibility to protect all business interest while guiding management about what should be drafted. All stakeholders have trust on company secretary for protecting their interest by guiding management towards better disclosure of all material information. The company secretary being a key managerial person having knowledge of legal and ethical behaviour takes position of conscience keeper of the company. As a focal point for all stakeholders of organisation, company not only guide them but also face pressure from all of them. He is not at an ornamental position but have a duty of fair play. He practices and advises best practices of corporate governance and responsible business. He acquires the position of referee. A conscious referee could not be a toothless tiger. He has power within, power of love for stakeholders, the power of awaken mind, the power of truth, power to stand for his conscience and above all; power to stand for conscience of his organisation, humanity and all stakeholders. The conscience keeper is a fearless person. He can blow the whistle. This is his ultimate power to keep corporate conscience alive and everlasting.

The conscience keeper could be a whistle blower. The term whistle-blower comes from the whistle a referee uses to indicate an illegal or foul play. US civic activist Ralph Nader coined the phrase in the early 1970s to avoid the negative connotations found in other words such as "informers" and "snitches".⁴

A whistle blower is a person who tells the public or someone in authority about alleged dishonest or illegal activities (misconduct) occurring in a government department, a public or private organization, or a company. The alleged misconduct may be classified in many ways; for example, a violation of a law, rule, regulation and/or a direct threat to public interest, such as fraud, health/safety violations, and corruption. Whistleblowers may make their allegations internally or externally.

4 Nader, Petkas, and Blackwell, Whistleblowing (1972).

Persecution of whistleblowers has become a serious issue in many parts of the world. Although whistleblowers are often protected under law from employer retaliation, there have been many cases where punishment for whistle blowing has occurred, such as termination, suspension, demotion, wage garnishment, and/or harsh mistreatment by other employees. Many whistleblowers report there exist a widespread "shoot the messenger" mentality by corporations or government agencies accused of misconduct and in some cases whistleblowers have been subjected to criminal prosecution in reprisal for reporting wrongdoing.

As told earlier, the whistle blowing is an essence of conscience keeping. Here, blowing whistle does not mean shouting over the wall. A conscience keeper has duty to blow whistle whenever he find anything which is not as per standard of conscience. Conscience keeper simply pointed out wrong to stakeholders depending upon circumstances of the case. It may be through, denial of issuing a certificate, qualification of internal or external audit report or reporting to statutory authority like SEBI, RBI or SFIO etc. Essentially all auditors and consultants are whistle blowers for their respective field.

The company secretary is a focal point for all stakeholders of an organisation. All important decisions and communications passes through him. In majority of cases, company secretary has to give his opinion or has option to give his opinion. He has to draft minutes of various meetings, filing almost all forms, returns and documents with various authorities and bodies and have to draft various policies for organisation. Company Secretary is compliance officer.

As per para 13.11 of SEBI's Stock Exchange Model Bye Laws, 2003, "The compliance officer shall be responsible for submitting a report to the Exchange or Clearing Agency, as the case may be, with regard to compliance with each of the requirements set out herein below at such time and in such manner, as may be specified by SEBI or the Exchange or Clearing Agency, pointing out any non-compliance, delay in compliance or violation observed by him." Further, para 13.15 reads "Every company listed on the Exchange shall be required to notify to the Exchange the name, address, telephone numbers, fax numbers, e-mail address and such other particulars as may be required from time to time in relation to the compliance officer, who shall be a qualified Company Secretary and who shall be solely and fully responsible for the purpose of sending a report to the Exchange, for every calendar quarter, within such time as may be provided in the relevant Regulations from time to time, pointing out the violations, non-compliances or delays in compliance, specifically with respect to various requirements, as may be contained in the Listing Agreement entered into by the company with the Exchange or such other requirements, as may be advised by the Exchange to the company from time to time, with a view to safeguarding and protecting the interests of the investors and for ensuring market integrity and fairness in trading."⁵

Leading blog on Corporate Laws "IndiaCorpLaw" commented on SEBI's order dated 29 November 2011, in respect of Mr. G. Jayaraman in the matter of Satyam Computers Services Limited⁶ opine that "This approach seems to elevate the responsibilities of the compliance

5 <http://www.sebi.gov.in/bylaws/ch13.pdf>

6 http://www.sebi.gov.in/cms/sebi_data/attachdocs/1322550235791.pdf

officer under the internal codes of conduct of companies (on insider trading) to the next level than might have been previously thought. It also seems to suggest an independent and impartial role to be played by the compliance officer in a manner that is independent of the board. Allegiance of the compliance officer is not owed to the company or its board, but rather, it appears, indirectly to the regulator. While it signals SEBI's greater reliance on self-regulation as a method of enforcement, this is bound to raise some practical difficulties within companies' organisational structures and reporting lines.”⁷

IRDA in Para 12.4 of its Corporate Governance Guideline says “Each insurer should designate an officer as the Compliance officer whose duty will be to monitor continuing compliance with these guidelines.” IRDA in Para 13.2 of same Guideline says, “The appointed actuary and the statutory/internal auditors have the duty to ‘whistle blow’, i.e., to report in a timely manner to the IRDA if they are aware that the insurer has failed to take appropriate steps to rectify a matter which has a material adverse effect on its financial condition.”

Plain reading of all these regulatory provisions suggest that role of Compliance Officer is moving towards the role of Conscience keeper with whistle blowing as a tool in his hands.

When we want to protect corporate conscience, we should protect our conscience keeper, our whistle blower.⁸

7 <http://indiacorplaw.blogspot.in/2011/12/insider-trading-role-of-compliance.html>

8 http://www.irdaindia.org/Investment/corpo_gov_anx_2_050809.pdf

CONSCIENCE CENTRIC CS

CS NAYANA DAS*

Let noble thoughts come to us from everywhere - The Vedas

Sweet sounds of trinkets of wisdom, conscience and sense of pride fills the air when a Company Secretary(CS) forges forward backed by the high degree of trust stakeholders place on the responsible professional. Whistle blowing is to postmortem while conscience keeping is to the pre conception stage of an idea, action or decision. CS in India being christened by the high ideals of the Institute of Company Secretaries of India (ICSI), Law makers and faith of social forces has the onus to be conscience keeper at every stage of professional life. Only the role playing of a whistle blower does not suffice. The “inner voice” must rule. CS is envisioned and designed by the creators of the position with this spirit. The collective wisdom of the worshippers of goodness, godliness and prosperity sacrosanct with purity of hearts need to be chanted, internalized and followed. The professionals need to be puritanical to be seen at the highest place of honour if one is certain of following the religion of company secretary in the interest of our profession and the Nation. The “fire in the belly” may at times squeeze the CS into whistle blower oriented mindset, but meaningful growth happens when our moves are conscience centric. Conscience is what we are born with. It prevails if we have the “fire in the belly” to be conscience keepers. The two words “company” and “secretary” put together have an enormous synergetic effect. Based on the views of the ICSI, the role of CS may be sketched as:

- CS is an important professional aiding the efficient management of the corporate sector;
- CS is designated as an officer under the Companies Act;
- CS has to interact, coordinate, integrate and cooperate with various other functional heads in a company.

A member of the ICSI may also practice independently as a professional after obtaining a certificate of practice as provided in the Company Secretaries Act, 1980 and can be a dynamic professional in the corporate sector.

* ACS, B.Com. (H)(University of Delhi), Company Secretary, Assam Power Generation Corporation Limited, Guwahati. The views are personal views of the author and may not be perceived as view of the employer of the submitter of this paper.

ICSI's Vision is stated to be a global leader in promoting Good Corporate Governance and the mission of the ICSI is To develop the high caliber professionals facilitating good Corporate Governance.

Following these noble thoughts is understood to be the motto of every member and prospective members.

"It is with the heart that one sees rightly; what is essential is invisible to the eye."-ANTOINE DE SAINT-EXUPÉRY- The Little Prince.

The role of conscience keeper appeals more than the role of a compliance keeper in the light of the following observations of Pt. Jawaharlal Nehru :“India is a geographical and economic entity, a cultural unity amidst diversity, a bundle of contradictions held together by strong but invisible threads.” Our professional colleagues are reflections of their diverse geo-cultural roots, existing as economic centres, faced with “bundle of contradictions” but held together by the “strong invisible threads” of vision of our institute. In his Discovery of India, Pt. Nehru stated what John Stuart Mill wrote in his autobiography. It is; ‘I am now convinced that no great improvements in the lot of mankind are possible, until a great change takes place in the fundamental constitution of their modes of thought.’ Further, Pt. Nehru had stated that “And yet that fundamental change in the modes of thought itself comes from a changing environment and the pain and suffering that accompany life’s uneasing struggles. And so, though we may try to change those modes of thought directly, it is even more necessary to change the environment in which they grew and found sustenance. Each depends on and influences the other. There is an endless variety of men’s minds. Each one sees the truth in his own way and is often unable to appreciate another’s viewpoint. Out of this comes out conflict. Out of this interaction also a fuller and more integrated truth emerges.”

The relevance of those thoughts stands in professional dealings too.

India is a young nation. CS is a young profession. Youth is the best phase to forge ahead. Dynamism in innovative professional dealings backed by the “inner voice” has to exist.

The Whistle Blower may be a person who informs people in authority or the public that the organisation they work for is doing something wrong or illegal. Conscience is “the part of your mind that tells you whether your actions are right or wrong”, it also means “the fact of behaving in a way that you feel is right even though this may cause problems”. The Whistle blowing evolves from one’s conscience. However, for better governance and more effective discharge of corporate social responsibility, conscience should be an ingredient of all decisions, including the routine, everyday work of a professional.

After all, a professional is a person who does a job that needs special training and a high level of education and also means a person who has a lot of skill and experience. With education the mind evolves. An evolved mind has to act on conscience. It is said that a rose by any other name would smell as sweet. A conscience based professional is like a rose. Its perennial fragrance in the midst of bushy thorns is its hallmark.

“A voice of one calling in the desert,

.....

Make straight paths for him.

Every Valley shall be filled in,

Every mountain and hill made low.

The crooked roads shall become straight,

The rough ways smooth.....”

With due acknowledgement, the following from www.gita-society.com may be referred to while charting out value system wherein the professionals should be wedded into.

While Arjuna described the evils of war he had said:“.... when immorality prevails, O Krishna, people become corrupted”

“WHEN THE GOING GETS TOUGH, EVEN TOUGH ONES CAN GET DELUDED” which is reflected by what Lord Krishna had to say:

“How has the dejection come to you at this juncture? This is not fit for a person of noble mind and deeds. It is disgraceful, and it does not lead one to heaven,....” “Do not become a coward, O Arjuna; because it does not befit you. Shake off this trivial weakness of your heart and get up for the battle,”

It was noted that “ 'Dharma' may be defined as the eternal law governing, upholding, and supporting creation and the world order. It is the eternal relationship between the creator and His creatures. It also means way of life, doctrine, principle, prescribed duty, righteousness, right action, integrity, ideal conduct, custom, virtue, nature, essential quality, commandments, moral principles, spiritual truth, spirituality, spiritual values, and a function within the scriptural injunction or religion.”

It was further stated that the indestructible spirit transcends mind and speech.

“Some look upon this Spirit as a wonder, another describes it as wonderful, and others hear of it as a wonder. Even after hearing about it, very few people know what the Spirit is..... the Spirit that dwells in the body of all beings is eternally indestructible.”

The Spirit of good corporate citizenship should never be compromised by us, Company Secretaries.

“Treating pleasure and pain, gain and loss, and victory and defeat alike engage yourself in your duty. By doing your duty this way, you will not incur any sin.”

Lord Krishna said that even the violence done in the line of duty with a proper frame of mind, as discussed in the above verse, is sinless. This is the starting verse of the theory of KarmaYoga, the main theme of the Gita.

The wise should wholeheartedly welcome pleasure and pain, joy and sorrow, without

becoming discouraged..... Two types of people are happy in this world: Those who are completely ignorant and those who are truly wise. All others are unhappy...”

The National Campaign for People’s Right to Information (NCPRI), Inclusive Media for Change, Foundation for Media Professional and Accountability Initiative, held discussions to strengthen the Whistleblowers’ (Protection in Public Interest Disclosures) Bill, 2010, so as to protect those who speak up against wrong doings. Shri Vinod Mehta, former Editor-in-Chief of Outlook said that the law should be on the side of whistleblowers so they can be protected. It was also added that there is a sense of fear against speaking up. Highlighting the contribution of whistleblowers to media he had said that “Make the whistleblower a hero. The law should protect him and so should public opinion,” Another journalist added that whistleblowers should use the available digital technology to the fullest. It may be noted that Whistleblower Protection Bill as introduced in the Rajya Sabha in May this year defines a whistleblower as “any individual making public interest disclosure”. Further it was stated that the designated authority shall not entertain any anonymous complaints of any manner. Critics say that the Bill will benefit from a clearer definition of a whistleblower. Anonymous complaints can be scrutinised and stringent punishment for false complaints will discourage potential whistleblowers to come forward and make disclosures.

Further, a few lacunae in the Bill were also pointed out:

- A. regarding the sanctions against false complaints: complaints could be made in good faith but with poor information.
- B. there is no punishment for not acting on a complaint.
- C. also highlighted was the importance of giving the complainant the option of going to the media with the information and was observed that “Certain provisions can be built in”.
- D. matter of protection extended to family members of the whistleblower and to those who become witnesses in the case.

Further, NCPRI also suggested that the Bill be expanded to cover the private sector, especially agencies that enter into contracts with public authorities and public private partnerships. The shortcomings of the Grievance Redress Bill, 2011, perhaps need to be addressed too.

We professionals need to be wise in the truest senses of the term, in the risk infested, volatile circumstances, whenever our professionalism is challenged. After all, happiness with a sense of spirituality is what matters while we trudge our path while discharging our duties wholeheartedly. Whistle Blowing is preferred to silence; but professional role does not suffice with whistle blowing. We must act on our instincts, and prevent any wrong doing with all our knowledge, experience and integrity. Otherwise, we get minimized and smaller. To have the trust of stakeholders in our profession, we must chose to be heard, find the means to be taken seriously, stick to our conscience and do not remain only the corporate law custodians. Tendency to make their presence felt only after they discover the wrong must be nabbed. Whistle blowing should be the last resort when the actions by a conscience centric CS is

overcome or bulldozed. First, we must be the chief campaigner to an environment where conscience prevails and percolates throughout every level, everyone related. Whistle blowing is fine if all else fails. Secondly, a CS must evolve into a multi tasking professional. There are laws on Human Assets, Financial Assets, Safety, Security apart from Civil and Criminal jurisprudence. Tendency of human mind, mostly, is to outsmart the loopholes in them. CS must take charge of happenings under these heads too. Response from other subsets in the broader set of stakeholders may be lukewarm in the beginning, but firm and bold initiatives must make inroads. CS may be sidelined by other professionals managing those arena, but time has come to make greater strides and leap out of the cocoon of Company Laws only mindset. Authority has to be established in these areas, since a CS is responsible as a principal officer, as well as officer in default in many domains under Indian laws. It is sad indeed whenever the CS professionals are restricted to their role as an Officer whose position is created out of legal requirements and is not given the due responsibility backed by proper authority to be Corporate Governors, who can be the chief catalyst of a conscience centric corporate environment. Corporate architecture should not be filled with empty barrels of talks of Corporate Social Responsibility. They should be filled with canons of good thought, good actions and good vision. Bravery not slavery to rise above small thoughts and easy dealings must be encouraged. There should be initiatives to protect such conscience centric professionals. They should be nurtured in every step to stand up tall and lead.

Armed with the knowledge and guidelines on ethics vetted by our institute, the members can surely say:

“Jodi tor dak sune keu na ashe,

Tobe ekla cholo, ekla chalo, aekla chalo re,

Aikla cholo re.....”

“If no one answers your call, Then walk alone,

(be not afraid) walk alone my friend.”

“If no one talks to you,

O my unlucky friend, if no one speaks to you,

If everyone looks the other way and everyone is afraid,

Then bare your soul and let out what is in your mind,

(be not afraid) Speak alone my friend.”

“When dark clouds cover the sky, when darkness engulfs the truth,

When the world cowers and bows before fear,

You be the flame, The flame that burns you and banishes darkness from the world,

(be not afraid) Burn alone my friend.”

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PREVENTION, CURE OR INACTION ?

CS JAEE GOSWAMI*

'Olympus Corporation faces setback in the Court' reported Economic Times in its edition published on June 30, 2012. Olympus Corporation lost a court battle against an employee, Mr. Masaharu Hamada who sued the Japanese camera maker for retaliating against him after he complained about the unethical conduct of his boss.

Similarly in the GlaxoSmithKline case where company's improper marketing practices extended across a wide range of its prescription drug portfolio, the whistleblowers shared lot of invaluable insider information with the Government that led to a civil settlement in July, 2012.

The concept of whistle blowing evolved from the 'Qui Tam' philosophy. History finds the genesis of Qui Tam provisions in medieval England, during a time when no organized police force existed to enforce laws. English common law adopted various Qui Tam provisions in an attempt to provide for the enforcement of the law by those who suffered injury as a result of violations of the law. In effect, Qui Tam provisions allowed, and in fact encouraged private parties to act as policemen. The government paid a reward or bounty to the private party to make the effort worthwhile, and to give incentives to other individuals to bring similar suits.

Now-a-days many companies have whistleblower policies in place wherein a Compliance Officer is appointed. The employees are supposed to approach the Compliance Officer with their complaints. The Compliance Officer then takes up the matters with the management and the Board of the Company. By and large the first step of the whistleblower is to inform the malpractices through the internal communication system within the organisation.

However, there may be strong repercussions of this on a whistleblower. Many a time a feeling of mistrust is developed towards the employee. He may be subjected to resentment and hostility from the peers and superiors. At times pressure techniques may be used to suppress the employee by asking him to stay quiet putting his job at stake. Sometimes employees even lose their job in this process or even if they are retained they may face difficulty in future promotions or could face demotion.

Inspite of the consequences, in a few cases, like the ones reported above, the employee gathers courage to go further and make these problems public by approaching the media or

* Practising Company Secretary.

the authorities such as regulators or courts of law. Antagonising the whistleblower is certainly not healthy for the growth of the company.

Installation of a whistleblower policy and its execution is the responsibility of the Company Secretary in companies. The Company secretary is the Compliance Officer, the 'Ombudsman'. He/she is the one who ensures that best management practices and work ethics are followed towards wealth creation in the company. Merely installing the policy may not prove to be effective and hence may not give tangible results. The term 'execution' has a very wide scope. Whistleblowing should not be undertaken impulsively. The whistleblower must bear in mind that his/her action to blow the whistle will have dire consequences on the Company and its officers and therefore a strong moral justification must exist for blowing the whistle. This calls for training the executives, employees and trade unions on the various aspects of the policy so that the whistleblower is in a position to evaluate whether there is a situation to blow the whistle. The parameters for evaluation could be:

- Grave injustice or wrongdoing is occurring.
- Presence of reasonable evidence to support the complaint.
- Degree of intensity of the unethical practice or behaviour.
- Primary loyalty of the whistleblower is to the organization in which he/she is employed unless other compelling moral reasons override this loyalty.
- Presence of a prima-facie case where blowing the whistle will cause more good than harm to the Company.

The next pre-requisite for execution of the policy is the company culture. Such a policy cannot thrive in absence of a conducive culture where the employees are silent employees. The role of the Compliance Officer is further enhanced with the responsibility of promoting such organisational culture of mutual trust between the management and the employees in which individuals take the responsibility for communicating problems to management before those problems get out of hand.

What could be the modus operandi on receipt of a complaint? A whistleblower wanting to disclose certain unethical practices should not be shunned because:

- firstly he/she may be having a valid point towards the interest of the Company and its management;
- secondly if his/her complaint is not taken to the logical conclusion wherein he is satisfied that some disciplinary action to curb the unethical practices is taken, he may be tempted to divulge the information to outsiders.

This is a tough situation to handle because it not only tarnishes the image of the company but also may burden the company with stiff financial penalties by way of damages if the victim approaches the authorities.

In such situations the Company Secretary must act as a mediator between employees and the Board of Directors as far as unethical practices and its reporting are concerned.

When any employee approaches with a complaint of unethical practices being carried out within the Company, the Company Secretary as an ombudsman must intervene and, if satisfied of the merits of the case, put it before the management and the Board counselling them to keep a positive approach towards the complaint. The management and the Board must also take responsibility for honest investigation of allegations and for the proper treatment of informers. This will only help to win the faith of the employee towards the management and the Board of his/her company. In such a case the employee will willingly cooperate in the investigation process and will not be urged to make the matter public.

All in all the Company Secretary plays a crucial role in keeping the conscience of the Company and its management awake and guiding them to making correct and ethical decisions.

However, sometimes there may be situations wherein the top management of the Company is adamant and not paying heed to the views of the Compliance Officer. In such cases the Compliance Officer may not be in a position to act as a conscience keeper. Ethically and practically as well, it may be a wise decision to bring the information in the public domain. One cannot overlook the fact that the Company Secretary is accountable to instil and execute corporate governance and ethical practices in a company. Turning a blind eye and avoiding reporting the unethical practices may have serious repercussions on him/her. He/she may be made responsible for the wrongdoings by government officials and consequent charges may follow. Additionally, it will taint his/her image.

Having said this, one cannot forget the fact that there are no stringent laws for the protection of whistleblowers in India and corporate terrorism against honest employees is on the rise. A genuine whistleblower may be threatened and terrorised by the company management to keep silent on voicing his/her concerns at the cost of his/her career, job, family, and their lives, etc. There have been a number of whistleblower cases in India where the whistleblower was almost compelled to go further and make the information public due to failure of the internal reporting system to combat the unethical practices.

With this background, it is imperative and urgent to have laws protecting whistleblowers in India. The Whistleblowers' Protection Bill, 2011 passed in the Lok Sabha is awaiting clearance in the Rajya Sabha. The United States of America already has several such laws – The False Claims Act (revised in 1986), Lloyd – La Follette Act, 1912, Dodd – Frank Wall Street Reform and Consumer Protection Act, 2010 and such others. These laws even promise a certain percentage of the money recovered or the damages to the whistleblower. The United Kingdom and Australia also have legislations in place for protection of whistleblowers.

Unless stringent laws are enforced the future of genuine whistleblowers is rather bleak. Absence of conducive corporate culture and protection laws for whistleblowers will only discourage the process of good corporate governance.

Legislation combined with right attitude of the company management will take the process of whistleblowing further. Having a plan for handling whistleblowing situations is a way of making sure that managers make the right decisions even under the inevitable pressure of

ensuing crises. Essentially, the success of whistleblowing to a very large extent depends on the receptivity of the top management and the good spirit with which its executives deal with the disclosures of whistleblowing to the advantage of the organization.

Whistleblowing is not a career in itself. Most of the business dealings are genuine and above-board. However when one stumbles across some wrong-doing, a dilemma arises. Unlike a traffic cop who hides behind a kiosk and then traps those who jump the signal, a Company Secretary should try to prevent a wrong act rather than allowing it to take place and then blowing a whistle.

WHISTLE BLOWING – AN IMPORTANT ASPECT IN CORPORATE GOVERNANCE AND ROLE OF COMPANY SECRETARY AS EFFECTIVE WHISTLE BLOWER

CS SHILPI THAPAR*

“You need the freedom of Association. You need the freedom of Information.

You need the freedom to challenge and to monitor Government and other Officials. Without that kind of Society, Democracy becomes a Ritual.” - Frene Ginwala.

Corporate Governance

As per The Institute of Company Secretaries of India (ICSI), Corporate Governance is defined as “The application of best management practices, compliances of law in letter and spirit and adherence to ethical standards for effective management and distribution of wealth and discharge of social responsibility for sustainable development of all stakeholders.”

The main objective of Corporate Governance policies and practices should be wealth creation, wealth management and wealth sharing. Adherence to laws and regulations, financial goals and communications with stakeholders are major factors that make up the way in which corporations is governed.

Frits Bolkestein, the European Union’s internal market Commissioner highlighted some of the wider impacts of corporate governance in a speech. “Economies only work if companies are run efficiently and transparently. We have seen vividly what happens if they are not- Investment and jobs will be lost and in the worst cases –of which there are too many- Shareholders, employees, creditors and the public are ripped off.”

The financial meltdowns of Enron, Tyco, AIG, WorldCom, and Xerox have increased the concerns about corporate governance, which is system of regulations and policies to hold corporate leaders accountable and protect company stakeholders.

The most important feature of ICSI definition on Corporate Governance as discussed above is that corporate governance practices should be adhered to in letter and spirit. It is high time for companies to embrace the spirit of the corporate governance practices rather than settle for the chore of compliances.

Hence, to create, manage, share the wealth, only an inclusive approach to corporate governance can sustain. For this inclusive approach, the model of corporate governance should

* Practising Company Secretary, Ahmedabad.

be such that it promotes the interest of all the stakeholders, namely the employees, customers, shareholders, investors, creditors, the community at large.

According to me, the top five mechanisms, which are vital for implementing better and effective Corporate Governance in any organisation, are:

1. Independence of Board
2. Role of Auditors (Internal and Statutory) and Audit Committee
3. Whistle Blowing
4. Shareholder Activism
5. Fast Track Redressal Forums and Independent compliant mechanisms.

Any code on corporate governance can only provide the framework or structure to ensure that companies are governed to the best interest of stakeholders at large.

Whistle Blowing- An Indispensable Tool of ensuring good Corporate Governance Practices in Spirit

A very famous quote by Edward Thurlow (1731-1806):

“Did you ever expect a corporation to have a conscience, when it has no soul to be damned, and no body to be kicked ?”

The above quote describes that corporations have neither bodies to be punished nor souls to be condemned, they there fore do as they like.

Whistle blowing is relevant and plays a critical role in implementing Corporate Governance Practices. This was evident when Sherron Watkins blew the whistle on Enron’s Management in the U.S and when Harry Templeton challenged Robert Maxwell’s prowl of the pension fund, better known as the “Maxwell Saga” in the U.K. Our society has become so entrenched in doing wrong that corruption and violation has become the inherent part of the public and private life of the society. This issue is to be tackled by adopting best approach, which encourages and requires corporate to set up channels for blowing the whistle.

What is Whistle Blowing ?

In common Parlance, it is speaking out on Malpractices, Corruption, Misconduct or Mismanagement. Whistle Blowing can be defined in a number of ways. In its simplest form, whistle blowing involves the act of reporting wrongdoing within an organisation to internal and external parties. It is raising a concern about malpractices within an organisation or through an independent structure associated with it.

Mathews (1987:40) defines whistle blowing as the act by an individual who believes that the interest of the public overrides the interest of the organisation he or she serves. The act of whistle blowing can have an extraordinary influence on the organisation, on society and on the whistle blower.

The Association of Certified Fraud Examiner’s 2012 “Report to the Nation on occupational

Fraud and Abuse “pointed out that more than \$ 3.5 trillion in annual losses is attributed to fraud.

The scenario of whistle blowing is very complicated in India. References of whistle blowing and whistle blowers is made in various committee reports (for e.g. : in 1998 by CII Code of Corporate Governance, in 1999 by Kumar Mangalam Birla Committee, in 2002 by Naresh Chandra Committee and in 2003 by N.R Narayana Murthy Committee), listing agreement and Voluntary Guidelines of Corporate Governance . There is Whistle blower Protection Laws in US, UK, Norway but in India, awareness is yet to come.

Developing an Effective Whistle Blower Policy

All business entities often struggle with an appropriate level of segregation of duties making a whistle blower policy a good mitigating tool. The Whistle blower policies effective implementations not only reduce the fraudulent activities but also send a signal to both internal and external agencies that organisations exercises good corporate governance.

The Whistle Blower Policy may be drafted and implemented by management but it should be submitted to Audit Committee and Board of Directors. The foundation of Whistle Blower Policy is a clear and specific definition of Whistle Blowing. The key aspects are:

1. Clear definition of individuals covered by the Policy
2. Non retaliation provisions
3. Confidentiality
4. Process
5. Communication

The Whistle Blower Policy should include the methods to encourage employees, vendors, customers and shareholders to report evidence of fraudulent activities. It should properly address the processes that the employees should follow in filing their claims. Specific Reporting Mechanisms within the process could include telephone, emails, hotlines, websites or suggestion boxes. The first steps of creating an environment where a whistleblower will report problems that exist is the crucial one, to be fully effective whistle blower policy must be consistently implemented, claims investigated and evaluated and proper enforcement taken when necessary. Clause 49 of the Listing Agreement keeps whistle blowing as non-mandatory item but it should be mandatory.

Company Secretaries – Effective Whistle Blowers

A very famous quote by Napoleon:

“The World suffers a lot not because of the violence of bad people but because of the silence of good people.”

Economic Volatility, Global Competition, Growth risk appetite demands the governance professionals, the Company Secretaries to prioritise their role as whistle blowers.

Employees are usually the first to witness dangers and wrongdoings on Job. Although most employees remain silent, many chase to speak out and bear witness in corporate crimes that has not been addressed when flagged through normal company channels i.e Corporate Security, Audits, Inspections, Law enforcement combined.

Company Secretaries rank among the most productive, valued and committed members of their organisations. As they are the part of Top management and Board of Directors, they have a strong conscience; they are committed to formal goals of their organisation and have strong sense of professional responsibility.

Company Secretaries is also Corporate Governance Officer (CGO) and required to perform following roles:

1. To ensure the effective running of the activities of the Board and its Committees.
2. To ensure compliances of all listing rules, other Regulatory Codes and Acts.
3. Keep under review all legal and regulatory developments affecting the company operations and make sure that directors and management are properly informed of the same.
4. Manage relations with all stakeholders with regard to Corporate Governance, Corporate Social Responsibility, etc.
5. Work with Board of Directors, Management to ensure that all regulatory reporting is correct and does not lead to errors resulting in offences under Various Acts.
6. Act as the Conscience Keeper of the Company.
7. Act as the Primary point of contact for Board of Directors and source of guidance in order to assist their decision making process.
8. To assess, manage the compliances in the governance domain, governance processes, tracking of outcomes of governance processes and disseminate the information and documents for proper governance.

In ensuring implementation of proper corporate governance practices in the organisation, Company Secretary requires Governance Management and Reporting which includes:-

1. Development of Board framework and to determine the level of Independence
2. Monitoring and reporting on the Independence of Audit Committee
3. Development and Maintenance of a Board Charter to ensure that Board decisions can be measured against it
4. Acting as Board voice for providing shareholders feedback
5. Participating in Strategic Planning process, Risk Management process, Internal Control process, MIS, Corporate Communications, Succession Planning, Board performance evaluation process.

In light of above, Company Secretary acts in the capacity that ensures high level corporate administration in accordance with best governance practices which results to well run, governed and sustainable business for the benefit of its stakeholders at large.

Company Secretary can be useful aid to implement whistle blowing as an internal regulator for ensuring good corporate governance in spirits. As he is a part of Board decisions process and recipient of all important information flowing in the organisation, he can easily smell the rat. He can suspect the improper activities/unethical practices adopted by organisations or some of its members.

Some of the instances of unethical practices/improper activities adopted by certain organisations, which is required to be reported or for which whistle should be blown are:

1. Theft
2. Harassment
3. Unethical practices
4. Fraud
5. Dishonesty
6. Discrimination
7. Lack of Independence of Board/Committees
8. Improper Director Remuneration Packages
9. Lack of Independence of Auditors
10. Violation of Regulations and Code of Conduct
11. Insider Trading
12. Corruption
13. Bribery
14. Lack of Work Place Safety Hazards
15. Financial Statement Misrepresentation
16. Lack of Proper Internal Controls.

He can also support the ombudsman function with the Board by establishing a symbiotic relationship between the governance and compliance. According to the Association of Certified Fraud Examiners 2010 Report to the Nations on Occupational Fraud and Abuse, 40 percent of fraud cases studied in public companies were detected by tips- three times as many as by any other method. The presence of hotlines i.e may be Audit Committee Chairman or Ombudsman greatly facilitated tip reporting.

Company Secretary can adopt internal or external whistle blowing system. He can make his allegations internally to other people or committees i.e. Chairperson of Audit Committee or any hotline developed by company or can make allegations to external agencies like regulators, law enforcement agencies, media, etc.

Before Reporting or Whistle Blowing, Company Secretary should consider following factors:

1. Whether he has enough facts and evidences to support his allegations?
2. Under which situation and circumstances, he should opt for Whistle Blowing?
3. Whether there is any other mechanism or channel other than whistle blowing for reporting and which system should be opted to blow whistle, Internal or External?
4. What Protections the Company or law will provide for whistle blowing and whether there are any chances of success?
5. Whether any actions or investigations will be initiated after whistle blowing i.e. whether management or regulators will positively participate?

Practical Challenges for Company Secretary as Whistle Blower

Company Secretary as key recipient of almost all information can face reprisal, sometimes at the hands of the organisation or group, which he accused, sometimes under law. There is often a fear of losing their relationship at work or outside work. They may get punished, terminated, suspended or at risk of their own well beings. Few instances where whistleblowers have to face harsh consequences to the extent of losing their life:

1. The Satyendra Dubey Fate (2003),
2. Majunath Shanmugham Incident (2005), and
3. Most recent case of sudden demise of colleague CS Shasheendran (2011).

Hence, in order to encourage whistle blowing as an indispensable ingredient for ensuring good corporate governance in spirit, proper law should be enacted in India which should provides rewards and protection to whistle blowers similar to which is prevalent in USA under Dodd –Frank Whistle Blower rules. Organisations should protect, compensate whistle blowers, proper mechanisms should be set up, and identity of whistle blowers should be protected. Whistle blowing should be made mandatory requirement under Listing Agreement and even disclosures on corporate fraud risks should be made mandatory by Directors in Directors Responsibility Statement annually. Under US Corporate Governance law, Sarbanes-Oxley Act, 2002 has made it criminal offence, which is punishable by fine and up to 10 years in prison, for taking any action harmful to a person who provides truthful information about a federal offence to a law enforcement officer. There should be strict rules for hiding identity of Whistle Blowers, Ombudsman should be appointed by the company for dealing with such allegations who will directly report to Shareholders, Contentions of frivolous complaints should be taken care by imposing heavy penalties on malicious complaints.

Conclusion

Today with Scandals like Satyam, Tyco, AIG, Enron, Worldcom, zerox, need for more ethical governance has arisen. Whistle blowing has already been described as one of the basic tenets of Corporate Governance, but in India, there is no definite Whistle Blower laws. If this tool of

Corporate Governance is used in true letter and spirit, it can be saviour for protecting the stakeholders and the larger public interest. It can be success factor for survival of corporates, build their brand image, which will support in raising funds. It can be effective tool in curbing and reporting corporate frauds, which earlier used to go unreported.

As it is always said, norms of Corporate Governance are not merely to be complied with but have to be adopted as day-to-day practice of any organisation. Hence, Corporate Governance is a mixture of meeting both the letter and spirit of law. It is high time India Inc, which is an emerging economic powerhouse, to strive to raise the standards of Corporate Governance Practices to Global Benchmark.

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INDIAN FINANCIAL MARKETS — A POWERFUL GROWTH ENGINE

SURESH THAKUR DESAI*

The World Bank has projected India as one of the five countries poised to become large emerging market economies in the world. A World Bank study suggests that the share of these five biggest emerging markets in world output will double to 16.1% in 2020 from 7.8% in 1992. India being one of the largest and fastest growing emerging economies is slated to become the fifth largest consumer economy with aggregate consumption reaching US\$ 1.53 trillion in 2025. Rapid expansion of the banking sector and financial markets will underpin and support this growth trajectory.

Indian banking sector has expanded rapidly during the last two decades. Though large it has enormous potential for further growth on the back of unbanked population, growing activity in financial markets, expanding foreign trade and high rate of economic growth. As only 40% of the population enjoys access to banking services, the residual large un-banked population presents huge opportunities and challenges. Growing banking activity is also experienced due to privatization of banking sector and consolidation and entry of foreign banks. Financial inclusion of unbanked population, small and medium industries, new entrepreneurs in a variety of sectors will boost activity in financial markets for coming decades. Use of newer technologies will lubricate this process and hasten its expansion. Financial sector reforms will provide a shot in arm to sustain this growth momentum.

This paper deals with various issues that affect the stimulation and growth of financial markets in India. Major among them are the process of financial inclusion which can integrate the financial markets over the entire country, infrastructure financing which can unleash the hidden potential of the economy and propel the growth in a variety of sectors, capital and commodity market reforms which can boost industrial and agricultural growth. The paper concludes by suggesting a cohesive approach to various segments of financial markets to sustain the growth of Indian economy.

In India, the growth of the financial markets is largely influenced by the banking sector. The global banking landscape is changing rapidly, and our domestic banking system needs to gear up in order to keep pace with its global counterparts. To sustain itself amidst fierce competition, the Indian banking industry needs to undergo transformation from a strategic viewpoint, focusing on aspects of scale, scope, prudence and knowledge. These focus areas

* FCS

in turn, should be targeted to bolster productivity, efficiency and profitability, with the aid of customized technology.

Financial Inclusion

Financial inclusion is a process which ensures ease of access, availability and usage of financial services by the under-privileged and excluded section of society at an affordable cost. The drive for financial inclusion needs to be tempered with an equal measure of financial literacy which includes awareness and knowledge of the target group (low income group) to make decision on savings, borrowings and some planning for future income.

Statistics indicate that in India, there exists a large un-banked population with only around 40% having access to banking services. Another set of statistics indicate, that only 37% of bank branches of Scheduled Commercial Banks are present in rural areas, with only around 40% of the population holding bank accounts. Moreover, out of the 600,000 habitations in the country, only about 30,000 have a commercial bank branch. These statistics clearly emphasise the need for people to get connected with the banking system. Increasing penetration in un-banked areas is a key challenge for the banking industry and currently, all efforts are being concentrated in this direction.

RBI initiatives for inclusive growth

It has been RBI's endeavour to remove all hurdles in the way of its regulated entities in achieving financial inclusion objectives. Some of the salient measures undertaken in this regard are:

1. *Introduction of new products*

- *Opening of 'No-Frills' accounts (introduced as per RBI directive in 2005) :* A 'No Frills' account is one for which no minimum balance is insisted upon and for which there are no service charges for not maintaining the minimum balance. Small Over Drafts are also provided in these accounts.
- *General Credit Cards (GCC)/Kisan Credit Cards (KCC) :* GCCs/KCCs help purvey credit in the nature of a revolving credit entitling the holder to withdraw upto the limit sanctioned based on the assessment of household cash flows without insistence on security or purpose. Interest rate on the facility is completely deregulated.

2. *Relaxed regulatory requirements*

- *Relaxed regulatory dispensation on Know Your Customer (KYC) norms :* KYC requirements for small accounts were relaxed in 2005 by stipulating that introduction by an account holder, who has been subjected to full KYC drill, would suffice for opening such accounts, or, that the bank can take any evidence to its satisfaction as to the identity and address of the customer. Further, it is stipulated that job card issued by NREGA duly signed by an officer of the State Government or the letters issued by the Unique Identification Authority of India containing details of name, address and AADHAAR number would be a valid identity proof.

- **Simplified branch authorisation:** To increase the reach of banking network, domestic scheduled commercial banks have been permitted to freely open branches in Tier 2 to Tier 6 centres (with population of less than 1,00,000) under general permission, subject to reporting. Further, domestic scheduled commercial banks have also been permitted to open branches in rural, semi urban and urban centres in the North Eastern States and Sikkim, without the need to take permission from RBI.
3. **Road map for providing banking services in unbanked villages with a population of more than 2,000 :** Banks were advised to draw up a road map to provide banking services in every unbanked village having a population of over 2,000 by March 2012. Such banking services need not necessarily be extended through a bricks and mortar branch, but could also be provided through any of the various forms of ICT-based models. About 73,000 such unbanked villages were identified and allotted to various banks through state-level bankers' committees.
 4. **Financial inclusion plans of banks for three years :** RBI advised all public and private sector banks to submit a board-approved, three-year financial inclusion plan (FIP) starting April 2010. These plans broadly include self-set targets in respect of rural bricks and mortar branches opened; BCs employed; coverage of unbanked villages with a population above 2,000 as also other unbanked villages with population below 2,000 through branches; BCs and other modes; no-frills accounts opened, including through BC-ICT; KCCs and GCCs issued; and other specific products designed by them to cater to the financially excluded segments. Banks were advised to integrate board-approved FIPs with their business plans and to include the criteria on financial inclusion as a parameter in the performance evaluation of their staff.
 5. **Special Dispensation scheme for opening of branches in NER :** To improve banking penetration in hitherto unbanked North-East region, the Reserve Bank asked the State Governments and banks to identify centres where there is a need for setting up either full-fledged branches or those offering forex facilities, handling government business or meeting currency requirements. It has also offered to fund the capital and running costs for five years, provided the State Government concerned is willing to make available the premises and put in place appropriate security arrangements.
 6. **Measures specific to UCBs:** UCBs have been advised to step up their financial inclusion efforts by utilizing appropriate technology. Certain other measures such as enhancing maximum limits on unsecured loans and advances, revising credit limits permitted for individual housing loans, extension of area of operations for UCBs, permitting lending to SHGs and JLGs and permitting the use of BCs have been undertaken to further the financial inclusion drive.

Key challenges in financial inclusion drive

- **Coverage** - The huge population of India makes it cumbersome for any program to be completely inclusive. Especially in the case of migrant labour, money flows freely through unorganized channels, making it difficult to keep an account.

- *Infrastructure* – Infrastructure development in India has not kept pace with the economic growth in the country and lags behind to a great extent. It is essential to develop road, rail, digital connectivity and adequate power and infrastructure facilities which are important prerequisites for operation of a banking outlet.
- *Financial Products* – Simplicity and flexibility of products are two basic constituents of financial products. These products should suit the requirements of the masses and be made available at affordable costs.
- *Technology* – Integrating technology in the banking system is essential to move a step closer to inclusive growth. The technology solutions offered, should be standardised, interoperable and cost effective. There is a high transaction cost associated with providing banking services in the rural areas. Technology, if used appropriately can help in reducing the cost of transactions by a considerable extent.

To overcome the obstacles to inclusive growth, efforts need to be channelised to identify an appropriate delivery or business model for financial inclusion. The traditional brick and mortar bank branches may not be a viable option for many of the villages, specially those situated in remote areas. Banks need to adopt a slow and tedious process of experimenting with all options of delivery models like satellite branches, mobile branches, business correspondents (BC), and mobile services.

Until now, the BC model has been observed as a strong facilitator, but their functioning needs to be scaled up considerably to prove effective in the long run. The Working Group appointed by the Reserve Bank to review the BC model has recommended new entities that could be appointed as BCs. Coupled with Information and Communication Technologies (ICT) solutions, this delivery model has the potential to reach out to the un-banked areas.

Regulatory Intervention as part of Financial Inclusion, is required to foster Inclusive growth. To make financial inclusion a reality, a strong regulatory framework is necessary to bring in financial stability, which can act as an enabler for this initiative. To aid financial intermediaries in delivering their services effectively to the low income group segment of the population, technology needs to be leveraged with economies of scale. Regulation of these entities succeeds in instilling confidence in lenders and investors, in bringing in more organized funding.

- The success of credit unions and community banks across the world have succeeded in providing financial services to local communities, suggesting that smaller regional banks could be an ideal solution for financial inclusion. However, India's experience with local entities such as cooperative banks, deposit taking NBFCs and regional rural banks reflect poor governance, connected lending, geographic concentration indicating vulnerability to downturns.

The finance minister in his Union budget announced that RBI will consider giving additional banking licenses to private sector players and NBFCs. This has been proposed with a view to increase geographical coverage, moving a step closer to financial inclusion. In addition, granting of new licenses will give a boost to competition, resulting in reduced costs and improved efficiency.

A draft discussion paper has been released by RBI to that effect, discussing the various criteria enlisting their pros and cons. Currently, RBI is holding discussions with various industry bodies to get feedback to the various options, mentioned in the said paper.

Some of the more important criteria which the RBI will be keeping in view would be:

- Business model for new banks
- Eligibility of industrial houses to promote banks
- Conversion to NBFCs to banks or NBFCs to promote a bank
- Cap on foreign shareholding
- *Promoting financial literacy* - Use of creative adult learning techniques, and adequate investment in literacy programs to benefit the target group and the service providers.
- *Structure of MFIs (having shown very high growth rates)* – MFIs need a proper product design and model. They need to be well equipped with information on various products to pass it on to the target group. Also, in order to sustain MFIs and achieve the desired objective, accountability and credibility needs to be wedged.
- *Regulate and monitor the SHGs (very good reach to the ultimate borrower)* – There is a need to measure and monitor the performance of SHGs. Regulation of these intermediaries will place inclusive growth on a better footing.
- *Technology support* – Inclusive growth cannot be achieved without the required technology support. The advent of mobile technology is being leveraged to reach out to the under-banked and the un-banked population.
- *Product offerings* – The product portfolio needs to be customized to cater to the requirements of the target group. Complex products needs to be avoided and offerings should be designed keeping in mind transparency, simplicity and flexibility. Credit products should be given priority over other products like insurance and savings.

A well designed business model needs to be devised, in order to sustain a cost-effective delivery model for penetration in the rural areas. Banks need to refine and review their delivery models to ensure greater operating efficiency.

A well-developed financial system skewed towards banking inclusion plays an important role in economic development. Therefore, there is a need to develop a financial inclusion index, which will help evaluate the degree of achievement towards inclusive growth.

In a study done by the Indian Council for Research on International Economic Relations (ICRIER), in 2008, India ranked 50 in the index of financial inclusion. Referring to India, the ICRIER study said that although there was a low density of bank branches, the usage of banking system in terms of volume of credit and deposit seems to be.

Infrastructure Financing

The Economic Survey 2011-12 said delay in infrastructure projects may affect

competitiveness of the economy in long run and called for and "new models of financing" the sector whose funding requirement in the 12th Plan is estimated at around \$ 1 billion whereas there is an expected gap of 30% in financing infrastructure projects.

Currently, India spends only 6% of its GDP on provision of infrastructure, as compared to China which spends as much as 20% on infrastructure development. The sector has also suffered due to a time lag in the physical capacity creation and time overruns. Infrastructure project developers are lapping up credit, and banks are focusing on this category of borrowers to enhance their balance sheets. However, there is a risk of exposure attached to banks with such long term financing considering the mismatches from an Asset-Liability Management perspective.

Prudential norms have been relaxed by RBI for infrastructure projects, but RBI is circumspect to allow further relaxations in exposure norms. It is important to note that infrastructure finance requirements cannot be met solely by banks and consequently, this sector needs long term finance support from insurance companies and pension funds.

Most of the infrastructure projects are financed by the government, but the role of the private sector has become increasingly important in enhancing the flow of funds and improving efficiency. It is necessary to create conducive environment for private sector participation with a transparent and credible regulatory mechanism for financing the infrastructure projects, so that to reduce the pressure on public-sector funding. However, as the returns attached to these projects are low, and carrying multiple risks and uncertainty, there arises a need to incentivise private investment.

Some of the sectors like irrigation, water supply, electricity and gas are the specific cases where user charges need to be defined and contract enforcement mechanisms need to be strengthened further, to ensure an uninterrupted flow of investments from private sources.

The Road ahead for Infrastructure financing

Some of the ways in which the deficit in financing can be bridged are as follows:

- Participation from pension funds and insurance companies
- Pivotal Role of the private sector to bridge the gap between demand and supply
- Strengthen the corporate bond market

The Deepak Parekh Committee on India Infrastructure Debt Fund (IIDF) has given certain recommendations towards regulatory changes to permit foreign insurance and pension funds to invest in the proposed IIDF. The committee proposes that the IIDF be set up and managed as a trust, with an initial corpus of Rs 50,000 crore, approved and regulated by SEBI. These recommendations follow from similar practices followed in the US.

Long way to go

As indicated above, while India has made enormous strides towards greater financial inclusion, there is a long way to go. About 500,000 villages are yet to be provided with banking services.

In a networked India in which banking services are extended to all villages, ultimately, a so-called model will emerge where customers will have the option to transact with the bank of their choice in any village by using UID (unique identity)-enabled micro-ATMs (automated teller machines), thereby reducing the dependence on cash and lowering transaction costs. The task is gigantic, but definitely achievable by following a systematic approach.

Indian Capital Markets

Capital markets in any country play a pivotal role in the growth of economy and meeting the country's socio-economic goals. Just to give some perspective, it is estimated that India will require capital flows of USD 500 billion merely for developing its infrastructure.

As per latest available statistics of 2009-2010, the Indian economy's current size was approximately USD 1 trillion with the savings rate of 33.4% by Indian households. In the next decade or so, it is expected that the economy will grow at an average rate of 8%. This translates into incremental savings of USD 5 trillion over the next decade. Comparatively, the US economy's size was around USD 13.22 trillion in 2010. Assuming a savings rate of 5%, it may not be a surprise if the amount of savings of Indian households exceeds savings of US households in absolute terms by 2020.

Indian households have traditionally preferred safety of bank deposits and government saving schemes and much less than 10% of their investments in financial assets are in shares, debentures and mutual funds, which is very low as compared to some of the developed economies. Given the quantum of savings, the need to mobilise savings into productive channels and the opportunity for financial intermediation, the next decade will be an opportunity of a lifetime for Indian capital markets players.

The Government, the Regulators and the financial institutions have an important role to play in building a strong and robust capital market as the growth trajectory of a country's capital markets is significantly influenced by the actions of these stakeholders. Their concerted efforts supported by a long-term vision and clarity in action can significantly help in fostering a climate that is conducive to growth and investments.

Equity Market

The equity market comprises of the primary market and the secondary market with key constituents being Domestic Institutional Investors (such as mutual funds), Foreign Institutional Investors and Retail Investors who directly participate in the capital markets.

Domestic Institutional Investors

The size of the Indian Mutual Fund industry (comprising both, equity and debt funds) is estimated at USD 162 billion. Since the 1990s when the mutual fund space opened up to the private sector, the industry has traversed a long path. Assets under Management have grown at a Compound Annual Growth Rate (CAGR) in excess of 25% over the last four years, slowing down only over the last four years, as a consequence of the global economic slowdown and financial crisis.

As a Regulator focused on protecting retail investors' interests, SEBI has done a

commendable job in the regime with the changes it has introduced in recent past such as abolition of entry load and additional management fee for schemes launched on “no load” basis, compliance with documentation/KYC norms, transferability of units of mutual funds, etc.

However, the industry continues to be plagued by low margins and stiff competition from other investment products such as those offered by the life insurance industry and the portfolio managers. To develop the industry in a manner that is fair to all the stakeholders of the industry, amongst others, the following suggestions could be considered –

- Allowing Asset Management Companies (AMCs) the flexibility to charge management fees: In a “perfect competition” scenario, the price of goods or services is efficiently determined by the market itself. There are more than 35 AMCs with many other in the pipeline. Over a period of time, the market should be able to price the services provided by AMCs in an efficient manner such that their interests are also protected.
- Mutual fund distributors in India are largely unregulated. Further, there are instances of distributors rendering investment advice without requisite qualification, information of mutual fund schemes/investor and consideration of the investor’s needs. Distribution supported by quality investment advice is clearly the need of the hour. Herculean effort is required and the entire asset management industry should work towards this goal. Regulation of the distributors by a Regulator can be a point worth debating. More importantly, SEBI should strongly reach out to create/support infrastructure to train the distributors to meet the needs of the investors. More diversified products such as Real Estate Mutual Funds will help in optimising the utility of mutual funds as well.
- As regards investment by pension funds, the current regulations in India allow only about 10 % of the pension fund corpus to be invested in the equities market directly or through mutual funds as against 50% internationally. Also there are certain restrictions on the exposure of insurance companies to the capital markets which reduces the much needed inflow of long term investments into the capital market. Moving the Indian pension funds and insurance companies closer to international levels could give a much needed boost to domestic institutional investor participation.

Foreign Institutional Investors

The number of FIIs/sub-accounts and the amount invested by them in the Indian capital markets is a reflection of the potential of the Indian economy. In the last decade, the investment by FIIs/sub-accounts has multiplied 7 times and in the current fiscal (in the first half), as on 23rd August 2012 the net total investments of FIIs was USD 30.35 million.

From time to time, SEBI has brought in changes which have supported the growth of investments by FIIs/sub-accounts. Some of the key changes include -

- Qualified Institutional Buyers (QIBs) defined to include FIIs.
- Allowing FIIs to invest in debt markets including corporate debt, government securities and security receipts issued by Asset Reconstruction Companies.

- Permitting stock exchanges to allow Direct Market Access (DMA) to institutional clients for better and faster execution of orders with avoidance of leakage of sensitive information of trades. An institutional investor can access broker's system from its office and can book orders directly into the system thereby bypassing the brokers' infrastructure. However, the trade and settlement obligations will continue to apply to the broker, as will the risk management compliance.

The concessional taxation regime for listed securities and for FIIs has also supported the growth of FII investments though more certainty around the taxation consequences and eligibility of treaty benefits is desirable.

A key change that could bring a paradigm shift in the asset management industry is allowing domestic fund managers to manage funds raised from offshore investors for investment in India. But for a taxation issue, such funds are being currently managed from more tax efficient jurisdictions such as Singapore. If the taxation regime were to be amended to provide for "safe harbour" rules exempting foreign funds from Indian taxation (in a manner similar to Singapore), then the asset management industry would grow exponentially.

Retail investors

One of the daunting challenges before the Indian capital markets is expanding the investor base and providing them access to high quality financial services. With a population of more than a billion, a mere 1% of the population participates in capital markets, and of that only a fraction is active. Trading volumes in Indian Capital Markets are lower as compared to other markets such as US, UK, Germany, China etc. Similarly, Indian households invest much less in equity markets than their developed market counterparts, particularly US and UK. As a result, retail equity ownership (non-promoter) amounts to only around 10 % of total equity ownership, and has come down by 3% over the last seven years. While corporates see markets to raise low cost risk capital, investors see liquid secondary markets for exit options. The regulated markets have grown significantly, but the markets need greater depth and liquidity.

Another challenge faced by the investors is the costs involved in trading (brokerage, commission, taxes etc.), which are comparatively higher in India than in developed markets. The investor participation is fairly shallow considering the size of the economy.

In order to overcome the above bottlenecks and to deepen the capital markets' participation of retail investors, intermediaries such as mutual funds and portfolio managers needs to be further promoted. This can be achieved only through investor education initiatives, development of quality independent financial advisors and using the Information Technology to reach out across the length and breadth of the country. Happily ICSI under the aegis of Investor Education and Protection Fund has put in good efforts to organize investor awareness programs. While this is quite commendable initiative, it is more in metropolitan areas. Similar programs need to be organized in small towns to tap new investors.

Indian Depository Receipts (IDRs)

IDRs are instruments in the form of depository receipts created by a depository in India against the underlying equity shares of the issuing foreign company. IDRs are an important

step towards integrating Indian capital markets with foreign markets and enabling Indian investors to hold stake in foreign securities.

For various reasons, IDRs have taken more than couple of years to be operationalised. There are certain unresolved tax issues relating to taxation of income from IDRs for eg: the concessional tax regime for listed securities does not extend to IDRs. Also, there is no clarity on taxability of conversion of IDRs into underlying foreign equity shares.

IDRs could be made more attractive by introducing two-way fungibility of IDRs and removing the mandatory lock-in of a year in case of conversion of IDRs into equity shares of the foreign company.

Securities Lending and Borrowing (SLB) Scheme

SLB facilitates short-selling, increasing liquidity, improving pricing and arbitrage between derivatives and cash markets. SEBI amended the SLB scheme in January, 2010 with a view to make short-selling more accessible to investors. This move provides the investors including FIIs to have greater opportunity to access the Indian securities market. However, there are certain issues revolving around this amendment like the use of stock lending by promoters, applicability of insider trading regulations and the takeover code. In case of corporate action in SLB contract period, the lending and borrowing gets suspended. This condition should be relaxed. Insurance companies should also be allowed to lend their securities, which is currently not permitted. Presently, very high margins are required to be maintained under the SLB. SEBI should consider relaxing the same in the due course.

SMEs

Small and Medium Enterprises (SMEs) play a vital role for the growth of Indian economy by contributing 45% of industrial output, 40% of exports, employing 60 million people, creating 1.3 million jobs every year and producing more than 8000 quality products for the Indian and international markets. SMEs are the fountain head of several innovations in manufacturing and service sectors, the major link in the supply chain to corporate and the PSUs.

SMEs face a road block in the form of high cost of raising capital. SMEs lack access to formal capital market due to low credibility and low profitability. In order to enable SMEs to raise finance through Capital Markets, SEBI encourages promotion of dedicated exchanges and / or dedicated platforms of the exchanges for listing and trading of securities issued by SMEs. Certain relaxations are provided to the issuers whose securities are listed on SME exchange.

To ensure success of a SMEs-designated exchange, SEBI has offered several incentives not available to other exchanges. The most striking one relates to doing away with Disclosure guidelines for SMEs. This means that SMEs seeking to list on stock exchanges need not have a track record of a minimum of three years in making profits and paying dividend. Some concession is also proposed to be given to companies to reduce the cost and strain of publishing quarterly results. Thus companies seeking listing on the SMEs exchange will be

allowed to publish their results every six months. While this measure will surely give a fillip to companies' interest in listing on the exchange; it would have to be ensured that it doesn't lead to excessive drop in investors' interest owing to an increased risk perception.

The SME exchange could prove to be a landmark development and help in promoting the vibrancy of our capital markets. But the challenge before SEBI is to attract enough investors as many of them may act cautiously while subscribing to shares of these companies because of fewer disclosures norms.

Exchange Traded Derivatives

Exchange traded derivatives like options and futures are hedging tools, used especially in a bearish market with lower transaction cost as compared to some of the other instruments. Since they are exchange traded, their pricing and transaction volume are transparent and highly liquid. However, there is a risk of adverse price movement resulting into losses.

The trading of foreign exchange traded derivatives has emerged as very important financial activity all over the world just like trading of equity-linked contracts or commodity contracts. India's ranking in the global exchange-traded derivatives market continues to rise. According to volume rankings for the first half of 2010 by the Futures Industry Association (FIA), National Stock Exchange (NSE), India's ranking has improved by two places and it's now the fifth largest derivatives exchange in the world.

SEBI recently allowed physical settlement in equity derivatives and subsequently BSE Ltd. also decided to replace the decade-old cash settlement procedure in the equity derivatives segment with physical settlement as a mechanism for better price discovery. SEBI's nod for physical settlement is a regulatory response to the vulnerability of domestic markets and is perhaps aimed at ring fencing the stock markets from excessive shorting, which can often bring stock markets crashing down. Basically, it is a move to check excess volatility in the underlying cash market.

New Legislations in Capital Markets

With increased complexities and challenges facing corporates world-over, the regulatory environment across jurisdictions has been facing "catch up" especially over the past few decades. Regulators, the world over, are concerned about transparency and corporate governance while at the same time working overtime for providing laws that facilitate competition and encourage investment.

Regulators in India are no exception and have also felt the need to be up-to-speed to meet the growing and diverse needs of corporates while at the same time have "teeth" for malpractices. That explains the current plethora of new legislation spanning a proposed new company law, a new direct tax code, introduction of GST, competition (anti-trust) law, new Takeover Code etc.

New Takeover Code

SEBI notified new Take over Regulations in September 2011. The new regulation is

indeed a path breaking legislation which is likely to change the landscape of corporate India in the near future. Some of the key amendments in the new code are as under:

1. New thresholds for attracting public offer (15% to 25%).
2. Increase of creeping acquisition range from 15-55% to 25-75% — 5% limit for creeping acquisition remains same.
3. Facilitating consolidation through increase in Offer Size from 20% to 26% and also introduction of concept of voluntary offer (i.e. open offer for minimum 10% stake).

Of course, at a practical level, the experience in open offers has been that the public does not fully subscribe to such public offers. However, the fact that the regulatory mechanism has been enabled is commendable.

Public Issue Regulations

SEBI notified the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009 (ICDR Regulations) repealing the erstwhile SEBI (Disclosure and Investor Protection) Guidelines, 2000 (DIP Guidelines). The ICDR Regulations attempts to streamline the framework for public issues by removing unnecessary stipulations, introducing market-driven procedures and simplifying the clutter of legality.

Minimum Public Shareholding

The Ministry of Finance recently brought the minimum threshold of public shareholding for all listed companies to 25%. The amendment was a move towards providing better liquidity to public shareholders and to reduce the scope of price manipulation.

Corporate and Government Bonds

A well-developed capital market consists of both the equity market and the bond market. In developed economies, bond markets tend to be bigger in size than the equity market. In India, equity markets are more popular and far developed than the debt markets.

The Indian debt market is composed of government bonds and corporate bonds. However, the government bonds are predominant (constituting 92% of the volume) and they form the liquid component of the bond market.

The corporate bond market is still at the nascent stage. Although we have the largest number of listed companies on the capital market, the share of corporate bonds in GDP is merely 3.3%, compared to 10.6% in China, 41.7% in Japan, 49.3% in Korea among others. Further, close to 80% of corporate bonds comprises privately placed debt of public financial institutions. The secondary market, therefore, has not developed commensurately. An active corporate bond market is essential for India.

Over the past few years, some significant reforms have been undertaken to develop the bond market and particularly the corporate bond market.

SEBI has made efforts to facilitate trading of corporate bonds on the stock exchange

platforms. The listing requirements for corporate debt have been simplified. Issuers now need to obtain rating from only one credit rating agency unlike earlier. Further, they are permitted to structure debt instruments, and are allowed to do a public issue of below investment grade bonds. One more welcome change was, the exemption of TDS on corporate debt instruments issued in demat form and on recognized stock exchanges.

In a recent move, SEBI has also stipulated that all trades in corporate bonds would now be routed through stock exchange platform. This would help in reducing settlement risk and reduce transaction costs. At the same time the exchanges would document the trades, thus creating transparency as well as assist in price discovery. The transparent dissemination of corporate bond prices and quantities traded will also facilitate better participation by market participants. Based on the feedback received from market participants, SEBI also relaxed the exposure margin requirement for stock derivatives.

However, government securities trading have turned out a better performance owing to several structural changes introduced by the Government and RBI.

In view of the current macroeconomic environment in India, the government increased the FII investment limit in Government Securities and Corporate Bonds by USD 5 billion. Increased limits would open up new avenues for FII investment in debt and cater to the growth of debt markets in the country.

The challenges involved in developing the bond market in India include generating demand from domestic investors along with boosting market infrastructure and rationalizing the taxation regime. A liquid secondary market is necessary as investors get easy exit route. However, we do not have an active secondary market too. The exchange market is not active and the market is largely OTC.

The price of bonds is influenced by cost of rating, listing and marketing which makes them costly for investors. Stamp duty rates for primary issue of bonds are very high and differ from state to state.

Other markets have a much more diversified mix, with interest rate futures, foreign exchange futures and corporate bonds accounting for a sizable share of exchange trading. Deeper corporate debt markets also provide the required support to make a balanced capital markets.

Effective reforms in corporate debt market could help support the growth of overall capital markets. Some of them have been listed below:

- Required changes that can lead to the expansion of the Corporate Bond market would be - means to uniform stamp duty, screen based trading, clearing house settlement, increase in secondary market activity and thereby assist in transparent price discovery and avenue for early exits for investors and consequently also lead to more issuers of long tenor debt.
- There should be a gradual relaxation of investment restrictions and forced rule based buying on long-term investors such as insurance companies, pension funds and Banks.

This will give the required flexibility in deciding the investments based on its merit. The insurance and pension segments will be crucial not just for increasing social security, but are also likely to emerge as a catalytic factor in development of long term debt markets in India, a crucial feature for the massive financing needs for infrastructure projects.

- Consolidation of existing series of Government bonds to improve liquidity and facilitate better price discovery.
- Relaxing FII limits for corporate bond participation when needed. Allow greater participation for FIIs (Not just limited by their exposure) as it will help create liquidity.
- Interest-rate derivatives are needed to hedge rate risks, the largest macro-economic risk. Make interest rate futures available on a broader range of securities (both long- and short-term).
- Introduce interest rate options to attract a wider investor base.
- Credit trading is an essential prerequisite for the development of the corporate debt market. Regulatory reforms are required in this space keeping in mind the learnings from the International space.
- The current withholding tax of 20% should be removed to encourage investors to invest in debt securities.

Islamic Bonds and other Shariat compliant investment products

Another debt instrument that has gained popularity in the worlds markets since 2007 is the Islamic Bonds. Islamic Bonds are asset backed interest free bonds. Islamic finance does not involve payment of interest and is based on sharing of both profit and loss. In India, the concept of Islamic bonds and other Shariat compliant products is yet to take-off but it certainly has immense potential. The RBI should take the lead to encourage efforts to enhance the legal and regulatory framework required for Islamic finance to ensure uniformity with international practices. Also, steps should be taken for creation of awareness within the financial system and investor community and engage Shariat advisors to provide consensus, guidance to uphold Islamic financial products and structures.

Commodity Market

Commodities are emerging as an important asset class that can help market savvy investors diversify risks. The commodity markets have been growing at a phenomenal pace, as evident from the number of commodity exchanges set-up and proposed to be set-up (pending approval from the Regulator). In addition to augmenting capital markets, commodity markets have an important role to play in development of a country's agricultural sector and related eco-systems.

Commodity markets have traditionally been quite volatile and hence, it is important to allow institutional investors to invest in commodity markets as they bring significant trading experience. Internationally, there are different ways in which mutual funds invest in commodity markets. Domestically, gold is the only commodity where retail investors can

participate. Further, presently, other investors such as FIIs, banks, etc. are not permitted to invest in the commodities markets. These investors should be allowed to take exposure in commodity markets. If there are any concerns around excessive speculation, then, the same could be addressed by limiting exposures to certain amounts/percentages, etc. or through other methods.

Another key element for development of commodity markets is the presence of a strong regulator. Currently, the Forward Markets Commission (FMC) acts as the regulator. As compared to SEBI, FMC has limited autonomy in making regulations or policy changes. The Bill to grant additional authority to the FMC has been pending enactment for several years now. It is imperative to pass the law as it will lead to the strengthening of the FMC and the commodity markets.

Currency Market

The currency derivatives segment on the NSE and MCX has witnessed consistent growth both in traded value and open interest since its inception. India already has an active over-the-counter (OTC) market in currency derivatives. The exchange-traded currency futures market is an extension of this already available OTC market, but with added benefits of greater accessibility to potential participants; high price transparency; high liquidity; standardised contracts; counterparty risk management through clearing corporation and no requirement of underlying exposure in the currency. As the market participants are realising these benefits of exchange-traded market in currency, they are choosing this market over OTC.

Stock exchanges in India will also be launching Options in Currency Derivatives soon. The RBI and SEBI have given in-principle clearance to launch options in Currency Derivatives. Similarly, the Currency market should provide for diversified products such as futures and options on cross currencies and currency ETFs.

The Way Forward for the capital markets

Summarised below are some recommendations which could move Indian Capital Markets closer to efficiency and scale greater heights -

- Investor education and regulation of mutual fund distributors
- Allowing AMCs the flexibility to charge fees
- Innovative products across different asset classes including operationalisation of REMFs (Real Estate Mutual Funds)
- Amending tax regime to encourage domestic AMCs to manage foreign funds from India
- Allowing higher investment by domestic institutional investors such as insurance companies, pension funds and provident funds to make investments in capital markets
- Make tax regime friendly for issuers/investors of IDRs

- Reduction in the current withholding tax of 20% on income from debt securities to encourage investment in debt market
- Developing a legal and regulatory framework for Islamic finance and structure new capital market products that are Shariah compliant
- Allowing institutional investors to participate in commodity markets
- Strengthening the autonomy of the FMC

The contours of the financial markets are expanding with the advent of new technology, innovations in products and fast changing customer expectations. The Indian financial services sector comprises a good blend of domestic and foreign participants. Opening up of the financial markets has resulted in competition and greater efficiency; however, foreign participation could also bring in the baggage of increased risk and exposure as recent events have shown. Stability is therefore a critical need for financial markets for which safeguarding mechanisms need to be established, to prevent systemic risks and absorb shocks.

The equity market in India is extremely vibrant, but equity based funding solely, cannot lead the economy to growth. The debt market remains under-developed, with a huge potential for increased activity. A strong bond market is required to drive long term financing of infrastructure, housing and private sector development. The role of capital markets is vital for enhancing growth in wealth distribution and increasing availability of funds for infrastructure development.

One of the underlying challenges that the banking and financial services sector is dealing with is the issue of increasing the out-reach & enhancing financial inclusion. The huge scale of the drive towards inclusive growth is intimidating, as various stakeholders like banks, insurance companies and AMCs struggle to move a step closer to the untapped areas and newer target consumers. The challenge lies in devising a cost-effective delivery model to reach out to the low income group of society, penetrating the remote areas. A debate on new banking licenses, banks developing and formulating strategies for inclusive banking and an increasing thrust on infrastructure financing, have been some of the initiatives which have been taken to give an added impetus to financial inclusion.

The road ahead for deepening the financial markets needs to be paved by the formulation of a strong linkage between the development of the economy and the capacity of the financial system. The global financial environment is moving towards an integrated financial system, and will serve in good stead to standardise compliance norms and procedures. A greater measure of transparency is also required to be built into regulatory procedures, to bring in a new dimension to financial markets, and take it to the next level.

ROLE OF FINANCIAL MARKET IN ECONOMIC GROWTH OF INDIA

DEVENDRA JARWAL*

Introduction

In financial market, the securities in trade is money which could be raised through various instruments, under well governed rules and regulations, carefully administered and adhered to by different institutions or market operators. It is true that the rate of economic growth of any nation is inextricably linked to the sophistication of its financial market and specifically its capital market efficiency. Virile financial markets assist the nations of the world to muster needed financial resources and skills for growth and development. Equity markets in developing countries until the mid-1980s generally suffered from the classical defects of Bank dominated economies that are shortage of equity capital, lack of liquidity, absence of foreign institutional investors and lack of investor's confidence in the stock market. Financial market and its sub-unit, capital market are constituted whenever participants, with the aid of infrastructures, technology and other devices try to facilitate the mobilization and channeling of funds into productive investment. The importance of financial market lies in its financial intermediation capacity to link the deficit sector with the surplus sector of the economy. The absence of such capacity robs the economy of investment and production of goods and services for societal advancement. Funds could thereby be idle at one end, while being sought at the other end in pursuit of socio-economic growth and development.

Universally, financial markets are primarily created to provide avenues for effective mobilization of idle funds from surplus economic units to be channeled into deficit units for generation of economic activities including long term investments. On large scale, suppliers of funds are basically individuals and corporate bodies as the government even in mixed or socialist economies, finds itself unable to fulfil all the financial fund requirements of the market. The deficit units by contrast consist of only corporate bodies and government. In otherwords, individuals (households) who are major suppliers of funds to the financial market conspicuous by their absence in the category of fund users. This is because conventionally, individuals cannot access the sub unit of financial market (i.e. capital market) for funds. Moreover, capital markets through secondary arm provide opportunities for the purchase and sale of existing securities among investors thereby encouraging the populace to invest in securities and fostering economic growth.

* FCS, Assistant Professor, Moti Lal Nehru College, University of Delhi.

The funding requirements of corporate bodies and governments are often colossal, sometimes running into billions of rupees. It is therefore, usually difficult for these bodies to meet such funding requirements solely from internal sources, hence they often look up to the financial market. This is because the financial market is the ideal source as it enables corporate entities and government to pool monies from a large number of people and institutions. Thus the socio – economic function of the financial market is well established. It does not only encourage and mobilize savings but also efficiently allocates such savings to areas of need.

The Indian Financial Market consists of capital market, derivative market, money market and the debt market. It is further categorized into primary and secondary markets. New financial securities are issued in the primary market, and companies/institutions issuing these securities receive the proceeds of sale. The secondary market provides a forum for the sale of financial securities by one investor to another investor. Thus, the efficient functioning of the market paves way for the primary market by making investors more willing to purchase new securities in anticipation of selling in the secondary market. These securities are the major instruments used to raise funds at the financial market.

The institutional framework through which the financial market function in India include; the Reserve Bank of India, the Securities and Exchange Board of India, Banks and Financial Institutions, the Stock Exchanges, stock brokers and investors. The main objective of establishing the Indian Financial Market is to mobilize savings from numerous economic units for economic growth and development, provide adequate liquidity to investors, broaden the ownership base of assets as well as the creation of a buoyant private sector, provide alternative source of funds for government, to encourage more efficient allocation of new investments through price mechanism, to encourage more efficient allocation of a given amount of tangible wealth through changes in the composition and ownership of wealth, to create a built-in efficiency in the operation and allocation in the financial system to ensure optimal utilization of resources, and promote rapid capital formation. In the light of the above objectives, the point of departure of this research paper is to highlight the role of financial market in India's economic growth and development.

Development of Indian Financial Market

The history of Indian Financial Market dates back to the era of establishment of the stock exchanges in India. It got further acceleration with the establishment of the Reserve Bank of India in the year 1935 by the British Government. On independence from the British in 1947, India inherited not only one of the world's poorest economies (the manufacturing sector accounted for only one tenth of the national product), but also one with arguably the best formal financial markets in the developing world, with four functioning stock exchanges and clearly defined rules governing listing, trading and settlements; a well-developed equity culture only among the urban rich; a banking system with clear lending norms and recovery procedures; and better corporate laws than most other erstwhile colonies. After independence, with the starting of first phase of industrial revolution, many financial institutions were established such as IDBI, IFCI, UTI and insurance companies etc. In the

year 1969 Bank Nationalization was done to improve the banking system of the country. The 1956 Indian Companies Act, as well as other corporate laws and laws protecting the investors' rights, were built on this foundation. After independence, a decades-long turn towards socialism put in place a regime and culture of licensing, protection and widespread red-tape breeding corruption. In 1990-91 India faced a severe balance of payments crisis ushering in an era of reforms comprising deregulation, liberalization of the external sector and partial privatization of some of the state sector enterprises. There is hardly a facet of economic life in India that has not been radically altered since the launch of economic reforms in the early 90's. The twin forces of globalization and the deregulation have breathed a new life to private business and the long-protected industries in India are now faced with both the challenge of foreign competition as well as the opportunities of world markets. The end of the "License Raj" has removed major obstacles from the path of new investment and capacity creation. The effect is clearly visible in the ratio of capital formation in the private sector to that in the public sector for a decade preceding liberalization and for the period following it. The unmistakable ascent in the ratio following liberalization points to the unshackled private sector's march towards attaining the "commanding heights" of the economy. In terms of price stability, the average rate of inflation since liberalization has stayed put close to the preceding half decade except in the last few years when inflation has declined to significantly lower levels. Along with deregulation, globalization has played a key role in transforming the Indian economy in the past dozen of years. A quick measure of the rise in India's integration with the world economy is a standard gauge of "openness" – the importance of foreign trade in the national income. In just over a decade since liberalization, the share of foreign trade in India's GDP had increased by over 50%. While imports increased steadily and continued to exceed exports, the rise in the latter has been almost proportional as well. The "export pessimism" that marked India's foreign trade policy truly appears to be a thing of the past. The Indian rupee has largely stabilized against major world currencies, over the period. The economic reforms era began with a sharp devaluation of the rupee. As liberalization lifted controls on the rupee in the trade account, there were considerable concerns about its value. However, propped up largely by inflows of foreign investment the floating rupee stabilized in the late 90's and has appreciated somewhat against the US dollar in recent months. In fact, it is fair to say that the rupee is currently considerably undervalued against the dollar as its value is managed by the RBI.

A lot has changed in the world beyond India's borders during these years. Japan, the second largest economy in the world, has experienced a deep and long recession over much of the period. The Asian Crisis, one of the most widespread of all financial and currency crises ever, devastated South-East Asia and Korea in 1997. Continental Europe has entered into a monetary union creating the Euro that now rivals the US dollar in importance as a world currency. Several economies like Russia, Argentina and Turkey have witnessed financial crises. The internet bubble took stock markets in the US and several other countries to dizzying heights before crashing back down. More recently, US sub-prime market woes have sparked global sell-offs. India has emerged largely unscathed from the Asian crisis. Most observers attribute this insulation to the capital controls that continue in India. Nevertheless, Indian financial markets have progressively become more attuned to international market

forces. The reaction of Indian markets to the recent sub-prime meltdown bears testimony to the level of financial integration between India and the rest of the world.

Constituents of Indian Financial Market

Indian Capital Market

Indian capital markets have been one of the best performing markets in the world in the last few years. Fuelled by strong economic growth and a large inflow of foreign institutional investors (FIIs) as well as the development of the domestic mutual funds industry, the Indian stock market indices have registered truly explosive growth during the last 10 years rising over 3 times during the period. However, it would be a mistake to think that growth has happened only in valuation. During this period Indian capital markets have exhibited explosive growth in almost every respect. While the two major Indian exchanges, the Bombay Stock Exchange (BSE) and the National Stock Exchange (NSE) ranked 16th and 17th respectively among exchanges around the world in terms of market capitalization. In March 2006, the BSE market capitalization accounted for about 86% of Indian GDP while that of the NSE accounted for about 80%. In terms of risk and return, while the Indian markets have been more volatile than those in industrialized nations, the returns have been largely commensurate. The biggest development in the Indian capital markets in recent years is undoubtedly the introduction of derivatives – futures and options – both on indexes as well as individual stocks with turnovers growing 50 to 70 times in the past 5 years and the derivatives segments quickly becoming a crucial part of the Indian capital markets.

Debt Market

Government of India, public sector units and corporations together comprise a dominant issuer of debt markets in India. Local governments, mutual funds and international financial institution issue debt instruments as well but very infrequently. The Central Government mobilizes funds mainly through issue of dated securities and T-bills. Bonds are also issued by government sponsored institutions like the development financial institutions (DFIs), IFCI and IDBI, banks and public sector units. Some, but not all, of the PSU bonds are tax-exempt. The corporate bond market comprises commercial papers and bonds. At about 2% of the GDP, the corporate bond market in India is small, marginal, and heterogeneous in comparison with corporate bond market in developed countries. While a corporate debt market in India has existed since 1950s, the bulk of the debt has been raised through private placements. In 2004-05, close to Rs. 593 billion (\$ 14.3 billion) was raised by the corporate sector through debt instruments, of which private placements accounted for around 93 %. In 2005-06, the entire amount of over Rs. 794 billion (\$ 19.85 billion) was raised by 99 issuers through 362 privately placed issues, with no public issues at all. To promote the corporate debt market, especially secondary market regulators have taken several steps. Corporate Debt instruments are traded both on BSE and on capital market and the WDM segments of the NSE. SEBI has already mandated that all bonds traded on the BSE and NSE be executed on the basis of price/order matching. Thus, the difference between trading of government securities and corporate debt market securities is that the latter are traded on

the electronic limit order book like equities. Since June 2002, the CDSL and NSDL have admitted debt instruments such as debentures, bonds, CPs, CDs, etc. Also, banks, financial institutions and primary dealers have been asked to hold bonds and debentures, privately placed or otherwise, in electronic form.

Banking Sector

The Banking system in India can be broadly divided into three categories, viz. the central bank of the country known as the Reserve Bank of India, the Commercial Banks and the Co-Operative Banks. Another and more common classification of banks in India is between scheduled and non-scheduled banks. The Reserve Bank of India is the supreme monetary and banking authority in the country and has the responsibility to control the banking system in the country. It keeps the cash reserves of all scheduled banks and hence is known as the 'Reserve Bank'.

The Indian banking system had gone through a series of crises and consequent bank failures and thus its growth was quite slow during the first half of the 20th century. But after independence, the Indian banking system had recorded rapid progress. This was due to planned economic growth, increase in money supply, growth of banking habit, control and guidance by the Reserve Bank of India and, above all nationalization of banks in July, 1969.

Micro Finance in India

The microfinance sector is clearly one of the fastest growing segments of the Indian financial sector, and also the one where such growth has been sustainable for a very long period of time. In spite of a large banking sector, about 40% of the Indian population does not have bank accounts. Given that over 75% of the Indian population still lives below \$2 a day, and a vast majority in rural areas, microfinance – the provision of thrift savings, credit and other financial products and services accessible to the poor to enable them to raise their income and improve living standards – is key to financial inclusion in India. Traditionally, micro-credit in India has been the domain of village money-lenders, generally at exploitative interest rates that impoverished borrowers.

While special emphasis on rural and small loans have existed in India at least since the 1960s and India's apex specialized rural credit agency, the National Bank for Agricultural and Rural Development (NABARD) was established in 1982, microfinance in India has witnessed a dramatic increase in recent years with the involvement a large number of private players in addition to the government.

Contribution of financial market in economic growth of India

Financial Market plays an important role in promoting economic growth. It is commonly argued in the economic literature that a well functioning financial sector creates strong incentives for investment and also fosters trade and business linkages thereby facilitating improved resource use and technological diffusion. This argument is also true with the Indian

Economy. Some of the contributions of financial market in the economic growth are as mentioned below:

India's financial market took to its transformation path in the early 1990s. The introduction of Securities and Exchange Board of India (SEBI) and repealing of the Controller of Capital Issues (CCI) removed the administrative controls over the pricing of new equity issues. The capital market consisting primarily of debt and equity markets, played a significant role in mobilizing funds to meet the public and private entities' financing requirements.

The advent of exchange-traded derivative instruments in 2000, such as options and futures, also enabled investors to better hedge their positions and reduce risks. The debt market of India mostly comprised government and corporate bond. The contours of the government bond market began taking shape around 1992 as a result of the government's broad-based attempts to reform the financial sector. Moreover, the high fiscal deficits and public sector borrowings led to a bigger size of the government bond market. The size of the corporate bond market, in contrast, remained quite shallow during the mid-2000.

Significant growth acceleration in recent years is underlined by distinct increase in savings and investment rates. The period 2002-03 to 2007-08, observed a notable transformation in the level and composition of aggregate savings and investment in the economy. The investment rate between early 1990s and the first year of 2000 was about 24 per cent of GDP, in the next five years it recorded a meteoric rise and catapulted to 35.5 per cent in 2006-07. The rate then moderated from 37.7 per cent in 2007-08 to 34.9 per cent in 2008-09 mainly on account of a decline in the investment of private corporate sector. Gross domestic savings (GDS) as a proportion to GDP was 23.9 per cent in the 1990s with a simultaneous increase in the rates of financial savings of the household sector and private corporate sector. The rate continued to improve rising from 26.4 per cent in 2002-03 to 32.42 per cent in 2005-06 with an average of 31.4 per cent during the tenth five year plan.

In India, foreign direct investment (FDI) inflows amplified significantly in the post reform era with streamlining of regulations, radical changes in the policies, astounding corporate performance and increased confidence of the investors. The service sector in India became a major destination of FDI inflows and within the sector, financing, insurance, real estate and business services witnessed a large increase in their share in FDI inflows to India between 2002-03 and 2007-08.

With this performance of Indian Financial Market and performance of Indian Economy and increase in GDP growth it is evident that financial market has played a pivotal role in economic growth. In this regard, it is rightly observed by Chief Economist of United Nations Economic and Social Commission for Asia and the Pacific (ESCAP) that "we expect the growth rate to expand by about 7.5 percent in 2012-13, because as per a United Nation (UN) report, India is projected to see a faster growth of 7.5 percent this fiscal, on the back of higher savings and investment rates, even as most of the Asia-Pacific economies are likely to expand at a slower pace.' Further former Hon'ble President Ms. Pratibha Devi Singh Patil commented in her speech that "Today, India is among the most attractive destinations globally, for

investments and business and FDI had increased over the last few years and the Indian Economy has continuously recorded high growth rates and become an attractive destination for investments.”

Obstacles of financial market in economic growth of India

It is true that financial market is paving way for economic growth of India, but at the same time due to some shortcomings and limitations, it is also creating some obstacles interdicting economic growth. The anti-inflationary policies of RBI also affect the growth rate of the country. The higher SLR and CRR diverted banks funds away from loans and advances to industry and trade. The most serious damage to the public sector banks was the political and administrative interference in credit decision-making and over emphasis on priority sector lending.

Domestic financial scandals and the government’s large fiscal deficits are starving the Indian private sector of capital and keeping interest rates high. Financial scandals exacerbated by the downturn in equity markets had severely restricted access to private equity capital. High levels of non-performing assets undercut the ability of domestic financial institutions to extend term loans. Large government fiscal deficits are crowding out the limited supply of available credit, keeping real interest rates high.

Conclusion

The financial market plays an important role in promoting economic growth of India. By mobilizing savings for productive investment and facilitating capital inflows, it stimulates investment in both physical and human capital. The financial market also channels savings to more productive uses by collecting and analyzing information about investment opportunities. Thus, by creating an efficient mechanism for transactions in long term financial instruments, it provides a wide range of wealth creating opportunities for the Government, Corporations, Private individuals and other financial institutions. However, to overcome obstacles we need some strong measures by formulating investor friendly policies and environment, stability in stock market to gain investors confidence and by making international standards for banking system.

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CHALLENGES AND OPPORTUNITIES IN SME SECTOR

CS PRAMOD S SHAH*

*Small opportunities are often the beginning of great enterprise
- Demosthenes (384-322 BC)*

The Role of MSME's in a Developing Economy

The role of Micro, Small and Medium Enterprises (MSMEs) in the economic and social development of the country is well established. In most of the developing countries like India, these industries constitute an important and crucial segment of the industrial sector. They play an important role in employment creation, resource utilization and income generation. The MSME sector is a nursery of entrepreneurship, often driven by individual creativity and innovation. This sector contributes 8 percent of the country's GDP, 45 percent of the manufactured output and 40 percent of its exports.

The MSMEs make over 8000 products; provide employment to over 60 million persons through 26 million enterprises. The labour to capital ratio in MSMEs and to overall growth in the MSME sector is much higher than in the large industries. The geographic distribution of the MSMEs is also more even. Thus MSMEs are important for the national objective of growth with equity and inclusion.

The Ministry of Micro, Small and Medium Enterprises is the nodal Ministry for formulation of policies, programs and schemes, their implementation and related co-ordination, for the promotion and development of small scale industries in India. The role of the ministry is to assist the states in their efforts for the growth of the small scale sector, by enhancing their competitiveness in an increasingly liberalized economy. Parliament passed the Micro, Small and Medium Enterprises Act in 2006 as a comprehensive legislation looking into all matters related to the MSME sector. The Act also defined the MSME enterprises engaged in Manufacturing as-

- (a) Micro enterprises : The investment in plant and machinery does not exceed twenty-five lakh rupees.
- (b) Small enterprises : The investment in plant and machinery is more than twenty-five lakh rupees but does not exceed five crore rupees.

* B.A., B.Com, LL.B., FCS. Practising Company Secretaries, Pramod S Shah & Associates, Mumbai. Former Chairman, Western Region & Past Central Council Member, Former Committee Member of ICSI-CCGRT, Ex-Senior Executive of IIT, ACC & ABB Group of Companies.

- (c) **Medium enterprises** : The investment in plant and machinery is more than five crore rupees but does not exceed ten crore rupees.

In the case of the enterprises engaged in providing or rendering of Services, MSMEs are defined as-

- (a) **Micro enterprise** : The investment in equipment does not exceed ten lakh rupees.
- (b) **Small enterprise** : The investment in equipment is more than ten lakh rupees but does not exceed two crore rupees.
- (c) **Medium enterprise** : The investment in equipment is more than two crore rupees but does not exceed five crore rupees.

The important advantages of MSMEs in India which make them more relevant for the Country's development are as follows:

- (1) Small-scale industries are fairly labour-intensive. They provide an economic solution by creating employment opportunities in urban and rural areas at a relatively low cost of capital investment.
- (2) Small-scale industries are flexible in their operation. They quickly adapt to various factors that play a large part in daily management. Their flexibility makes them best suited to constantly changing environment.
- (3) A Small-scale unit is generally a one-man show. It is mostly set up by individuals. Even some small units are run as a partnership firm or a company; the activities are mainly carried out by one of the partners or directors. Therefore, they provide an outlet for expression of the entrepreneurial spirit. As they are their own boss, the decision making process is fast and at times more innovative.
- (4) Small-scale industries use indigenous raw materials and make intermediate and capital goods. They contribute to faster and balanced economic growth in a transitional economy through decentralization and dispersal of industries in the country. They generally restrict their operation to local areas in order to meet the local and regional demands of the people. They find it hard to enlarge their business activities due to limited resources.
- (5) Before the return on investment starts every enterprise faces a gestation period. It is the time period between setting the units and commencement of production. Small scale industries usually have a lesser gestation period than large industries. This helps the entrepreneur to start earning after a short period of time. Thus, capital is not blocked for a long period.

Objectives of Micro Small and Medium Enterprises Act, 2006

The Preamble to the Act, states that the primary objective of the Act is to facilitate, the promotion of micro, small and medium enterprises, development of micro, small and medium enterprises and enhancing the competitiveness of micro, small and medium enterprises.

The Act aims to achieve the above objectives through

- Skill development,
- Technological up gradation;
- Preference in procurement by government departments and government aided institutions, etc.

The salient features of the Act are:

- (a) The main feature of this law is that it seeks to be a comprehensive legislation concerning the micro, small and medium enterprises sector and also covers the services sector enterprises, which was hitherto not covered.
- (b) The emphasis was shifted to enterprise component from the earlier approach, namely, industry components.
- (c) The process of two-stage simplified registration of Micro and Small Enterprise is dispensed with and replaced by filing of memorandum. However filing of memorandum is optional except for medium enterprises in manufacturing sector and a prior manufacturing industry specified in the First Schedule to (I&DR) Act, 1951 having investment in plant and machinery or more than one crore rupees but not exceeding ten crore rupees.
- (d) The Act establishes the National Board for Micro, Small and Medium Enterprises to provide the necessary structure for overseeing and regulating the development of Micro, Small and Medium Enterprises in India.
- (e) The Act also provides for the formation of Micro and Small Enterprises Facilitation Council(s) in each State/Union Territory for conciliation and alternate dispute resolution.

Strategies

Redefine the ceiling limit of medium enterprises

The MSME sector in India, with some exceptions, is characterized by low technology levels, which act as a handicap in the emerging global market. Although MSMEs play an important role in India's economic growth, be it in terms of its contribution to manufacturing value-added exports or employment generation, not many units have ability to access technological expertise or mobilize resources for in-house innovation. Also, the cap on plant and machinery for the purpose of classifying the units as MSMEs does not encourage Indian MSMEs to move up the value chain. It may be mentioned that within the manufacturing sector, micro enterprises are classified as those with investment in plant and machinery not exceeding Rs. 25 lakhs. While investments in plant and machinery for a small enterprise has been kept in the range between Rs. 25 lakhs and Rs. 5 crores, a medium enterprise is defined with investment in plant and machinery in the range between Rs. 5 crores and Rs. 10 crores.

Challenges and Opportunities in SME Sector

Introduction

- The role of Micro, Small and Medium Enterprises in the economic and social development of the country is well established. In most of the developing countries like India, these industries constitute an important role in employment creation, resource utilization, creativity and innovation.
- The SME sector has demonstrated true Indian entrepreneurship and some of the biggest names in India Inc. have their roots in the sector. The SME sector today is facing a set of challenges which it has not experienced in the past and which could impact its future growth and in turn affect the Indian economy. With the impact of globalisation and de-reservation, the SME sector has become prone to threats not only from global players but also from MNCs.
- The importance of SME Sector in Indian economy can be gauged from the fact that the Sector contributes around 9% of national GDP, 45% of manufacturing output, nearly 40% of national exports, manufacturing over 6000 product groups, providing employment to over 70 Million persons. The labour to capital ratio in SMEs and the overall growth in the SMEs is also more even. Thus SMEs are important for the national objectives of growth with equity and inclusion.

Think for Growth, Not for Survival

- Worldwide, SMEs have been accepted as the engine of economic growth and a means of equitable development. Despite constituting more than 80% of the total number of industrial enterprises and supporting industrial development, SMEs face many problems such as sub optimal scale of operation, technological obsolescence, supply chain difficulties, increasing domestic and global competition, shortage of fund, change in manufacturing / marketing strategies and turbulent and uncertain market scenario.
- Until the first half of this decade of the new millennium, SMEs have been primarily known to have cited survival as their top priority. However, in recent times SMEs expect their companies to not just survive, but also grow. They are willing to take financial risks to fund expansion, incorporate technology into their marketing plans, take calculated risks and look forward to investing in social media networking.

Major Challenges in SMEs

(1) *Non availability of adequate skilled manpower*

The success of a every enterprise revolves around the entrepreneur and its employees, provided the employees are skilled and efficient. Inefficient human factor and unskilled manpower create innumerable problems for the survival of Business. Non- availability of adequate skilled manpower create problem for small-scale industries.

(2) *Credit Facilities*

Adequate and timely supply of credit facilities is a major problem faced by small-scale industries. This is partly due to scarcity of capital and partly due to weak credit worthiness of the small units in the country.

(3) *Shortage of raw material*

Shortage of raw materials, sometimes poor quality of raw materials and increased cost of raw materials and lack of knowledge of entrepreneurs regarding government policy are other few hindrances for small-scale sector.

(4) *Absence of organised marketing system*

Another major challenge faced by small-scale units is the absence of organized marketing system. In the absence of organized marketing, their products compare unfavorably with the quality of the product of large-scale units. They also fail to get adequate information about consumer's choice, tastes and preferences of the type of product. These problems do not allow them to stay in the market.

(5) *Outdated and traditional technology and equipment*

Lack of appropriate technology and equipment create a major stumbling block for the growth of small-scale industries.

(6) *Inadequate infrastructure*

Inadequate infrastructure is a major problem for SMEs to grow. Most of the SMEs are found in towns and cities, having one or more problems like lack of power supply, inadequate water and drainage system, poor roads etc.

(7) *Low price of Imported Products*

SMEs not only find it very difficult to compete with the product of large industries but also face competition from imported articles, which are comparatively very cheap and of better quality than products of small-scale units.

(8) *Complacency Setting*

Many SME entrepreneurs have started reaching the point of satisfaction. Asset price inflation has increased their wealth manifold in the last decade. Inflation in real estate and stock in trade (bought most of the time on leverage) has unexpectedly raised their net worth beyond their expectations.

This unexpected rise in wealth has dampened SME entrepreneurs' hunger for growth. The challenges of taking business to the next level in terms of investment, manpower and professionalizing the organisation, among others, are too much of a risk to take for the satisfied entrepreneur. Some SMEs are being run in neutral gear rather than in top gear.

(9) *Technological Obsolescence*

Majority of the SMEs use old techniques of production and outdated machinery and equipment. Upgradation of the technology and achieving economies of scale is one of the major problems facing the sector. They cannot afford new machines and

equipments and are therefore not in a position to use the latest techniques of production. They do not find it possible to conduct research and development on a continuing basis. Therefore, productivity and quality in SME firms tends to be low while unit cost of production is generally high.

(10) *Financial Problems*

Acquiring finance for technology upgradation, expansion, diversification is also a major problem. SMEs look to external sources of funding for expansion, modernization etc. as withdrawing money from business entails its own costs. Many SME entrepreneurs do not have sufficient knowledge of institutional credit and thus often fail to utilize the normal banking channels. Small asset base of SME does not enable them to avail bank loans.

Marketing Issues and Challenges

In terms of marketing, there are challenges in the field of consumer awareness, effective advertising and USP development for their products, creation of brand image, distribution and supply chain management.

Customer Awareness

Customer awareness is a major concern for MSMEs, especially when it concerns to expanding their markets in new territories. Due to the lack of implementation of proper advertising strategies using mass media channels, for communicating their product, MSMEs fail to create awareness in their target markets.

Clear STPD (Segmentation, Targeting, Positioning and Differentiation)

Identification of precise market segments to be targeted and crafting their product communication to compliment the proper positioning of the products in the target markets has not yet been considered as a vital marketing activity by MSMEs.

Advertising and Public Relations

Most of the MSME players go for advertising on local media due to low cost and effective target market coverage but they forget about creation of effective advertising message, due to lack of expert knowledge on this aspect of marketing.

Strong Branding

Absence of strong branding initiatives affect customer loyalty. MSME's are reluctant to focus upon branding strategies including an effective brand name, logo creation, compliance with quality norms of service or product. In the absence of advertising, they fail to create an image of a trustworthy brand in the minds of customers.

Effective USP Creation

Creation of an effective Unique Selling Proposition is also an important issue for most MSME players who predominantly focus on low cost products thus ignoring the need for

effective USP in any form like better value proposition, quality assurance or 'evening terms' of any sales promotional offer to boost up the sales.

Distribution and Supply Chain issues

MSMEs that are struggling with constraints like finance, infrastructure, human resources etc. find it very difficult to add modern Supply Chain Management practices into their strategist set-up. MSMEs fail to validate centralized organizations for supply chain management involving large corporate staffs in the various business functions.

Opportunities for SME Enterprises

Since the SME sector occupies an important position in the Indian economy, the Government of India set up the Ministry of Small Scale Industries and Agro Rural Industries (SSI&ART) in October, 1999 as the nodal ministry for promotion of policies and programmes, their accomplishment and related coordination, to supplement the efforts of the states for promotion and development of this category of industries in India. SMEs have been accepted as the Indian engine of economic growth and for promoting equitable development.

The Ministry of Agro Rural Industries and Ministry of Small Scale Industries were merged in to a single Ministry namely, "Ministry of Micro, Small and Medium Enterprises" from 2/10/2006. The Ministry of MSMEs addresses the issues and concerns relating to the MSME division at the national level through the formulation of policies and schemes which were implemented by the organizations approaching under its purview, the Ministry is assessed in the accomplishment of its policies and programmes by summit organisations like SIDO, NSIC, SIDBI, NCEUS and EDIs.

A performance and credit rating system for small scale industries has been formulated in discussion with various pledge holders that is small industries association and Indian banks, etc. and credit rating agencies like CRISIL, ICRA, DUN and Brad Street(B&D) and ONICRA. This has the approval of Government.

A large number of items have been reserved for exclusive manufacture by Micro and Small Enterprises Sector which include :

- (a) Chemicals and Chemical Products such as wax candles, laundry soaps, safety matches, fireworks & agarbatties.
- (b) Mechanical Engineering excluding Transport Equipment covering steel almirah, rolling shutter, steel chairs & tables, padlocks, utensils etc.
- (c) Food and Wood Products such as wooden furniture, pickles & chutneys bread, mustard oil etc.
- (d) Paper and Wood products.
- (e) Glass and Ceramics

The various schemes offered by the government for promotion of SMEs are:-

(1) *Financial Support Scheme*

Financial support will be given to SMEs for meeting fixed and working capital requirements. Credit will also be provided for creation of fixed assets like land, building, plant and equipment. Credit card schemes have been provided to SMEs where they can avail credit up to Rs 10 lakhs. Apart from this, credit facility up to a maximum of Rs. 25 lakhs is also provided by SIDBI and GOI.

(2) *Finances and Credit Policies*

The credit conveniences which are appropriate to be covered under Credit Guarantee Scheme provide working capital facilities up to Rs 100 lakhs per borrowing unit. The loan will be provided without any guarantee to a new or existing SME.

(3) *Schemes of WTO*

The WTO has started Credit Linked Capital Subsidy Scheme (CLCSS) which provides financial incentives to the SME sector and Credit Guarantee Fund Trust Scheme which provides assistance for technological upgradation.

(4) *Laghu Udyami Credit Card Scheme*

This scheme was introduced in November 2001. It has been implemented by the banks for providing borrower friendly credit facilities to small business, retailers, artisans, small entrepreneurs, professional and other self-employed persons. Credit provided under this scheme has been increased to Rs. 10 lakhs for the SME borrowers.

(5) *Credit Guarantee Fund Trust for SMEs*

This scheme was launched by NGO's and GOI and SIDBI.

This scheme provides money worth Rs 25 lakhs by way of term loan and working capital requirements. As on 31st March 2007 term loans to SMEs amounted to Rs 2200 crores.

(6) *Swarozgar Credit Card Scheme*

This scheme was launched on 15th August 2003 and banks are providing working capital to self-employed people engaged in running SME business.

(7) *Credit Linked Capital Subsidy Scheme*

This scheme was started in October, 2000 for a period of 5 years for encouraging the SMEs to bring about technological upgradation and installation of new production processes, equipment etc. Under this scheme 13 items were selected for which loans were provided at reasonable rate of interest. Recently the list of items have been increased to 30.

(8) *ISO 9000/14001 Certification Fee Reimbursement Scheme*

This scheme was introduced to incentivize technological upgradation, quality

improvement and better environment management by the SMEs. The scheme provides incentives to SMEs who have acquired ISO 9000/ISO14001/HACCP certifications.

(9) *Technology Bureau for Small Enterprises*

The SIDBI in collaboration with the United Nations- Asian Pacific Centre for Transfer of Technology has established the Technology Bureau for Small Enterprises to arrange finance and technology to the SME sector. This scheme aims to provide professional services for technology transfer in order to enhance market competitiveness of SMEs. Also ensure sustainable development, maintain database on technology options, information about sources of technology, provide background information on technology required by SMEs, help in foreign collaborations and also provide financial syndication from banks and financial institutions.

(10) *SME Exchange*

Since SMEs play an important role in the economic growth of India, NSE and BSE have launched their respective SME Platform to facilitate SMEs.

(11) *Electronic Registration*

The MSME Ministry also proposes to create a common platform for electronic registration of SME enterprises. The registration will be done at the District Industry Centre under the state governments, the Central Government is willing to provide a common platform which can be used for e-filing of forms and registration.

Marketing Opportunities

Role of IT

- The outline marketing arena has experienced significant growth over the past few years, while traditional marketing has deteriorated mainly due to its higher costs, specifically for MSMEs which go for cost effective marketing.

Cloud Technology

- A lot of MSMEs who previously did not have the ability to scale due to their lack of IT-infrastructure now have the ability to do so because of the cloud. But the number of businesses that actually end up scaling will depend on the grade of innovation.

Social Media Marketing

- With online communities to generate exposure , opportunities and sales, the number-one advantage is generating exposure for the small businesses, followed by increasing traffic and building new business partnerships.

Emergence of Digital Marketing

- MSMEs can adopt digital marketing very quickly as it offers tremendous advantage to them at lower cost as compared to conventional marketing.

Challenges or change: Digital market opportunities for SMEs:

- Small and Medium Enterprises (SMEs) should know the challenges and changes of digital markets, represented by methods like electronic tendering in order to achieve competitiveness and access to international supply markets.
- Electronic tender portals can comprise many different hitches such as language barriers, lack of experience, diverse procedures and structures or legacy factors. Application forms or instructions are also often unclear and overly complex.
- Then again, electronic tender portals open a widely unrecognised door to approach new customers and markets especially for companies that have limited resources for sales and marketing activities.
- Therefore, operators of e-tendering portals have recognised the need for improved usability and easier access for SMEs. Additionally, SMEs themselves accepted the strategic use of digital procurement opportunities.

SMEs dealing with electronic tender services are as follows:

- (1) Personal contacts as a key success factor.
- (2) Marketable products and services.
- (3) Co-operations with potential business partners.
- (4) Strengthen competences of SMEs.

Transfer of Operations to Supplement Venure

Tough labour laws, poor productivity of organized labour, poor patent protection and absence of product patent, extreme Customs, Excise Duty and Sales Tax Controls, stringent health, safety and environmental pollution controls, stricter quality requirements of the Originating Company made big industries transfer some of their operations to supplier's premises.

Emergence of Japanese total quality practices including Quality Circles, JIT Inventory Management , Kaizan , Kanban, 1984 Philips Crosby's Quality Improvement Process, 1986 ISO Standards, Malcolm Baldrige Quality Management Model of 1987, GE's Six Sigma Methodolgy.

Conclusion

The SME sector has performed extremely well and enabled our country to attain wide-ranging events of industrial amplification and diversification.

This sector has made significant contribution to income generation, employment generation and economic growth. The promotion and development of SME sector depends upon improving communication, investment in technological upgradation, R&D initiatives, developing human resources, improving credit flows, developing better marketing and distribution channels, ensuring efficient after sales services.

Small Industries Development Organisation (SIDO) is the apex organization under the ministry that provides a comprehensive range of common facilities, technology support services, marketing assistance, etc. The National Small Scale Industries Corporation Ltd. was set up with a view to promoting, aiding and fostering the growth of small scale industries in the country with focus on commercial aspects of these functions. NSIC continues to implement its various programs and projects throughout the country to assist SME units.

Role of Company Secretary

The role of company secretary in SME Sector is immense right from inception to the listing of IPO on SME (BSE/NSE). He/she can take care of various compliances connected to MSME ACT, 2006 & other applicable statutes. He/she can also help & also act as a catalyst for arranging institutional and bank finance for working capital etc. He/she can render assistance in promoting and managing the SME companies and provide day to day guidance to the entrepreneurs. He /she can perform secretarial /legal functions including board approvals, compiling of minutes, research and budgeting, approvals from regulatory bodies and filing of documents, listing with stock exchanges ,settling investor's grievances, allotments, transfers/ transmission of shares, maintenance of statutory records, devising investment policies. He/she can undertake internal audit. He/she can act as an arbitrator (as per alternative disputes resolution) He/she can establish liaison with Government & related agencies. He /she can develop BPO,KPO & LPO (business process outsourcing , knowledge process outsourcing & legal process outsourcing to aid and support the SMEs.

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THE COMPANY SECRETARY AND THE MSME SECTOR

CA RAJKUMAR S ADUKIA*

Introduction

No longer is the Indian Company Secretary bound by geographical boundaries. Technology and globalization has made the world into a small village.

Our profession commands a very high degree of respect in society and if we are to continue to live up to these expectations, we need to constantly develop our professional skills. This is indeed a never-ending process. Evolution never ever stops.

The Company Secretary is a 'Sutradhar' in the true sense of the term. Sutra, meaning 'solution; trick', the origin of the word sutradar (troubleshooter; problem-solver) dating back to Lord Krishna as the original problem-solver and saviour. The Company Secretary is a vital link between the company and its Board of Directors, shareholders, Government and Regulatory Authorities.

The profile of a Company Secretary has catapulted to a professional with a high-level of managerial skill with multi-disciplinary talent. He/She is now looked upon as a complete business provider. Improved information technology is enabling them to automate the more mundane tasks, allowing them time to develop their skills and further their knowledge in all areas of business.

With the country liberalizing its policies and approach, opportunities are expected to grow further and the profession is likely to be more challenging and demanding. The emphasis is on consolidating the quality of knowledge, skills and capacities that the profession possesses.

The Company Secretary is being reinvented and is assuming a comprehensive portfolio and a dash of glamour. Nothing is permanent except Change, and therefore VISION 2020 - TRANSFORM, CONFORM AND PERFORM. In tomorrow's world knowledge will be power.

Role of Company Secretary in Growth of MSME Sector

The development of the micro, small and medium enterprises (SME) sector is on the priority of Government Agenda. As per the Results-Framework Document (RFD) for Ministry of Micro, Small and Medium Enterprises (2012-2013), the Mission of the government is to –

* B.Com (Hons.), FCA, ACS, ACMA, LL.B., M.B.A., Dip in IFRS (UK), Dip in LL & LW

“Promote growth and development of globally competitive Micro, small and Medium Enterprises, including Khadi, Village and Coir industries, in cooperation with concerned Ministries / Departments, State Governments and other stakeholders by providing support to existing enterprises and encouraging creation of new enterprises. To endeavor to achieve a cumulative growth of 40%-50% in the number of registered enterprises by the end of 12th Plan and enhance this sector's contribution to GDP from the present 8% to 10% by the end of 12th Plan.”

The Company Secretaries as financial advisors are key players in the SME Sector. They play an important role in educating the promoters and management of the SMEs and also perform the following functions:

1. Help large scale enterprises form systems to ensure that they comply with the deadlines for payment of any goods or services supplied by MSMEs.
2. Counselling of MSMEs for the rights and benefits available to them.
3. Advisory role in formation, registration, taxation and foreign direct investment.
4. Assistance in compliance with the technicalities laid down by the MSMED Act 2006 itself like:
 - Classification of industries
 - Registration under the Act
 - Procedure of Filing of Entrepreneurs Memorandum
 - Disclosure Requirement.
5. MSMEs even though small in size, are an enterprise, and a huge list of laws of the country become applicable to them. The entrepreneurs may not necessarily have such technical knowledge and expertise to comply with the innumerable requirements expected of the MSMEs. The Company Secretaries being aptly equipped with their varied knowledge are the ideal person to assist the MSMEs in this respect.
6. Assistance in obtaining several clearances or permissions depending upon the nature of unit and products manufactured.

Worldwide, the micro and small enterprises have been accepted as the engine of economic growth and for promoting equitable development. The micro, small and medium enterprises constitute over 90% of total enterprises in most of the economies and are credited with generating the highest rates of employment growth and account for a major share of industrial production and exports.

Micro, small and medium enterprises are also referred to as Small and medium enterprises or SMEs, and small and medium-sized businesses or SMBs in some countries.

The abbreviation SME occurs commonly in the European Union and in international organizations, such as the World Bank, the United Nations and the WTO. The term small and medium-sized businesses or SMBs is predominantly used in the United States of America (USA).

In South Africa the term SMME for Small, Medium and Micro Enterprises is used. Elsewhere in Africa, they use MSME for Micro, Small and Medium Enterprises.

In India, the sector is generally referred to as the Micro, Small and Medium Enterprises (MSMEs). MSMEs play a pivotal role in the overall industrial economy of the country. In recent years the MSME sector has consistently registered higher growth rate compared to the overall industrial sector. The major advantage of the sector is its employment potential at low capital cost.

Development and Administration of MSMEs

In India the Micro, Small and Medium Enterprises Development (MSMED) Act, 2006 (which has come into force from 2nd October, 2006), is the main legislation governing MSMEs. With the enactment of MSMED Act, 2006, the concept of “enterprise” and a classification of enterprises on the basis of investment into Micro, Small and Medium were introduced.

The administration of the MSME sector falls under the jurisdiction of the Ministry of Micro, Small and Medium Enterprises (Sukshma Laghu Aur Madhyam Udyam Mantralaya), of the Government of India.

It designs and implements policies and programmes through its field organisations and attached offices for promotion and growth of MSME sector.

The Office of Development Commissioner (Micro, Small and Medium Enterprises) functions as the nodal Development Agency under the Ministry of Micro, Small and Medium Enterprises (MSME). It is the apex body to advise, coordinate and formulate policies and programmes for the development and promotion of the MSME Sector. The office also maintains liaison with Central Ministries and other Central/State Government agencies/organisations financial institutions.

The Development Commissioner (MSME) have a network of:

- 30 MSME-Development Institute (MSME-DI),
- 28 Br. MSME-Development Institute (Br. MSME-DI),
- 4 MSME-Testing Centres (MSME-TCs),
- 7 MSME-Testing Stations (MSME-TSs),
- 21 Autonomous bodies which include 10 Tool Rooms (TRs) and Tool Design Institutes (TDI)
- 4 MSME-Technology Development Center(MSME-TDC),
- 2 MSME-Technology Development Center-Footwear(MSME-TDC),
- 1 Electronics Service & Training Centre (ESTC),
- 1 Institute for Design of Electrical Measuring Instruments (IDEMI)
- 2 National Level Training Institutes, and
- 1 Departmental Training Institute and
- 1 Production Center.

Importance of MSME Sector

The role of micro, small and medium enterprises (MSMEs) in the economic and social development of the country is well established. As per the Report of the Working Group on Micro, Small and Medium Enterprises (MSMEs) Growth for 12th Five Year Plan (2012-2017), the sector accounts 45% of the manufacturing output and 40% of total exports of the country. The sector provides employment to about 69 million persons through 26 million enterprises throughout the country. Over 6000 products ranging from traditional to high-tech items are being manufactured by the MSMEs in the country. The labour to capital ratio in MSMEs and the overall growth in the sector is much higher than in the large industries. The geographic distribution of the MSMEs is also more even. Thus, MSMEs are important for the national objectives of growth with equity and inclusion.

Over the years, the small scale sector in India has progressed from the production of simple consumer goods to the manufacture of many sophisticated and precision products like electronics control systems, micro wave components, electro medical equipments, etc. The process of economic liberalization and market reforms has further exposed these enterprises to increasing levels of domestic and global competition.

The MSME sector in India is highly heterogeneous in terms of the size of the enterprises, variety of products and services produced and the levels of technology employed. While one end of the MSME spectrum contains highly innovative and high growth enterprises, more than 94% of MSMEs are unregistered, with a large number established in the informal or unorganized sector. The sector has a high growth potential and performs a critical role in the manufacturing and value chains. Micro, small and medium enterprises (MSME) sector is characterized by low investment requirement, operational flexibility and location wise mobility.

As per the quick estimates of 4th All-India Census of MSMEs, the number of enterprises is estimated to be about 26 million and these provide employment to an estimated 60 million persons. Of the 26 million MSMEs, only 1.5 million are in the registered segment while the remaining 24.5 million (94%) are in the unregistered segment.

The State-wise distribution of MSMEs show that more than 55% of these enterprises are in 6 States, namely, Uttar Pradesh, Maharashtra, Tamil Nadu, West Bengal, Andhra Pradesh and Karnataka. Further, about 7% of MSMEs are owned by women and more than 94% of the MSMEs are proprietorships or partnerships.

MSMEs in the country manufacture over 6,000 products. Some of the major subsectors in terms of manufacturing output are food products (18.97%), textiles and readymade garments (14.05%), basic metal (8.81%), chemical and chemical products (7.55%), metal products (7.52%), machinery and equipments (6.35%), transport equipments (4.5%), rubber and plastic products (3.9%), furniture (2.62%), paper and paper products (2.03%) and leather and leather products (1.98%).

The importance and contribution of the SME sector to the economic growth and prosperity is well established. Towards this, Government's policy initiatives like enactment of the Micro Small and Medium Enterprises Development (MSMED) Act, 2006, pruning of reserved SSI

list, advising Financial Institutions to increase their flow of credit to the SME sector, are all initiatives towards boosting entrepreneurship, investment and growth. Reservation of items for exclusive manufacture in MSME sector statutorily provided for the Industries (Development and Regulation) Act, 1951, has been one of the important policy measures for promoting this sector.

Major Challenges concerning the MSME Sector

As per the Report of the Subgroup on Unorganized Sector (of the Working Group on MSMEs Growth during 12th Plan), although Indian MSMEs are a diverse and heterogeneous group, they face some common problems, which are briefly indicated below:

- Lack of availability of adequate and timely credit;
- High cost of credit;
- Collateral requirements;
- Limited access to equity capital;
- Problems in supply to government departments and agencies;
- Procurement of raw materials at a competitive cost;
- Problems of storage, designing, packaging and product display;
- Lack of access to global markets;
- Inadequate infrastructure facilities, including power, water, roads, etc.;
- Low technology levels and lack of access to modern technology;
- Lack of skilled manpower for manufacturing, services, marketing, etc.;
- Multiplicity of labour laws and complicated procedures associated with compliance of such laws;
- Absence of a suitable mechanism which enables the quick revival of viable sick enterprises and allows unviable entities to close down speedily; and
- Issues relating to taxation, both direct and indirect, and procedures thereof
- Lack of Social Security

A prominent drawback of the MSME sector is that a predominant number (94%) of the enterprises are in the unorganized sector. Due to this, there is lack of reliable and updated database and it hampers monitoring of development initiatives and formulation of appropriate schemes to meet the differential needs of the heterogeneous profile of the enterprises.

One of the major problems facing these enterprises is the access to equity and credit. Most of the time, the equity is coming from savings and loans from friends and relatives rather than through banking systems. Very often, the credit is coming from operations or domestic savings rather than established systems of cheap banking credit for working capital.

This sector also has poor paying capacity and therefore faces shortage of skilled manpower resulting in absence of managerial capabilities, marketing channels and brand building capacity.

The Working Group on Micro, Small and Medium Enterprises (MSMEs) Growth for 12th Five-Year Plan (2012-2017)

To identify issues preventing the growth of the sector, the Prime Minister set up a Task Force in 2009. Further, the Planning Commission constituted a Working Group on MSMEs Growth for the 12th Five Year Plan (2012-2017) under the Chairmanship of Secretary, (MSME) with 46 members representing various Ministries/ Offices of Government of India, representatives of selected State Governments and Industry Associations, NGOs etc. in May 2011. The Working Group submitted its Report on 13th January 2012.

The Working Group classifies the issues relating to growth of MSME sector under six important verticals viz. (i) Credit & Finance, (ii) Technology, (iii) Infrastructure, (iv) Marketing & Procurement, (v) Skill Development & Training and (vi) Institutional Structure, to provide theme based focus while devising any strategy for the sector.

The Working Group has made various recommendations to facilitate growth of MSME sector and separate recommendations for the Khadi & Village Industries and Coir Sector also. Similarly, concerns of unorganized sector and special areas & groups have also been given due consideration while formulating any programme /scheme under above six major verticals.

Also, the Working Group has noted that the National Manufacturing Policy envisages increasing the sectoral share of Manufacturing in GDP to 25 % over the next decade and generating additional 100 million jobs in manufacturing sector through an annual average growth rate of 12-14 % in manufacturing sector. MSME sector being the major base of manufacturing sector in India, with its contribution of over 45% in the overall industrial output, the Working Group is of the view that the achievement of the NMP targeted growth of the manufacturing sector would necessitate substantial enhancement of the growth rate of MSME sector during the 12th Plan from the current growth rate of 12-13%. This would call for quantum jump in plan allocation for the sector during the 12th Plan to address major bottlenecks facing the sector.

Summary of Recommendations of Working Group to facilitate growth of MSME Sector

1. Improving the availability of finance by way of facilitating access to bank credit, opening alternate routes for equity funding through angel funding, venture capital, private equity etc. as well as facilitating entry to capital markets through IPOs and specialized exchanges for SMEs.
2. Improving marketing and procurement facilities through preferential treatment for MSMEs in public procurement, development of B2B portals and establishing cluster based marketing networks.
3. Improving the skill level of work force through harmonization of training programmes

under the Ministry with the mission of the Prime Minister's National Council for Skill Development.

4. Improving infrastructure for the MSME sector by ensuring availability of work places, common facility centres and specialized growth centres for start ups.
5. Improving technology and innovation through continuation of National Manufacturing Competitiveness Programme (NMCP), facilitating technology transfer and creation of intellectual properties and wide spreading adoption of information and communication technologies.
6. Facilitating entry of young/first generation entrepreneurs through entrepreneurial support, access to venture/equity funding, ensuring collateral free credit, providing ready-to-move workplaces, enabling entrepreneur friendly policy environment and finally ensuring access to market.
7. Developing an institutional framework for handholding of the Micro & Small entrepreneurs to move up the value chain and facilitating global competitiveness of the small & medium enterprises.
8. Projecting Khadi as eco-friendly and heritage product and leveraging KVI sector to achieve 11% growth in khadi, 13% growth in V.I. production and 12% growth in the flagship scheme PMEGP (Prime Minister's Employment General Programme).
9. Acquiring new dimensions for Coir Sector through diversification of products and market as also technological interventions to enhance quality and competitiveness so as to double the exports from present level of Rs.800 crore within 5 years.

The Working Group's Game Changers

While all the recommendations of the Working Group are considered to be important to facilitate growth of the MSME sector during the 12th Five Year Plan period, the Group specifically mentions the following Game Changers in the recommendations, implementation of which will be crucial for the ski-jumping of MSME Sector in the global market place:

Finance

- Operationalization of SME exchanges for enabling access to Equity Finance

Technology

- Scheme for acquisition and up-gradation of technology

Infrastructure

- Developing clusters of excellence
- Setting up of 100 Tool Rooms and Process cum Products Development Centre (PPDCs)

Marketing

- Procurement policy for Goods/services from MSEs by the Government Deptts. and Central PSUs.

- B2B International portal.
- Enabling global footprints of MSMEs
- Leveraging Defence Offset Policies in favour of MSMEs

Skill Development

- Revamped Skill Development & Capacity Building Programme.
- Encouraging young/ first generation entrepreneurs by upscaling PMEGP and other programmes.

Institutional Structure

- Strengthening of Institutions – MSME-DIs, EDIs and KVI Institutions
- Application of E-tools in promotional and regulatory matters for facilitating easy entry.
- Real time Statistical & Policy Analysis through strengthening of Database

Items reserved for exclusive manufacture by MSME Sector

The present policy of encouraging growth of micro and small scale industries is based on several promotional measures - one of these is reservation of products for exclusive manufacture in the small scale sector in areas where there is techno-economic justification for such an approach. Large/Medium units can, however, manufacture such reserved items provided they undertake to export 50% or more of their production.

The issue of reservation/dereservation of product is examined on a continual basis by an Advisory Committee on Reservation constituted under the I(D&R) Act 1951, which is presently headed by the Secretary (MSME) as Chairman. Other Members of the Committee are Secretary (Commerce), Secretary (IP&P), Advisor (VSI) Planning Commission with Additional Secretary & DC(MSME) as Member Secretary.

**List of Items Reserved for Exclusive Manufacture
by Micro and Small Enterprise Sector
(As on 30 July 2010)**

<i>S.No.</i>	<i>S.No. (As per Gazette Notification)</i>	<i>Product Code</i>	<i>Name of the Product</i>
		20-21	Food and Allied Industries
1.	3	202501	Pickles & chutneys
2.	7	205101	Bread
3.	11	21100102	Mustard Oil (except solvent extracted)
4.	13	21100104	Ground nut oil (except solvent extracted)

40th National Convention of Company Secretaries

<i>S.No.</i>	<i>S.No. (As per Gazette Notification)</i>	<i>Product Code</i>	<i>Name of the Product</i>
		27	Wood and Wood Products
5.	47	276001	Wooden furniture and fixtures
		28	Paper Products
6.	79	285002	Exercise books and registers
			Other Chemicals and Chemical Products
7.	253	305301	Wax candles
8.	308	314201	Laundry soap
9.	313	317001	Safely matches
10.	314	318401	Fire works
11.	319	319902	Agarbatties
			Glass and Ceramics
12.	335	321701	Glass bangles
		33-35	Mechanical Engg. excluding Transport Equipment
13.	364	340101	Steel almirah
14.	394	341004	Rolling shutters
15.	402	34200602	Steel chairs - All types
16.	404	34200702	Steel tables - All other types
17.	409	342099	Steel furniture - All other types
18.	428	343302	Padlocks
19.	447A	345207	Stainless steel utensils
20.	474	345202	Domestic utensils – Aluminium

Programmes and Schemes for MSME sector

1. Schemes implemented directly by the Ministry of MSME
2. Schemes implemented through National Small Industries Corporation (NSIC)
3. Schemes implemented through Khadi & Village Industries Commission (KVIC)
4. Schemes implemented through Coir Board
5. Schemes implemented by the Office of the DC (MSME)

Implemented directly by Ministry

- Scheme for International Cooperation
- Market Development Assistance on Production Scheme
- Scheme for Assistance to Training Institutions
- Scheme of Surveys, Studies and Policy Research
- Scheme of Fund for Regeneration of Traditional Industries (SFURTI)
- Rajiv Gandhi Udyami Mitra Yojana (RGUMY)

Implemented through NSIC

- Marketing Assistance Scheme
- Performance and Credit Rating Scheme

Implemented through KVIC

- Prime Minister's Employment Generation Programme (PMEGP)
- Rural Employment Generation Programme (REGP)
- Scheme of Fund for Regeneration of Traditional Industries (SFURTI)
- Export Incentive Scheme
- Interest Subsidy Scheme

Khadi Schemes

- Insurance for Khadi Artisans
- Scheme for enhancing productivity & competitiveness of Khadi Industry & Artisans
- Workshed Scheme for Khadi Artisans and Schemes under Science & Technology
- Mahatma Gandhi Institute for Rural Industrialization (MGIRI)
- S&T formats for agreement
- R&D activities under KVIC-Technical Interfaces
- Scheme for "In House Test Laboratory" for Khadi and Village Industries
- Scheme for implementation of "ISO 9001-2000"
- Scheme for "New R & D Projects"

Implemented through Coir Board

- Rejuvenation, Modernization and Technology Upgradation of the Coir Industry
- Scheme of Fund for Regeneration of Traditional Industries (SFURTI)
- Skill Upgradation and Quality Improvement Scheme
- Science and Technology Scheme
- Export Market Promotion Scheme
- Domestic Market Promotion Scheme
- Trade and Industry Related Functional Support Services Scheme
- Welfare Measures Scheme

- Sub-schemes:
 - External Market Development Assistance for the period 2007-08 to 2010-2012
 - Marketing Development Assistance Scheme (Domestic)
 - Personal Accident Insurance Scheme for Coir workers

Schemes implemented by the Office of the DC(MSME)

- National Manufacturing Competitiveness Programme (NMCP) Schemes Under XI Plan
- Micro & Small Enterprises Cluster Development Programme (MSE-CDP)
- Credit Linked Capital Subsidy Scheme for Technology Upgradation
- Credit Guarantee Scheme
- ISO 9000/ISO 14001 Certification Reimbursement Scheme
- Market Development Assistance Scheme for Micro/ Small manufacturing Enterprises/ Small & Micro exporters (SSI-MDA)
- Mini Tool Rooms
- Assistance to Entrepreneurship Development Institutes
- Scheme of Micro Finance Programme
- Scheme of National Award

International Co-operation

Memorandum of Understandings (MOUs) entered by Ministry of Micro, Small and Medium Enterprises

<i>Country</i>	<i>Partner Ministry/Organisation</i>	<i>Date signed</i>
Republic of Indonesia	MOU between the Ministry of MSME of the Republic of India and Ministry for Cooperatives and Small and Medium Enterprises of the Republic of Indonesia	25/01/2011
Republic of Mozambique	Memorandum of Understanding on Cooperation in the field of Micro, Small and Medium Enterprises, Republic of India and The Ministry of Industry and Commerce, Republic of Mozambique	30/09/2010
Republic of Korea	MOU between Ministry of MSME of the Republic of India and Small and Medium Business Administration of the Republic of Korea	18/06/2010
Republic of Botswana	MOU between the Government of the Republic of India and Government of the Republic of Botswana on Cooperation in the field of Small, Medium and Micro Enterprises	17/06/2010

The Company Secretary and the MSME Sector

<i>Country</i>	<i>Partner Ministry/Organisation</i>	<i>Date signed</i>
Arab Republic of Egypt	Joint Active Plan on Cooperation in the field of Micro, Small and Medium Enterprises between the Ministry of Trade and Industry of Arab Republic of Egypt and the Ministry of Small, Medium and Micro Enterprises of the Republic of India	29/10/2009
Cote d'Ivoire	The Ministry of Small Scale Industries of India and Ministry of Industry and Promotion of Private Sector of Cote d'Ivoire	14/02/2007
Government of Tunisia	Cooperation agreement in the field of Small and Medium-Sized Enterprises between the Government of the Republic of Tunisia and the Government of the Republic of India	08/02/2007
Government of Romania	The Ministry of Small Scale Industries of India and The National Agency for Small and Medium-Sized Enterprises and Co-Operatives of Romania	23/10/2006
Republic of Rwanda	The Ministry of Commerce, Industry, Investment Promotion, Tourism and Cooperatives, Republic of Rwanda	30/08/2006
United Mexican States	The Secretariat of Economy of the United Mexican States	27/03/2006
The Government of Republic of Uzbekistan	The Government of Republic of Uzbekistan	05/04/2005
Government of the Republic of Lesotho	The Government of the Republic of Lesotho	10/09/2004
Democratic Socialist Republic of Sri Lanka	Democratic Socialist Republic of Sri Lanka	27/01/2004
Democratic Republic of Algeria	Ministry of Small and Medium Size Enterprises and Handicraft in the People's Democratic Republic of Algeria	10/10/2003
Republic of Sudan	Government of the Republic of Sudan	09/04/2000

International Cooperation Scheme

Technology infusion and/or upgradation of Indian micro, small and medium enterprises (MSMEs), their modernisation and promotion of their exports are the principal objectives of assistance under the International Cooperation Scheme. The Scheme would cover the following activities:

- (i) Deputation of MSME business delegations to other countries for exploring new areas of technology infusion/upgradation, facilitating joint ventures, improving market of MSMEs products, foreign collaborations, etc.
- (ii) Participation by Indian MSMEs in international exhibitions, trade fairs and buyer-seller meets in foreign countries as well as in India, in which there is international participation.
- (iii) Holding international conferences and seminars on topics and themes of interest to the MSME.

Opportunities in MSME Sector

1. *Technology and Innovation*

Entrepreneurship is driven by technology and innovation. Presently, the MSME sector is associated, in public perception, with low quality standards. It is envisioned that the MSME sector will be upgraded through modern and new technologies to achieve global quality standards. Niche markets will be identified and developed for MSME products, including khadi and coir products.

Technology will be the foremost factor for enhancing the global competitiveness of Indian MSME Sector. There will be tremendous opportunity in technology acquisition and support. There are emerging innovative sectors of bio-tech, nano-tech, defence, civil aviation, aero-space, homeland and internal security, items etc.

The Working Group on MSMEs Growth for 12th Five Year Plan identifies that the immediate challenge is development of appropriate technologies for various manufacturing processes which will lead to substantial reduction in cost of manufacturing by enhancing labour productivity, reducing material wastage and minimising energy consumption. Such technologies could be developed by close interaction of R&D institutions with industries and through innovative projects of techno-preneurs. Accordingly, a multi-tier support system may be required for inducing technology based competitiveness of the sector with the collaboration of government, industry clusters, industry associations and private R&D institutions.

2. *Skilled Manpower*

India has a large capital of human resources. There is tremendous opportunity in the MSME sector for skilled manpower. Skill development and training of existing workers and entrepreneurs is necessary for enhancing managerial capabilities, brand building capacity and developing new marketing channels.

The Working Group on MSMEs Growth for 12th Five Year Plan has recommended some actions in this regard viz :

- Up-scaling of training capacity of the Ministry of Micro, Small and Medium Enterprises, through public private partnership mode.
- Besides existing programmes for entry level/new entrepreneurs, training programmes also be conducted for skill up-gradation of Chief Executives/ Owners of the MSMEs with some element of subsidy from the government.
- Launching of web-based management information system to ensure quality of training programmes conducted and transparency in the process of selection-registration-administration of the trainees. The respective portal should also host the details of the training curriculum, trainer/faculty and process of training.
- Setting up of a virtual SME University has also been recommended. The proposed University will standardise the training curriculum, certify the trainers and certify the trainees on completion of the programme. Ultimately, the University will be a repository of the details of the persons trained under various programmes of the Ministry as well as other Ministries and function as a virtual Employment Exchange.

3. *Credit and Finance Availability*

Credit availability in the MSME sector is a major cause of concern. Apart from access to bank credit, alternate routes for equity funding through angel funding, venture capital, private equity etc. as well as facilitating entry to capital markets through Initial Public Offers (IPOs) and specialized exchanges for SMEs is on the cards.

The Working Group on MSMEs Growth for 12th Five Year Plan has proposed to set up a SME exchange. The SME Exchange has already operationalised. The success of the MSME listings on the MSME Exchange would depend a lot on the final investors of the Exchange. The final investors comprise of (i) High – net worth individuals and corporate, (ii) Qualified institutional buyers (QIBs) like Venture Capital Funds, Private Equity funds, etc and (iii) Banks. The Government proposes to attract these investors by appropriate regulatory framework and other incentives.

4. *Carbon Credits for MSMEs*

Public awareness of the threat of climate change has risen sharply in the last couple of years and an increasing number of businesses, organizations and individuals are looking to minimize their impact on the climate. Reaping the benefits of the new instruments like carbon credit, environment and ecological balance have gained global significance. The MSME sector is required to be empowered to face the future challenges.

The MSMEs can implement technological improvement programmes to avail the benefits of carbon credits. However the MSMEs will need the help of professionals in the field of carbon credits and environmental issues and experts from Government sector to help them to get the benefit of carbon credit.

SME LISTING – A PERSPECTIVE

DEEPAK SHARMA & MAHAVIR LUNAWAT*

Overview

Micro Small and Medium Enterprises (MSMEs, also called generally as SMEs) are the backbone of a fast developing economy and India is no exception. The Indian SMEs contribute significantly to the GDP, exports and employment. As per Government statistics, MSMEs provide 45% of the manufactured output, and accounts for 40% of the Country's exports. As an estimate, there exist about 2.6 crore MSMEs which are the biggest generators of employment in the economy.

Special role for SMEs were earmarked in India with the advent of planned economy from 1951 and through subsequent industrial policies. The Micro, Small and Medium Enterprises Development (MSMED) Act, 2006 provided for facilitating the promotion, development and enhancing the competitiveness of MSMEs and for the related matters.

In 2010, the Prime Minister's Task Force recommended setting up a dedicated stock exchange Platform for MSMEs. SEBI vide circular dated May 18, 2010 laid down regulations for setting up a stock exchange trading platform or an 'SME Exchange'.

Some Well-known SME Exchanges

<i>Country</i>	<i>SME Exchange</i>
UK	AIM (Alternate Investment Market)
Canada	TSX Ventures
Hong Kong	GEM (Growth Enterprise Market)
Japan	MOTHERS (Market of the high-growth and emerging stocks)
Singapore	Catalist
China	Chinext

An 'SME Exchange' is a stock exchange dedicated for listing and trading of shares of SMEs which otherwise find difficult to get listed on the main exchanges. SME exchanges or

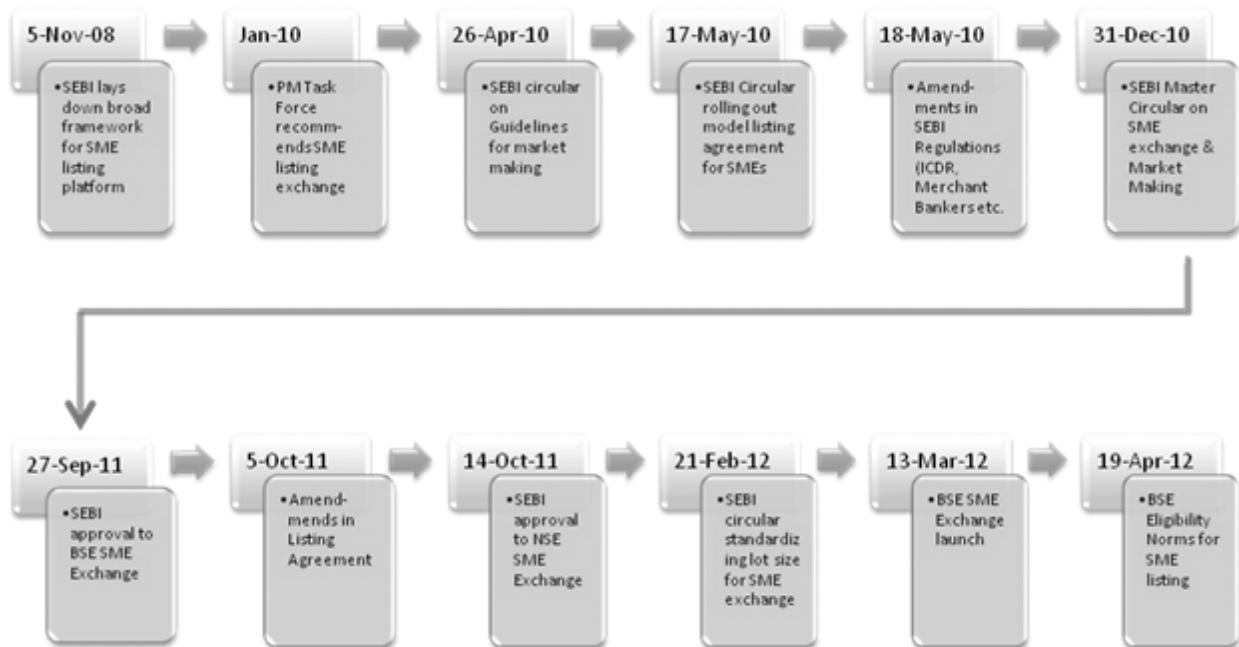
* Directors, Sarthi Capital Advisors, Mumbai.

trading platforms are prevalent globally albeit known by different names, such as 'Alternate Investment Markets' or 'Growth Enterprises Market', 'SME Board' etc.

In India, "SME Exchange" is defined in Chapter XB of the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009 ('SEBI ICDR Regulations') as a trading platform of a recognized stock exchange or a dedicated exchange permitted by SEBI to list the securities issued in accordance with Chapter XB of SEBI (ICDR) Regulations and this excludes the Main Board (which is in turn is defined as a recognized stock exchange having nationwide trading terminals, other than SME exchange).

Both BSE and NSE have launched their respective platforms for SMEs; MCX too is gearing up for SME Exchange. The move aims at providing an opportunity to SME entrepreneurs to raise growth capital and reap benefits of listed space. Both BSE and NSE are leveraging their existing equity platforms for SME Exchange Platforms.

SME Listing Evolution



Regulatory Norms for SME Listing

SEBI Regulations - Highlights

- An issuer with post issue face value capital of up to Rs. 10 crores is covered under the SME Exchange. An issuer with post issue face value capital between Rs. 10 crores to Rs. 25 crores may get listed on either SME Exchange or main board. An issuer with

post issue face value capital exceeding Rs. 25 crores cannot be listed on an SME Exchange and needs to approach main board for listing.

- Suitable provisions for migration to/ from main board from/ to SME Exchange.
- The minimum application and minimum trading lot has been kept at Rs. 100,000.
- All the issues will be 100% underwritten, and merchant bankers to the issuer shall be underwriting 15% in their own account.
- Market making is compulsory for all scrips listed and traded on SME Exchange. All existing trading members are eligible to participate without any further registration.
- The merchant bankers shall be responsible for ensuring market making for a minimum period of 3 years.
- Minimum number of investors at the time of IPO is 50.

Key Requirements and Eligibility norms of Stock Exchanges - Synopsis

<i>Norms</i>	<i>BSE</i>	<i>NSE</i>
Post Issue Capital (Face Value)	<ul style="list-style-type: none"> — Maximum of Rs. 25 crores — Minimum of Rs. 1 crores 	
Track Record	<ul style="list-style-type: none"> — Net Tangible Assets of Rs. 1 crores — Net Worth (Excluding Revaluation Reserves Rs. 1 crore or Rs. 3 crores, if no track records. — Track record of distributable profits for at least 2 years out of preceding 3 completed financial years. 	<ul style="list-style-type: none"> — Track record of at least 3 years. — Positive cash accruals (EBDT) from operations and positive net worth for at least 2 financial years preceding the application. — In case the above conditions are not fulfilled, Exchange Authority (MD & Joint MD) to decide.
Other Requirements	<ul style="list-style-type: none"> — Mandatory facilitation of trading in Demat Securities. — Certificate that no winding up petition or reference is been made to BIFR. — Mandatory Corporate Websites. — Promoters to attend to interview with Listing Advisory Committee of BSE. 	<ul style="list-style-type: none"> — Mandatory facilitation of trading in Demat Securities. — Certificate that no winding up petition or reference has been made to BIFR. — Mandatory Corporate Website. — Promoters to attend to interview with Listing Advisory Committee. — Additional Certification/ Disclosures on litigation, etc.

Benefits of SME Listing

— Funding Convenience

- *Access to capital and financing opportunities* : What can be attributed more as a benefit of listing than the enormous financing opportunities that it presents both in terms of raising equity and the beneficial treatment in terms of cost at which funds can be raised. SME listing provides with the opportunity of raising funds and reaching to the investor class which otherwise may not be possible.
- *Avoid unlisted space discounting* : In valuing a company, investors do discount an unlisted company or non-transferable instrument because of limited mobility, lack of visibility and other similar perceptions. By listing, an SME can avoid such discounting.
- *M&A currency*: Listing offers an incentive to incorporate on a lookout for M&As. Listed securities act as a viable M&A currency and help avoid the cost and time involved in M&A transactions.
- *Entry/ Exit platforms for PE/ Other Investors* : The strategic investor community favors the investees having access to capital markets. Listing not only offers investors the flexibility in terms of entry and exit, but also base-level confidence.

— Tax Benefits

- *No long term capital gains* : Under Income-Tax Act, 1961, the long term capital gains are exempt on transfer of listed shares held for more than 12 months. SME listing offers the opportunity to avail this exemption, subject of-course to the holding period of one year. Even, short term capital gains tax is payable at a reduced rate of 15% in case of shares are listed.
- *No tax on equity infusion in the company* : As per the Finance Act, 2012, a company is liable to tax on equity infusion, if the equity shares are issued to an investor other than a register venture fund at premium exceeding the fair price. Such a tax is not applicable in case the shares are listed.
- *No tax on distressed business purchase* : As per the Income-Tax Act, there lies a tax liability on the investor if the shares of an unlisted company are bought below its book net-worth. Such a tax incidence could be mitigated if the shares are listed.

— Other Benefits

- *Unlocking Value* : The value is often locked or not benchmarked for the companies not having trading platform. The companies listed on an exchange are in a position to unlock / benchmark their fair value.
- *ESOPs - Talent retention tool* : ESOPs, typically, serve as a tool for retaining/ incentivizing the talent and also act as a wealth creator for employees. The benefits of listing can be attributed to unlocking the value of the company and making ESOPs effective, thus aiding to talent retention.
- *Visibility – Profile Building* : The companies listed in the stock exchange get recognition, as well as are followed by investors and analysts. Listing of a company provides a platform for recognition and visibility.

— *Corporate Governance – Internal Systems* : Though the requirements for a company listed on SME Exchange are not as stringent, but in it is adequately drawn up so as to incentivize the company for putting in place the internal control systems and corporate governance.

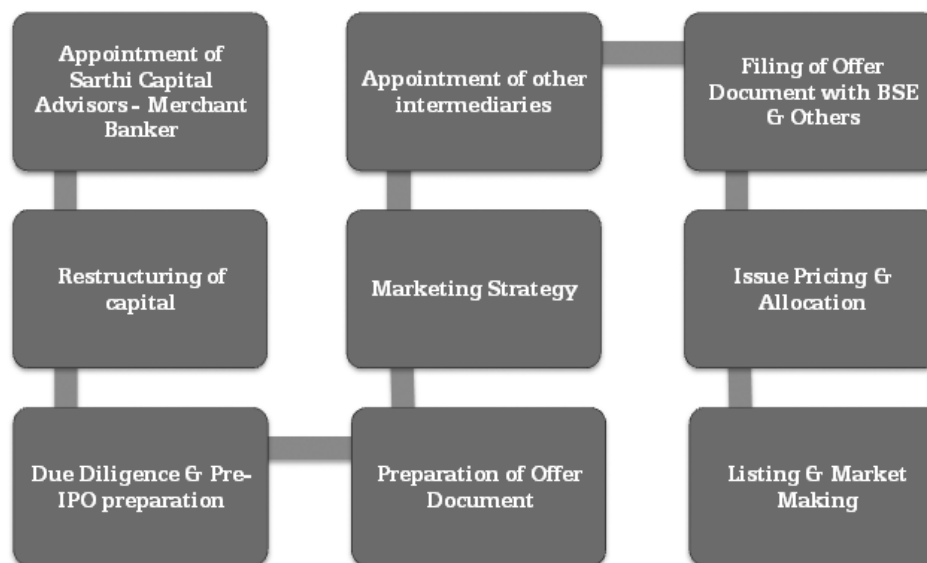
SME IPO Modes – Fixed Price & Book Building

Like any IPO, an SME IPO can also be made through either the fixed price method or book building method :

<i>Particulars</i>	<i>Fixed Price Issues</i>	<i>Book Building Issues</i>
Offer Price	Price at which the securities are offered and would be allotted is made known in advance to the investors	A 20 % price band is offered by the issuer within which investors are allowed to bid and the final price is determined by the issuer only after closure of the bidding.
Demand	Demand for the securities offered is known only after the closure of the issue	Demand for the securities offered, and at various prices, is available on a real time basis on the BSE website during the bidding period.
Payment	100 % advance payment is required to be made by the investors at the time of application.	10 % advance payment is required to be made by the QIBs along with the application, while other categories of investors have to pay 100 % advance along with the application.

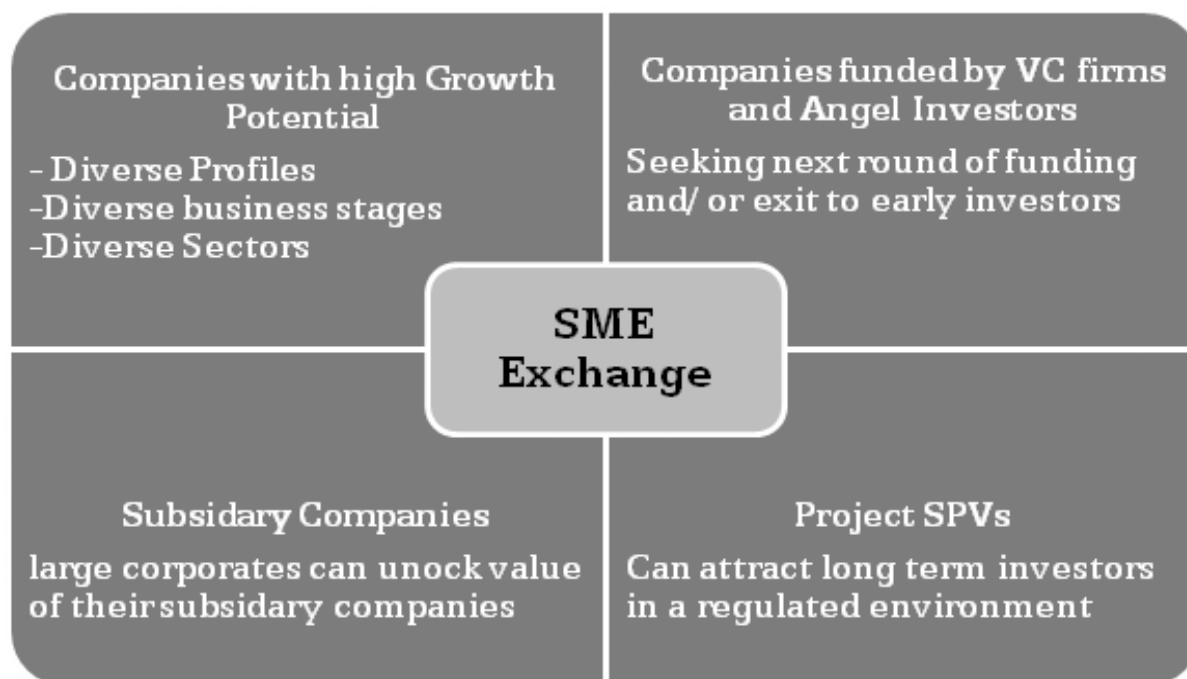
Source : BSE

Typical Process of an SME IPO



Concluding Remarks

Indian SMEs represent a diverse asset class of emerging companies from both traditional sectors and new age economy sectors like IT, ITES, organized retailing, education, entertainment, media, etc. representing the new and modern face of Indian entrepreneurs.



In recent years, several Indian companies scaled up their businesses rapidly providing high returns to the early stage investors. They have also demonstrated impressive management bandwidth by successfully managing high growth, cross border operations, and complex inorganic transactions. SME Exchange is expected to be an ideal platform for growing companies wishing to raise growth capital for capex, working capital, acquisitions, R&D, marketing and the like.

CHALLENGES AND OPPORTUNITIES FOR SME SECTOR

H KARUNAKAR PRABHU*

Introduction

Small and medium enterprise or small and medium-sized enterprise (SMEs, small and medium-sized businesses, SMBs and variations thereof) are companies whose personnel numbers fall below certain limits. The abbreviation "SME" is used in the European Union and by international organizations such as the World Bank, the United Nations and the World Trade Organization (WTO). The term "small and medium businesses" (or "SMBs") is predominantly used in the USA.

In Europe, EU member states have had individual definitions of what constitutes an SME.

For example, the definition in Germany had a limit of 255 employees, while in Belgium it could have been 100.

In United States, the Small Business Administration sets small business criteria based on industry, ownership structure, revenue and number of employees (which in some circumstances may be as high as 1,500, although the cap is typically 500). Both the US and the EU generally use the same threshold of fewer than 10 employees for small offices (SOHO).

Indian Concept

Micro-enterprise

A micro-enterprise is one where the investment in plant and machinery (their original cost excluding land, building and items specified by the Ministry of Small Scale Industries in its notification No. S.O. 1722(E) dated October 5, 2006) does not exceed Rs. 25 Lakhs.

Small enterprise

A small enterprise is one where the investment in plant and machinery (see above) is more than Rs. 25 Lakhs but does not exceed Rs.5 crores.

Medium enterprise

A medium enterprise is one where the investment in plant and machinery (see above) is more than Rs. 5 crores but does not exceed Rs.10 crores.

* ACS, Company Secretary in Practice.

The definition of MSMEs in the service sector is:

- Micro-enterprise: Investment in equipment does not exceed Rs.10 Lakhs.
- Small enterprise: Investment in equipment is more than Rs.10 Lakhs but does not exceed Rs.2 crores
- Medium enterprise: Investment in equipment is more than Rs.2 crores

The Indian micro- and small-enterprises (MSEs) sector plays a pivotal role in the country's industrial economy. It is estimated that in value, the sector accounts for about 39 percent of manufacturing output and about 33 percent of total exports. In recent years, the MSE sector has consistently registered a higher growth rate than the overall industrial sector. The major advantage of the MSE sector is its employment potential at a low capital cost. According to available statistics, the sector employs an estimated 31 million people in 12.8 million enterprises; labor intensity in the MSE sector is estimated to be nearly four times that of large enterprises.

The President under Notification dated 9th May 2007 has amended the Government of India (Allocation of Business) Rules, 1961. Pursuant to this amendment, Ministry of Agro and Rural Industries (Krishi Evam Gramin Udyog Mantralaya) and Ministry of Small Scale Industries (Laghu Udyog Mantralaya) have been merged into a single Ministry, namely, "MINISTRY OF MICRO, SMALL AND MEDIUM ENTERPRISES (SUKSHMA LAGHU AUR MADHYAM UDYAM MANTRALAYA)"

Worldwide, the micro small and medium enterprises (MSMEs) have been accepted as the engine of economic growth and for promoting equitable development. The major advantage of the sector is its employment potential at low capital cost. The labour intensity of the MSME sector is much higher than that of the large enterprises. The MSMEs constitute over 90% of total enterprises in most of the economies and are credited with generating the highest rates of employment growth and account for a major share of industrial production and exports. In India too, the MSMEs play a pivotal role in the overall industrial economy of the country. In recent years the MSME sector has consistently registered higher growth rate compared to the overall industrial sector. With its agility and dynamism, the sector has shown admirable innovativeness and adaptability to survive the recent economic downturn and recession.

As per available statistics (4th Census of MSME Sector), this sector employs an estimated 59.7 million persons spread over 26.1 million enterprises. It is estimated that in terms of value, MSME sector accounts for about 45% of the manufacturing output and around 40% of the total export of the country.

Micro, small and medium enterprises (MSME) sector has been recognised as an engine of growth all over the world. The sector is characterised by low investment requirement, operational flexibility, location wise mobility, and import substitution. In India, the Micro, Small and Medium Enterprises Development (MSMED) Act, 2006 is the first single comprehensive legislation covering all the three segments. In accordance with the Act, these

enterprises are classified in two:- (i) manufacturing enterprises engaged in the manufacture or production of goods pertaining to any industry specified in the first schedule to the Industries (Development and Regulation) Act, 1951. These are defined in terms of investment in plant and machinery; (ii) service enterprises engaged in providing or rendering of services and are defined in terms of investment in equipment.

India has a vibrant micro and small enterprise sector that plays an important role in sustaining the economic growth, by contributing around 39 per cent to the manufacturing output and 34 per cent to the exports in 2004-05. It is the second largest employer of human resources after agriculture, providing employment to around 29.5 million people (2005-06) in the rural and urban areas of the country. Their significance in terms of fostering new entrepreneurship is well-recognized. This is because, most entrepreneurs start their business from a small unit which provides them an opportunity to harness their skills and talents, to experiment, to innovate and transform their ideas into goods and services and finally nurture it into a larger unit.

Over the years, the small scale sector in India has progressed from the production of simple consumer goods to the manufacture of many sophisticated and precision products like electronics control systems, micro wave components, electro medical equipments, etc. The process of economic liberalization and market reforms has further exposed these enterprises to increasing levels of domestic and global competition. The formidable challenges so generated for them have led to a novel approach of cluster development for the sector. As a result, private and public sector institutions, both at the Central and State levels are increasingly undertaking cluster development initiatives.

CLUSTERS are defined as sectoral and geographical concentration of enterprises, particularly, small and medium enterprises, faced with common opportunities and threats which give rise to external economies; favour the emergence of specialized technical, administrative and financial services; create a conducive ground for the development of inter-firm cooperation to promote local production, innovation and collective learning. Clustering and networking has helped the small and medium enterprises in boosting their competitiveness. India has over 400 SME clusters and about 2000 artisan clusters.

It is estimated that these clusters contribute 60 per cent of the manufactured exports from India. Almost the entire gems and jewellery exports are from the clusters of Surat and Mumbai. Some of the small scale enterprise clusters are so big that they account for 90 per cent of India's total production output in selected products. For example, the clusters of Chennai, Agra and Kolkata are well known for leather and leather products.

The Government has been encouraging and supporting the sector through policies for infrastructural support, technology up gradation, preferential access to credit, reservation of products for exclusive manufacture in the sector, preferential purchase policy, etc. It has been offering packages of schemes and incentives through its specialized institutions in the form of assistance in obtaining finance; help in marketing; technical guidance; training and technology up gradation, etc.

Opportunities to SME Sector

The SME business market of India is large and bubbling with newer opportunities. Increased purchasing power and consumerism is what drives the business scenario in India. Thus, there is an opportunity for competitive advantage that can benefit investors and entrepreneurs to a large extent. An investment in any best small business opportunity promises lucrative returns and success in less time.

There are various reasons due to which the small scale business in India has witnessed a spurt of growth. Some of these factors are: -

1. Less Capital Intensive
2. Extensive Promotion & Support by Government
3. Reservation for Exclusive Manufacture by small scale sector
4. Project Profiles
5. Funding - Finance & Subsidies
6. Machinery Procurement
7. Raw Material Procurement
8. Manpower Training
9. Technical & Managerial skills
10. Tooling & Testing support
11. Reservation for Exclusive Purchase by Government
12. Export Promotion
13. Growth in demand in the domestic market size due to overall economic growth
14. Increasing Export Potential for Indian products
15. Growth in Requirements for ancillary units due to the increase in number of green-field units Coming up in the large-scale sector.

Great Potential

SMEs sector has performed exceedingly well and enabled our country to achieve a wide measure of industrial growth and diversification. By its less capital intensive and high labour absorption nature, SMEs sector has made significant contributions towards employment generation and rural industrialization. SMEs sector in India creates largest employment opportunities for the Indian populace, next only to agriculture. It has been estimated that 100,000 rupees of investment in fixed assets in the SMEs sector generates employment for four persons.

Statistics from Ministry of Micro, Small & Medium Enterprises also reflect the growth trajectory of SSI industry in India. The number of SSI units has increased from 6.79 million in 1990-91 to 13.37 million in 2009-10 providing employment to more than 32 million people in India.

SMEs Sector plays a major role in India's present export performance. 45%-50% of the Indian Exports is contributed by the sector. Direct exports from the sector account for nearly 35% of total exports. Besides direct exports, it is estimated that small-scale industrial units contribute around 15% to exports indirectly. This takes place through merchant exporters, trading houses and export houses. They may also be in the form of export orders from large units or the production of parts and components for use for finished exportable goods. The exports from SMEs sector have shown excellent growth rates in this decade. The product groups which dominate the exports from SMEs sector include sports goods, readymade garments, woollen garments and knitwear, plastic products, processed food and leather products. The SMEs sector is reorienting its export strategy towards the new trade regime being ushered in by the WTO.

Promising Outlook

This sector is ideally suited to build on the strengths of the traditional skills and knowledge, by infusion of technologies, capital and innovative marketing practices. This is the opportune time to set up projects in the sector. It may be said that the outlook is positive, indeed promising, given some safeguards. This expectation is based on an essential feature of the Indian industry and the demand structures. The diversity in production systems and demand structures will ensure long term co-existence of many layers of demand for consumer products / technologies / processes. There will be flourishing and well grounded markets for the same product/process, differentiated by quality, value added and sophistication. This characteristic of the Indian economy will allow complementary existence for various diverse types of units. The promotional and protective policies of the Government of India have ensured the presence of this sector in an astonishing range of products, particularly in consumer goods. However, the bottleneck of the sector has been the inadequacies in capital, technology and marketing. The process of liberalisation coupled with Government support will therefore, attract the infusion of these in this sector.

The capability of Indian MSME products to compete in international markets is reflected in its share of about 34% in national exports. In case of items like readymade garments, leather goods, processed foods, engineering items, the performance has been commendable both in terms of value and their share within the MSME sector while in some cases like sports goods they account for 100% share to the total exports of the sector. In view of this, export promotion from the small scale sector has been accorded high priority in India's export promotion strategy which includes simplification of procedures, incentives for higher production of exports, preferential treatments to MSMEs in the market development fund, simplification of duty drawback rules, etc. Products of MSME exporters are displayed in international exhibitions free of cost under SIDO Umbrella abroad.

Scientific Packaging

Role of packaging for exports has gained much significance in view of trends in the world markets. The need for better and scientific packaging for exports from small sector was recognised long back. With a view to acquaint MSME Exporters of the latest Packaging standards, techniques etc. training programmes on packaging for exports are organised in

various parts of the country. These programmes are organised in association with Indian Institute of Packaging which has requisite expertise on the subject. Basic objective of these programmes is to generate the much needed consciousness in the industry and to educate the entrepreneurs about the scientific techniques of packaging. Technical & managerial consultancy services to the MSME manufacturers/exporters is also provided through a network of field offices of this office so as to ensure higher level of production and generation of higher exports.

Motivation

In order to encourage the small scale units for producing Quality goods, National Awards for Quality Products are given to the outstanding small scale units, who have made significant contribution for improving quality of their products. The scheme is being operated since 1986. Winners of National Awards get a Trophy, a Certificate and a Cash Prize. National Awards encourage Small Scale Industries units to produce quality goods which further enable them to enter into export market.

The performance of the SMEs Sector has been promising till date. If adequate assistance is provided by the Government towards marketing of SSI products, this sector will increase employment opportunities as well as earn valuable foreign exchange.

Challenges to SME Sector

Despite its commendable contribution to the Nation's economy, SME Sector does not get the required support from the concerned Government Departments, Banks, Financial Institutions and Corporate, which is a handicap in becoming more competitive in the National and International Markets. SMEs faces a number of problems - absence of adequate and timely banking finance, limited capital and knowledge, non-availability of suitable technology, low production capacity, ineffective marketing strategy, identification of new markets, constraints on modernization & expansions, non availability of highly skilled labour at affordable cost, follow-up with various government agencies to resolve problems etc.

Small and Medium Enterprises (SMEs) are often confronted with problems that is uncommon to the larger companies and multi-national corporations. These problems include the following: -

(a) Lack of IT Support

IT personnel are in high demand and are often attracted to bigger companies and MNCs. It is very difficult for SMEs to attract good IT personnel. It is even more difficult to retain them. Moreover, good IT personnel are expensive and may not be affordable by most SMEs.

(b) Lack of IT Literacy

Many of the employees in SMEs started from the ground up after working with the company for many years. Some of them are often holding supervisory and managerial positions. These employees may not be IT literate and often have high resistance to the changes in the working process that they are comfortable with after many years.

(c) *Lack of Formal Procedure and Discipline*

Most SMEs do not have formal procedure or often these are not documented. Furthermore, there is tendency for these procedures to change frequently. This makes it difficult for third party and newcomer to understand the existing business practices and match them with the IT process.

(d) *Uneven IT Awareness and Management Skill*

As company grows, new managers are often introduced into the company. There will also be old managers who are promoted from the rank and file. Some of these managers may not been trained in the leadership and management skill. These uneven skill among the managers often caused conflicts during the implementation.

(e) *Lack of Financial Resources*

As a SME/SMI, financial resources are often limited. This often forces company to select a solution, which appear to be cheap initially. However, the hidden costs will start to emerge during implementation. This sometime causes the project to be abandoned or sometime send the company into further financial crisis.

(f) *Lack of Human Resources*

Implementations of some bigger scale IT project especially those that involve business process across different departments or require large amount of initial data entries require human resource during the implementation. Some SMEs are often in the stage of frequent fire fighting and shortage of manpower. This makes it very difficult for them to allocate time to carry out implementation. Furthermore, there is always a conflict between getting the daily routing work going and to do the "Extra" IT implementation.

(g) *Lack of Experience of Using Consultants*

A good consultant often save time and effort, and help to prevent pitfalls during the IT projects. However, most SMEs lack experience in working with consultants. The lack of knowledge in the field of IT makes it difficult in identifying good consultant for the projects. They often feel that the consultant costs are too high and they can handle it with their own staff. If the company has no staff that are experienced and knowledgeable in the IT project, avoiding external help often costs more to the company eventually.

Measures Taken by Government of India

In most developing countries, small and medium enterprises (SMEs) constitute the bulk of the industrial base and contribute significantly to their exports as well as to their GDP or GNP. For instance, India has nearly three million SMEs, which account for almost 50 per cent of industrial output and 42 per cent of India's total exports. It is the most important employment-generating sector and is an effective tool for promotion of balanced regional development. These account for 50% of private sector employment and 30–40% of value-

addition in manufacturing. It produces a diverse range of products (about 8000), including consumer items, capital and intermediate goods.

However, the SMEs in India, which constitute more than 80% of the total number of industrial enterprises and form the backbone of industrial development, are as yet, in technological backwaters *vis-a-vis* advances in science and technology. These suffer from problems of suboptimal scales of operations and technological obsolescence. While most of the large companies, even in developing countries, have financial as well as technical capacity to identify technological sources and evaluate alternate technologies that would suit their requirements, unfortunately, this capacity is conspicuously missing in most SMEs. It is these features of SMEs that make them an ideal target for technological up gradation through technological cooperation with foreign and local enterprises, with R&D institutions and centers of technology development. As the countries integrate into the global village, these SMEs will have to respond accordingly and thus deserve special attention. To enable SMEs to mitigate problems of technological backwardness and enhance their access to new technologies, it is imperative to give them a conducive environment, which in the present context of globalization, calls for an human-centered approach with tacit knowledge playing a predominant role. As knowledge resides only in the human mind, it can only be harnessed by focusing on increasing human capabilities through the process of increased communication, cooperation and linkages, both within the enterprise as well as across enterprises and knowledge-producing organizations.

Need for access to new technology

Small enterprises in India, with their dynamism, flexibility and innovative drive are increasingly focusing on improved production methods, penetrative marketing strategies and modern scientific management capabilities to sustain and strengthen their operations. They are poised for global partnership and have the potential to absorb latest technologies in diverse industrial fields.

Small in India is more than beautiful – it is efficient, adaptable and adds value in economic and social spheres. As the country integrates into the global village, the small and medium sectors will have to respond accordingly. They deserve special attention as they play a pivotal role in a country's socio-economic development. The problems faced by the SMEs, particularly in accessing technology and maintaining competitiveness have been formidable. The reasons for the inability of SMEs to identify their technology needs are:-

- Poor financial situations and low levels of R&D;
- Poor adaptability to changing trade trends;
- Desire to avoid risk;
- Non-availability of technically trained human resources;
- Emphasis on production and not on production costs;
- Lack of management skills;

- Lack of access to technological information and consultancy services;
- Isolation from technology hubs.

To enable SMEs to mitigate the above problems and enhance their access to new technologies for increasing their competitiveness in the international market, it is imperative to give them a conducive environment which includes: -

- (1) Formulation of appropriate national policies and programmes
- (2) Building up technological capacity;
- (3) Knowledge flows and technology databases;
- (4) R&D and inter firm linkages.

(1) *Formulation of policies and programmes*

Conducive policy environment is a pre-requisite. Major policy reforms aimed at substantially deregulating industrial sector and liberalizing foreign investment as well as technology imports, have been the most significant development since 1991. The post-liberalization era in the Indian economy has enhanced opportunities and challenges for the small industries sector. The ultimate objective of promotional policies is to enhance SMEs capacity to grow so that they become viable units. The national policies and programmes may be oriented to: -

- Setting up Industrial Districts/Technology Parks/Clusters to promote sourcing of new technology, innovation and effective transfer;
- Organizing local level information services, data banks and seminars in collaboration with Professional bodies;
- Sending experts to SMEs to assist them with the introduction of new technologies;
- Establishing training centers for human resource development for SMEs;
- Establishing business centers;
- Promoting strategic alliances with R&D institutions, universities and other enterprises at National, Regional and International level.

This calls for promoting indigenous industrialization with emphasis on self-reliance, through use and creation of local resources and at the same time adoption, absorption and diffusion of the imported technologies. This strategy involves an expanded role of SMEs which can alleviate high levels of unemployment and income inequality.

(2) *Building up technological capacity*

Access to advanced technologies and assistance in its adoption is crucial to build up Indigenous Technological Capacity (ITC) to face international competition. In the present scenario of globalization, knowledge of and access to latest advances holds the key to international competition. In this venture the industrial sectors, which are

able to identify their technology needs and adopt in time, will benefit the most. In India, the traditional sector which has shown this remarkable ability to adapt to technological change is leather. Central Leather Research Institute (CLRI), Chennai, has successfully introduced microprocessor control in tannery wet operations at industrial level and promoted cleaner processing, quality consistency and international equivalence. Anticipating the impact potential of computer-aided techniques in footwear and garment design, CLRI alerted and prepared the industry so well that CAD is today widely employed by export manufacturers of footwear and garments.

In another example, under NISTADS Bankura Project, a software package called as 'MADHU' (Modernization of Artistic Design for Handloom Unit) was developed in collaboration with Indian Institute of Technology, Kharagpur. [National Institute of Science Technology and Development Studies (NISTADS) has set up a S&T field station at Bankura, India to upgrade the technologies for artisans and craftsmen by blending the traditional technologies with new technologies and promoting commercialization.] This CAD software package facilitates computerized digitization of the picture/design produced by the artist/designer. This package has been successfully demonstrated to designers and weavers of Bankura. As a result, a large number of craftsmen have adopted blending of this new technology to increase efficiency, quality, flexibility and cost effectiveness. The above shows how information technology can be of immense use to upgrade and modernize the small-scale sector. Man and the machine can work together (in contrast to the most advanced automated systems) to bring out products with more flexibility and which are consumer-oriented, as also advocated by Brandt and Cernetic. While a large number of CSIR laboratories all over the country help meet the technological needs of the SMEs, Mechanical Engineering Research and Development Organization (MERADO), Ludhiana, in particular, was established in 1965 to nurture the growing industrial clusters in Ludhiana in the field of knitwear, agro-industrial machine tools and bicycles industry.

Since then, it has contributed significantly towards design, development and standardization of industrial machinery, agriculture machinery, machine tools, special purpose machines, consumer durables, etc. Some of the notable examples are design and development of 10 TPD modern oil expeller, sugarcane harvester, electric cloth cutting machine, high-speed over lock machine, leather shaving machine, flat bed and post bed leather sewing machines, button hole attachment for domestic sewing machine, wool knitting machine, friction welding machine, etc. The technologies developed by MERADO have benefited not only the SMEs in the state, but also in other states like West Bengal, Haryana and UP. It also caters to major testing facilities for the SMEs in Ludhiana. However, in the present scenario of globalization and liberalization, stronger linkages still need to be promoted not only between technology support institutions and SMEs, but also between SMEs for horizontal transfer of technologies. In this direction human resource development in the technology support institution is one area of crucial importance, which needs attention.

Similarly, other SME sectors which need to be technologically upgraded are electrical

and electronics, light engineering, food processing, building materials, chemicals, drugs and pharmaceutical, ceramics and telecommunication. In this direction, a number of efforts are being made by the Indian government. For example, the National Small Industries Corporation (NSIC) has pioneered several schemes for the growth and development of the small-scale sector. In the initial stages of development of the small-scale industries after independence, it was the innovative and novel schemes of the NSIC such as government purchase, hire purchase, development of prototypes, technical training, etc. which led to the establishment of new enterprises, development of appropriate manufacturing technologies and creation of a strong first generation entrepreneurial base. These schemes of the Corporation acted as a catalyst for this sector. It has helped the small units in identification, adoption, absorption and transfer of technology, entrepreneurial and technical training, common production facilities, marketing and financial support. With the successful implementation of NSIC schemes, a number of financial institutions and banks have also come forward to assist this sector, thus creating an important constituent of the Indian economy. Further, Council of Scientific and Industrial Research (CSIR) is also an important technology generator in the country and have a lot of S&T inputs to offer to the small-scale sector. To further invigorate this sector, the NSIC, CSIR and Asia and Pacific Center for Transfer of Technology (APCTT) have pooled their resources and have formed a strategic alliance to help upgrade technology in the small-scale sector. APCTT has a comprehensive data bank of information on appropriate technologies in diverse industrial sectors with access in the ESCAP region and elsewhere. It has been assisting technology buyers and technology sellers from different countries to come together. The alliance of these three organizations will assist the small-scale industry (SSI) units through a single point in technology sourcing. APCTT, NSIC and the CSIR, India, have, thus, formed a consortium to assist SSIs in the country with emphasis on the following aspects – improve and secure access of SSIs to advanced technologies, strengthen linkages between R&D institutions and create and strengthen the local innovative system. To start with eight technology acquisition and modernization workshops (two days each) in selected industrial centers (New Delhi, Bangalore, Chennai, Mumbai, Ahmedabad, Ludhiana, Indore, Kolkata) were organized during 1994 to deliberate on specific technologies in identified sectors.

These workshops provided an opportunity to identify specific technological needs and capabilities of small-scale units and the nature of technical assistance sought from promotional and financial agencies. In India, most of the SMEs are building up ITCs through the process of 'learning by doing'. This is central to incremental innovation and technological change. It has been pointed out that engineers on the shop floor play a vital role in supporting the operator's effort to acquire new skills and come up with new ideas. This is a must for a learning organization. In such an organization, everyone in a group is an expert and can give his/her knowledge to the process of complex problem-solving. The fact that proper linkages between the managerial staff, including engineers and workers at the shop floor within an enterprise, are an important factor in the information flow and the innovation process

is exemplified by the studies on firms in the electronics sector in India. The studies show that learning by doing and entrepreneurial capabilities have been instrumental in strengthening humanware and technoware at the enterprise level.

(3) *Knowledge flows and technology databases*

Dynamism of SMEs is crucial for their long-term competitiveness. For this they need to focus on systems of knowledge accumulation rather than just production system. The SMEs should have capabilities for generating, accessing and diffusing knowledge and also have openness to external sources of knowledge, including new technology databases. For this efficient national information services and networks are essential. In developing countries, most of the SMEs do not have access to well researched technology databases that provide information pro-actively on a regular basis. The information usually remains in the banks untapped, while the purveyors of the information wait for the targeted beneficiaries to request it. In India, an important technology information data bank is the National Research and Development Corporation (NRDC), which serves as an important link between research and SMEs. NRDC acquires, evaluates, develops and transfers all worthwhile technologies generated at the various national laboratories. The technologies available with NRDC for commercial exploitation cover a wide range of products, namely drugs and pharmaceuticals, pesticides and herbicides, plasticizers, resins, electrochemical products, metals, paints and varnishes, leather chemicals and auxiliaries, electrical and electronic goods, building materials, etc. It provides a comprehensive international patent search and also has a few renowned international databases on-line for carrying out the search. Through the Ministry of Science and Technology, the Government of India has also established information centers in specific areas for assisting academic institutions and industry under the scheme called National Information System for Science and Technology (NISSAT). There are information banks on food, leather, drugs and pharmaceutical, machine tools and aeronautics. SME units can approach them for assistance, especially with regard to the latest developments in the field of technology. An important database on local innovations is the 'Honey Bee Database' supported by SRISTI. [The Society for Research and Initiatives for Sustainable Technologies and Institutions (SRISTI) is a voluntary organization in India, which has received national and international recognition as a centre of excellence for research on people's innovations]. This is one of the biggest stores of knowledge on local innovations by farmers and artisans, covering about 72 countries. It is a knowledge network, which pools the technological solutions developed by people around the world. Networking of these databases can be of immense use to mitigate the numerous technological problems of the SMEs.

(4) *R&D and inter firm linkages*

At present, there are 2900 R&D institutions in India, of which 1350 are in the private sector. Out of these, over 1250 are in-house R&D units, employing over 45,000 scientific and technical personnel and incurring an expenditure of the order of seven billion rupees per annum. However, the small-scale sector is largely devoid of such

facilities and is mainly supported by public R&D for acquisition of new technologies. In general, SMEs are encouraged to invest in localized technological development. As most SMEs lack financial resources, the best way is to enter into linkages and partnerships with other enterprises, academia and/or R&D institutions. Over the past decade, emphasis in the concept of technology transfer has gradually shifted towards a new set of strategies which can be described as 'creative partnerships' or 'strategic alliances' to form learning organizations. This underlines the idea that forms of technological cooperation are no longer 'one-way', but involve a longer-term mutual benefit beyond short-term financial success. According to Cooley, learning by doing is not enough, Those who know what they are doing – crafts people with skill and experience – are the ones who best understand what needs to be done. This depicts an inherent feature of entrepreneurial capabilities, which helps pushing the organization towards a learning organization. 'Learning by interaction' is an important feature of technological up gradation and can only happen when firms cooperate and interact through strategic alliances and other forms of linkages. For this to happen, the most viable systems are the clusters, which offer good opportunities for interaction and industrial upgrading. The common feature of these new forms lies in the sharing of knowledge in technological capabilities and in cooperative intentions, which may or may not include government incentives. The diverse forms of alliances include:

- (A) Long-term multi-project partnerships that pool the production, research and marketing divisions in a single country or across several countries to accomplish strategic goals;
- (B) Flexible networking mechanisms that promote research consortia at the pre-competitive and development phases.

Such partnerships have technical education, training and retraining, innovation and sustainability as inherent features.

Role of financial institutions

The availability of financial resources on affordable terms and in a non-bureaucratic manner is yet another problem the SMEs confront, hindering access to new technologies. It is imperative, therefore, to influence existing financial networks and, if need be, to set-up a separate mechanism for funding smaller enterprises, especially those categorized as micro-enterprises. One of the important ways to promote access to new technologies among SMEs in developing countries is to provide venture capital, which in a way helps in indigenous development of technologies. A large number of small innovations are also being supported by SRISTI Venture Capital Fund. One of the main factors of the success of knitwear cluster at Tiruppur is the state intervention in the supply of short-term credit to facilitate networked production. In order to create a business environment, with adoption and assimilation of new technologies that are resource-efficient and have little waste output, the supportive infrastructure also needs to be strengthened in many developing countries. There is a need for such institutions to deal exclusively with the myriad problems that SMEs face in their day-to-day work. In India Department of Scientific and Industrial Research (DSIR) is one

such institution. It is engaged in technology promotion, development, utilization and transfer activities. The department has launched several initiatives to encourage increased utilization of locally available R&D options through its major schemes, viz. Programme Aimed at Technological Self-Reliance (PATSER), and Scheme to Enhance the Efficacy of Transfer of Technology (SEETOT). Technology Bureau for Small Enterprises – a result of collaboration between APCTT and Small Industries Development Bank of India (SIDBI), represents under one roof, synergy of technology and finance which facilitates capability building and identifying market channels.

Assistance and Support Services for Indian SMEs by SME Chamber of India

- Export & Trade Promotion
- Bank Finance, PE/VC and Investments
- Technology Up gradation
- Joint ventures and technology transfers
- Contract manufacturing tie-ups
- International collaborations and alliance
- Marketing, Branding and Promotion
- Connectivity with potential business partners
- Survey and Research
- Mergers and Acquisitions
- Set up new Enterprises in India and abroad
- Conference, Seminars, Workshops and training programs
- Exhibition, Trade Fairs, Display Centers
- Delegation and Trade Missions
- Redressal of issues and problems with concerned authorities
- Rehabilitation / Revival of Sick Units
- Recognition and Appreciation Awards.

Conclusion

Small industry in India has found itself in an intensely competitive environment since 1991, thanks to globalisation, domestic economic liberalisation and dilution of sector-specific protective measures. The international and national policy changes have thrown open new opportunities and markets for the Indian small industry. Concerted effort is needed from the government and small industry to imbibe technological dynamism. Technological up gradation

and in-house technological innovations and promotion of inter-firm linkages need to be encouraged consciously and consistently. Financial infrastructure needs to be broadened and adequate inflow of credit to the sector be ensured taking into consideration the growing investment demand, including the requirements of technological transformation. Small industry should be allowed to come up only in designated industrial areas for better monitoring and periodic surveys. A technologically vibrant, internationally competitive small and medium industry should be encouraged to emerge, to make a sustainable contribution to national income, employment and exports. It is essential to take care of the sector to enable it to take care of the Indian economy.

MSMEs AND EMERGING ROLE OF COMPANY SECRETARIES

SURESH THAKUR DESAI* & KAUSHIK M JHAVERI**

Small and Medium Enterprises (SME) play an important role in the development of a country. There are around 26 million MSME units in India, of which 13 million are SMEs. SMEs contribute nearly 45% share of manufactured output, accounting for 40% in overall exports of the country. The Micro Small and Medium Enterprise (MSME) sector forms the largest generator of employment in the Indian economy. It provides employment to about 6 cr. people.

The performance of SMEs in India though impressive comes next to China where this sector provides employment to 94 million people with a network of 37 million units.

To make this sector to become more vibrant and significant player in development of the Indian economy, the Government of India has taken various initiatives. The definition and coverage of the MSME sector was broadened MSME Development Act, 2006 which recognized concept of 'enterprise' to include both manufacturing and service sector besides defining medium enterprises setting up a Board for developing policy frameworks and indicating procurement policy.

In accordance with provisions of this Act, the MSMEs in India are classified into two categories:

- i. Manufacturing Enterprises
- ii. Service Enterprises

Present ceiling limit on investment to be classified as Micro, small and Medium Enterprises is :

A. Manufacturing

<i>Enterprises</i>	<i>Investment in Plant & Machinery</i>
Micro Enterprises	Does not exceed Twenty Five Lakh Rupees
Small Enterprises	More than twenty five Lakh rupees but does not exceed five crores rupees
Medium Enterprises	More than five crore rupees but does not exceed ten crore rupees

* FCS

** PCS

B. Service enterprises

<i>Enterprises</i>	<i>Investment in equipment</i>
Micro Enterprises	Does not exceed Ten Lakh rupees
Small Enterprises	More than ten lakh rupees but does not exceed two crore rupees
Medium Enterprises	More than two crore rupees but does not exceed five crore rupees

Studies on SMEs

A quick analysis of various studies and data indicates that SMEs are going through a transition phase and are generally restructuring their strategies and capabilities to remain competitive and grow in the emerging world trade environment. The government are also evolving policies, strategies and modes of implementation to encourage and support SMEs for their growth, capacity building and international competitiveness. The issues and strategies vary with the level of development and priorities in national economies. Some of the countries such as Republic of Korea, Singapore and Taiwan have been able to adopt and implement new policies and measures to promote and support SMEs more successfully than many other countries. Innovation, technology, productivity and quality, though inter-related, are assuming greater significance for competitiveness in manufacturing and businesses. Foreign Direct Investments (FDI), networking and technical tie ups are being encouraged to facilitate access to newer technologies, strengthening technological and management capabilities, and access to market information. Creation of training and skill up gradation facilities, Information & Communication Technology (ICT) applications, and sharing of risks in financing and development, are the thrust areas.

In India, effective implementation of policies and delivery of results to the satisfaction of the SMEs, remain much below than desired, though there are a large number of institutional mechanisms and support measures available and concerns shown by the government. There is a need to critically review the existing policies and mechanisms, to assess the constraints and gaps in delivering the desired outputs. For example, there are overlapping agencies and programmes for development of technologies and technological assistance to the SMEs, but the SMEs continue to be weak in R&D, technology development, acquisition and induction of new technologies, productivity and quality among other factors. The technology support programmes are largely implemented from Delhi or the capitals of the states and the awareness about programmes and fiscal incentives available is limited among SMEs.

Proposals of National Manufacturing Competitiveness Council (NMCC) are praiseworthy, but the implementation mechanisms are not clear, and also the focused targets likely to be achieved. Hopefully these proposals will not be just an addition to the existing set of support measures, without effective monitoring and assessment mechanisms for the intended results. What is needed perhaps is a strong innovation & technology development policy with legal instruments for implementation, clearly meeting the needs of SMEs at different stages of

their development. National Knowledge Commission has been generally active in evolving strategies for education and skill up gradation, and employment or entrepreneurship opportunities in ICT and other areas. Digital divide has been an area of concern but at the same time offers opportunities for SMEs. National Small Industries Commission is engaged in evolving policy instruments and mechanisms to utilize and support SMEs.

Most SMEs, need easier access to new or modern technologies abroad, technology support facilities and easier access to finance, including technology finance, besides marketing information and incentives for training and skills development. Further, differentiated policies and mechanisms are needed for SMEs in different sectors, stages of their development, nature of operations. For example, the technological needs of SMEs in traditional sectors such as food processing, leather textiles, toys etc. would be different than those in new and advanced technological areas such as micro-electricals, pharma, precision instruments and so on. Perhaps, there is a need to have short term and long term strategies for enhancing competitiveness of SMEs in one broad based strategy. The R&D expenditure and technological capacities of most of the SMEs would continue to be limited because of their inherent constraints in the resources and vision. The support structures should recognize this fact. However, the SMEs have enormous potential for innovations and incremental development, which need to be nurtured for production of new goods and services at competitive costs.

The IT and auto-component SMEs are examples of the successes through innovations. Such policies should lead to wider dispersal of economic benefits, capacity building, and utilization of resources, creating employment, etc. across the society. Economic, education, trade, technology and society need to be interdependent. The SMEs development project should recognize the needs of internationalizing companies or those who have the potential to internationalize, differently than those of domestic oriented companies or stagnating companies. The analysis of FDI data for SMEs in India tend to show that some SMEs are internationalizing or willing to internationalize through various types of collaborations through FDI route since the amounts involved are small.

In the context of WTO and other emerging trade mechanisms including Regional Trade Agreements(RTAs), Free Trade Agreements (FTAs) and bilateral or special economic cooperation agreements, the technological preparedness of SMEs need to be studied and support mechanisms evolved to overcome the gaps or constraints being faced or likely to be faced by them in the international businesses. In view of the wide variations in definitions of SMEs in various economies, the harmonization of definition of SMEs in India, with those in developed or advanced developing countries would facilitate international assistance for technology transfer, development and evolving measures for enhancing competitiveness in export markets. Preparedness of SMEs for WTO is still another issue. Innovations and trade agreements are likely to be the thrust areas in near future.

The National Strategy for Manufacturing has recognized the need for a focused project on advance technology products and has recommended the constitution of a special group to study the potential for manufacture and export of such products. It has also recommended the establishment of technology parks around institutions of higher technological learning

on the lines of those existing in USA. Another important recommendation relates to setting up a "Global Technology Acquisition Fund" to enable Indian industry to acquire very high technology intensive companies abroad. (National Manufacturing Competitiveness Council, 2006)

The strategy suggests a cluster approach for improving the manufacturing competence. New and innovative approach to cluster development should be adopted. Further, small scale sector should be encouraged as breeding ground of innovation and technology development where it becomes the technology sources for large companies. Towards this, government must incentivize technology development in SMEs to enhance their competitiveness. A National Manufacturing Competitiveness Programme (NMCP) is being developed which includes objectives to support SMEs. A Design Clinic approach is suggested to bring Indian manufacturing sector and design expertise on to a common platform and to provide expert advice and cost effective solution, resulting in continuous improvement and value addition for existing products. Emphasis is also laid down to enable SMEs to be competitive through quality management standards and quality technology tools. These are only some of the strategies among those suggested in the Report.

NMCC seems to have prepared Rs. 1,000 crore National Manufacturing Competitiveness Programme for small and medium enterprises jointly with Ministry of Small Scale Industries. This aims to benefit over 10,000 firms in more than 500 SME Clusters. The thrust of the plan is towards technology infusion. The areas for support include "lean" manufacturing, ICT, technology and quality up gradation, increasing number of tool rooms, encouraging patents and so on). National Knowledge Commission has also identified SMEs as a thrust sector for education, skills upgradation, training and ICT encouragement. Various studies have shown that ICT and technology levels are higher in internationalized SMEs in sectors such as food processing, auto components, ICT, leather, engineering, garments etc. Compared to non-exporting or domestic SMEs.

Academic and R&D Organizations

Some of the engineering and technical institutions such as IITs, National Institutes of Technology and CSIR Research Laboratories, are also providing R&D and technology related support facilities and services to the SMEs including training and skill development programs. However, access to these facilities are generally not easy, and often lack the business needs of entrepreneurs. There are very limited start-up enterprises based on technologies or intellectual property from academic and R&D institutions. Ministry of Small Industries and Development Commissioner, have a wide network of technical, design, training, pro-type development, testing etc., facilities all over the country spread up to district levels. But, these facilities need to be modernized and tuned to emerging needs.

Foreign Tie Ups and FDI

Internationalization of SMEs usually refers to the SMEs engaged in international businesses, have developed cooperation, partnerships, linkages and networks with foreign companies and institutions. Imports and exports tend to enhance the efficiencies, capabilities, competitiveness and vision of SMEs. FDI is considered to be an important channel for

internationalization, besides catalyzing technology flows and investments. Most countries are aiming at attracting larger FDI which poses challenges and provide opportunities to SMEs. The domestic policies therefore need to be finely tuned to take full advantage of FDI and international aid/support measures or loans. However, the SMEs need to be growth oriented and forward looking, with innovative capacities, for internationalization.

A survey of over 8000 SMEs in Europe in 2003 revealed that internationalization spurs growth and competitiveness (<http://ec.europa.eu>). The foreign supply relationships are the most common forms of internationalization while exporting is the next and some establish foreign subsidiaries and branches. Access to know-how is a frequent motive for going abroad.

The study has interestingly revealed that smaller countries with small domestic markets are more internationalized. Further the study point to three elements as crucial for developing holistic measures with regard to internationalization.

SMEs' managers often have limited time and management skills. A policy measure should consider providing some practical tasks to support the manager, especially in the case of SMEs with low international experience.

Studies indicate that SMEs often need specific, targeted support. Such 'customized' support comprises, for instance, assistance in identifying an appropriate foreign business partner for a joint venture or collaboration. Moreover, recent studies indicate that SMEs' awareness of support measures is low due to the measures' traditional focus on export activities. The studies suggest that policy measures, in order to be effective, need to focus on the experience of the entrepreneur and on developing his/her qualifications in a broad sense.

Internationalization is more than just exporting. Policy measures, whether general or company-specific, need to encompass all the different approaches to internationalization and the support to include a wide range of international activities.

Foreign partnerships, foreign investments and cross boarder clustering represent new viable ways to strengthen the international business strategies of SMEs. Such diverse international activities may integrate different business functions (i.e. R&D, production and marketing) and thus involve elements across the entire value chain.

Most developing countries have adopted or are adopting a liberalized FDI regime in various sectors of development, though the degree of liberalization may vary. In case of SMEs, several countries have opened up to 100% FDI while in some it is restricted, say up to 24% in India, in general. Limited studies are available (UNCTAD 1998) related to FDI flows to SMEs, especially in developing countries. A study of technology financing through FDI, for SMEs in India and other select countries, (Agarwal, 2005) was carried out in 2004-05 at IIFT, based on the FDI approvals of the government. This study indicated that FDI approvals for SMEs accounted for about 6.0% of total approvals while the amounts were about 2% of the total amount approval. One can infer that FDI approvals were mainly perhaps intended to internationalize markets and technologies rather than investments. The extent of amounts and the number of approvals vary from sector to sector.

Measures Taken by Government of India

MSME is primarily responsible for promotion and development of SMEs in India, and has evolved several policies, institutional and support measures, spread all over the country, in order to enable SMEs to meet their changing needs. Small Industries Development Bank of India (SIDBI) has developed various financing schemes. Ministry of Science and Technology (DST, DBT, DSIR) has evolved several measures and programmes for technological assistance and development and transfer of technologies for SMEs. Some of the economic ministries such as Ministry of Textiles, Department of Food Processing and Department of Handicrafts etc. have also recently announced initiatives for technical assistance in various firms.

Some of the measures and new initiatives to promote SMEs include:

- SME development fund
- A specialized stock exchange for SMEs
- Encouragement for patenting and ISO Certification
- SME venture capital fund
- National Commission for Small Industries (informal sectors)
- SME development bill
- Credit Rating Agency
- Promoting special venture capital companies and risk financing companies for SMEs
- Improve the working of credit guarantee and export promotion institutions
- Progressively reduce protection measures and simplify implementation policies and control mechanisms
- SME Development Centres at SIDBI and IIFT
- Considering liberalizing FDI in SMEs and encouraging their linkages with TNCs and large companies
- Promoting industrial growth centres/clusters, EOUs, district industry centres, business incubators and business parks
- Market assistance and export promotion
- National Small Industries Corporation
- Small Industries Development Organization
- Limited Liability Partnership Act, 2008 and Limited Liability Partnership Rules, 2009.

SEBI initiative

MSME Sector must tap the capital market to meet financial needs. However, they should not be subjected to rigours of same rules. With this twin objectives Apex regulator of capital markets

SEBI decided to have separate dedicated platforms of the exchanges for listing and trading of securities issued by SMEs. In view of this SEBI amended SEBI (Issue of Capital and Disclosure Requirements) Regulation(s), 2009 (SEBI (ICDR) Regulations) by inserting a new chapter on "Issue of specified securities by small and medium enterprises".

SEBI has also specified "Model Equity Listing agreement" to be executed between the Issuer and Stock Exchange. Certain relaxations have been provided to the issuers whose securities are listed on SME exchange in comparison to listing requirements in Main Board, some of which are as under:

- a. Companies listed on the SME exchange may send to their shareholders, a statement containing the salient features of all the documents, as prescribed in sub clause (iv) of clause (b) of proviso to section 219 of the Companies Act, 1956, instead of sending a full Annual Report;
- b. Periodical financial results may be submitted on "Half yearly basis" instead of "Quarterly basis";
- c. SMEs need not publish their financial results, as required in Main Board and can make it available on their websites.

Company Secretaries can contribute towards improvement of standards of Corporate Governance among listed SMEs as per Clause 52 of the listing Agreement.

Clause 52 (VII) of Listing agreement relates to Compliance, which is as under:

The Issuer shall obtain a certificate from either the auditors or Practicing Company Secretaries regarding compliance of conditions of corporate governance as stipulated in this clause and annex the certificate with the directors' report, which is sent annually to all the shareholders of the Issuer.

The same certificate shall also be sent to the Stock Exchanges along with the annual report filed by the Issuer. Funding options for SMEs includes Angel Investors, Banks, Financial Institutions, SIDBI Initiatives, Venture Capital Funds (VCFs), Private Equity (PE), Initial Public offers (IPOs), Foreign Investments, External Commercial Borrowings (ECB)

Small and Medium Enterprises (SMEs) contribute to economic development in various ways such as creating employment opportunities for rural and urban population, providing goods & services at affordable costs by offering innovative solutions and sustainable development to the economy as a whole. SMEs in India face a number of problems - absence of adequate and timely banking finance, non-availability of suitable technology, ineffective marketing due to limited resources and non availability of skilled manpower.

India has registered a high economic growth (6-9%) consistently over the last one decade. For the sustainability of this kind of growth proper nurturing of SME sector is imperative. The need of the hour is to empower the SME Sector so that it is able to take its rightful place as the growth engine of the economy.

The paper throws light on various challenges being faced by SMEs in India at present and tries to find solutions to these problems, so that the SMEs become more vibrant and are able to make forays to new un-chartered areas such as infrastructure etc. It forms a major portion of the industrial activity.

Role of Company Secretaries

There are many ways in which a Company Secretary can guide/advise the SMEs:

1. Advisor to public Issue by SME.
2. Advisor/consultant for SMEs on listing at SME Exchange.
3. Acting as Compliance officer under SME listing Agreement.
4. Certifications under various clauses of SME Listing Agreement.
5. Maintaining the Statutory Registers.
6. Monitoring changes in the share ownership of the company.
7. Assisting MSME companies to file statutory information properly.
8. Monitoring changes in relevant legislation and the regulatory environment and helping the managements to take appropriate action.
9. Developing and overseeing the systems that ensures that the company complies with all applicable codes as well as its legal and statutory requirement.
10. Liasoning with banks and financial institutions and help MSMEs to obtain project financing and term loans.
11. Co-coordinating the process of obtaining funds from Angel Investors/Venture Capital Funds/PrivateEquity.
12. Conducting Secretarial Audit/Due Diligence which will be of great help before approaching for the funds.
13. Providing Compliance Certificate and ensure compliance of various regulatory prescriptions in case of an IPO.
14. Helping in converting sole proprietary or partnerships in to Companies.

Other Roles

1. *Secretarial Audit*

Proactive Secretarial Audit on a continuous basis would help the initiation of corrective measures and thereby strengthening the compliance mechanism and processes in the company.

A Company Secretary in Practice has been assigned the role of Secretarial Auditor in the Company Secretaries Act, 1980. Practising Company Secretary is the competent, fit and proper Professional to conduct Secretarial Audit. PCS is highly specialized professional in matters of statutory, procedural and practical aspects involved in proper compliances under the Corporate Laws.

2. *Diligence Report for Banks*

For availing Loans from any Bank, SMEs have to submit a Diligence Report obtained from a Practising Company Secretary (PCS). The PCS is required to certify compliance in respect of matters specified in the RBI Circular dated 19th September, 2008. The Diligence Report has to be made on a half yearly basis. The structure of Diligence report makes it mandatory for the PCS to make critical examinations of all the relevant records and documents with a high degree of care, skill and knowledge.

3. *Capital Market*

A Company Secretary has substantial role play in securities laws and capital market related matters. Some of the services provided by Company Secretaries (both in employment and practice) in Capital Markets include:

- (i) Advising companies on Compliance of legal and procedural aspects particularly under SEBI Act, Securities Contracts (Regulation) Act, Listing Agreement etc.
- (ii) Advisor/consultant in issue, listing, delisting, buy-back of shares and other securities in India and abroad.
- (iii) Drafting of prospectus/offer of sale/letter of offer/ other documents related to issue of securities and obtaining approvals in association with lead managers.
- (iv) Ensuring compliance with SEBI (Prohibition of Insider Trading) Regulations, 1992.
- (v) Certifications under various clauses of Listing Agreement.

IPO/FPO Certification

Company Secretaries Act, 1980 authorises a Company Secretary in Practice to perform the services as a share transfer agent, and issue house, a share and stockbroker, a secretarial auditor or consultant.

Compliance certificate on Initial Public offer/Further Public offer by a Company Secretary in practice would help Merchant Bankers to ensure compliance of the various regulatory prescriptions and also the stock exchanges to list the securities on offer under IPO/FPO.

Typical problems of MSMEs

Small and Medium Enterprises (SMEs) are often confronted with problems that is uncommon to the larger companies and multi-national corporations. These problems include the following:

Lack of IT Support

IT personnel are in high demand and are often attracted to bigger companies and MNCs. It is very difficult for SMEs to attract good IT personnel. It is even more difficult to retain them. Moreover, good IT personnel are expensive and may not be affordable by most SMEs.

Lack of IT Literacy

Many of the employees in SMEs started from the ground up after working with the company for many years. Some of them are often holding supervisory and managerial

positions. These employees may not be IT literate and often have high resistance to the changes in the working process that they are comfortable with after many years.

Lack of Formal Procedure and Discipline

Most SMEs do not have formal procedure or often these are not documented. Furthermore, there is tendency for these procedures to change frequently. This makes it difficult for third party and newcomer to understand the existing business practices and match them with the IT process.

Uneven IT Awareness and Management Skill

As company grows, new managers are often introduced into the company. There will also be old managers who are promoted from the rank and file. Some of these managers may not been trained in the leadership and management skill. These uneven skill among the managers often caused conflicts during the implementation.

Lack of Financial Resources

As a SME/SMI, financial resources are often limited. This often forces company to select a solution, which appear to be cheap initially. However, the hidden costs will start to emerge during implementation. This sometime causes the project to be abandoned or sometime sent the company into further financial crisis.

Lack of Human Resources

Implementations of some bigger scale IT project especially those that involve business process across different departments or require large amount of initial data entries require human resource during the implementation. Some SMEs are often in the stage of frequent fire fighting and shortage of manpower. This makes it very difficult for them to allocate time to carry out implementation. Furthermore, there is always a conflict between getting the daily routine work going and to do the "Extra" IT implementation.

Lack of Experience of Using Consultants

A good consultant often save time and effort, and help to prevent pitfalls during the IT projects. However, most SMEs are lacked of experience in working with consultants. The lack of knowledge in the field of IT makes them difficult in identifying good consultant for the projects. They often feel that the consultant costs is too high and they can handle it with their own staff. If the company has no staff that are experience and knowledgeable in the IT project, avoiding external help often costs more to the company eventually.

Can company Secretaries help in solutions ?

It is advisable that Company Secretaries form LLPs with IT professionals and offer a composite all inclusive package of services and help the SMEs. That would also provide to the Company Secretaries the new areas of practice and at the same time help technocrats entrepreneurs to concentrate more on their own with LLPs taking care of other matters.

PCS must change mindset

Company secretaries in practice must come out of their present groove and cash on the opportunities offered by this SME sector. Help them to grow and widen your scope of work.

MSMEs – POLICIES & INITIATIVES FOR GROWTH

SUBASHINI RADHAKRISHNAN*

Introduction

It is a well-recognized fact today that in the world over, the engine of growth shall be driven by small and medium scale businesses and this notion is held true of India too. Such micro, small and medium scale enterprises (MSMEs/SMEs) are seen to possess the entrepreneurial skills to identify opportunities and foray into emerging areas, aided by newer technologies and innovative tools. SMEs with their localized base have proved to be worthy contributors to Indian exports, to the country's GDP and to creating employment for our growing populace. While the tenaciousness of Indian businesses is laudable, the SME sector is not however without its failings. Start-up units that were fired with the vision and zeal of the promoters have been limited by lack of an external talent pool that can lead the business to its next platform of growth and mid-sized units that successfully outgrew the start-up phase have failed to leverage on its efforts to grow bigger. Many experts have studied the problems faced by the SME sector, both self-induced ones such as over-involvement of the promoters, lack of marketing support and strategy, inability for talent retention as well as circumstantial ones like lack of financing, regulatory bottlenecks, access to technology, availability of skilled manpower etc.

Having acknowledged that SMEs constitute an important segment for any nation aspiring economic prosperity and in view of the SME's contribution to social goals such as employment generation, the Government of India is keen to respond to the challenges surrounding the SMEs and provide them with a favourable environment to form and pursue businesses in India. The protectionist measures of the past have given way to more progressive mechanisms to incentivise SME sector and to enable them to more confidently secure a foothold in the global market that our world today is. Thus, the list with well over 700 items that were reserved for exclusive manufacture of only the SSI sector stand whittled to a bare 20¹; in its place, are other sector-specific reliefs and concessions such as setting aside of funds for financing SMEs, augmenting liquidity through a special stock exchange etc.

* FCS, Senior associate with ALMT Legal. Views expressed in the article are that of the author and not necessarily that of the firm.

1 List of items reserved for exclusive manufacture by micro and small enterprise sector, as on 30 July 2010; <http://www.dcmsme.gov.in/publications/reserveditems/reserved2010.pdf>

This article attempts to briefly examine such policies and initiatives, whether through statute or by regulatory actions, that have been brought about by the Government of India and its machineries in support of the SME sector.

A Statute for the MSME sector

Originally, the Industries Development and Regulation Act, 1951 [I (D & R) Act] provided the statutory framework for small scale industries. Section 11B of the aforesaid Act provides that the Central Government may identify small scale industrial undertakings and ancillary industrial undertakings that require government measures and initiatives on the basis of factors such as investments in plant and machinery, land and buildings, the nature of ownership of the enterprise, the number of workers employed in such enterprise etc. Further to the above, the Central Government issued notifications from time to time specifying the threshold for investment in fixed assets in plant and machinery as would entitle an entity to constitute a “small scale or ancillary industrial undertaking”. An undertaking whose investment limits in plant and machinery fell within the requirements as notified by the Government was exempted from the licensing provisions of the I (D & R) Act. Furthermore, such small scale and ancillary industrial undertakings benefited from the category of articles that were notified by the Government for exclusive manufacture by such undertakings.

Subsequently in the year 2006, the Micro, Small and Medium Enterprises Development Act, 2006 MSMED Act was enacted by the government with the view to facilitate “the promotion and development and enhancing the competitiveness of micro, small and medium enterprises” and incidental matters, demonstrating a shift in government motto from “control of certain industries” to ushering in growth and development for the MSME sector. The MSMED Act provided for the creation of the National Board for Micro, Small and Medium Enterprises to “examine the factors affecting the promotion and development of micro, small and medium enterprises and review the policies and programmes of the Central Government in regard to facilitating the promotion and development and enhancing the competitiveness of such enterprises and the impact thereof on such enterprises”.

But the more prominent feature of the MSMED Act is the new classification brought by it, in the place of the erstwhile small scale and ancillary undertakings. Accordingly, MSMEs are now differentiated into Micro Enterprises, Small Enterprises and Medium Enterprises. The distinction as above is once again made on the basis of investment in plant and machinery in the case of enterprises engaged in the manufacture or production of goods pertaining to an industry specified in the First Schedule of the I (D & R) Act and in the case of the enterprises engaged in providing or rendering of services, on the basis of the investment in equipment².

2. The threshold for investment in plant & machinery for a Micro Enterprise is “not exceeding Rs. 25 Lakhs”, for Small Enterprises, it is “exceeding Rs. 25 Lakhs but not exceeding Rs. 5 Crores” and for Medium Enterprise, it is “more than Rs. 5 Crores but not more than Rs. 10 Crores”. For enterprises engaged in services, the threshold for investment in equipment by a Micro, Small and Medium enterprises are not exceeding Rs. 10 lakhs, exceeding 10 lakhs but not exceeding Rs. 2 crores and exceeding Rs. 2 crores but not exceeding Rs. 5 crores, respectively.

The reservation of exclusive category of goods continues to apply under the I (D & R) Act, albeit only to the Micro Enterprise and Small Enterprise engaged in the production and manufacture of goods.

The exemption from licensing for small scale and ancillary undertakings has been modified in part under the MSMED Act and presently, a Medium Enterprise engaged in the manufacture or production of goods pertaining to any industry specified in the First Schedule to the I (D & R) Act, 1951 is required to file a memorandum with the District Industries Centre in the jurisdiction of which the enterprise is (or, is proposed to be) located while such filing is left to the discretion of a Micro Enterprise and Small enterprise and also for a Medium Enterprise engaged in providing services.

The SME sector is stated to comprise largely of unregistered units, mostly organized as partnership firms and the intended benefits of the MSMED Act will percolate to the sector only when more of such units are convinced of the merits of registration under this Act.

Statutes under which MSMEs are formed

While the MSMED Act sets out the framework for government support to the SME sector, an undertaking seeking to operate in the SME sphere may be formed or established as a “proprietary, HUF, association of persons, co-operative society, partnership firm or company” and to such extent, are also governed by the respective statutes relevant to the form of their constitution. Most SMEs are at least to begin with, structured as proprietary or partnership firms and one of the chief handicaps of such entities are that the liabilities of the firm can extend up to the personal assets of the proprietor or partners of the firm and any financial distress of such units may also result in erosion of the individual’s personal net worth. To overcome this concern, the Limited Liability Partnership Act, 2008 was enacted to enable individuals to form a partnership whose liability is restricted to the property of the limited liability partnership (“LLP”)³. A partner of a LLP is not personally liable for obligations of a limited liability partnership or for the wrongful acts or omissions of the other partners of the LLP.

To those deterred by the process for a formation of a company under the Companies Act, the Government brings hope under the Companies Bill, 2011⁴ which puts forth the concept of “One Man Company” whereby even a single individual may incorporate a private limited company and manage its affairs with a single director. The Bill further designates certain companies whose paid-up capital or turnover does not exceed the prescribed sums as “Small Company”⁵ and proposes relaxation from certain procedural compliances under the Companies Act.

3 Section 27(4) of the LLP Act, 2008.

4 http://mca.gov.in/Ministry/pdf/The_Companies_Bill_2011.pdf. The Bill is currently pending before the Parliamentary Standing Committee.

5 The Companies Bill, 2011 defines “Small Company” as a company, other than a public company,—

- (i) 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 five crore rupees; or
- (ii) turnover of which as per its last profit and loss account does not exceed two crore rupees or such higher amount as may be prescribed which shall not be more than twenty crore rupees

While the advent of the LLP does offer a feasible alternative to partnership firms, much remains to be done. Many experts have stressed on the need for a fast-track winding-up for companies and for a separate law to deal with bankruptcy and insolvency issues affecting proprietary and partnership concerns, which provide the entrepreneurs an opportunity to assess whether the ailing unit can be revived and if not, to facilitate an efficient and time-bound manner to liquidate the assets and meet its liabilities.

Financing – Government initiatives

One of the issues often mentioned as destabilizing the growth of the SME sector is the non-availability of finance and the high costs of obtaining regular financing. The nascent stage of the SME unit suggesting its inability to produce track record of viability, lack of organizational checks and balances in the business which is led more by promoter-strategy and efforts render external financing that much more difficult to procure. Sensing the importance of reliable financing channels at lower costs, the Government and its machineries are working on several initiatives to strengthen institutional finance as well as private funding for the SME sector.

The Reserve Bank of India has mandated that lending to the Micro and Small Sector is a part of the priority sector lending⁶ that banks are bound to observe. Banks have accordingly been provided with a mandate to achieve a 20 per cent year-on-year growth in credit to Micro and Small enterprises and a 10 per cent annual growth in the number of Micro Enterprise accounts. Banks have been directed to streamline their procedures for receiving applications for loan and for dealing with the same expeditiously. Banks shall not accept collateral security in the case of loans up to Rs.10 lakhs to the Micro and Small sector, which threshold can be raised up to Rs. 25 lakhs if the borrower-unit displays sound financials and good track record. All commercial banks have also been advised to implement a Corporate Debt Structuring only for units in the SME sector, both from corporate and non-corporate sector.

Also, the dismantling of the Prime-lending Rate in favour of the Base Rate system for determination of interest rates is also expected to benefit the smaller borrowers by introducing transparency and parity in interest rates.

SIDBI established with the primary objective of “Promotion, Financing and Development of the Micro, Small and Medium Enterprise (MSME) sector” offers several assistance such as term loan and other forms of funds infusion, bills discounting, Credit Linked Capital Subsidy Scheme (whereby a capital subsidy of 15% is offered on the purchase price of plant & machinery towards technology up gradation). SIDBI has also joined hands with the Government of India to set up the Credit Guarantee Fund Trust for Micro and Small Enterprises to encourage lenders to make available collateral-free credit facilities to SME units since the loan obligations of the SME are guaranteed by the said Trust.

6 Master Circular issued by RBI on Lending to Priority Sector vide RPCD. CO. Plan.BC 12/04.09.01/2012-13 dt. 2 July 2012.

In order to encourage the flow of private investment into the SME sector, the Securities & Exchange Board of India (“SEBI”) has categorised a separate fund targeting the SME sector – the SME Fund – from among other privately pooled investment vehicles. This distinction has been made by SEBI under the SEBI (Alternative Investment Fund) Regulations, 2012⁷ whereby all such funds as are covered thereby (“AIFs”) are required to register with SEBI under the respective category that its investment philosophy pertains to. SME Funds fall under the broader classification of “Category I AIF” and by definition, SME Funds are those that invests primarily in unlisted securities of SMEs or securities of those SMEs which are listed or proposed to be listed on a SME exchange or SME segment of an exchange. As a condition of its registration, SME Funds are required to invest at least 75% of its corpus in SME units. It is hoped that the definitive classification of the AIFs according to their investment mandates will aid the government to provide the necessary incentives to such SME Funds whose investments in SME units would have a positive spillover effect on the economy.

Another key measure in adding vibrancy to the SME sector is to build liquidity in SME stocks. SEBI has by inclusion of Chapter XB to the SEBI (Issue of Capital and Disclosure Requirement) Regulations, 2009 enabled the SME sector to list its securities on a recognized stock exchange. A SME unit that seeks to list its securities on the bourse would be entitled to do so under the aforementioned Chapter XB, if its post-issue share capital does not exceed Rs. 25 crores. An issue under this chapter must be 100% underwritten and supported by market-making for at least 3 years from the date of successful listing, there must be a minimum of 50 prospective allottees for such issue and the minimum application should be at least Rs. 1 lakh per application. Both BSE and NSE have launched bourses for the SMEs and as per an article published earlier this year in a leading newspaper, the SME sector is seen to have already begun to avail these provisions to list their stock⁸.

A step closely related to financing is credit-rating. Non-availability of adequate data about the borrower-profile causes lenders to hesitate in its lending and in order to overcome this obstacle, credit rating is being propagated as necessary for the SME sector. The SME Rating Agency of India Limited for instance, is focused on providing credit ratings solely to the SME sector. RBI too has encouraged MSME units to obtain credit rating from reputed credit rating agencies and advised banks to align the credit pricing of the loans with the credit rating of the borrower-units, if any.

A SME unit that aims to have a healthy financial position must also have an effective system of realizing its payments from its debtors. The MSME Act in fact contains provisions for enforcement of its claims by a SME unit before the Micro and Small Enterprises Facilitation Council for payments in respect of any supplies made by it to a buyer. However, ‘factoring’ may be a more superior arrangement for SMEs to release the monies tied in receivables and factoring agencies cognizant of the benefits of such arrangements, have begun to offer factoring services to clients in the SME sector. In order to provide for a regulatory mechanism

7 http://www.sebi.gov.in/cms/sebi_data/attachdocs/1337599839661.pdf

8 <http://www.business-standard.com/india/news/green-shoots-seen-in-sme-exchange-platform/477751/>

for factoring agencies and to regulate the factoring transactions, the Government has enacted the Factoring Regulation Act, 2011. The said Act states that the Reserve Bank may, among other factors keeping in mind the interest of SME units availing factoring services, give directions to the factors either generally or to any factor in particular in respect of any matters relating to or connected with the factoring business undertaken by such factors. It remains to be seen what further measures will be taken by RBI to strengthen the factoring arrangements availed by the SME sector.

Foreign Investment

The extant law on foreign investment is contained within the Consolidated FDI Policy under the Press Note 1 of 2012 and the intent of such policy is “to attract and promote foreign investment” but only to “supplement domestic capital, technology and skills”. Accordingly, the FDI Policy provides that non-Micro or Small scale undertakings engaged in the manufacture of items reserved for SME sector may receive foreign direct investment in excess of 24% only by obtaining prior Government approval and a license under the I (D & R) Act and subject to undertaking export obligations. Foreign direct investment in the SME sector on the other hand has been provided to be permitted subject to the sectoral caps, entry routes and other relevant sectoral regulations.

Another interesting opportunity that arises for the SME sector is in the context of foreign direct investment in retail trade. After battling intense political agitations, the Government has finally permitted foreign direct investment in the retail sector up to 100% subject to a host of conditions, the one among them that is worthy of attention of the SMEs being the condition for mandatory sourcing of at least 30% of the value of products sold from Indian small industries/ village and cottage industries, artisans and craftsmen, in cases where the foreign direct investment is in excess of 51%. 'Small industries' has been defined as industries which have a total investment in plant & machinery not exceeding US \$ 1.00 million, such valuation determined at the time of installation, without depreciation. While this is being seen as some as a welfare measure to benefit the smaller businesses so as to offset the risks posed to the unorganized retail sector by the advent of the foreign retailers, there are also several viewpoints that this requirement would actually result in no great practical benefits since the upper cap on valuation would limit any growth opportunity to the SME unit and thus, be a disincentive to the scaling-up of such units from the business opportunity.

Export promotion measures

Among the contributions from the SME sector to economic development, a significant one is that towards the total exports by the country and the Government continues to implement beneficial schemes so as to augment the export capabilities of this sector to raise its foreign exchange earnings and to foster Indian exports in global trade. In addition to the existing export promotion schemes, the Foreign Trade Policy 2009-14⁹ provides for measures to encourage diversification of Indian exports into newer markets, to boost technological up gradation and to supplement exports by specific sectors. The Focus Market Linked Product Scheme which provides for a duty credit for export of specified products to certain countries

9. <http://dgft.gov.in/exim/2000/policy/ftplcontentE1213.pdf>

has been increased in scope and breadth with an increase in the incentives, increase in the product list as well as the countries covered within it.

Labour law relaxations

Of the many archaic laws that continue to remain on the statute books, the gamut of labour laws that have failed to keep up with the changing times and business practices rank high. In order to lessen the cost of compliance with various labour legislations for smaller businesses that employ very few employees on its rolls, the Government had earlier brought in the Labour Laws (Exemption from Furnishing Returns and Maintaining Registers by Certain Establishments) Act, 1988¹⁰. This Act provided for exemption to such small establishments from filing multiple returns and to instead file a core return and maintain limited registers. Like the rest of the industry, the SME sector too has been demanding for an overhaul of the labour laws so as to be more relevant to today's business climate and it is reported that the Labour Laws (Exemption from Furnishing Returns and Maintaining Registers by Certain Establishments) Amendment Bill¹¹ is proposed to be passed to benefit establishments employing up to 40 workers in maintaining registers and submitting returns electronically under 16 labour laws. Since even a small reform in labour laws is most welcome, it is hoped that the bill will be made law soon.

Conclusion

As can be seen from the above summary, the Government has been at work, to advance the SME agenda and to pave the way for the SME sector to translate its economic goals but undeniably, a lot remains to be done. In January 2010, the high-level task force constituted under the directives of the Prime Minister to explore the issues raised by associations of SME units submitted its report with its deliberations on the same. The report discloses that the Task Force has indeed identified the areas of concern that are almost unanimously highlighted by experts as plaguing the SME sector and some of the measures that the Task Force urges the government to undertake are as follows:

- Government to ensure strict adherence to stipulated targets for lending by commercial banks;
- A separate fund be set-up by SEBI to meet the shortfall in lending by banks to the SME sector;
- Government to introduce a Public Procurement Policy for government purchases from the SME sector;

10 Under the Labour Laws (Exemption from Furnishing Returns and Maintaining Registers by Certain Establishments) Act, 1988, "small establishment" means an establishment in which not less than ten and not more than nineteen persons are employed or were employed on any day of the preceding twelve months and "very small establishment" means an establishment in which not more than nine persons are employed or were employed on any day of the preceding twelve months.

11 Press Release dated 16 September 2010 from Ministry of Labour and Employment; <http://pib.nic.in/newsite/erelease.aspx?relid=65805>

- To provide incentives for transition of SMEs from unorganized sector to the organized sector and for corporatization as entities;
- To introduce tax incentives to the SME sector such as graded tax structure, tax pass-through for venture investors;
- State governments to establish a mechanism for re-examination of viability of sick units and implementation of rehabilitation and RBI to ensure that such rehabilitation would be binding on all financial institutions;
- Government to expedite the formation of SME exchanges;
- Legal options to be developed for securitization of receivables and factoring services;
- Government to give wide publicity to structures like LLP, Single Person Company to enable companies to move from informal to formal sector;
- Insolvency laws to be comprehensively reviewed;
- Labour laws to be simplified;

Further to the above Prime Minister's task force, a working group was constituted by the Planning Commission to study the concerns ailing the SME sector as per the report of the Prime Minister's Task Force and to submit specific action plans for the 12th Five Year Plan (2012 – 2017). The Working Group focused on six specific areas and its key recommendations inter alia are as under:

- On Credit and Finance, it stressed on building an eco-system for enhancing credit flow to the SME sector such as cluster-banking, increased budgetary support to the Credit Guarantee Scheme, establishing and support factoring services companies, enlarging alternative avenues of funds to SMEs such as private equity, venture capital funds etc.
- On the Institutional and Legal framework, the Working Group notes that the primary responsibility lies with the State Governments with the Central Government supplementing their efforts. It has identified some immediate steps: (a) environmental policies be made uniform across the country, with some relaxations for the SMEs; (b) consolidation of the plethora of labour laws into a single user-friendly law; (c) strengthening of the MSMED Act by passing rules under its sections, re-engineering the offices of the functionaries under the MSMED Act, introducing e-governance in its processes etc.

As has been noted in our discussions above, several of the items above are being acted upon by the Government and while it remains to be seen if such measures will fulfill the desired objectives, these augur the Government's keen intent to enable the SME to leverage its potential and achieve a quantum jump in its growth. The recent budget 2012-13 had for instance, proposed an allocation of 1,000 crores to the National Skill Development Fund and introduction of a Public Procurement Policy requiring the Government to procure from SMEs. The Government has been indeed making policies with a sensitivity to the needs of the SME

sector, whether it be the raising of the turnover limit for compulsory tax audit and presumptive taxation of SMEs from 60 lakhs to 1 crore or the exemption to SMEs from migration to the IFRS standards of accounting.

While the Government is working on remedying the inherent weaknesses and systemic failures, the SME sector should also be introspective of the factors inhibiting its growth. The SME units must attempt to resolve its structural constraints that impede its development and only then, will they be able to fully and effectively harness the benefits of their regulatory environment and realise their entire potential.

CHALLENGE AND NEED FOR BUILDING AWARENESS OF IPRs IN MSMEs – INDIAN PERSPECTIVE

SAIBAL C PAL*

‘Chandika Oil’ (Chandika) is a local product. It is manufactured by Chandika Oil Mill (Mill) situated at Jalpaiguri in the state of West Bengal. Incidentally West Bengal has the largest number of small scale enterprises in India. Chandika Oil Mill is a micro enterprise within the meaning of The Micro Small and Medium Enterprise Development Act, 2006 (MSME). The creator, Sachindra Chandra Pal launched ‘Chandika Oil’ in 1950 for consumption and application on the body. Sachindra Chandra Pal (Textile Technologist by profession) died in 2000 but the product continues to be sold having stood the test of time for 62 years. Mothers in and around Jalpaiguri town are proud to apply the oil on their new born babies. Most babies of the town grow up using the oil being proud to belong to the ‘Chandika’ family. ‘Chandika Oil’ is a brand, an Intellectual Property Right (IPR) like any other oil brand, ‘Saffola’ and ‘Engine.’

MSME, 2006 was gazetted on 2nd October, 2006, the date of birth of Mahatma Gandhi. Mahatma Gandhi and Chandika Oil are both names and IPRs. While Mahatma Gandhi is an IP of which the country is proud, the right in the brand, ‘Chandika Oil’ lies with the family members of the creator. IPRs like human beings are born with the help of their creators. They live for a time span and die. Brands like ‘His Masters Voice’ and ‘Kodak’ continue to live for centuries. A brand which died in 2008 was ‘Lehman Brothers’ a US based Investment Banker. ‘JAL’ the Japanese airlines was another brand which made its exit from the international business scenario. Names and brands can be considered as local, regional, national or international. ‘Chandika Oil’ is a local brand, ‘Sreeleather’ enjoys regional popularity, ‘ITC’ is a national brand and the brand ‘Bata’ is known internationally. Names and Brands generate revenue for enterprises and are important tools of business.

An experience demonstrates the importance of name in business. I stood before a calendar to look up for the date. I referred to the date but what impressed me more was the name of firm and the way the calendar had the organisation’s name displayed on it. The name of the firm, ‘3VKar Group’ was written on the top and below it were the words, ‘The confidence we built’. The presentation of the calendar brings out the importance of the name of the firm to the promoters. The promoters want to tell everything about their organization through the name. A product symbolized by a name tells inter alia of the manufacturer, quality, price range, colour, promoter, age of the product. When one tells his friend that he owns a Nokia

* FCS.

608 E it means he owns a mobile the detail of which can be easily known by his friend even without seeing the mobile physically. This is the advantage of a brand. To-day in the commercial world names and brands suggest everything and they have eased things for all including manufacturers, consumers and all those connected with the market for the product.

IPRs are significant to all forms of business, big or small. While, IPRs form the back bone of enterprises, MSMEs are the pillars of business enterprises. Importance of MSMEs is not restricted to India alone. Their importance is world- wide. UNIDO estimates suggest that 90 per cent of industries in the world are MSMEs. They control 50 to 60 per cent of the total employment in the world. SMEs engaged in manufacturing often account for even larger share of manufacturing employment which may be as high as 80 per cent. As per estimates there are about 26 million MSMEs in India with about 60 million persons involved in the units. About 45 per cent of the total manufactured goods come from these enterprises. Exports aggregate to about 35 per cent of direct exports and about 45 per cent of total exports. Further, MSMEs manufacture about 8000 products and these units are spread out throughout the country. In the year 2010-11, survey revealed that micro units contributed 94.94%, small units produced 4.89 per cent and medium units contributed 0.17 per cent of the total output of industrial goods in the country. The MSMEs are dependent on indigenous technology. Capital investment in the enterprises is low and accordingly its operations do not permit them to modernize freely. However, such enterprises are the main source of employment the main concern of an economy. The above facts reveal the importance of MSMEs for the economy and their need for IPR support and protection.

World Trade Organisation (WTO) was formed in 1994 as a common platform for international trade. Members of WTO are required to abide with the Trade Related Aspects of Intellectual Property Rights (TRIPS) in pursuing trade. TRIPS emphasizes minimum protection and enforcement of IP in trade among the member countries. It advocates among others technical advancement of business through protection. As per the MSME Act, enterprises are classified into micro, small and medium enterprises as per their respective investments in plant and machinery. Manufacturing and Services are the two segments of activities for the enterprises. Investment criteria categorizing the enterprises into micro, small and medium are given as under:

<i>Sl.no.</i>	<i>Type of Unit</i>	<i>Manufacturing Sector</i>	<i>Service Sector</i>
1.	Micro	Upto Rs 25 lacs	Upto Rs 10 lacs
2.	Small	More than Rs 25 lacs and upto Rs 5 Crores	More than Rs 10 lacs upto Rs 2 crore
3.	Medium	More than Rs 5 Crores to 10 Crores	More than Rs 2 Crores to Rs 5 Crore

MSME Act facilitates promotion, builds capacity of an enterprise to face competition. The act is the first-ever legal frame work for recognition of an `enterprise' and the three tiers of manufacturers and service providers namely, micro, small and medium enterprises. Considering the need to inject finance into the enterprises, Central Government recently

announced a policy package for stepping up credit to SMEs by Banks/Financial Institutions to assure inter alia 20 per cent year-to-year growth in credit flow. Significant improvements have also been made in the credit linked capital subsidy scheme for technological up gradation of the units. This has led to rise in the number of enterprises availing benefits contained in the policy.

When it comes to IPR awareness, survey reveals that there is least awareness among MSME enterprises. There is hardly any presence of IPR use in framing their business strategy. It is common that these units do not know the distinction between Patents and Trade Marks. To overcome the scenario and strengthen the enterprises operating in the segment, Government has adopted policies to speed up the spread of awareness of IPRs for value addition to the output of MSMEs to withstand global competition prevalent in the market place due to globalization, liberalization and privatization.

Intellectual Property (IP)

IP is created out of one's thought, idea or intellectual power. Ideas generated constantly and applied to business become immovable business property which generates revenue for business. IPs are Balance Sheet items. With the popularity of IPs it is realized that such assets needed protection. Several Acts were enacted for their establishment and protection as the existing laws did not provide for their protection. Accordingly, new laws were enacted. All WTO countries have the same set of laws for IP protection. However, countries have localized them according to the practices prevalent in their respective countries. The laws enacted to create and protect assets category-wise are as under:

1. Patent Act, 1970 (amended in 2005) was enacted to protect innovations for manufacturing new products. The Patent Act, 1970 protects inventions to benefit industrial development. Patent Co-operation Treaty ('PCT') provides rules for members of WTO for international patent filing.
2. Industrial Designs Act, 2000 was enacted to promote and protect industrial products and their designs. It covers creative packaging and textile designs.
3. Trade Mark Act, 1999 was formerly the Trade and Merchandise Marks Act, 1958 was amended and the Act was re-named the Trade Marks Act, 1999. The Act provides protection to distinctive brand names and helps them in building strong brand recall value through recognition and their protection.
4. Geographical Indication Act, 1999 protects goods manufactured possessing high value and reputation from a particular geographical area.
5. Copyright Act, 1957 protects and administers rights for artistic work and softwares applied on computers.
6. Protection of Plant Varieties & Farmers Rights Act, 2001 protects plant varieties either by a patent or by an effective sui generis system or by combination of the two.

7. The Biological Diversity Act, 2002 conserves bio-diversity in the country for regulating access to biological resources by bona fide end users for various purposes including scientific research, commercial activities and sustainable use of non-timber forest produce.
8. The above Acts are all TRIPS compliant.
9. Trade Secrets protection does not fall under any act except that there are no specific laws in place. As per TRIPS there is a requirement of formulating a policy on protection of trade secrets. With the introduction the foreign investors and local businessmen are bound to develop a sense of security.

Current MSME Scenario

MSMEs have to change their approach to take advantage of the IP laws into valuable property for business operation. In spite of the contribution of MSMEs to the national economy, the enterprises continue to remain weak and the treatment meted out to them from all quarters remain cause of concern. This can be better understood from the words of the Deputy Governor of RBI K.C.Chakrabarty, "*When it comes to restructuring our banks have a substantial bias towards more privileged borrowers vis-à-vis small borrowers.*" The words sum up all. The treatment of Banks/Financial Institution towards small borrowers can be well understood from the above words.

According to AIMA Study – August, 2003, constraints faced by MSME's include the following:

- (i) Market related aspects being 25 per cent,
- (ii) Finance related matters being 70 per cent,
- (iii) Government Policy related issues 12.78 per cent,
- (iv) Power / Infrastructure related matters issues being 14.0 per cent,
- (v) Technology related issues being 14.6 per cent.

Further issues and challenges being faced by MSMEs towards growth and development are summarized as follows:

- (i) They are unable to reap the benefit of market opportunities which require large production facilities, economies of scale, homogenous standards and regular supply.
- (ii) The enterprises experience difficulties in purchase of inputs such as raw materials, machinery and equipment's, obtaining required finance, consulting services, new technology, highly skilled labour etc.
- (iii) Small size hinders the internalization of functions such as market research market

intelligence, supply chain, technology innovation, training and division of labour that impedes productivity.

- (iv) Emphasis to preserve narrow profit margins makes the SMEs myopic about the innovative improvements to their product and processes and capture new markets.
- (v) They are unable to compete with big players in terms of product quality, range of products, marketing abilities and cost.
- (vi) Absence of a wide range of finance raising avenues and other services to sustain the business.
- (v) Absence of Infrastructure, quality labour, business acumen and limited options/opportunities to widen the business.
- (vi) Poor IT and knowledge infrastructure which mostly remain out of reach causing them to fall back in competition despite the availability of product strength.

Vodafone Initiative for SMEs.

Contrary to the above there are instances which suggest concern for MSMEs by large industry in the country. Vodafone initiative is the one which requires mention. Vodafone has invited SMEs to associate with the event organised by them under the name and style, 'Drive into the Big League'. Through the event, one SME will have a chance to have its logo fixed on the two Vodafone McLaren cars to be driven by motor racing champions Lewis Hamilton and Jenson Button at the Delhi's Buddh International Circuit (BIC) to be held between 26th and 28th October, 2012. The winning logo of the SME will be displayed along with other international brands before the audience drawn from various countries. This will give the logo of the SME international exposure.

Vodafone has pioneered for the cause of SMEs in India. Through this approach SMEs would get exposure to come into reckoning without having to incur the image building cost. Brand names have to overcome number of hurdles. To launch a brand an enterprise has to adopt expensive marketing practices and branding exercises. In the first contest organized in 2011, about 80,000 SMEs participated. ABC Consultants Ltd., a Delhi base SME was declared the winner by the Jury. The enterprise experienced publicity online, through television and print media. Vodafone's step is indeed a novel way for brand exposure for SMEs in the country. The contest meant for small businesses resulted in bringing into a life character. This is substantiated through the words of Mr Agarwal of ABC Consultants Ltd who stated that his organization and logo earned recognition among peers and provided nation-wide exposure. Other finalists of the contest namely, Mr Vijay Chadda, CEO, GVC Systems, Mr Siddharth Puri, Business Head, Tyro Direct spoke highly of the contest and how it brought their names and brands into reckoning to leverage profits. The publicity was not restricted to India alone. It was an act which provided them opportunity to put their head above water to ward off threat of being an unknown entity in the fierce competitive world.

MSMEs, IPR and Economy

MSMEs are significant contributors to the GDP of the country. Contribution of SMEs is expected to be 30 per cent of GDP by 2019 -20. With little awareness of IPRs, MSMEs can become a force to reckon to withstand the onslaught of cut throat competition. Such a change will bring in value addition to business of the MSMEs. Ignorance of IPR ultimately causes financial loss. Either the enterprises violate laws or if they are prosperous their IPRs are copied to affect their performance which even force pioneers to go out of business. In fact MSMEs most of the time do not get fair market price for their products and this deepens further when it comes to poor, uneducated or less educated artisans engaged in manufacture of their goods.

India has a number of traditional arts and crafts famous world-wide but the artisans are not paid fair price for their handicrafts/products. Mediators get the maximum margin and in some cases act as original producers throwing actual producers to the back ground. The artisans are treated as labourers for their products. Accordingly, artisans never can know their value. Ignorance causes them to be exploited, however, this situation can be rooted out and their originality can be maintained by adoption of IPR protection measures. Steps to spread IPR literacy is on but a full-proof mechanism to spread awareness of IPRs to the roots is yet to percolate.

Government is aware of the need to spread IPR consciousness specially to the micro and small enterprises. Several schemes have been formulated for the purpose. It is well understood that unless IPRs of products of micro and small enterprises are protected growth of large industries cannot be witnessed. In its drive to spur growth of MSMEs Government has recently framed a policy requiring Ministries and Central Public Sector Enterprises (CPSEs) to purchase each year from MSMEs a minimum of 20 per cent of their total procurement. However, 4 per cent of such procurement will be earmarked for MSMEs owned by SC/ST entrepreneurs.

IPR protection initiatives for MSMEs undertaken by Government include the following:

(i) *IP Facilitation Centre for MSMEs*

Ministry of MSME has set up IP Facilitation Centre for assistance of MSMEs for their unfettered access to the best practices in IPR adoption starting from identification to protection and finally management of IPs as a business tool.

(ii) *Financial Assistance to MSMEs*

Ministry of MSME provides financial support upto Rs 25,000/- per grant of an Indian patent and Rs 2 lac for obtaining foreign patent. For obtaining Geographical registration Rs 1 lac is given as grant.

(iii) *Financial Assistance to MSMEs is provided for filing International Patent applications*

Ministry of Communication and Information Technology has formulated a policy by

which expenses upto Rs 15 lac or 50 per cent of total expenses incurred for filing an international patent applications are paid.

(iv) *Business Incubators for MSMEs*

Ministry of MSME has proposed to set up 100 Business Incubators in Technology (Host) Institutions. Ministry provides financial assistance between Rs 4 lac to Rs 8 lac per idea/unit for encouraging protection of such idea/unit.

Business Awareness of IPR for MSMEs

Strategies to generate business awareness of IPRs in MSMEs are stated to be as under:

1. Generation of awareness among MSMEs may be made by the adoption of various means of IPR system and management of the same under the various enactments. Conditions required to be satisfied by the MSMEs to be IPR protection compliant must be communicated to the enterprises individually. For this even visit by a team to all registered enterprises may be introduced. Enterprises should be made aware of the means of getting in touch with the Authorities and the way financial support may be obtained by them may be explained.
2. Encouragement of participation in Research & Technological Development should be made and the way such practices may be undertaken may be explained. Apart from mass contact through online, television and print media arrangement for personal visit by a team of experts to such enterprises may be undertaken.
3. Enhancing Brand strategy using IPR tools for sustainable production and marketing ultimately resulting in growth and rise in profitability needs to be adopted.
4. Leveraging strengths of Institutions to deliver standard products for consumers is considered necessary in a technology driven enterprise and if technology is protected and upgraded the products will survive keeping the organization afloat.
5. Promoting Innovation is a must and without it an enterprise cannot survive. Patenting is a method of bringing in protected innovation but it is possible only at a huge cost. To reduce incidence of the cost it is important to share such cost through the employers associations.

MSME and Green Financing

Internationally green financing is a new means of development for MSMEs. It is yet to gain ground in the country. A step in the direction has been taken by IFCI which launched the "Green India Venture Fund". CII- Godrej has come out with the "Green Business Centre" to support green entrepreneurs to raise investment with the aid of energy efficiency technologies and cleaner production measures. Under the Energy Efficiency Scheme, SIDBI provides concessional direct credit to MSMEs at interest rates ranging from 9.5 per cent to

10 per cent which is 100 to 150 Basis Point System (BPS) below PLR of SIDBI. SMEs are also rated. To encourage SMEs to avail of green rating, SIDBI provides concession in interest rate upto 50 bps in its loan assistance to MSMEs if they obtain green rating from the SME Rating Agency of India (SMERA) with `SMERA Green 3' rating .

IPR and Film Industry

Bollywood leads in film production in the country. To-day entertainment has earned recognition as an industry. As an industry it has representation at all levels. To-day the parliament has a number of film personalities as members. Entertainment industry is dependant on IPR which requires protection. Unless protected its contribution will disappear causing harm not only to the industry but to the viewers and all those who follow the industry closely. Recently, the industry witnessed a few notable deaths. Actors Dev Anand, Shammi Kapoor, Joy Mukherjee, Dara Singh, Rajesh Khanna and A.K.Hangal left one after another. The actors have left this world but what they have left behind is intellectual property which need to be protected. When the death of Rajesh Khanna was announced, electronics and print media covered the death to draw attention of the fans and viewers. The media industry generated revenue by reporting on the star. So, Rajesh Khanna as an IPR needs to be protected in the interest of entertainment Industry. With stronger IPR protection practices the film industry will benefit the entertainment industry as a whole. Each participant in the film is distinct and holds his own identity through his performance which needs preservation as no two creations can be alike unless copied. Copying is the biggest threat to the industry. One need not be a hero to have his identity noticed and preserved. While the words, `*Babu Moshai*' in the film Anand on the lips of Rajesh Khanna is an IP deserving protection, similarly the dialogue by A.K.Hangal in the film Sholay, `*Yeh itna sannata Kyu hai bhai*' deserves to be preserved. An IP can thus be distinct from personality. This is its uniqueness and makes it stand apart.

Conclusion

Economy of the country is witnessing stagnation. Industrial production dipped to 1.6 per cent during the month of June, 2012. RBI has lowered its growth projection for the economy to 6.5% from 7.3% in the financial year March, 2013. However, the economy grew at 8-9 per cent every year between 2003 to 2008. It is accepted by all quarters that the development of MSMEs in modern lines is the answer to India's development. Areas of their contribution has also been identified and their growth would mainly rest on five aspects being ,skill development, adopting a protected market strategy, diffusion of technology at subsidized rates, provision of infrastructure and credit facility. Credit facility is considered the back bone of the other four aspects. It is necessary that the Government announces a Policy on spreading IP for MSMEs but also for inclusion of IP education from elementary level at schools. It is only education at the grass root level that will spread consciousness and help industry to prosper and the economy to march ahead so that RBI can project higher percentage of growth so that India can match international competition. With the last word of this article penned, I browsed through the 'The Telegraph' lying beside me. My eyes struck the news item on Page 3, `*Puzo son, Paramount in Godfather rights battle.*' The news stated that the

future of `The Godfather' franchise moved to court today as the son of the creator Mario Puzo wants a judge to end Paramount Pictures' rights to make future films'. The film Godfather is popular among viewers. The news demonstrates the importance and power of IPR in films and also its place in our life, such that nothing can be done without IPR protection.
