

Serious Fraud Investigation Office – An office with more teeth

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They said to "think outside the box."
Naturally, I assumed "box" meant "law"

Introduction

- Indian business is marred by policy uncertainty, bureaucratic paralysis and the ever increasing fraud cases reported in corporate sector in the last decade has further taken a toll on the market sentiments of the investors. All this has not only adversely affected the foreign direct investment in India but has created immense opportunity loss for Indian growth story.
- Corruption not only diverts money but also increases the transaction cost and thus hampers growth. While it is certainly the responsibility of the government to improve the business opportunity, government alone cannot be considered as the precursor of any change. The private sector will also have to share the responsibility to introduce transparency, curb fraud and resist the temptation to pay bribe in order to facilitate healthy economic growth.
- The purpose of any corporate law is to ensure sound financial growth of the company, protection of the stakeholders from unscrupulous management, and to equip the governmental authority to look into the affairs of a company and thereafter to impose punishment on any person who is guilty of misconduct and wrong doing. With the steadfast growth in economic crimes in India, the new Companies Act, 2013 (**CA 2013**) has introduced the provisions related to fraud and consolidated the provisions pertaining to punishment of fraud committed by officials of a company.
- In this present write-up, we focus on the provisions related to fraud under the CA 2013 and Serious Fraud Investigation Office (**SFIO**).

Provision of Punishment

The CA 2013 provides that a person accused of any offence punishable under Section 447 cannot be released on bail or his own bond unless the Public Prosecutor has been given an opportunity to oppose the bail application. In the event the Public Prosecutor opposes the bail application and the court is satisfied that there are reasonable grounds for believing that he is not guilty of such offence and that he is not likely to commit any offence while on bail, the court may grant bail in such cases.

Instances of Fraud

The CA 2013 specifically sets out in various sections such omissions and/or commissions which may amount to fraud and which are liable for punishment under section 447. In fact, under the CA 2013, there are several such instances like:

- if at the time of incorporation of company, any person furnishes false or incorrect information or suppresses any material information to the Registrar of the Companies in relation to the registration of a company;
- any default in complying with the requirements for formation of companies with charitable object;
- furnishing false statement, mutilation, destruction of documents, misstatements
- issuance of duplicate certificate of shares with the intent to defraud;
- inducing any person to invest money, personation for acquisition of securities, not complying with the provisions for transfer and transmission of securities, reduction of share capital, removal, and resignation of auditor.

In case it is proved that the company has accepted deposits with the intent to defraud the depositors, the CA 2013 provides for stringent punishment and makes every officer of the company personally responsible, without any limitation of liability for all or any loss or damage that may have been incurred by the depositors.

Establishment of SFIO

The CA 2013 not only identifies instances of fraud as punishable crime but also under section 211 provides for the establishment of Serious Fraud Investigation Office (**SFIO**) by a notification. Here it is pertinent to note that the Government of India has way back in January, 2003 by a notification set up SFIO under the Ministry of Company Affairs to undertake investigation of corporate frauds committed by the companies. The provision of the CA 2013 reiterates the composition, roles, responsibilities and powers of SFIO and provides for investigation by SFIO of frauds relating to a company, however the provisions pertaining investigative powers of the SFIO are yet to be notified by the Central Government.



Investigation of Affairs

- The provision of section 447 is restricted to corporate fraud wherein the companies, its shareholders, the creditors, the investors are victim of fraudulent act. Any investigation of affairs of the company can be initiated by the Central Government under various circumstances such as (i) on receipt of report from the Registrar of Companies or inspector under section 208, (ii) by special resolution passed by the company that the affairs of the company requires to be investigated, (iii) in public interest; and (iv) on request of any department of the Central Government or the State Government.
- Under the current arrangement, an investigation has to be ordered by the government as SFIO cannot independently take up investigations. While initiating investigations, the government may consider the gravity, enormity of the fraud and not simply the financial ramifications. The investigation report of SFIO filed with the Court for framing of charges is treated as a report filed by a police officer. In addition, SFIO also has also been granted with the power to arrest in respect of certain offences which attract the punishment for fraud.

Vigil Mechanism

Considering that financial frauds are generally done in collusion, the CA 2013 provides that every listed company or such other class of companies as may be prescribed shall have a vigil mechanism. The requirement for a vigil mechanism is set out in Clause 49 of the Listing Agreement entered between listed companies and stock exchanges, which provides for a non-mandatory requirement of a whistleblower policy.

OUR VIEW

This new provision incorporated under the CA 2013 has far reaching implications and unlike most civil suits which once filed can be withdrawn, complaint filed in the nature of "fraud" under the CA 2013 by the shareholders will be difficult to withdraw in case such shareholders and the company decide to amicably settle the matter. Further, where a matter has been assigned by the Central Government to SFIO, no other investigating agencies shall have the right to proceed with the investigation and if some other agency is investigating the matter, the relevant agency will transfer the documents and records of the matter to SFIO. Under the CA 2013, the offences which attract punishment under section 447 are cognizable and non-bailable, which means a police officer has the authority to make an arrest without a warrant. It is then on the company and its officials to prove that the intent was not to defraud.

Considering the nature and quantum of penalty introduced in the CA 2013, it should ideally bring about greater transparency, accountability and address the menace of corporate fraud through proper investigation and enforcement structure.

Contributed by:

Shisham Priyadarshini

Amish Shroff

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