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**TEST
SERIES**



SUGGESTED SOLUTION

CS PROFESSIONAL

Subject – Multidisciplinary Case Studies

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Answer to Q1.

(a) Yes, above case is an example of intentional fraud by the top executives of the Company. Since the Chief Executive himself confessed to having orchestrated an accounting fraud for several years. He admitted to manipulating the firm's accounts to report profits that were more than 10 times the actual figures and reported a cash balance of US\$1 billion that was non-existent.

Fraud is a deliberate action to deceive another person with the intention of gaining some things. Fraud can loosely be defined as "any behavior by which one person intends to gain a dishonest advantage over another". In other words, fraud is an act or omission which is intended to cause wrongful gain to one person and wrongful loss to the other, either by way of concealment of facts or otherwise.

Section 25 of the Indian Penal Code, 1860 defines the word, "Fraudulently", which means, a person is said to do a thing fraudulently if he does that thing with intent to defraud but not otherwise. The Companies Act 2013 has also explained fraud.

Explanation to Section 447 defines "fraud", which reads as under: "fraud" in relation to affairs of a company or anybody corporate, includes any act, omission, concealment of any fact or abuse of position committed by any person or any other person with the connivance in any manner, with intent to deceive, to gain undue advantage from, or to injure the interests of, the company or its shareholders or its creditors or any other person, whether or not there is any wrongful gain or wrongful loss. Reporting of fraud under the Companies Act, 2013:

Frauds by executives in the company can be reported under the Act under the Section 143(12) of the Companies Act, 2013 which requires the statutory auditors or cost accountant or company secretary in practice to report to the Central Government about the fraud/suspected fraud committed against the company by the officers or employees of the company. It includes only fraud by officers or employees of the company and does not include fraud by third parties such as vendors and customers.

Consequence of non-compliance: Sub-section 15 of section 143 states that if any auditor, cost accountant or company secretary in practice do not comply with the provisions of sub-section (12), he shall be punishable with fine which shall not be less than one lakh rupees but which may extend to twenty-five lakh rupees.

(4 MARKS)

(b) Schedule IV of the Companies Act 2013 provides that the independent directors shall have certain duties like seek appropriate clarification or amplification of information and, where necessary, take and follow appropriate professional advice and opinion of outside experts at the expense of the company;

I participate constructively and actively in the committees of the Board in which they are chairpersons or members;

I where they have concerns about the running of the company or a proposed action, ensure that these are addressed by the Board and, to the extent that they are not resolved, insist that their concerns are recorded in the minutes of the Board meeting;

I keep themselves well informed about the company and the external environment in which it operates;

I not to unfairly obstruct the functioning of an otherwise proper Board or committee of the Board;

I 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;

I report concerns about unethical behaviour, actual or suspected fraud or violation of the company's code of conduct or ethics policy;

I ["act within their authority"], assist in protecting the legitimate interests of the company, shareholders and its employees etc.

So, it is expected from independent directors that they perform duties properly. However, Section 149(12) of the Companies Act 2013 provides that an independent director and a non-executive director not being promoter or key managerial personnel, shall be held liable, only in respect of such acts of omission or commission by a company which had occurred with his knowledge, attributable through Board processes, and with his consent or connivance or where he had not acted diligently.

Regulation 25(5) of SEBI (LODR) regulations, 2015 provides that an independent director shall be held liable, only in respect of such acts of omission or commission by the listed entity which had occurred with his knowledge, attributable through processes of board of directors, and with his consent or connivance or where he had not acted diligently with respect to the provisions contained in these regulations.

(4 MARKS)

(c) The audit committee must be equipped to assess, monitor and influence the tone at the top to aim at enforcing a zero-tolerance approach to fraud. The audit committee should be sensitive to the various business pressures on management – to meet earnings estimates and budget targets, meeting incentive compensation targets, hiding bad news, etc. – and how small adjustments can trigger bigger problems. The audit committee's objective should be to ensure that arrangements are in place for the receipt and proportionate independent investigation of alleged or suspected fraudulent actions and for appropriate follow-up action.

Some of the Symptoms of potential fraud are –

Overly complex and / or opaque corporate structures.

Overly dominant senior executives with unfettered powers and highly leveraged reward schemes.

Frequent changes in finance, other key personnel or auditors.

Implausible explanations as to surpluses, or projections those are "too good to be true".

Organisations significantly outperforming the competition.

Aggressive accounting policies and frequent changes thereto.

Key questions for audit committees to consider:

Is management taking sufficient responsibility for the fight against fraud and misappropriation?

Is the tone from the top unequivocal in insisting on an anti-fraud culture throughout the organisation?

Do record-keeping policies and procedures minimize the risk of fraud?

Are appropriate diagnostic assessments of fraud risks performed and updated periodically?

Are all significant fraud risks properly included in the enterprise risk management approach, linked to relevant internal controls and monitored?

Do codes of conduct contain adequate, user-friendly and up-to-date behavioral guidelines in respect of fraud and other misconduct?

Are they adopted across the organisation and do they apply evenly to business partners and subcontractors?

What is the level of assurance gained related to the effectiveness of anti-fraud controls by management, internal and/or external audit and is it appropriate in the circumstances?

Are anti-fraud controls designed to detect or prevent financial reporting fraud from the early stage (i.e. before small adjustments snowball into bigger issues)?

Are fraud-tracking and -monitoring systems and fraud response plans in place and are they fit for purpose?

Do staff members at all levels have appropriate skills to identify the signs of fraud and do they receive fraud awareness training relevant to their role?

(4 MARKS)

Answer to Q2.A. - Company Law

Alibaba Nabibasha (Petitioner) vs. Small Farmers Agri-Business Consortium & Ors.(Respondents)

After resignation, Director can't be held responsible for daily affairs of Company including Cheques issued and dishonoured.

Therefore, Mr.Vihaan will not succeed.

(6 MARKS)

Answer to Q2.B. - Insolvency Law

George Vinci Thomas (Appellant) Vs. Capedge Consulting Pvt. Ltd. & Ors (Respondent)

Merely asking for further information does not qualify as pre-existing dispute.

Therefore, the contention of KPT Ltd. is not valid.

(6 MARKS)

Answer to Q3.A. - Interpretation of Law

State Of Maharashtra (Appellant) Vs. Sayyed Hassan Sayyed Subhan (Respondent)

Where an act or omission constitutes an offence under both Food & Safety Standards Act and Indian Penal Code, the proceedings can be initiated under both the enactments.

(6 MARKS)

Answer to Q3.B. - Company Law

Joint Commissioner of Income Tax (OSD), Circle (3)(3)-1, Mumbai (Appellant) vs. Reliance Jio Infocomm Ltd. & Ors. (Respondents)

Mere fact that a Scheme of Compromise or Arrangement may result in reduction of tax liability does not furnish a basis for challenging the validity of the same.

Therefore, contention of Income Tax Department is not valid.

(6 MARKS)

Answer to Q4.A. - FEMA & Other Economic Laws

Govt of N.C.T OF Delhi (Petitioner) vs. Yasikan Enterprises Pvt. Ltd. (Respondent)

The company being a separate legal entity from sole proprietorship, the arbitration clause does not automatically devolve upon the company as there was no arbitration agreement between the parties.

Therefore, the ground to challenge the arbitral award is tenable.

(6 MARKS)

Answer to Q4.B. - Governance Issues

Employees State Insurance Corporation (Appellant) Vs. Venus Alloy Pvt. Ltd. (Respondent)

Yes. The Directors of the Company, who are receiving remuneration, come within the purview of "employee" under sub-section (9) of Section 2 of the Employees' State Insurance Act, 1948 ('the ESI Act').

(6 MARKS)

Answer to Q5.A. - Securities Law

M/s Therm Flow Engineers Pvt. Ltd. (Appellant) vs. SEBI (Respondent)

Merely for violation of 0.03%, penalty of giving open offer is disproportionate.

Therefore, SAT allowed the appeal.

(6 MARKS)

Answer to Q5.B. - Competition Law

Competition Commission of India Vs. JCB India Ltd. and Ors

Authorization for search includes authorization of seizure as well.

DG has the power of search and seizure under the Companies Act Read with Competition Act.

(6 MARKS)