40

STANDING COMMITTEE ON FINANCE

(2005-06)

FOURTEENTH LOK SABHA

MINISTRY OF COMPANY AFFAIRS

DEMANDS FOR GRANTS (2006-07)

FORTIETH REPORT

LOK SABHA SECRETARIAT
NEW DELHI

May, 2006/Jyaistha, 1928(Saka)

FORTIETH REPORT

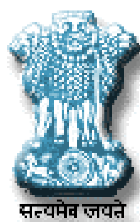
STANDING COMMITTEE ON FINANCE
(2005-2006)

(FOURTEENTH LOK SABHA)

MINISTRY OF COMPANY AFFAIRS

DEMANDS FOR GRANTS (2006-07)

Presented to Lok Sabha on 22.May, 2006
Laid in Rajya Sabha on 22 May, 2006.



LOK SABHA SECRETARIAT
NEW DELHI

May, 2006/Jyaistha, 1928(Saka)

CONTENTS

PAGE

COMPOSITION OF THE COMMITTEE……………………………… (iii)

INTRODUCTION…………………………………………………… (iv)

REPORT………………………………………………………………..

STATEMENT OF CONCLUSIONS/RECOMMENDATION ……

Appendices

I. Minutes of the sittings of the Committee held on 19th, April, 2006……..

II. Minutes of the sittings of the Committee held on 19th May, 2006……..

COMPOSITION OF STANDING COMMITTEE ON FINANCE – 2005-2006

Maj. Gen. (Retd.) B.C. Khanduri - Chairman

MEMBERS

LOK SABHA

2. Shri Jaswant Singh Bishnoi
3. Shri Gurudas Dasgupta
4. Shri Bhartruhari Mahtab
5. Shri Shyama Charan Gupta
6. Shri Gurudas Kamat
7. Shri A. Krishnaswamy
8. Shri Bir Singh Mahato
9. Dr. Rajesh Kumar Mishra
10. Shri Madhusudan Mistry
11. Shri Rupchand Pal
12. Shri Danve Raosaheb Patil
13. Shri Shriniwas D. Patil
14. Shri K.S. Rao
15. Shri Jyotiraditya Madhavrao Scindia
16. Shri Lakshman Seth
17. Shri G.M. Siddeshwara
18. Shri Ajit Singh
19. Shri M.A. Kharabela Swain
20. Shri Vijoy Krishna
21. Shri Magunta Sreenivasulu Reddy

RAJYA SABHA

22. Shri M. Venkaiah Naidu
23. Shri Yashwant Sinha
24. Shri Chittabrata Majumdar
25. Shri S.P.M. Syed Khan
26. Shri Amar Singh
27. Shri C. Ramachandraiah
28. Shri Mangani Lal Mandal
29. Shri Santosh Bagrodia
30. Smt. Shobhana Bhartia
31. Vacant

SECRETARIAT

1.	Dr. (Smt.) P.K. Sandhu	-	Additional Secretary
2.	Shri A. Mukhopadhyay	-	Joint Secretary
3.	Shri S.B. Arora	-	Deputy Secretary
4.	Smt. Anita B. Panda	-	Under Secretary

INTRODUCTION

I, the Chairman, Standing Committee on Finance having been authorised by the Committee to submit the Report on their behalf, present this Fortieth Report on the Demands for Grants (2006-07) of the Ministry of Company Affairs.

2. The Demands for Grants of the Ministry of Company Affairs were laid on the Table of the House on the 11th March, 2006. Under Rule 331E of the Rules of Procedure and Conduct of Business in Lok Sabha, the Standing Committee on Finance are required to consider the Demands for Grants of the Ministries/Departments under their jurisdiction and make Reports on the same to both the Houses of Parliament. Thereafter, the Demands are considered by the House in the light of the reports of the Committee. However, this year, the Demands for Grants of the Ministry of Company Affairs were passed by Lok Sabha on the 17th March, 2006 prior to their consideration by the Standing Committee on Finance. Nonetheless, the Committee examined the Demands for Grants (2006-07) of the Ministry of Company Affairs and issues arising out of these.

3. The Committee took oral evidence of the representatives of the Ministry of Company Affairs at their sitting held on 19th April, 2006 in connection with Demands for Grants (2006-07) of the Ministry of Company Affairs. The Committee considered and adopted the draft Report at their sitting held on 19th May, 2006.

4. The Committee wish to express their thanks to the officers of the Ministry of Company Affairs for the co-operation extended by them in furnishing written replies and for placing their considered views and perceptions before the Committee.

5. For facility of reference, the observations/recommendations of the Committee have been printed in thick type.

NEW DELHI;
19 May, 2006
29 Vaisakha,1928 (Saka)

(MAJ. GEN. (RETD.) B.C. KHANDURI)
***Chairman*,**
Standing Committee on Finance

REPORT

CHAPTER – I

Introductory

"Ministry of Company Affairs", earlier known as Department of Company Affairs under Ministry of Finance, was designated as a separate Ministry in May, 2004 to function under Minister of State with Independent Charge. It is now headed by a Cabinet Minister since January, 2006. The Ministry is primarily concerned with the administration of the Companies Act, 1956, other allied Acts and rules & regulations framed thereunder mainly for regulating the functioning of the corporate sector in accordance with law. The Ministry is also responsible for administering the Competition Act, 2002 which will eventually replace the Monopolies and Restrictive Trade Practices Act, 1969 under which the Monopolies and Restrictive Trade Practices Commission (MRTPC) is functioning. Besides, it exercises supervision over three professional bodies, namely, Institute of Chartered Accountants of India (ICAI), Institute of Company Secretaries of India (ICSI) and Institute of Cost and Works Accountants of India (ICWAI) which are constituted under three separate Acts of the Parliament for proper and orderly growth of professions of Chartered Accountants, Company Secretaries and Cost Accountants in the Country. The Ministry also has the responsibility for carrying out the functions of the Central Government relating to the administration of the Partnership Act, 1932, the Companies (Donations to National Funds) Act, 1951 and Societies Registration Act, 1860.

Review of Report on Demands for Grants (2005-06)

2. The Committee in their 20th Report on the examination of Demands for Grants (2005-06) of the Ministry of Company Affairs had examined detailed Demands for Grants under the Demand No. 17 as well as the following issues related to the overall performance of the Ministry.-

1. Discrepancies in the Demands for Grants
2. Office Expenses – SFIO
3. Serious Fraud Investigation Office
4. Competition Commission of India
5. Investor Education and Protection Fund (IEPF)

6. Vanishing Companies

7. Inspection of companies

8. Filing of statutory returns by companies

3. The Report contained eight recommendations.. Action Taken Notes were received from the Government with regard to all the recommendations contained in the Report. As per the Action Taken Notes furnished thereon as well as the statement made by the Minister of Company Affairs on the floor of the House on 23.12.2005 under Direction 73A of the Directions by the Speaker. The Committee had accepted replies of the Government pertaining to five recommendations/observations. The recommendations mainly covered the following aspects:-

1. Utmost care should be taken by the Government to prevent discrepancy in figures while furnishing Demands for Grants before Parliament.
2. Government should take suitable measures to further strengthen SFIO.
3. The legislation in regard to 'operationalisation of Competition Act, 2002' has already been delayed on account of legal tangles. There should not be further delay in bringing conformity amendments.

4. In respect of one recommendation, the Committee did not wish to pursue the matter keeping in view the reasons cited in the Government's replies.

5. As regards remaining two recommendations/observations, the replies of the Government were not accepted by the Committee and, thus, were again commented upon. These recommendations pertained to Vanishing Companies, the efforts of the regulators to find ways to ensure that investors who had thus been duped, get back their money, penal action against the promoters and directors of the Vanishing Companies and stringent penalties for inconsistencies in filing of annual returns by companies.

CHAPTER – II

6. In the present report, the Committee examined following issues arising out of the Budget Proposals (2006-07) and other related matters:

(i) Comprehensive revision of the Companies Act, 1956
(ii) Functioning of Serious Fraud Investigation Office
(iii) Vanishing Companies
(iv) Utilisation of the accruals to Investor Education and Protection Fund
(v) Liquidation of Companies

COMPREHENSIVE REVISION OF THE COMPANIES ACT, 1956.

7. As per the Ministry, a comprehensive revision of the Companies Act, 1956 had been undertaken by them on the basis of a broad based consultative exercise. A concept paper on Company Law, drawn up in the legislative format, was exposed on 4th August, 2004 for viewing on the electronic media so that all interested may not only express their opinion on the concept evolved but may also suggest formalities on various aspects of Company Law. Comments and suggestions from a large number of organizations, professional bodies and individuals have been received. This consultative process not only allowed ideas, comments and suggestions to flow in form all quarters, but also enabled the Ministry to work out appropriate legislative proposal to meet the requirements of India's growing economy in the years to come.

8. In this regard, the Committee take note of their recommendation contained in 5th Report on Demands for Grants (2004-05) of the Ministry of Company Affairs.

> "The Committee do appreciate the endeavour of the Government to take up the exercise for developing the concept paper for comprehensive overhaul of the Companies Act, 1956. They are given to understand that the said concept paper has been circulated to all the interested parties e.g. corporates, regulatory bodies, stakeholders and autonomous professional institutions. They want that adequate publicity may also be made through print and electronic media so that public at large may also involve

themselves in the exercise and make suggestions. The Committee expect that the exercise would be completed in a fixed time and Government will come forward with a new look Companies Bill which meets the requirements of all concerned without any delay."

9. The Government had in their "action taken reply" stated that a concept paper on Company Law was placed on the Ministry website and a large number of responses had been received. Detailed consultations were being held with various industry associations, professional bodies etc. On the basis of consensus achieved through this process, a revised Companies Bill would be drafted. It is expected that the preparation of a new, revised Companies Bill would be possible by the first quarter of Financial Year 2006-07.

10. The Ministry further informed that in order to have an expert opinion in this direction, the Government constituted an expert committee on 2nd December, 2004 under the Chairmanship of Dr. J.J. Irani, Director, Tata Sons to advise the Government on Company Law. Terms of reference of the Expert Committee were as follows:

1. Issues arising from the revision of the Companies Act, 1956
2. Response received from various stakeholders on the concept paper.
3. Bringing about compactness by reducing the size of the Act and removing redundant provisions.
4. Enabling easy and unambiguous interpretation by recasting the provisions of the law.
5. Providing greater flexibility in rule making to enable timely response to ever-involving business models.
6. Protecting the interest of stakeholders and investors including small investors.
7. Any other issue, related or incidental, to the above.

11. The Expert Committee has since submitted its report on 31st May, 2005. The Ministry, in their written reply, furnished the major findings, observations and recommendations as contained in this Committee Report, which is appended as Annexure-I.

12. When asked by the Committee about the recommendations of the Irani Committee Report accepted by the Government, the Ministry, in a written reply,

informed *inter-alia* that presently, the process of consultation with concerned Ministries/Departments is progressing. Based on the above inputs, a Bill would be introduced in the Parliament that would enable comprehensive revision of the Companies Act, 1956.

13. Asked specifically about the date by which the Ministry is likely to come out with the comprehensively revised version of the Companies Law, the Ministry in a written reply, submitted as under:-

> "The Bill on the revised Company Law is likely to be introduced in the Parliament once the process of consultation and approval is completed. However, this requires appropriate inter-ministerial consultations and approvals. Draft proposals for a new Companies Bill have already been circulated for comments by various Ministries. With requisite approvals and proper vetting by the Legislative Department, a new Companies Bill would be prepared for introduction in the Parliament. Efforts are being made to introduce the above in the Parliament as early possible".

14. Asked about the details of the difference in the recommendations of the Narayana Murthy and Irani Committees, the Ministry of Company Affairs in their written replies inter-alia informed that the Narayana Murthy Committee's recommendations related to issues concerning Corporate Governance in Companies, whereas the Irani Committee was constituted to examine issues arising from the revision of the Companies Act, 1956. It was further added that the scope and mandate given to the Irani Committee is far wider and more comprehensive as compared to the scope of the Narayana Murthy Committee Report. Corporate Governance is one of the issues addressed by the Irani Committee and the inputs provided by the Irani Committee constitute a component of the broad exercise for a comprehensive revision of the Companies Act.

15. When the Committee asked the Ministry to elaborate efforts made by them to invite comments/suggestions on the J.J. Irani Committees recommendations, the Ministry of Company Affairs informed as under:-

"During the meetings of the Expert Committee, representatives of Investors' fora were given a hearing by the Committee. The full text report and recommendations of J.J. Irani Committee have been placed on this Ministry's web-site. A copy of this report has also been circulated, to all the Central Government Ministries and Departments, and to the Chief Secretaries of all the States for comments."

16. It was further added:-

"Subsequent to the publication of the Irani Committee Report, a number of comments have been expressed through the media, mostly favouring and commending the recommendations made by the Committee. The recommendations of the Committee have also been discussed in various seminars/workshops organized by the bodies representing industries and professionals. The response has been largely positive and supporting.

The Ministry has taken up consultation with various regulatory and statutory bodies, Ministries/Departments on the proposals for revision of the Companies Act.

The inputs received by the Ministry on issues relating to Company Law are under examination of the Ministry."

17. During the evidence before the Committee, the Secretary, Ministry of Company Affairs further informed as under:-

"…a comprehensive revision of the Companies Act is now being proposed and we hope to bring it to the Parliament very shortly. In this, while introducing good corporate governance practices, it was felt that some constraints need to be removed. Equally, there has to be a clear perception to have accountability of all stakeholders towards good corporate governance, credibility and value enhancement through transparency and accountability with proper regulatory practices. Therefore, a substantial review of the Companies Act was found to be merited which is presently at a very advanced stage. The process of consultation has been taken up already with various Ministries and Departments and we have good

response from various Departments and we hope to now bring this legislation to the Parliament very shortly.

…besides this, we also got introduced a small Companies Amendment Bill. This was focused to enable e-governance of the Ministry of Company Affairs keeping in mind that we have introduced new ways of doing business in India. We have introduced complete e-governance in the Department. Meanwhile, the Ministry has introduced a limited amendment to the Companies Act to enable smooth implementation of MCA-21 e-governance project. These are required to provide clarity and enable digitizing the support documents submitted. The amendment also provide for enabling security to the document filed digitally. Further, keeping in view the concerns expressed regarding vanishing companies, a provision has been made for allotment of a Unique Identity Number for the Directors. The Bill has been passed by Rajya Sabha which is expected to come before Lok Sabha once the Parliament reconvenes."

18. At the behest of the Committee, the Ministry elaborated upon their MCA-21 project as follows:-

"The MCA-21 system provides for all filings using digital signatures (DSCs) with multiple modes of payments including on-line payments through internet Banking and Credit cards. All transactions in the MCA-21 system are fully secured and follow the industry standards prescribed in this behalf. Security issues have also been subjected to independent third party audit and certification by STQC in addition to its validation by the NISG.

The main objectives sought to be achieved with the implementation of this project relate to the ease of doing business in India through facilitation and effective compliance of the law. Once operational at all locations, the system would provide facilities for all services delivered through the offices of Registrars of Companies on-line which would facilitate completion of all transactions from the comfort of offices or homes of various stakeholders. It is intended to introduce ease of use, speed and transparency in delivery of services while strengthening the compliance regime. Following are

some of the benefits that shall accrue from the implementation of the program:

- (i) Centralised Name Availability and Allocation
- (ii) Expeditious incorporation of companies
- (iii) Simplified and ease of convenience in filing of Forms/ Returns
- (iv) Better compliance management and regulatory monitoring
- (v) Total transparency through e-Governance
- (vi) Customer centric approach
- (vii) Building up a centralised database repository for data mining
- (viii) Enhanced service level fulfilment
- (ix) Inspection of public documents of companies anytime from anywhere
- (x) Easy registration and verification of charges
- (xi) Timely redressal of investor grievances
- (xii) Creation of conducive environment to promote efficiency and effectiveness of employees

19. From the information furnished before the Committee, they take note of the fact that out of the total grant of Rs 145 crore, the Ministry have proposed Rs 70.84 crore towards the implementation and operation of MCA 21 e-governance project and starting work on the second phase to cover the liquidation process.

20. During oral evidence of the representatives of the Ministry of Company Affairs, the Committee expressed their dismay over the lack of provision in the Companies Act on the issue concerning Independent Directors of the Companies and their liabilities. In this connection, the representative of the Ministry stated the following:-

> "…at the present point of time, the Companies Act does not specify Independent Directors. This is a requirement which has come as a result of the list of conditions prescribed by SEBI."

They further inter-alia stated as follows:

> "This is an issue which needs to be examined very carefully. It should be done in the light of inputs that we have and the solution in terms of how it will apply to the corporates across the board, how to come out through the amendment to the Companies Act. We are looking at various proposals for a comprehensive revision of the Companies Act. So, this will be one of the

areas which needs careful examination. I think some of the suggestions made and concerns expressed during the discussion will be taken note of."

21. It is widely known that the Companies Act, in its present form, is quite unweildly and complicated. In this connection, reducing the number of sections/provisions alone will not help in simplifying, rationalizing and modernizing the law. What is needed is that the new law must provide a flexible framework for proper growth of companies, have dynamic orientation and take into account the new developments that have taken place in the corporate world. The Committee recall in this regard, their earlier recommendation as contained in the 5th Report on Demands for Grants (2004-05) wherein they have urged the Government to expedite the matter relating the Comprehensive Review of the Companies Act, 1956. From the response of the Government, they gather the impression that the Comprehensive Bill amending provisions of Companies Act may be Tabled on the floor of the House shortly. They expect that this long awaited piece of legislation will soon see the light of the day and many provisions of the Companies Act needing reforms, as per the requirements of modern day corporate governance practices as well as investors protection, may be amended suitably. The Committee would also find it equally necessary to ensure the use of simple and understandable language as compared to the existing complicated structure of provisions, explanations and multiple cross references in the Companies Act. Moreover, Company law should not be viewed in isolation and must be in harmony with other economic legislations. In this connection, the Committee note that the Expert Committee to advise the Government on new Company Law, under the Chairmanship of Shri J.J. Irani, have already submitted their Report on 31st May, 2005 and subsequently the Government is in the process of consultation and approval on the recommendations of the same.

22. In the course of examination of Budget Proposals for the year 2006-07, another issue concerning Independent Directors of Companies came up before the Committee. As the existing Companies Act is silent on this issue, the Committee note that this requirement was prescribed by SEBI (Securities and Exchange Board of India) as one of the listing conditions. The Committee feel that absence of a relevant provision in the Companies Act has contributed in further ambiguity in so far as the responsibilities of Independent Directors are concerned.

23. The Committee further note that the Government have introduced a limited amendment to the Companies Act to enable 'smooth implementation of MCA-21 e-governance project'. This project aims at providing clarity and security and enabling the digitization of support documents submitted by the companies. The Committee also note that once operational at all locations, this system would provide facilities for all services delivered through the offices of Registrars of Companies on-line and facilitate completion of all transactions from the comfort of homes/offices of stakeholders. In this regard, the Committee endorse the view that there is an urgent need for such e-governance project taking into account the internationally accepted best practices in the ever evolving corporate world, and hope that the operationalisation of the project would be done expeditiously. They also desire to be kept apprised of the concrete measures taken in this direction.

FUNCTIONING OF SERIOUS FRAUD INVESTIGATION OFFICE

24. The Serious Fraud Investigation Office was set up by the Government in 2003 in pursuance of the recommendation by the Joint Parliamentary Committee on Stock Scam. The organization is a multidisciplinary investigating agency, wherein experts from the banking sector, capital market, company law, forensic audit, taxation, investigation, income tax etc., carry out investigation of serious corporate frauds. This organization has completed more than two years of its functioning. In the current year, 5 cases were handed over to the SFIO for investigation. So far 31 cases have been referred to the SFIO for investigation. The SFIO has already submitted investigation reports in 11 cases.

25. The Ministry, in reply to a query, furnished the following details of the mandate under which SFIO was set up:-

> "The Serious Frauds Investigation Office (SFIO) is functioning as an administrative organization attached to the Ministry of Company Affairs. It has also been decided that SFIO would bring to bear multi-disciplinary teams to investigate complex corporate frauds and enable adequate infrastructure and funds to carry out investigations into alleged fraud under the existing legal framework.
>
> It was proposed to set up SFIO under MCA in two stages.
>
> - The first stage involved putting together a multi-disciplinary team and providing it with infrastructure and funds to carry out investigations into alleged fraud. The SFIO, at this stage, would function within the existing legal framework of the Companies Act 1956. Largely, this would involve carrying out investigations u/s 209A and 235 to 247 of the Act.
> - In the second stage, it was envisaged that legislative changes could be contemplated, if necessary, to invest the office with adequate powers and reach. To examine issues related to this aspect, a Committee has been constituted on 23.02.2006.

Investigations into Corporate Fraud: The SFIO is intended to investigate corporate frauds committed by companies, firms or individuals who indulge in frauds, concealments, deceptions, misstatements etc.; companies that do not act in good faith, who cheat or deceive creditors, shareholders, or depositors; and companies which carry out fraudulent purchase/sales, insolvencies, conveyance or transfer of property, especially in the course of carrying out a fraud or committing breach of trust. It has also been stated that the proposed SFIO would primarily cover frauds on, or cheating of, shareholders, investors and depositors. In the course of this investigation, it could cover such institutions that might have been involved in the fraud on creditors, statutory authorities, mutual funds, collective investment schemes, etc.

Presently, this involves carrying out investigation u/s 235 to 247 of the Companies Act, 1956 (hereinafter called as 'the Act'). More specifically, the SFIO is to take up investigation of frauds characterized by:

a) Complexity, and having inter-departmental and multi-disciplinary ramifications.
b) Substantial involvement of public interest to be judged by size, either in terms of monetary misappropriation, or in terms of the persons affected.
c) The possibility of investigations leading to, or contributing towards a clear improvement in systems, laws or procedures.

SFIO not intended for routine investigations: The SFIO is conceived as a professional unit, in the business of investigating white-collar crime. It is not, therefore, to be burdened with routine complaints or inspections. That work will continue to be done by MCA's Directorate of Investigations."

26. Elaborating on the basis of referring the cases to SFIO, the Ministry of Company Affairs, in a written reply, informed as under:-

"Under section 235 of the Companies Act the Central Government, on a report being received from the Registrar in pursuance of section 234 of the

Act may appoint one or more competent persons as inspectors to investigate the affairs of a company and to report thereon in such manner as the Central Government may direct. Similarly, u/s 237 the Central Government may have the investigation carried out likewise if the company itself by special resolution, or Court/CLB, acting under section 237 of the Act, by order declares that the affairs of the company ought to be investigated.

The investigation of companies under sections 235/237 of the Companies Act, 1956 is assigned by the Central Government to Inspectors drawn from the SFIO on the following basis :

(i) where the size of the alleged fraud is estimated to be at least Rs. 50 crore or more, or;
(ii) such companies which are listed or where the paid up capital of the company is more than Rs. Five crores, and 20% or more capital is subscribed by the public; or
(iii) when the alleged fraud involves widespread public concern estimated to affect at least more than 5000 persons; or
(iv) where investigation requires specialized skills and multi-disciplinary approach."

27. When asked to explain the mechanism of SFIO investigation and subsequent procedure for prosecution and other action over the reports of SFIO, the Ministry, in their written reply, have stated as under:-

"The SFIO has a team of experts drawn from the various disciplines like finance, Income Tax, CBI, SEBI etc who assist the inspector drawn from SFIO, appointed to investigate the companies by the Central Government.

In carrying out the investigation the Inspector and his team apply various provisions of the Companies Act, 1956, relating to inspections and investigations, and including investigations into affairs of related companies or of managing agents or associates, production of documents and evidence, seizure of documents by the Inspector, submission of Inspector's report and prosecution etc.

The reports received from SFIO are considered in the Ministry and instructions issued for prosecution under the Companies Act, 1956 and the Indian Penal Code, 1860. Where violations/offences relating to other agencies/organizations/regulators such as Income Tax, RBI, SEBI, etc come to note, copies of the investigation reports are forwarded to the concerned agencies for necessary action at their end under their respective statutes.

So far the Ministry has received investigation reports of eleven companies from SFIO. Out of these, instructions for prosecutions have already been issued in respect of nine companies. Reports in respect of two companies are under examination."

28. The Committee further sought to know about the vacancies in the SFIO, which may be hampering the effective functioining of the organization. Ministry, in their response submitted the following details:

"The vacancy position in SFIO as on date is contained in the following statement:

S/ No.	Designation of Post	Sanctioned Posts	Officers in Position	Vacancies
01.	Director	01	01	**-**
02.	Addl / Joint Directors	12	11	**01**
03	Dy Director (Admn)	01	-	**01**
03	Sr ADs/ ADs	27	25	**02**
04.	Private Secretary	01	01	**-**
05.	Personal Assistants	13	13	**--**
06	Assistants	02	02	**-**

Regional Office Mumbai

S/ No.	Designation of Post	Sanctioned Posts	Officers in Position	Vacancies
01	Addl / Joint Director	01	01	Selection has been made, yet to join.
02	Assistant Directors	02	02	--
03	Personal Assistants	02	--	**02**
	Total			**06**

As per the Ministry, the process to fill up these vacancies is already on.

29. The Ministry of Company Affairs also informed the Committee that an Expert Committee has been constituted to advise the Government on issues concerning the Serious Fraud Investigation Office under the Chairmanship of Shri Vepa Kamesam, Ex-Deputy- Governor, RBI. The Terms of Reference of the Expert Committee are:-

To make recommendations to the Government on:-

(a) Assessment of the need for the details of a separate Statute to govern the constitution and functioning of SFIO;

(b) The nature and details of the legislative changes as may be required in existing laws, to enable effective functioning of SFIO including prosecution of offences detected by it;

(c) The mechanism for referral of cases to SFIO and coordination of activities of SFIO with other agencies/organizations of the Central and State Governments, including investigation;

(d) Powers of SFIO and its investigating officers;

(e) Specification of offences and penalties to enable effective conduct of investigation agencies and the need for Special Courts for trial of corporate fraud cases; and

(f) Other matters consequential to or in pursuance of the above.

30. During oral evidence of the representatives of the Ministry, the Committee expressed concern over the functioning of the SFIO. In this connection, the J.J. Irani Committee have also in their recommendations inter-alia stated that investigation and prosecution procedures need to be simplified to enable SFIO to move swiftly and purposefully for successful prosecution of the guilty. They have also recommended that a separate statute might be framed to regulate and guide the functioning of the SFIO and to address such issues to enable successful investigation and prosecution of cases of corporate fraud. They have recommended that SFIO should serve as a Nodal Agency for unveiling corporate frauds.

31. During the evidence also, similar views were conveyed by Director, SFIO as follows:-

“We are thinking of a separate Act for the SFIO…. It was asked whether we are functioning the way we ought to be functioning as mandated. Yes, we are functioning. In the first phase, we were to cobble up a team of experts drawn from various disciplines and to start working within the given legal framework of the Company Law. In the second stage, we have to go for a separate legislation for SFIO.”

32. The Committee note that SFIO has been functioning since October, 2003 as a multi-disciplinary administrative organization attached to the Ministry of Company Affairs to investigate complex corporate frauds and enable adequate infrastructure and funds to carry out investigation into alleged fraud under the existing legal framework. The Committee note that till now 31 cases have been referred to the SFIO for investigation. Out of these, SFIO has already submitted inspection reports in 11 cases and out of these instructions for prosecutions have already been issued in respect of nine companies. From the replies furnished by the Government, the Committee note that in most of the cases the investigation of SFIO is *sub-judice.* The Committee are dismayed to learn that despite being in existence for more than two years, certain crucial posts e.g. Additional/Joint Director//Deputy Director (Admn.), Sr. ADs/ADs etc. are lying vacant in SFIO. Although the Government is stated to be in the process of filling up the posts, the Committee are not sure as to how much time will it take before these posts are actually filled up. The Committee feel that with the passing of time, more and more cases will be referred to the SFIO, with the result that its work will be increased enormously. Keeping this in view, they recommend that apart from filling the vacant posts immediately, additional posts in various categories may be created so that the cases referred to SFIO are disposed of expeditiously and the purpose for which it came into existence is fulfilled. Since SFIO, conceived as a professional unit requiring specialized skill and multi-disciplinary approach, is intended to investigate corporate frauds, the personnel for this prestigious office may be drawn from finance, income tax, SEBI, CBI etc.

33. The Committee also feel that officers of SFIO should be suitably trained for this purpose. They also recommend that, in this regard, the training and investigation mechanism of SFIO should be of international standard yet keeping in mind the trends and peculiarities of the Indian Corporate World.

34. The Committee further take note of the fact that in pursuance of J.J. Irani Committee recommendation, an expert Committee namely Vepa Kamesam Committee has been constituted to assess the need for and details of a separate statute to govern the constitution and functioning of the SFIO. In this regard, they feel that there is a need to strengthen SFIO with adequate powers to act as a nodal agency in unveiling intricate and complex corporate frauds, in coordination

with other agencies/organizations at the Centre and State levels and, therefore, recommend that a separate Statute to regulate and guide the functioning of SFIO may be framed.

VANISHING COMPANIES

35. The Capital market had witnessed a boom during 1993-94 and 1994-95 when many new companies tapped the capital market and collected funds from the public through issue of shares/debentures. Some of these companies defaulted in their commitments made to the public while mobilising funds. The Securities and Exchange Board of India (SEBI) had originally identified 229 listed companies as “vanished”. A High Powered Central Coordination and Monitoring Committee (CMC) co-chaired by Secretary, Department of Company Affairs (DCA) and chairman, SEBI was set up to monitor the action taken against the vanishing companies, and unscrupulous promoters who misused the funds raised from the public. It was decided by this Committee that seven Task Forces be set up at Mumbai, Delhi Chennai, Kolkata, Ahmedabad, Bangalore, Hyderabad with RDs/ROCs of respective regions as convenor, and Regional Offices of SEBI and Stock Exchanges as Members. Subsequently, the number of Task Forces was reorganized from 7 to 4 corresponding to the Regions falling under the jurisdiction of the four Regional Directors of DCA. The main task of these Task Forces was to identify the companies, which have disappeared, or which have misutilised their funds mobilized from the investors, and suggest appropriate action in terms of Companies Act or SEBI Act.

36. As a result of concerted efforts made by these Task Forces, prosecutions had been launched against the promoters of the vanishing companies under Section 63/68/628 of the Companies Act, 1956.

(i) “63. Criminal liability of mis-statement in prospectus.

(ii) 68. Penalty for fraudulently inducing persons to invest money and

(iii) 628. Penalty for false statements.

37. Besides an effort was also made to bring to the notice of the public, at large, the list of vanishing companies, names and addresses of their directors against whom prosecution proceedings have been launched under section 62/68/628 of the Companies Act, 1956, along with the names of the Lead Manager, Merchant Bankers, Underwriters to the issue etc. who helped these companies in raising the funds.

38. The Committee desired to know the reasons while referring to the fact that SEBI had issued notices to only 22 Merchant Bankers who had handled the public issues of 15 companies that had subsequently vanished after raising money, instead of

all merchant bankers who may have handled public issues of all companies identified to have vanished. The Ministry, in their written reply, stated as follows:-

(a) SEBI issued Show Cause Notices (SCNs) to 22 merchant bankers who handled the public issues of 15 companies, which were subsequently identified as “Vanishing Companies” by Coordination and Monitoring Committee (CMC) after following a process explained in the following paragraphs.

(b) Early in 2000-02, SEBI started the exercise of taking action against the Merchant Bankers (MBs) by collecting information from various sources like Merchant Bankers, Bankers to the Issue, Registrar to the Issue etc. The information so collected was verified with the information given in the prospectus and instances indicating the probable lack of due diligence on the part of Merchant Bankers were noted. Based on above, charges could be framed in the case of public issues of 15 such “Vanishing Companies” and, therefore, Show Cause Notices were issued to 22 Merchant Bankers only, which had handled public issues of these companies.

(c) During this process, SEBI has stated that they faced various operational constraints such as (i) expiry of registration of most of such MBs (ii) SEBI not having any information, whatsoever, about the present whereabouts and / or activities of such MBs (iii) MBs not having the relevant records pertaining to the issue as regulations mandate preserving records for a minimum period of five years only etc.

(d) Further, as per SEBI, they faced certain legal constraints which include (i) a company can not be a “vanishing company” at the time of initial public issue as the act of vanishing is subsequent to the public offering process (ii) MB is appointed by the issuer company at the time of Initial public Offer (IPO) and its responsibilities are to ensure veracity and adequacy of disclosures in the offer documents and to exercise due care and diligence in carrying out the activities related to the issue. Hence initiating actions against MBs who had handled IPOs of companies which are subsequently

identified as “vanishing companies” as an accomplice in the ”act of vanishing” by such companies, becomes legally unviable.

(iii) SEBI invoked its powers u/s 11b of SEBI Act and has so far passed orders against 100 vanishing companies (which include companies which were subsequently put on watch list by CMC and 378 promoters/directors thereby debarring them from accessing the capital market for a period of five years.”

39. During oral evidence, the Committee desired to know whether there exist a confusing state of affairs among the regulators as to who and at what time action would be taken against ‘Vanishing Companies’. It was informed by the representative of the Ministry that a company cannot be a vanishing company at the time of IPO, as the act of vanishing is subsequent to the public offering process and, initiating action against MBs (responsible to ensure veracity of disclosures) as accomplice in the act of vanishing is legally unviable. The Ministry, in their post evidence written reply, further informed as under:-

“The phenomenon of companies vanishing after mobilizing funds from the investors through IPOs has been viewed very seriously by the Government. As a matter of fact, the decision to set-up a Coordination and Monitoring Committee (CMC) to initiate and monitor action against these companies has resulted in a consistent follow-up in the matter. It is with the intervention from the CMC that prosecutions have been filed under various provisions of the Companies Act, FIRs have been registered under the IPC against the promoters of a number of vanishing companies and details of the vanishing companies along with their promoters/directors have been published for wide dissemination to the public. Further, four Task Forces have been assigned the responsibility of identifying companies which might have vanished during the period 1998-2001.

40. It may be further submitted that the scrutiny of prospectus, conduct of Merchant Bankers and other intermediaries vests in the domain of SEBI and the SEBI has been taking action to the extent possible within their regulations. As the fact of vanishing of a company is always after mobilizing funds from the public, the Ministry has taken a decision to take up technical scrutiny of the Balance Sheets of all such

companies which come out with IPOs so as to monitor the utilisation of funds raised from the public. It is expected that this measure should help in early detection of any attempt to mis-use/divert the funds raised from the public.

41. Asked about the present status of taking penal action against the companies reported to have vanished, the Ministry of Company Affairs in their written reply informed that SEBI invoked its powers u/s 116 of SEBI Act and has so far passed orders against 100 vanishing companies (which include companies which were subsequently put on watch list by CMC and 378 promoters/directors thereby debarring them from accessing the capital market for a period of five years.

42. Referring to some media reports stating that about 10 vanishing companies have been identified for special scrutiny, the Committee desired to know the components of the special scrutiny and why was it limited to only 10 vanishing companies. To this, the Ministry, have *inter-alia* replied as follows:-

> "While reviewing action taken against vanishing companies, it was decided that the feasibility of taking appropriate action against the Chartered Accountants (CAs) associated with the public issue of securities made by Vanishing Companies should be explored. It was observed that there were 10 such vanishing companies which had mobilized funds in excess of Rs. 10.00 crore from the market. Accordingly, it was decided to concentrate the available resources on following action against these top 10 companies in the first instance (in relation to the quantum of funds mobilized from the market through public issues) and to examine the role played by the auditors of such companies."

43. When asked about the details of the action taken or planned against auditors/auditors firms, which may have been found to be guilty of wrong doing while auditing the accounts of companies, the Ministry of Company affairs furnished the following information in their written reply:-

a) The details of firms of Chartered Accountants/Auditors involved in these companies have been provided to the office of the Comptroller & Auditor General of India so that the C&AG may exercise due caution while appointing these firms as statutory auditors for conducting the audit of public sector companies.

b) Approval has been accorded to the concerned Registrar of Companies for legal action u/s 233 of the Companies Act after going through the process as laid down u/s 234 of the Act against the Auditors of such companies. Reports justifying action u/s 233 have since been received in respect of three companies against whom prosecution has been approved. Evidence in respect of the remaining seven companies is being gathered and examined.

c) Further, the Ministry is also in the process of making a reference to the Institute of Chartered Accountants of India for initiating disciplinary proceedings against the auditors of the three companies referred to at (b) above."

44. Elaborating the definition of a 'Vanished Company', the Committee were apprised by the Ministry that one of the criteria for identifying a company as 'vanished' is that 'no correspondence has been received by the Exchange from the company for a long time'. When asked to specify as to what is meant by 'long time' in the criteria and whether this meant that only listed companies could be categorized as 'vanishing' as per the criteria applicable, the Ministry, in a written reply, *inter-alia* stated as under:-

"For identifying a company as vanished, following Criteria has been adopted by the CMC:

(i) Companies, which have not complied with listing requirements/filing requirements of Stock Exchange/ROC respectively for a period of 2 years;

(ii) No correspondence has been received by the Exchange from the company for a long time;

(iii) No office of the company is located at the mentioned registered office address at the time of Stock Exchange inspection.

45. All the prescribed conditions have to be met for treating a company as a vanishing company and companies satisfying one or more but not all conditions are not to be considered as vanishing. Though the expression 'long time' has not been specifically defined in the criteria, the Task Forces, in practice, take any period between 2 to 3 years as long time. The criteria is applicable only to the

public limited companies, which raised public money through issue of prospectus."

46. As informed by the Ministry, about 115 "vanishing" companies had since been traced back. A watch on these companies was being kept and inspection of books of account etc. of most of these companies had been ordered. In this connection, the Committee desired to know whether this will bring these defaulting companies to book and ultimately fetch desired results in favour of the investors. The Ministry, in a written reply submitted as under:-

> "Inspection of Books of Accounts of companies serve two-fold purpose i.e. to enhance the supervision and scrutiny of the activities of these companies and, secondly, to ensure compliance of the provisions of Companies Act. Compliance of various provisions of the Act results in bringing about transparency in the working of the company which takes care against any fraudulent activities such as siphoning of funds. A close watch is being kept to ensure that these companies do not indulge in any fraudulent activities again after re-surfacing. Further, the inspections may bring out substantial evidence on record for establishing the allegations made against these companies to enable successful prosecution under provisions of companies Act, 1956 against the defaulting companies. There are four Task Forces, one each corresponding to a Region, falling under the jurisdiction of four Regional Directors of Ministry of Company Affairs (MCA). Other members of these Task Forces are representatives of SEBI, Regional Stock Exchange and concerned Registrars of Companies. Representatives from the State Governments (from Home/Police Department) are also invited to the Task Force meetings for monitoring action under the Indian Penal Code (IPC). The main responsibility of these Task Forces is to identify the companies which have vanished after mobilizing funds from the investors, to suggest/take appropriate action in terms of Companies Act or SEBI Act or any other law applicable, and monitor the action initiated in different cases.
>
> The system of allotment of a Director Identification Number (DIN) to all the Directors has been brought in under the MCA21 e-governance project. This Number is generated electronically and a database of all the

Directors of all the Companies registered with the ROC will be maintained by the system. With this system in place, it would be easier to track a Director's whereabouts."

47. As per the information furnished to the Committee by the Government, the Samir Biswas Committee on safeguarding the interests of the depositors/investors had inter-alia recommended for setting up of a coordination mechanism involving Ministry of Company Affairs, Department of Economic Affairs and SEBI. When asked whether the existing coordination mechanism involving Ministry of Company Affairs and SEBI for the purpose of keeping a track on the "Vanishing Companies" could also involve the Ministry of Finance (Department of Economic Affairs), the Ministry in a written reply stated that the matter is to be considered by the Ministry of Finance.

48. The Committee note that the Government have so far traced back about 115 vanishing companies. However, it remains to be seen whether the investors duped by these companies, will ultimately get some relief. The Committee are convinced that the issue of vanishing companies is inextricably linked with the issue of 'Vanishing funds', which first of all implies that the investors who have been lured into investing in a company that has vanished must get back his/her legitimate dues. They, therefore, feel that the matter of vanishing companies does not only rest with just tracing out the vanishing companies and their inspection of books of accounts etc, but equal attention should be paid to the prosecution mechanism so that the investors could get their money back. Equally important is to keep a watch on the vanishing companies so that they do not resurface in a different name to dupe the investors again. The Committee feel that utmost vigilance is required to prevent efforts by a 'vanishing company' or a defaulting company to restart its operations in another name or disguise.

49. The Committee also recommend that special care should be taken at the time of registration of a company as this marks its arrival and possibility of raising capital. Therefore, the Committee recommend that Government should be more alert during the process of registering the companies so as to assess their potential viability to survive in the competitive environment and benefit their investors.

50. The Committee feel that the auditors/auditing firms who either fail in their duties to audit the companies/properly or knowingly shut their eyes to any impending misfortune for the investors should also be held equally responsible. The Committee desire that the Government should, within the extant provisions of the law, try to pinpoint erring auditors and their firms equally responsible, otherwise the very idea of the auditors acting as whistleblowers would be defeated. The Committee find that the Government are toothless in this regard as they gather the impression, from the replies of the Government, that all they can do is to ask CAG to exercise due caution while appointing the 'guilty' firms as statutory auditors for conducting the audit of public sector companies, while they are free to operate in the private sector. The Committee, in this regard, would like

to see the 'guilty' auditors/auditing firms to be treated as accomplices in the eyes of the Government.

51. The Committee also find that even the definition of vanishing companies is ambiguous thereby leaving loopholes in the law. From the information furnished to them, they note that one of the criteria which states that 'no correspondence has been received by the Exchange from the company for a long time', is interpreted by the Task Forces concerned to imply a period between 2 to 3 years of absence of correspondence between the exchange and the company. The Committee feel that any company which has duped its investors, can continue to operate and avoid being classified as 'vanishing' just by sending a piece of correspondence, at intervals of 2-3 years. They, therefore, feel that the criteria for identifying a company as vanished/vanishing needs streamlining and call upon the Government to have a re-look at the definition, so that all such companies, having the slightest intention of duping investors of their hard earned money, could be classified as 'vanishing or potentially vanishing companies'.

52. In this regard, the Committee also note the recommendations of the Samir Biswas Committee that the coordination mechanism may involve Ministry of Finance (Department of Economic Affairs) in addition to Ministry of Company Affairs and SEBI. The Committee feel that the present mechanism may be extended to also incorporate representatives of Department of Economic Affairs, as they are primarily responsible to oversee the implementation of Government's policies in regard to regulation of Capital Market.

53. The Committee note the Government's efforts to prepare a database of all Directors of the companies under the system of allotment of DIN (Director identification Number) under the MCA-21 e-governance project and urge the Government to expedite completion of the same. The Committee also note the Government's decision to take up a technical scrutiny of Balance Sheets of all such companies, which come out with IPOs, so as to monitor the utilization of funds raised from the public. The Committee while appreciating the Government's decision, desire that the Government may fix a suitable time limit in this direction so that the investors in the secondary market may also be benefited.

Utilisation of the accruals to the Investor Education and Protection Fund

54. In pursuance of sub-section (1) of Section 205C of the Companies Act, 1956, the Government/ established the Investor Education and Protection Fund (IEPF) with effect from, 1st October, 2001 for promotion of investor awareness and protection of their interests.

55. Asked to furnish the percentage of funds under IEPF, which have been utilized by the Ministry in each of the last three years, the Ministry have informed as under: -

Amount in Rupees			
Financial Year	**Budget**	**Expenditure**	**Percentage**
2002-2003	3,02,00,000	1,79,40,000	59.40%
2003-2004	3,00,00,000	2,83,55,000	94.52%
2004-2005	3,00,00,000	1,63,37,684	54.46%
2005-06 (up to 31.12.05)	2,50,00,000	2,16,81,245	86.72%

56. As per the reply furnished by the Ministry, the total credit to IEPF in the last 3 years was as follows:-

Financial Year	Amount
2002-03	Rs. 108,69,29,558.18
2003-04	Rs. 103,85,02,945.05
2004-05	Rs. 124,43,30,796.51

57. When asked to explain the reasons for inconsistency in utilizing the proceeds of the funds under IEPF over the years and the action which is being taken by the Ministry to ensure that the funds available under the IEPF could be more fruitfully utilized, the Ministry, in a written reply stated as under:-

"Every year a budgetary allocation is made to IEPF by the Finance Ministry. IEPF rules prescribe well-defined procedure for utilization of the allocated funds. Financial assistance is provided to any association/organization only after the pre-sanction scrutiny of its

proposals. Indian Institute of Capital Markets (IICM), Mumbai has been engaged by this Ministry to conduct Pre-Sanction scrutiny. IICM examines the proposal of the organisatino/association with a view to checking the genuineness of the organization and reasonableness of the proposal. The recommendations of the IICM are, thereafter, placed before the Sub-Committee/ Committee on IEPF for a final decision on the approval of the proposal. Financial assistance under IEPF is provided to the extent of 80% of the total project cost only and the remaining 20% is required to be borne by the organization itself. In the first instance, only 80% of the approved funding is released to the organization. For the release of balance 20% organization is required to submit an Utilisation Certificate in respect of the grant provided under IEPF. The Utilisation Certificate so submitted is scrutinized by the IICM. After its post-sanction scrutiny only, the final installment is released.

The proposals received for funding under IEPF are put through a strict scrutiny with a view to ensuring the genuineness and track records of the applicants concerned and the effectiveness of the proposal towards achievement of the defined objectives. It may thus be appreciated that the actual utilization of funds depends upon the number of viable proposals received during the year, which are approved by the Sub-Committee/Committee on IEPF."

58. It was further added as under:-

"Action is being taken by the Ministry to spread awareness and educate the investors which includes launching of an aggressive media campaign through advertisements in the print media and capacity building programmes including training of trainers sessions organized through IICM (especially for new organizations which are active at taluka level). As a matter of fact, the Ministry organized a meet of the various VOs/NGOs involved in Investor Education along with the representatives of SEBI, NSE, BSE and Mutual Funds Association of India on this subject."

59. In view of the fact that all the vanishing companies were listed companies and the primary responsibility for regulating these companies rest with SEBI, the Committee desired to know whether a part of the corpus of the fund could be assigned

to SEBI in addition to the Ministry of Company Affairs or whether the Ministry would favour the fund to be placed under the Central Monitoring Committee jointly chaired by the Ministry and SEBI. The Ministry, in a written reply, informed as under:-

> "The Ministry do not support the idea of either assigning the funds under IEPF under the Companies Act, 1956 to SEBI or placing the funds under the Central Monitoring Committee jointly chaired by Ministry and SEBI since IEPF has been created by the Government after expropriating the moneys, which belong to investors by exercising its sovereign right through Statute. The money thus expropriated gets credited to the Consolidated Fund of India and any expenses incurred for meeting the cost of Investor Education and Protection activities have to be made out of annual appropriations from the budget allocated to it by the Parliament of India. This task is entrusted to the Ministry of Company Affairs under the Statute. Therefore, under section 205C of the Companies Act 1956, the funds can be utilized for promotion of investors' awareness and protection of the interests of investors in accordance with the rules notified under the Act. In any case, SEBI is represented on the IEPF Committee."

60. Under IEPF, various programmes on investor education and awareness have been funded and organized through NGOs/Societies/Associations/ Institutions etc. As per the Annual Report (2005-06) of the Ministry, fourteen new NGOs/VOs/Institutions have been registered under IEPF till date during the current Financial Year.

61. To make investors aware, the Ministry are also stated to have been launching campaigns through electronic and print media. As per their Annual Report, 2005-06, it has been stated that two series of investors education publicity campaign have already been completed, which aimed at educating investors on investing in market instruments, Initial Public Offers (IPOs) and mutual funds. A media campaign was launched in various national as well as regional language newspapers wherein besides the above said educative message, NGOs/VOs involved in Investor Education and Protection activities, especially those with a rural outreach, had been invited to apply for financial assistance/grants under IEPF schemes. Further, the organizations, which are

keen to carry out research on investor protection/education-related issues, had also been invited to submit their proposals to the IEPF. Investor Education message was aired on All India Radio through Prasar Bharti to create awareness on the issues concerning investors and about the IEPF.

62. When asked by the Committee to furnish details of the ways, by which the funds already available under the IEPF could be more fruitfully utilized, the Ministry have stated as under:-

"The funds already available under the IEPF, which are available to Ministry, could be more fruitfully utilized in the following ways:-

(i) Awareness programmes through Media (Electronic as well as print media);
(ii) Registration of voluntary associations or institutions or other organizations engaged in Investor Education and Protection activities and by providing financial assistance to them for projects for Investor's Education and Protection including research activities;
(iii) Coordinating with institutions engaged in Investor education, awareness, and protection activities and taking up initiatives in close coordination;
(iv) Under the Capacity Building programmes, conducting "Training of Trainers" programme through IICM especially for the new organizations, preferably those active at Taluka level, even if such organizations had not been registered with the IEPF;
(v) Expansion of activities under IEPF by taking up the Financial Literacy Programme in a big way.
(vi) Engagement of a professional agency under the IEPF to conceptualise and implement financial literacy programmes.
(vii) Strengthening the concept and adoption of good corporate governance practices through the National Foundation for Corporate Governance, including a focus on the Small and Medium Enterprises.

63. In this regard, the J.J. Irani Committee have recommended as under:-

"(The Committee) noted that the Ministry of Company Affairs, who administer the fund, had already invited some schemes in this regard. The Committee recommend that the structure and administration of the fund should be revamped and schemes should be made more comprehensive and their scope expanded to enable flow of current information to the investors as well as their education in respect of their rights. Such programmes should have special components for education at school/college level, on line and distance learning, support genuine efforts in the Non-Governmental sector, information collection, research and analysis on matters of small investor concerns, enable capacity building of adjudications such as consumer courts on issue involved in legal redressal of investor complaints."

64. Keeping in view the fact that the matter of investors' grievances largely related to complaints of investors regarding shares etc. and also that the funds allocated to the IEPF largely remain under-utilised, it was suggested that the funds might be given to the SEBI instead of vesting their control with the Ministry of Company Affairs. Asked by the Committee whether a mechanism could be evolved whereby a part of the corpus could be assigned to SEBI in addition to the Ministry of Company Affairs, the Ministry stated as under:-

"IEPF has been set-up by the Government under the provisions of Section 205C of the Companies Act. The Central Government carries out the mandate provided by the Statute by expropriating the moneys which belong to the investors under the conditions specified in the Act by exercising its sovereign powers. The funds so collected under the law for the Investor Education and Protection Fund are credited to the Consolidated Fund of India and a budgetary allocation is made by the Parliament for carrying out various activities by the Central Government under IEPF every year.

During last three years, on an average 69.46% of the budget allocated to the IEPF, have been utilized for carrying out various activities under IEPF. A number of new initiatives have been taken under the IEPF.

It may be mentioned that the interests of small investors relate to corporate actions spanning over different classes of companies e.g. payments on dividends, Deposit and Debenture holders etc. SEBI, as a capital market regulator, is required to regulate interrelationships between various stakeholders of listed companies participating in the capital market, including investors, so that the interests of each are addressed in a fair and balanced manner. The interventions by SEBI are to be viewed in context of its primary regulatory role and are not intended to a substitute for the duties required to be discharged by the Central Government under the statute.

However, the Ministry has been making efforts to improve the utilization of funds through many new programmes. Besides, issues relating to appropriately addressing the refund claims of investors, whose funds are expropriated to the IEPF, also need to be addressed for which the Ministry is considering legislative proposals.

It is understood that SEBI is encouraging certain activities for Investor Education through the National Stock Exchange/ Bombay Stock Exchange which have made provision of funds for this purpose. It is open to the Central Government in the appropriate Ministry to make grants to the regulator to fund such of its activities as are found consistent with the provisions of the relevant Act."

65. The Committee note that the utilization of the proceeds of the funds under IEPF have shown an inconsistent trend. The percentage of expenditure in 2002-03 was 59.4%, in 2003-04 it was 94.52%. Again in 2004-05 it plunged to 54.46% and in 2005-06 it was 86.72%. While taking note of the Government's efforts for a more effective utilization of the funds available under IEPF, the Committee still feel that such efforts are not adequate enough. The Committee feel that the Government have not been able to utilise the amount of fund available to their credit. This calls for restructuring of schemes under IEPF. The Committee also take note of the J.J. Irani Committee's recommendations in this regard and express agreement over their suggestion that the structure and administration of the fund should be revamped and schemes should be made more comprehensive and their scope expanded to enable flow of current information to the investors about their rights.

66. Besides, in view of the spurt in various scams related to capital market in the last few years, the Committee feel that the time has come to utilize the IEPF on the education of small investors, who are more gullible due to lack of proper information.

67. The Committee note that the Government do not support the idea of either assigning the funds under IEPF created under the Companies Act, 1956 to SEBI or placing the funds under the Central Monitoring Committee jointly chaired by the Ministry and SEBI on the ground that since IEPF has been created by the government after expropriating the moneys from the budget allocated to it, which belong to investors by exercising its sovereign right through Statute. Moreover SEBI is already represented in IEPF committees. The Committee are, however, of the view that the broad issues on which complaints from the aggrieved investors are being received relate to refund claims of investors, shares/debenture certificates, dividend amount, interests etc. which are generally looked after by SEBI. They further feel that since SEBI is the primary market regulator and cases of unscrupulous persons duping investors is also one of its concerns, it would, perhaps, be appropriate if SEBI is given a bigger role not only in preparation and approval of schemes relating to IEPF but also in the approval for disbursement of funds. The Committee hope that the

Government will consider the concern expressed by them and will administer the Investor Education and Protection Fund (IEPF) in coordination with SEBI.

LIQUIDATION OF COMPANIES

68. The Indian system provides neither an opportunity for speedy and effective rehabilitation nor for an efficient exit. The process for rehabilitation, regulated by the Sick Industrial Companies (Special Provisions) Act 1985 through the institutional structure of BIFR is amenable to delays and does not provide a balanced or effective framework for all stakeholders. The process of liquidation and winding up is costly, inordinately lengthy and results in almost complete erosion of asset value.

69. Thus, one of the major problems relating to corporate functioning in the country has been identified to be the slow process of liquidation whereby the value of assets is significantly reduced due to considerable delays. Asked about the steps taken by the Ministry to bring about insolvency reforms and improve upon recovery rate within the existing legal system, the Minister of Company Affairs in a written reply stated as under:-

> "The existing statutory framework to address issues relating to corporate insolvency is prescribed under the Sick Industrial Companies (Special Provisions) Act, 1985 (SICA) in terms of rehabilitation of companies and under the Companies Act, 1956 in respect of liquidation and winding up of companies.
>
> Through the Companies (Second Amendment) Act, a revised framework for rehabilitation and revival of companies as well as their liquidation and winding up was provided for, to be adjudicated by the National Company Law Tribunal and the National Company Law Appellate Tribunal. However, due to legal challenge faced to the constitution of the NCLT/NCLAT, the other provisions of the above amendment Act are yet to be notified.
>
> As per the Companies (Second Amendment) Act, 2002 with the constitution of the NCLT/NCLAT, SICA would be repealed and the functions performed by BIFR and AAIFR for revival and rehabilitation of companies would be transferred to NCLT/NCLAT. Simultaneously, matters relating to liquidation and winding up of companies would be transferred from High Courts to NCLT/NCLAT. As mentioned above,

these provisions are yet to be notified since the NCLT/NCLAT have not been constituted.

At present, under the existing Companies Act, 1956 liquidation and winding up of companies and disposal of assets of such liquidated entities along with distribution of proceedings amongst stakeholders is carried out in accordance with a process laid down under the Companies Act, 1956 as per the directions of the High Courts."

70. The Ministry have also delineated the present status of the NCLT/NCLAT as under:-

"Constitution of the National Company Law Tribunal and the National Company Law Appellate Tribunal was envisaged through the Companies (Second Amendment) Act, 2002. However, when the provisions relating to the constitution of the NCLT/NCLAT were notified, there was a legal challenge to the above enactment in the Madras High Court. The Madras High Court gave its ruling in April, 2004 whereby some of the provisions of the said amendment Act were held to be unconstitutional. The operation of the above amendment Act was also stayed until the suitable rectification was made. The Central Government filed a Special Leave Petition against the above ruling of the Madras High Court in May, 2004. The SLP filed by the Central Government is under consideration of the Supreme Court. This matter was last heard on 5th October 2005 and was scheduled for further hearing on the 8th November, 2005. The matter is yet to be re-listed for which efforts are being made. Thus the final orders of the Court on the above matter are yet to be received. Therefore, it has not been possible to set up/constitute NCLT/NCLAT."

71. The Irani Panel in their recommendation stated that "a recent survey by World Bank (Doing Business in 2005-India- A Regional Profile) has pointed out that it took 10 years on an average to wind up/liquidate a company in India as compared to 1 to 6 years in other countries.

72. The Ministry have in a written reply informed that 6259 companies were under liquidation by 31/03/2005.

73. When asked specifically whether the Ministry plans to take steps within the existing laws to expedite and simplify the procedure for the "exit" of companies, they have in a written reply stated as under:-

"Cases of companies that become defunct are processed for striking off their names from the register of companies under the Companies Act, 1956 (u/s 560, as per the procedure laid down therein.)

From time to time, the Ministry brings about special exit schemes to enable exit of defunct companies through special schemes. In pursuance of this, Simplified Exit Schemes (SES) were launched in 2003 and 2005. In pursuance of SES, 2003, a total of 28,050 number of companies applied for exit from the companies register. Out of these, processing in respect of 21,004 companies has been completed. In response to SES, 2005, a total of 26,626 companies have applied for exit from the companies register of which 14,947 have been processed and the remaining case are under process."

74. Asked specifically about the time taken for a company to get liquidated in India as compared to the International standards in this regard being followed in select developed nations of the world, and the reasons therefor, the Ministry have in their replies to supplementary list of points furnished as under:-

"The World Bank Report "Doing Business in 2005" has taken some indicators relating to different aspects of doing business to benchmark regulatory environment in countries. One such indicator is 'Closing a Business'. According to this report, it takes about 10 years in India to conclude insolvency proceedings. As per the World Bank report, the time taken in China, Malaysia and Thailand is between 2-3 years.

In India, a company can be closed under the Companies Act, 1956 through a legal process, under the orders of the High Court. However, a company can also be closed voluntarily or on a petition filed by its stake holders or by the Central Government but in all cases the closure is with the approval of High Court.

Pressure of work on the Courts, the nature of judicial procedure, multiplicity of Court proceedings, provision for rehabilitation of sick

companies before winding up are some of the factors for delay in the process of liquidation of companies.

Steps are being taken for reforms in this areas, which are as under:-

(a) The Second Amendment Act, 2002 was enacted and provided for constitution of specialized quasi-judicial tribunal, called the National Company Law Tribunal (NCLT) which would *inter-alia* deal with rehabilitation and winding up of companies in a time bound manner. However, the Act, though enacted, could not be notified on account of legal challenge in Madras High Court. The Madras High Court ruled that certain provisions of the above Amendment Act required modification in order that the same was consistent with the Constitutional scheme of division of powers. Subsequently, an SLP was filed in Supreme Court by the Central Government against the Madras High Court ruling, which is under consideration of the Apex Court since May, 2004.

(b) Ministry has taken an exercise for comprehensive revision of the Companies Act. On the basis of broad-based consultation process, a Committee of experts headed by J.J. Irani was also constituted to advise the Government on the matter. In view of the recommendations made by the Irani Committee as also the other inputs, a draft Bill for comprehensive review of the Companies Act, is at an advanced stage of preparation.

The framework of speedy liquidation and winding up of companies is expected to be available subject to the decision of the Supreme Court on the SLP referred to above and the revision of the Companies Act, 1956."

75. During the briefing meeting, the representative of the Ministry of Company Affairs informed the Committee about the special schemes for exit of companies as under:-

"One part of the question dwelt on those companies which are not functional. Those companies had been registered and had come into force as legal entities but they are not carrying on any business. These

are defunct companies. Schemes which are taken up are actually for weeding out those defunct companies. When you carry out a special scheme, basically during the period of that scheme, you observe the same requirement which are there in the law only you do it as a campaign and you do it on a time frame basis. Therefore, you have got about 6.75 lakh companies on the companies register. It is possible that a large number of them may not be functional. Even if they are not functional, their exit has to follow this process."

76. Explaining the reasons for inordinate delays and lengthy procedures for the exit of companies, the Committee was briefed as under:-

"If you are in the companies register then a host of liabilities are associated with the rest of the world whether it is the financial institution, banks or so on and so forth. There is a host of liabilities surrounding your presence on the companies register. Therefore, the exit from the companies register is a carefully monitored process."

77. Supplementing the replies, it was added:-

"Second part of the question dealt with those companies which are there in the register but they are not functional. But they are not filing the documents. In other words, we do not know whether they are functional or non-functional. They may be functioning but they are not complying with the requirement of filing the documents. If a company does not comply with the requirement of filing the document, the Companies Act deals with it in a different way. You can file documents after the time which is prescribed for that document. The act of non-filing immediately becomes violation of the Act. You can rectify that violation on the payment of an additional fee. Therefore, the act of non-filing by itself does not automatically lead to prosecution. If there is persistent default for more than one year even after time allotted for payment of additional fee and so and so forth, you do not file it, then the prosecution becomes a possibility. Therefore, the prosecution figures which relate to non-filing will not reflect a large number of cases where these violations have been rectified on the payment of additional fee. Now the logic in this is that in the operation of a corporate, there will be a large number of

procedural issues are involved. On the payment of additional fee or the additional charges, opportunity is given to the corporate to rectify it."

78. Coming to the query of the serious problem of inordinate delay and lengthy procedure it was further submitted:-

"Now the third aspect of the question which is much more serious problem and which we encountered comes up. We are talking of exit from the companies register of non-functioning companies. We can do it in certain circumstances. The second part relates to insolvency which a number of Hon. Members have mentioned and which is a common issue also. Insolvency also refers to exit which is in different set of circumstances where the exit from the companies register takes place under specific section and the procedure laid down under that section of the Companies Act. A company wanting to exit, can make an application under Section 560 and start the exit proceedings. In insolvency which comes under the liquidation or winding up, there is a different kind of procedure. The administrative and judicial or statutory process which is there under section 560 will not be open or available to the company under liquidation or winding up. The winding up of that company has to take place under the strict guidance the High Court on all stages. As you know, insolvency and liquidation in India take a long time. The amendment was brought out about it in 2002 to provide a special and specific forum which, in addition to other things will also take over the function of liquidation and winding up from the High Courts. So, this forum called the National Company Law Tribunal (NCLT) was thought of and it also provided for an Appellate Tribunal called the National Company Law Appellate Tribunal. Increasingly the world over, the insolvency is being recognized as semi-judicial or semi-economic or semi-commercial process. It is not purely and entirely a judicial exercise. There has to be a way out so that it could become functional and return to the economy. "

79. Subsequent to the briefing, the Ministry have in their post-evidence written reply informed as under:-

"Companies can be struck off from the register of companies pursuant to provisions of section 560 of the Companies Act, 1956 (Act). The Ministry

of Company Affairs (MCA), however, has introduced from time to time, special schemes for allowing defunct companies, on their own applications, to exit from the Companies Act, 1956. Recently, two such schemes namely, Simplified Exit Scheme (SES) 2003 and Simplified Exit Scheme (SES), 2005 were operated by the Ministry. SES 2003 was in operation from 25.3.2003 to 31.3.2004 and SES 2005 was in operation from 1.2.2005 to 31.8.2005.

The ROC have also been instructed during November, 2005 to detect and strike out the names of defunct companies i.e. companies which had not filed their Balance Sheets or Annual Returns for three consecutive years, pursuant to 'suo moto' powers vested with them u/s 560 of the Companies Act, 1956.

However, it is to be noted that the process of exit of a company from Register of Companies has many legal implications for the creditors, members, employees and other stakeholders of the company. For this reason, the Law prescribes a procedure that provides opportunity to be given to all concerned. Such procedure therefore needs to be followed fully.

As for the liquidation and winding-up of companies, it is done under the provisions of the Companies Act, 1956 through a Court driven process. Revival and rehabilitation of sick industrial companies is done pursuant to the provisions of the Sick Industrial Companies (Special Provisions) Act, 1985 (SICA) through Board for Industrial and Financial Reconstruction (BIFR) and Appellate Authority for Industrial and Financial Reconstruction (AAIFR)."

80. The Committee note that the J.J. Irani Committee have already taken up the issue of exit or liquidation of companies in detail in view of the inordinate delays and lengthy procedure for companies to exit. The Committee also note from the reply of the government referring to the observation in a World Bank Report that the time taken for a companies to exit is between 2-3 years in China, Malaysia and Thailand whereas it is about 10 years in India. They further note that the Government have attributed this delay to the lengthy nature of judicial process. The Committee are of the view that it is essential to provide a sound framework for winding up and liquidation of companies. In this connection, the Committee recommend that in the extant legal provisions, the Government should strive work in such a time-bound manner that, excluding the time taken for obtaining the approval of the High Court, all other formalities could be completed within a period of 2-3 years. Moreover, the Committee hope that efforts by the Government to get the NCLT second Amendment Act, 2002 passed at the earliest in their favour by the Supreme Court, would pave way for its establishment ultimately. This, the Committee hope will help in reducing time for getting required judicial approval for exit of companies overall, the Committee opine that simplifying the existing liquidation process and speeding up the winding up of sick companies having no chance of revival would be steps in the right direction. Besides the modified framework should seek to preserve the estate and maximize the value of assets of the existing company so that those could be redeployed suitably.

NEW DELHI;
19 May, 2006
29 Vaisakha, 1928 (SAKA)

MAJ. GEN. (RETD.) B.C. KHANDURI
Chairman,
STANDING COMMITTEE ON FINANCE

ANNEXURE-I

Major recommendations of Dr. Irani Committee

(a) Small and Private Companies should be provided greater flexibility and freedom of operation while enabling compliance at low cost. Law should recognize One Person Company (OPC). Such companies should be provided with a simpler legal regime through exemptions;

(b) Special dispensations for Producer Companies and Public Financial Institutions (PFIs) need not be provided through the Companies Act;

(c) Limited liability partnerships should be facilitated through a separate enactment;

(d) Law should provide for only the minimum number of directors necessary for various classes of companies. There need not be any limit to maximum number of directors. Government should not intervene in the process of appointment and removal of directors in non-Government companies. No age limit for directors need be specified in the Act other than procedures for appointments to be followed by prescribed companies for appointment of directors above a particular age;

(e) Every company to have at least one director resident in India;

(f) Presence of independent director on the boards of companies having significant public interest would improve corporate governance. Law should recognize the principle of independent directors;

(g) Decision on remuneration of directors should not be based on a “Government approval based system” but should be left to the company;

(h) Certain committees such as Remuneration Committee, Audit Committee, Stake Holder’s Relationship Committee to be constituted with participation of independent directors should be mandated for certain categories of companies where the requirement of independent directors is mandated;

(i) Every company should be required to appoint, a Chief Executive Officer, Chief Financial Officer and Company Secretary as its Key Managerial Personnel whose appointment and removal shall be by the Board of Directors;

(j) Law should impose a duty on every director to disclose to the company the contracts in which he has any interest or concern. Transactions in which directors are interested should take place subject to approval of Board of directors and beyond a limit subject to approval of shareholders;

(k) 'Minority' and 'Minority Interest' should be defined in the substantive Law;

(l) Law should prescribe a regime in which minority rights are fairly protected without enabling any interest group to obstruct corporate processes. There should be recognition of principle of valuation of shares through an independent valuer whenever company causes an exercise of merger/ restructuring etc.;

(m) A separate enactment for investor protection is not required. Corporate processes should recognize the investors as a stakeholder;

(n) Monitoring the end use of funds collected from public should be the responsibility of the shareholders of the company. The insurance option should be explored for deposits with the companies. Credit rating need not be mandated except for companies seeking deposits;

(o) An effective investors grievance redressal mechanism by way of recourse to consumer courts and capital markets ombudsman should be provided for safeguarding interests of investors;

(p) Rights of investors in respect of unclaimed dividends etc. to be recognized even after 7 years period;

(q) Timeframes prescribed for processes of issue of capital be rationalized to be at par with international practices;

(r) Concept of Shelf Prospectus may be extended to other class(es) of companies who access capital market more frequently as Well Known Seasoned Issuers (WKSI), in a manner to be prescribed by the capital market regulator;

(s) Enabling provisions for Tracking Stock and Treasury Stocks could be made in the new Law;

(t) Companies should be permitted to issue perpetual/longer duration preference shares;

(u) The regime of acceptance and invitation of Public Deposits should be made stricter;

(v) Non-cash consideration for allotment of shares should be valued through independent valuers. Provisions relating to inter-corporate loans and investments should be strengthened to ensure that there is no mis-use of these provisions for price rigging or by diversion of funds. Penalties to be increased in case of non-compliance;

(w) In case of unlisted public companies, preferential allotment should be made on the basis of valuation by an independent valuer;

(x) Nidhi Companies to be regulated by RBI;

(y) Consolidation of financial statements should be made mandatory. Requirement of attaching financial statements of subsidiary company(ies) with the holding company to be done away with;

(z) Small Companies should be given exemptions/relaxations in respect of disclosures relating to financial statements;

(aa) The financial statements should be signed by MD/ CEO/ CFO/ Company Secretary, wherever applicable, even if they were not present in the meeting which approved the financial statements. All directors present in relevant meeting to sign financial statements. Dissenting director also to sign with dissent note;

(bb) Listed companies should put full financial statements on their websites;

(cc) The Companies (Transfer of Profits to Reserves) Rules, 1975 and The Companies (Declaration of Dividend out of Reserves) Rules, 1975 may be done away with. Provisions relating to payment of Interest out of capital [existing section 208] may be deleted;

(dd) Rotation of auditors not be mandated in Law. Auditor to be prohibited from performing certain non-audit functions/services to be specified in Law/rules. Disqualification of auditors to be suitably mentioned in the Law/rules;

(ee) Enabling provisions for empowering Central Government to order Cost audit in certain cases should be retained. Government approval for appointment of Cost Auditor for carrying out such audit is not necessary. Special Audit need not be continued;

(ff) A single forum for approval of mergers and acquisition schemes in a time bound manner to be provided.

(gg) concept of "Deemed approval" concept to be provided in cases where the different regulators do not intimate their comments timely;

(hh) Valuation of shares of companies involved in schemes of mergers and acquisition by independent registered valuers (rather than court appointed valuers) should be made mandatory;

(ii) The concept of Electronic registry should be evolved. Jurisdictional issues vis-à-vis stamp duty should be resolved to enable single registry;

(jj) 'Contractual mergers' and 'Cross Border mergers and acquisition' may be suitably addressed in the new Act;

(kk) Instead of separate provisions for both inspection and investigation under the Act, a single comprehensive process of investigation, may be provided for, including powers to inspect;

(ll) The Government may appoint an officer of the Government or any private professional as inspector to carry out investigation;

(mm) The Serious Frauds Investigation Office (SFIO) should be strengthened. A separate statute may be framed for SFIO;

(nn) There is need for a regime of penalties commensurate with the offences. Penalties regime for corporates should be in the nature of monetary fine since company being an artificial economic person can not be imprisoned;

(oo) The liability of the Board of directors to be clear and absolute. A clear regime for identification of Officers-in-default also to be necessary. Specific rules for fixing criminal liability in appropriate cases should be framed. The liability of CEOs/CFOs/Company Secretaries as well as other officers of the company who are in default to be specifically provided for. The professionals advising the companies on various matters also to be held liable if found not to be diligent or law compliant;

(pp) The Company Law to provide for an in-house structure for levying non discretionary monetary penalties only (i.e. in respect of offences not involving imprisonment);

(qq) The penalties may be classified in the form of two self-contained schedules – one for monetary penalties and the other for those involving imprisonment, with or without fine; The Law to lay down the maximum as well as minimum quantum of penalty for each offence. The Law to provide for suitable deliverance in respect of repeat offences;

(rr) In case of fraudulent activities/actions, provisions for recovery and disgorgement to be suitably provided for. The issue of "Phoenix problem" to be suitably addressed through a combination of disclosures, insolvency processes and disqualification of delinquent directors. The Law to provide for lifting of the corporate veil to check any fraudulent activity;

(ss) A definitive and predictable time frame is needed for rehabilitation and liquidation process;

(tt) Both debtors and creditors should have fair access to insolvency system. Rather than net worth erosion principle, test for insolvency should be default in payment of matured debt on demand within a prescribed time [liquidity

test]. Debtors seeking rehabilitation should be able to approach Tribunal only with a draft scheme. Creditors being at least 3/4th in value may also file scheme;

(uu) Provisions should be made for setting up of Committee of secured creditors to safeguard their interest and provide a suitable platform for creditors' participation in the process. The law should also provide for mechanism to recognize and record claims of unsecured creditors;

(vv) A Panel of Administrators and liquidators should be prepared and maintained by an independent body out of experienced and knowledgeable Insolvency Practitioners. Private professionals should play a meaningful role in all aspects of insolvency process. The law should encourage and recognize concept of Insolvency Practitioners;

(ww) The law should prescribe a flexible but transparent system for disposal of assets efficiently and at maximum value. Secured creditors' claim should rank *pari passu* with workmen. Public interests, Government claims should not get precedence over private rights. Revival plan should be required to be approved by secured creditors holding 3/4th of total value to be binding on all creditors;

(xx) Provisions relating to rehabilitation cess should be replaced by the concept of "Insolvency Fund" [Fund] with optional contributions by companies;

(yy) A suitable framework for Cross Border Insolvency which provides for rules of jurisdiction, recognitions of foreign judgments, co-operation and assistance among courts in different countries and choice of law is required. The Government may consider adoption of UNCITRAL Model Law on Cross Border Insolvency with suitable modifications at an appropriate time.

STATEMENT OF CONCLUSIONS/RECOMMENDATIONS OF THE STANDING COMMITTEE ON FINANCE IN THE FORTIETH REPORT (2006-07)

Sl. No.	Para No.	Ministry/Department Concerned	Conclusions/Recommendations
1	2	3	4
1.	21,22,23	Ministry of Company Affairs	It is widely known that the Companies Act, in its p form, is quite unweildly and complicated. In this conn reducing the number of sections/provisions alone will not simplifying, rationalizing and modernizing the law. W needed is that the new law must provide a flexible framew proper growth of companies, have dynamic orientation an into account the new developments that have taken place corporate world. The Committee recall in this regard earlier recommendation as contained in the 5th Rep Demands for Grants (2004-05) wherein they have urg Government to expedite the matter relating the Compreh Review of the Companies Act, 1956. From the response Government, they gather the impression that Comprehensive Bill amending provisions of Companies A be Tabled on the floor of the House shortly. They expe this long awaited piece of legislation will soon see the l the day and many provisions of the Companies Act ne reforms, as per the requirements of modern day cor governance practices as well as investors protection, m amended suitably. The Committee would also find it e necessary to ensure the use of simple and understa language as compared to the existing complicated struc provisions, explanations and multiple cross references Companies Act. Moreover, Company law should not be v in isolation and must be in harmony with other eco legislations. In this connection, the Committee note th Expert Committee to advise the Government on new Co Law, under the Chairmanship of Shri J.J. Irani, have a submitted their Report on 31st May, 2005 and subsequen Government is in the process of consultation and appro the recommendations of the same. In the course of examination of Budget Proposals f year 2006-07, another issue concerning Independent Di of Companies came up before the Committee. As the e Companies Act is silent on this issue, the Committee no this requirement was prescribed by SEBI (Securitie Exchange Board of India) as one of the listing condition Committee feel that absence of a relevant provision Companies Act has contributed in further ambiguity in so the responsibilities of Independent Directors are concerne The Committee further note that the Government introduced a limited amendment to the Companies Act to ‘smooth implementation of MCA-21 e-governance project’ project aims at providing clarity and security and enabli digitization of support documents submitted by the comp The Committee also note that once operational at all loc

			this system would provide facilities for all services del through the offices of Registrars of Companies on-lin facilitate completion of all transactions from the comf homes/offices of stakeholders. In this regard, the Com endorse the view that there is an urgent need for su governance project taking into account the internat accepted best practices in the ever evolving corporate and hope that the operationalisation of the project wou done expeditiously. They also desire to be kept apprised concrete measures taken in this direction.
2.	32,33,34	Ministry of Company Affairs	The Committee note that SFIO has been functioning October, 2003 as a multi-disciplinary adminis organization attached to the Ministry of Company Affa investigate complex corporate frauds and enable ade infrastructure and funds to carry out investigation into a fraud under the existing legal framework. The Committe that till now 31 cases have been referred to the SF investigation. Out of these, SFIO has already sub inspection reports in 11 cases and out of these instructio prosecutions have already been issued in respect o companies. From the replies furnished by the Governme Committee note that in most of the cases the investiga SFIO is *sub-judice.* The Committee are dismayed to lea despite being in existence for more than two years, crucial posts e.g. Additional/Joint Director//Deputy D (Admn.), Sr. ADs/ADs etc. are lying vacant in SFIO. Alt the Government is stated to be in the process of filling posts, the Committee are not sure as to how much time take before these posts are actually filled up. The Com feel that with the passing of time, more and more cases referred to the SFIO, with the result that its work v increased enormously. Keeping this in view, they recom that apart from filling the vacant posts immediately, add posts in various categories may be created so that the referred to SFIO are disposed of expeditiously and the pu for which it came into existence is fulfilled. Since conceived as a professional unit requiring specialized sk multi-disciplinary approach, is intended to investigate cor frauds, the personnel for this prestigious office may be from finance, income tax, SEBI, CBI etc. The Committee also feel that officers of SFIO sho suitably trained for this purpose. They also recommend t this regard, the training and investigation mechanism of should be of international standard yet keeping in mi trends and peculiarities of the Indian Corporate World. The Committee further take note of the fact that in pursuance of J.J. Irani Committee recommendation, an expert Committee namely Vepa Kamesam Committee has been constituted to assess the need for and details of a separate statute to govern the constitution and functioning of the SFIO. In this regard, they feel that there is a need to strengthen SFIO with adequate

			powers to act as a nodal agency in unveiling intricate and complex corporate frauds, in coordination with other agencies/organizations at the Centre and State levels and, therefore, recommend that a separate Statute to regulate and guide the functioning of SFIO may be framed.
3.	48,49,50, 51,52,53	Ministry of Company Affairs	The Committee note that the Government have traced back about 115 vanishing companies. Howe remains to be seen whether the investors duped by companies, will ultimately get some relief. The Committ convinced that the issue of vanishing companies is inext linked with the issue of 'Vanishing funds', which first implies that the investors who have been lured into inves a company that has vanished must get back his/her legi dues. They, therefore, feel that the matter of var companies does not only rest with just tracing out the var companies and their inspection of books of accounts e equal attention should be paid to the prosecution mechani that the investors could get their money back. Equally imp is to keep a watch on the vanishing companies so that th not resurface in a different name to dupe the investors The Committee feel that utmost vigilance is required to p efforts by a 'vanishing company' or a defaulting comp restart its operations in another name or disguise. The Committee also recommend that special care be taken at the time of registration of a company as this its arrival and possibility of raising capital. Therefor Committee recommend that Government should be mor during the process of registering the companies so as to their potential viability to survive in the competitive enviro and benefit their investors. The Committee feel that the auditors/auditing firm either fail in their duties to audit the companies/prope knowingly shut their eyes to any impending misfortune investors should also be held equally responsible Committee desire that the Government should, within the provisions of the law, try to pinpoint erring auditors an firms equally responsible, otherwise the very idea of the a acting as whistleblowers would be defeated. The Com find that the Government are toothless in this regard a gather the impression, from the replies of the Governme all they can do is to ask CAG to exercise due caution appointing the 'guilty' firms as statutory auditors for cond the audit of public sector companies, while they are f operate in the private sector. The Committee, in this r would like to see the 'guilty' auditors/auditing firms to be t as accomplices in the eyes of the Government. The Committee also find that even the definit vanishing companies is ambiguous thereby leaving looph the law. From the information furnished to them, they no one of the criteria which states that 'no correspondenc been received by the Exchange from the company for time', is interpreted by the Task Forces concerned to i

			period between 2 to 3 years of absence of correspon between the exchange and the company. The Committe that any company which has duped its investors, can co to operate and avoid being classified as 'vanishing' ju sending a piece of correspondence, at intervals of 2-3 They, therefore, feel that the criteria for identifying a co as vanished/vanishing needs streamlining and call upo Government to have a re-look at the definition, so that al companies, having the slightest intention of duping inves their hard earned money, could be classified as 'vanish potentially vanishing companies'. 52. In this regard, the Committee also not recommendations of the Samir Biswas Committee th coordination mechanism may involve Ministry of Fi (Department of Economic Affairs) in addition to Minis Company Affairs and SEBI. The Committee feel that the p mechanism may be extended to also incor representatives of Department of Economic Affairs, as th primarily responsible to oversee the implementatio Government's policies in regard to regulation of Capital Ma 53. The Committee note the Government's effo prepare a database of all Directors of the companies und system of allotment of DIN (Director identification Nu under the MCA-21 e-governance project and urg Government to expedite completion of the same. Committee also note the Government's decision to take technical scrutiny of Balance Sheets of all such comp which come out with IPOs, so as to monitor the utilizat funds raised from the public. The Committee while appre the Government's decision, desire that the Government m a suitable time limit in this direction so that the investors secondary market may also be benefited.
4.	65,66,67	Ministry of Company Affairs	The Committee note that the utilization of the proce of the funds under IEPF have shown an inconsistent tr The percentage of expenditure in 2002-03 was 59.4% 2003-04 it was 94.52%. Again in 2004-05 it plunge 54.46% and in 2005-06 it was 86.72%. While taking not the Government's efforts for a more effective utilization o funds available under IEPF, the Committee still feel that s efforts are not adequate enough. The Committee feel tha Government have not been able to utilise the amount of available to their credit. This calls for restructuring of sche under IEPF. The Committee also take note of the J.J. Committee's recommendations in this regard and exp agreement over their suggestion that the structure administration of the fund should be revamped and sche should be made more comprehensive and their sc expanded to enable flow of current information to the inves about their rights. Besides, in view of the spurt in various scams relate capital market in the last few years, the Committee feel the time has come to utilize the IEPF on the educatio

			small investors, who are more gullible due to lack of pr information. The Committee note that the Government do not sup the idea of either assigning the funds under IEPF cre under the Companies Act, 1956 to SEBI or placing the fu under the Central Monitoring Committee jointly chaired by Ministry and SEBI on the ground that since IEPF has b created by the government after expropriating the mo from the budget allocated to it, which belong to investor exercising its sovereign right through Statute. Moreover S is already represented in IEPF committees. The Comm are, however, of the view that the broad issues on w complaints from the aggrieved investors are being rece relate to refund claims of investors, shares/deben certificates, dividend amount, interests etc. which generally looked after by SEBI. They further feel that s SEBI is the primary market regulator and cases unscrupulous persons duping investors is also one o concerns, it would, perhaps, be appropriate if SEBI is giv bigger role not only in preparation and approval of sche relating to IEPF but also in the approval for disbursemen funds. The Committee hope that the Government will cons the concern expressed by them and will administer Investor Education and Protection Fund (IEPF) in coordina with SEBI.
5.	80	Ministry of Company Affairs	The Committee note that the J.J. Irani Committee already taken up the issue of exit or liquidation of compa detail in view of the inordinate delays and lengthy proced companies to exit. The Committee also note from the re the government referring to the observation in a World Report that the time taken for a companies to exit is betwe 3 years in China, Malaysia and Thailand whereas it is ab years in India. They further note that the Government attributed this delay to the lengthy nature of judicial pr The Committee are of the view that it is essential to pro sound framework for winding up and liquidation of comp In this connection, the Committee recommend that in the legal provisions, the Government should strive work in s time-bound manner that, excluding the time taken for obt the approval of the High Court, all other formalities co completed within a period of 2-3 years. Moreove Committee hope that efforts by the Government to get the second Amendment Act, 2002 passed at the earliest in favour by the Supreme Court, would pave way f establishment ultimately. This, the Committee hope will h reducing time for getting required judicial approval for companies overall, the Committee opine that simplifyin existing liquidation process and speeding up the winding sick companies having no chance of revival would be st the right direction. Besides the modified framework should to preserve the estate and maximize the value of assets existing company so that those could be redeployed suitab

Minutes of the Twenty- second sitting of Standing Committee on Finance

The Committee sat on Wednesday, 19th April, 2006 from 1030 to 1315 hrs and 1430 to 1630 hrs.

PRESENT

Maj. Gen.(Retd.) B.C. Khanduri - Chairman

MEMBERS

LOK SABHA

2. Shri Jaswant Singh Bishnoi
3. Shri Bhartruhari Mahtab
4. Shri Bir Singh Mahato
5. Shri Jyotiraditya Madhavrao Scindia
6. Shri M.A. Kharabela Swain

RAJYA SABHA

7. Shri C. Ramachandraiah
8. Shri Mangani Lal Mandal
9. Shri Santosh Bagrodia
10. Smt. Shobhana Bhartia

SECRETARIAT

1. Dr. Smt. P.K. Sandhu - Additional Secretary
2. Shri A.M. Mukhopadhyay - Joint Secretary
3. Shri S.B. Arora - Deputy Secretary
4. Smt. Anita B. Panda - Under Secretary

Part – I
(1030 to 1145 hrs.)

Witnesses

Ministry of Company Affairs

1. Smt. Komal Anand, Secretary
2. Shri M. Deendayalan, JS & Financial Adviser
3. Shri Y.S. Malik, Joint Secretary
4. Shri Jitesh Khosla, Joint Secretary
5. Shri O.P. Arya, Director, SFIO
6. Dr. Joseph Abraham, Economic Adviser
7. Shri A.K. Kapoor, Adviser, Cost
8. Shri Ajay Nath, Director General (DGIR)
9. Shri R.K. Arora, Director, MRTP Commission
10. Shri Vyas Ji, Secretary CCI
11. Shri L.M. Gupta, Director (Inspn. & Investigation)
12. Shri B.M. Anand, Director (Inspn. & Investigation)
13. Smt. Vibha Pandey, Chief Controller of Accounts

2. At the outset, the Chairman welcomed the representatives of the Ministry of Company Affairs to the sitting of the Committee and invited their attention to the provisions contained in direction 55 of the Directions by the Speaker.

3. The Committee then took oral evidence of representatives of the Ministry of Company Affairs on issues arising out of Budget Proposals (2006-07) of the Ministry of Company Affairs and other related matters.

4. Thereafter, the Chairman requested the representatives of Ministry of Company Affairs to furnish notes on certain points raised by the Members to which replies were not readily available with them during the discussion.

5. The evidence was concluded

6. A verbatim record of proceedings has been kept.

The witnesses then withdrew

Part – II
(1200 to 1315 hrs.)

7. XX XX XX XX XX

Part – III
(1430 to 1630 hrs.)

8. XX XX XX XX XX

Minutes of the Twenty-sixth sitting of Standing Committee on Finance

The Committee sat on Wednesday, 19 May, 2006 from 0930 to 1030 hrs.

PRESENT

Maj. Gen (Retd.) B.C. Khanduri - Chairman

MEMBERS

LOK SABHA

2. ri Bhartruhari Mahtab
3. Dr. Rajesh Kumar Mishra
4. Shri Madhusudan Mistry
5. Shri Rupchand Pal
6. Shri Jyotiraditya Madhavrao Scindia
7. Shri M.A. Kharabela Swain
8. Shri Vijoy Krishna

RAJYA SABHA

9. Shri S.P.M. Syed Khan
10. Shri Santosh Bagrodia

SECRETARIAT

1. Dr.(Smt.) P.K. Sandhu - Additional Secretary
2. Shri A. Mukhopadhyay - Joint Secretary
3. Shri S.B. Arora - Deputy Secretary
4. Shri T.G. Chandrasekhar - Under Secretary
5. Smt. Anita B. Panda - Under Secretary

2. At the outset, the Chairman welcomed the Members to the sitting of the Committee.

3. XX XX XX XX

4. The Committee then took for consideration draft Reports on the Demands for Grants (2006-07) of the following Ministries/Departments and adopted the same subject to the modification as shown in Annexure-I in respect of the draft Report at Sl. No. (v) :-

(i) XX XX XX XX

(ii) XX XX XX XX

(iii) XX XX XX XX

(iv) XX XX XX XX

(v) Ministry of Company Affairs

5. The Committee authorised the Chairman to finalise the Reports in the light of modification as also to make verbal and other consequential changes arising out of the factual verification and present the same to both the Houses of Parliament.

The Committee then adjourned.

ANNEXURE

[MODIFICATION/AMENDMENT MADE BY STANDING COMMITTEE ON FINANCE IN THEIR DRAFT REPORT ON DEMANDS FOR GRANTS (2006-07) OF THE MINISTRY OF COMPANY AFFAIRS AT THEIR SITTING HELD ON 19 MAY, 2006]

Page No. 28 Para No. 53 Line 4 from below	
For	The Committee while appreciating the Government's decision, desire that the Government may fix a suitable time limit in this direction so that the investors, in the secondary market may also be benefited.
Substitute	The Committee desired that in view of the current developments in the IPO Market, the Government may expedite the same within a specific time frame so that the interests of the investors may be safeguarded.