

Role of Serious Fraud Investigation Office (SFIO) in Protection of Investor's Interest: An Overview

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I-Introduction

A Company is basically a form of business organization and it runs according to the business traits and commercial practices. Being a sub system of the economic-social system operating in the society, it affects and is affected by the economic and cultures of the society. The concept of social responsibilities of companies is now so widely accepted that it is rare to bear any view expressed to contrary. Even those who stoutly defend company's primary object to make profits agree that the profit-making should be pursued in a socially responsible way, by which they usually mean that it should be done for the well being of their employees giving due regards to public, its shareholders and keeping paramount also the national interest. The Companies Act 2013, guarantees several rights to investors and also regulates the affairs of a company with a view to ensure efficient functioning of a company so that investors may receive their due returns of the capital invested by them and their rights and interests are adequately protected. Investors are the real owners of a company but the power of management of the company is vested in the Board of Directors.

There are chances to abuse of power like committing fraud, by few directors of the company. As we know that there is close nexus between corporate governance and ethics but conflicts between these two are also bound to occur. Corporate fraud, an inevitable incident occurring, in recent, is an aggravated form of corruption in corporate world. It is difficult to prevent and to catch such white collar crimes. Such incidents reduce the interest and trust in corporate investments and in turn reduce the confidence on the government. The Companies Act empowers the Central Government with the right to investigate the affairs of the company, especially in cases of an alleged fraud or even in the oppression of the minority shareholders.

There are three types of investigation mentioned in the Companies Act 2013

1. An investigation into the affairs of the Companies¹
2. An investigation into company's affairs in other cases²
3. An investigation into the ownership of the Companies³

The Central Government is empowered to appoint inspectors to investigate either on its own if it is of the opinion that such investigation is required on the report of the Registrar or Inspector under section 208 or in public interest or on the request of the company on the basis of a special resolution or on the Direction of the court/tribunal or from such members of the company having requisite number of shares as specified in section 213 of the Companies Act, 2013.

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¹ section 210 of the Companies Act, 2013

² s. 213

³ s. 216

The Central Government has also set up the Serious Fraud Investigation Office (SFIO) in the ministry of corporate affairs, a specialized, multi-disciplinary organization to deal with serious cases of corporate fraud. This was also a major recommendation made by the Naresh Chandra Committee which was set up by the government on 21 August 2002 on corporate governance. Headquarters of this office is located in New Delhi, with field offices located in major cities throughout India. The SFIO is headed by a director not below the rank of a Joint Secretary to the Government of India having knowledge and experience in dealing with the matters relating to corporate affairs and also consist of experts from various disciplines⁴. The SFIO will only deal with investigation of corporate frauds characterized by

- a) Complexity and having inter- departmental and multi-disciplinary ramifications.
- b) Substantial involvement of public interest in terms of monetary misappropriation or in terms of number of persons affected and
- c) The possibility of investigations leading to or contributing towards a clear improvement in systems, law of procedure⁵.

The other experts are appointed by the Central Government from amongst persons of ability, integrity and experience in the field of banking, Corporate Affairs, Taxation, Forensic audit, Capital Market, Information Technology, Law, or Other fields as required.

II-Role of Serious Fraud Investigation Office (SFIO)

SFIO, in following circumstances, investigate into the affairs of a company when the Central Government assigns⁶ –

- (a) on receipt of a report of the Registrar or inspector under section 208 where further investigation into the affairs of the company is necessary;
- (b) on intimation of a special resolution passed by a company that its affairs are required to be investigated;
- (c) in the public interest; or
- (d) on request from any Department of the Central Government or a State Government,

Director of SFIO, may designate such number of inspectors, as he may consider necessary for the purpose of such investigation and such investigating officer have the power of the inspector according to section 217 of the Act⁷. Hence, inspectors may also be empowered to investigate the affairs of -

- (a) any other body corporate which is, or has at any relevant time been the company's subsidiary company or holding company, or a subsidiary company of its holding company;
- (b) any other body corporate which is, or has at any relevant time been managed by any person as managing director or as manager, who is, or was, at the relevant time, the managing director or the manager of the company;
- (c) any other body corporate whose Board of Directors comprises nominees of the company or is accustomed to act in accordance with the directions or instructions of the company or any of its directors; or

⁴ s.211

⁵ Ramaiya, Guide to the Companies Act, 16th edn. p. 2525

⁶ s. 212(1)

⁷ s. 212(4)

(d) any person who is or has at any relevant time been the company's managing director or manager or employee, he shall investigate into and report on the affairs of the other body corporate or of the managing director or manager, in so far as he considers that the results of his investigation are relevant to the investigation of the affairs of the company⁸.

The case shall not be investigated by other departments when assigned to SFIO

In order to bring integrity and acceleration in investigation in serious corporate frauds, when any case has been assigned by the Central Government to the SFIO for investigation under this Act, no other investigating agency of Central Government or any State Government shall proceed with investigation in such case in respect of any offence under this Act and in case any such investigation has already been initiated, it shall not be proceeded further with and the concerned agency shall transfer the relevant documents and records in respect of such offences under this Act to SFIO⁹. The company and its officers and employees, who are or have been in employment of the company, shall be responsible to provide all information, explanation, documents and assistance to the investigating officer as he may require for conduct of the investigation. SFIO shall conduct the investigation in the manner and follow the procedure provided in chapter XIV of the Companies Act, 2013 and submit its report to the Central Government within such period as may be specified in the order.

Power of SFIO to arrest the accused

Director, Additional Director or Assistant Director of SFIO, if authorized by Central Government by general or special law, may arrest such person, who is found guilty of cases of fraud as mentioned above. Every person arrested shall, as soon as possible, be intimated the ground of arrest and within twenty-four hours, be taken to a Judicial Magistrate or a Metropolitan Magistrate, as the case may be, having jurisdiction; provided that the period of twenty-four hours shall be excluded the time necessary for the journey from the place of arrest to the Magistrate's court.¹⁰

No person accused of any offence under those sections shall be released on bail or on his own bond unless

1. the Public Prosecutor has been given an opportunity to oppose the application for such release; and
2. where the Public Prosecutor opposes the application, the court is satisfied that there are reasonable grounds for believing that he is not guilty of such offence and that he is not likely to commit any offence while on bail.

A person, who, is under the age of sixteen years or is a woman or is sick or infirm, may be released on bail, if the Special Court so directs. The Special Court shall not take cognizance of any offence except upon a complaint in writing made by

1. the Director, Serious Fraud Investigation Office; or

⁸ s. 219

⁹ s. 212(2)

¹⁰ s. 212(6)

2. any officer of the Central Government authorised, by a general or special order in writing in this behalf by that Government.

Submission of Investigation Report by SFIO

Submission of Interim Investigation Report- the Central Government if so directs, the SFIO will submit an interim report to the Central Government within stipulated time. This report may contain the preliminary findings related with seriousness, wrongdoers of the fraud etc.

Submission of final Investigation Report- SFIO shall submit the detail and final investigation report, on completion of the investigation to the Central Government. A copy of the investigation report may be obtained by any person concerned by making an application in this regard to the court. On receipt of the investigation report, the Central Government will, after examination of the report (and after taking such legal advice, as it may think fit), may direct the SFIO to initiate prosecution against the company and its officers or employees, who are or have been in employment of the company or any other person directly or indirectly connected with the affairs of the company.

The investigation report filed with the Special Court for framing of charges shall be deemed to be a report filed by a police officer under section 173 of the Code of Criminal Procedure, 1973. In case SFIO has been investigating any offence under this Act, any other investigating agency, State Government, police authority, income-tax authorities having any information or documents in respect of such offence shall provide all such information or documents available with it to the SFIO.

The SFIO will also share any information or documents available with it, with any investigating agency, State Government, police authority or income tax authorities, which may be relevant or useful for such investigating agency, State Government, police authority or income-tax authorities in respect of any offence or matter being investigated or examined by it under any other law.¹¹

III-Criminal Liabilities of Company in cases of Fraud

The following corporate activities have been regarded as fraud and kept under the category of cognizable as well as non-bailable offences and punishable under section 447 of the Companies Act, 2013

(a) **Furnishing False or incorrect information during registration of company-** If any person furnishes any false or incorrect particulars of any information or suppresses any material information, of which he is aware in any of the documents filed with the Registrar in relation to the registration of a company¹².

(b) **Incorporation of company by fraudulent means-** Any company incorporated by furnishing any false or incorrect information or representation or by suppressing any material fact or information in any of the documents or declaration filed or made for incorporating such company, or by any fraudulent action.¹³

¹¹ s. 212(17)

¹² s. 7(5)

¹³ s. 7(6)

(c) **Untrue or Misleading Prospectus**- When a prospectus issued, circulated or distributed includes any statement which is untrue or misleading in form or context in which it is included or where any inclusion or omission of any matter is likely to mislead.¹⁴

(d) **Inducing a person to enter into financial matter**- Any person who, either knowingly or recklessly makes any statement, promise or forecast which is false, deceptive or misleading, or deliberately conceals any material facts, to induce another person to enter into, or to offer to enter into

- any agreement for, or with a view to, acquiring, disposing of, subscribing for or
- underwriting securities; or
- any agreement, the purpose or the pretended purpose of which is to secure a profit to any of the parties from the yield of securities or by reference to fluctuations in the value of securities; or
- any agreement for, or with a view to obtaining credit facilities from any bank or financial institution.¹⁵

(e) Any person who **makes or abets** making of an application in a fictitious name to a company for acquiring, or subscribing for, its securities; or makes or abets making of multiple applications to a company in different names or in different combinations of his name or surname for acquiring or subscribing for its securities; or otherwise induces directly or indirectly a company to allot, or register any transfer of, securities to him, or to any other person in a fictitious name.¹⁶

(f) If a company with **intent to defraud** issues a duplicate certificate of shares.¹⁷

(g) Without prejudice to any liability under the Depositories Act, 1996, where any depository or depository participant, with an intention to defraud a person, has transferred shares.¹¹⁸

(h) If any officer of the company knowingly **conceals the name of any creditor** entitled to object to the reduction; knowingly misrepresents the nature or amount of the debt or claim of any creditor; or abets or is privy to any such concealment or misrepresentation as aforesaid.¹⁹

(i) When the **auditor of the company has acted fraudulently or abetted or colluded** in any fraud by, or in relation to, the company or its directors or officers, such auditor are held liable for fraud and may be removed from office.²⁰

(j) Where business of a company has been or is being carried on for a fraudulent or unlawful purpose, or if the **grievances of investors are not being addressed**, every officer of the company who is in default shall be held liable for fraud.²¹

(k) if after investigation it is proved that the business of the company is being conducted with **intent to defraud its creditors**, members or any other persons or otherwise for a fraudulent or unlawful purpose, or that the company was formed for any fraudulent or unlawful purpose; or any person concerned in the formation of the company or the management of its affairs have in connection therewith

¹⁴ s. 34

¹⁵ s. 36

¹⁶ s. 38(1)

¹⁷ s. 46(5)

¹⁸ s. 56(7)

¹⁹ s. 66(10)

²⁰ s. 140(5)

²¹ s. 206(4)

been guilty of fraud, then, every officer of the company who is in default and the person or persons concerned in the formation of the company or the management of its affairs shall be held liable of fraud.²²

(l) **Furnishing false statement mutilation, destruction of documents-** Where a person who is required to provide an explanation or make a statement during the course of inspection, inquiry or investigation, or an officer or other employee of a company or other body corporate which is also under investigation,—

- (i) **destroys, mutilates** or falsifies, or conceals or tampers or unauthorisedly removes, or is a party to the destruction, mutilation or falsification or concealment or tampering or unauthorised removal of, documents relating to the property, assets or affairs of the company or the body corporate;
- (ii) makes, or is a party to the making of, a **false entry** in any document concerning the company or body corporate; or
- (iii) provides an explanation which is false or which he knows to be false.²³

(m) **Fraudulent application for removal of name-** Where it is found that an application by a company under sub-section (2) of section 248 has been made with the object of evading the liabilities of the company or with the intention to deceive the creditors or to defraud any other persons, the persons in charge of the management of the company shall, notwithstanding that the company has been notified as dissolved—

- (i) be jointly and severally liable to any person or persons who had incurred loss or damage as a result of the company being notified as dissolved; and
- (ii) be punishable for fraud as per section 447.²⁴

(n) **Fraudulent conduct of business-** If in the course of the winding up of a company, it appears that any business of the company has been carried on with intent to defraud creditors of the company or any other persons or for any fraudulent purpose, the Tribunal, on the application of the Official Liquidator, or the Company Liquidator or any creditor or contributory of the company, may, if it thinks it proper so to do, declare that any person, who is or has been a director, manager, or officer of the company or any persons who were knowingly parties to the carrying on of the business in the manner aforesaid shall be personally responsible for fraud.²⁵

(o) **False Statement**²⁶-any return, report, certificate, financial statement, prospectus, or other document required by, or for the purposes of any of the provisions of this Act or the rules made there under, any person makes a statement,—

- (i) which is false in any material particulars, knowing it to be false; or
- (ii) which omits any material fact, knowing it to be material.

IV-Punishment for Fraud

It is worth to discuss here the punishment of various fraud prescribed by the Companies Act, 2013. The Act prescribes punishment for following frauds-

²² s. 213

²³ s. 229

²⁴ s. 251

²⁵ s. 339

²⁶ s. 448

- (a) any person who is found to be **guilty of fraud**, shall be punishable with imprisonment for a term which shall not be less than six months but which may extend to ten years and shall also be liable to fine which shall not be less than the amount involved in the fraud, but which may extend to three times the amount involved in the fraud.²⁷
- (b) where the **fraud in question involves public interest**, the term of imprisonment shall not be less than three years.
- (c) **giving false statement** in any return, report, certificate, financial statement, prospectus, statement or other document required by, or for, the purposes of any of the provisions of this Act, shall be punishable as per section 447.²⁸
- (d) **giving intentionally false evidence** upon any examination on oath or solemn affirmation, authorised under this Act; or in any affidavit, deposition or solemn affirmation, in or about the winding up of any company or otherwise in or about any matter arising under this Act, shall be punishable with imprisonment for a term which shall not be less than three years but which may extend to seven years and with fine which may extend to ten lakh rupees.²⁹
- (e) punishment where no specific penalty or punishment is provided³⁰- If a company or any officer of a company or any other person contravenes any of the provisions of this Act or the rules made there under, or any condition, limitation or restriction subject to which any approval, sanction, consent, confirmation, recognition, direction or exemption in relation to any matter has been accorded, given or granted, and for which no penalty or punishment is provided elsewhere in this Act, the company and every officer of the company who is in default or such other person shall be punishable with fine which may extend to ten thousand rupees, and where the contravention is continuing one, with a further fine which may extend to one thousand rupees for every day after the first during which the contravention continues.
- (f) punishment in case of **repeated default**- If a company or an officer of a company commits an offence punishable either with fine or with imprisonment and where the same offence is committed for the second or subsequent occasions within a period of three years, then, that company and every officer thereof who is in default shall be punishable with twice the amount of fine for such offence in addition to any imprisonment provided for that offence.³¹

V-Evaluation of the role of SFIO

SFIO is a specialist organisation that investigates only the most serious type of corporate frauds. It has been empowered by the Companies Act, 2013 to investigate all the matters pertaining to frauds occurred in any company where the investors lost their hard earned money. An inspector can examine on oath any person involved in the fraud and may thereafter be used in evidence against him. In this work of inspector, the officers of the Central Government, State government, police or statutory authorities shall

²⁷ s. 447

²⁸ s. 448

²⁹ s. 449

³⁰ s. 450

³¹ section 451

provide assistance to him. They enjoy all the powers as are vested in a civil court under the Code of Civil Procedure, 1908, while trying a suit in respect of the following matters, namely³²:—

- (i) the discovery and production of books of account and other documents, at such place and time as may be specified by such person;
- (ii) summoning and enforcing the attendance of persons and examining them on oath; and
- (iii) inspection of any books, registers and other documents of the company at any place.

Here, it is worth to mention that investigation proceedings are not judicial proceedings but only investigatory and quasi-judicial in nature³³. If any director or officer of the company disobeys the direction issued by the Registrar or the inspector, the director or the officer shall be punishable with imprisonment which may extend to one year and with fine which shall not be less than twenty-five thousand rupees but which may extend to one lakh rupees.

If a director or an officer of the company has been convicted of an offence under section 217, the director or the officer shall, on and from the date on which he is so convicted, be deemed to have vacated his office as such and on such vacation of office, shall be disqualified from holding an office in any company. The notes of examination of the person as mentioned above are to be taken down in writing and to be read over to, or by, and signed by, the person examined, and may thereafter be used in evidence against him. If any person fails without reasonable cause or refuses—

- (i) to produce to an inspector or any person authorised by him in this behalf any book or paper which is his duty to produce; or
- (ii) to furnish any information which is his duty to furnish; or
- (iii) to appear before the inspector personally when required to do so or
- (iv) to answer any question which is put to him by the inspector in pursuance of that; or
- (v) to sign the notes of any examination referred to;

he shall be punished with imprisonment for a term which may extend to six months and with fine which shall not be less than twenty-five thousand rupees but which may extend to one lakh rupees, and also with a further fine which may extend to two thousand rupees for everyday after the first during which the failure or refusal continues.³⁴

Satyam Computers Scam was investigated by the SFIO in record three months of time. This scam of worth Rs.7,200 crore and caused loss of Rs. 14,162 crore (approx.) to its investors in 2009, has happened with the help of audit firm PricewaterhouseCoopers which is big blow for corporate governance in India. The role and liability of Independent director were also held suspicious. Satyam Computer Services Ltd was founded in 1987 by B.Ramalinga Raju.

The company offers information technology (IT) services spanning various sectors, and was also listed on the New York Stock Exchange and Euronext. Satyam's network has covered 67 countries across six continents. The company employed 40,000 IT professionals across development centers in India, the United States, the United Kingdom, the United Arab Emirates, Canada, Hungary, Singapore, Malaysia, China, Japan, Egypt and Australia. It was serving over 654 global companies, 185 of which were Fortune 500 corporations. Satyam has strategic technology and marketing alliances with over 50 companies. Apart from Hyderabad, it has they

³² section 217(5)

³³ Coimbatore Spinning & Weaving Co. Ltd v. M.S Srinivasan (1959) 29 Comp. Cases 97 (Mad).

³⁴ s. 217(8)

Bhubaneswar, and Visakhapatnam.³⁵ SFIO questioned the independent directors and found that allegedly at the behest of the chairman and other top executives of the IT giant. SFIO concluded had no knowledge about the falsification of accounts and overstated profits that happened development centers in India at Bangalore, Chennai, Pune, Mumbai, Nagpur, Delhi, Kolkata, that the Independent directors of Satyam were not involved in the multi-crores accounting fraud in the IT company and were kept in the dark by the chairman.

SFIO has also investigated **Deccan Chronicle Holding Ltd (DCHL)** loan default case of Rs. 1,230 crore (approx).³⁶ This is Hyderabad based company, which owns the English dailies Deccan Chronicle and Asian Age, was under probe for alleged financial irregularities and failure to repay loan during 2009-11. In a report to the ministry, the SFIO has pointed to violations of several provisions of the Companies Act, 1956. The SFIO report has confirmed that the money was availed by the company's management from various banks through sale of non-convertible debentures and other commercial papers. Later, DCHL declared itself sick and registered with the Board for Industrial and Financial Reconstruction (BIFR). Although the BIFR has accepted the company's plea under the Sick Industries Act, the move does not deter DCHL's lenders from taking action against the company under the Securitisation Act.

The famous **Saradha Chit Fund scam** of West Bengal is, now, being investigated by the SFIO. The investigation was ordered by the Corporate Affairs Ministry, in 2013, following huge public outcry over the scam that duped hundreds of gullible investors by running fraudulent money-pooling schemes in the garb of chit funds. More than 60 companies, most of them from the eastern states of the country, which are believed to have cheated the public of their money, are being probed by SFIO. In its interim report, SFIO had said that companies under the scanner indulged in serious financial mismanagement besides siphoning off the funds by their promoters, who exploited regulatory gaps³⁷. There has been proliferation of innovative financial products in the market due to technological advancement and extensive use of the internet to market such products to investors.

It has been observed that SFIO has no power to settle cases on its own. It deals with investigation of corporate frauds characterized by complexity and having inter- departmental, multi-disciplinary ramifications and also having substantial involvement of public interest in terms of monetary misappropriation or in terms of number of persons affected. It submits the detail and final investigation report, on completion of the investigation to the Central Government.

The Central Government, after examination of the report (and after taking such legal advice, as it may think fit), may direct the SFIO to initiate prosecution against the company and its officers or employees, who are or have been in employment of the company. In U.K., the Serious Fraud Office (SFO) is an independent department which investigates and also prosecutes serious and complex fraud and corruption cases. SFO is the principal enforcer of new UK bribery Act, 2010 which has been designed to prevent fraud and to encourage good corporate governance in that country. Therefore, it is suggested that, in India, SFIO should also be given power of, at least, imposing penalties on such company involved in fraud. This will provide speedy relief to investors and also reduce the burden of the court, up to certain extent.

³⁵ Tabrez Ahmad, Satyam Scam in the Contemporary Corporate World, retrieved from SSRN

³⁶ The Hindu, Hyderabad, Jul 09, 2013.

³⁷ The Hindu, New Delhi, April 20, 2014.

It is concluded that SFIO is performing well to find out the corporate frauds, during recent time which reflects the good corporate governance in our country. Minister of State for Corporate Affairs Nirmala Sitharaman has informed the Lok Sabha on 25 July, 2014, in a written reply that corporate frauds worth more than Rs 10,800 crore have been detected by SFIO during its probes in nearly three-and-half years. It has completed probes in 78 cases of corporate frauds since 2011-12 till June-end of this year. Now, Market Research and Analysis Unit (MRAU) has been set up in SFIO to analyse media reports relating to financial frauds and for conducting market surveillance of such corporate. In order to strengthen MRAU's functioning, an expert committee was constituted and on the basis of its recommendations a forensic lab with appropriate technology and skilled technical manpower has been set up in SFIO. This will, certainly protect the investor's interest and will also bring back the confidence of investors in Indian capital market.