
AN OVERVIEW OF CORPORATE SCAMS THAT HAVE EFFECTUATED THE CHANGES IN COMPANY LAW

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ABSTRACT

On numerous occasions, it is observed that numerous businesses or persons engage on behalf of the organisation in ways that ultimately show to be quite fatal. Corporate fraud is the term used to describe such misrepresentations made by any company or person while operating within the corporate culture. When such activities are discovered, the corporation frequently has to deal with very serious repercussions for the crimes that its personnel committed. These days, white collar crimes are dominating corporate culture, which hurts our nation's trade and economy as well as the statistics of the relevant firms or organisations.

This research article is meant to emphasise the significance, types, and punishments under numerous laws, along with determining corporate culpability and significant case laws, as well as the biggest corporate frauds performed in India.

Keywords: Fraud, Scam, Corporate, Violation etc

Introduction

“White collar crimes are the kinds of offences committed by honourable people in high-ranking positions in both governmental and private organisations. Because such actions are carried out in great secrecy and go unreported, it is almost impossible for bureaucratic agencies to follow and uncover such frauds. The Federal Bureau of Investigation describes these crimes as "illegal acts characterised by deceit, concealment, or breach of trust, which are not dependent upon the use or threat of physical force or violence." According to the FBI, "individuals and organisations commit these behaviours in cases of white-collar crime to get money, property, or services; to prevent payment or loss of money, or to secure personal or business advantage." Nowadays, organisations are the centre of attention for white collar crimes rather than individuals, who either act alone or in concert with others to conduct crimes. Corporate fraud is one of these white-collar crimes.”

A fraud, in the broadest meaning, is an intentional misrepresentation done for monetary gain or to harm another person or organisation. Fraud vitiates everything, or "Fraus Omnia Vitiare." Corporate fraud occurs when a company knowingly disseminates false information with the objective to conceal the truth, fool the recipient of the information, and gain an advantage.

“Corporate fraud is when a business or other entity purposefully alters and hides crucial data, making the organisation appear to be in better shape. Companies use a variety of operating procedures to carry out such corporate frauds, which may include providing inaccurate information in the prospectus, falsifying financial records, hiding debt, etc. False accounting entries, false trades to inflate profits, disclosure of price-sensitive information that falls under the purview of insider trading, and showing false transactions that have the effect of luring in additional investors and lenders for funding are some of the aspects of falsifying financial information.”

There are many reasons why businesses engage in such fraud, including increasing the amount of fake money they make, fabricating the company's reputation in the marketplace, and misleading the government to conduct tax evasion. According to the report of the Commission on "Prevention of Corruption" in India, "the advancement of technological and scientific development is contributing to the emergence of mass society with a large rank in file and a small controlling elite, encouraging the growth of monopolies, the rise of a managerial class,

and complex institutional mechanisms."¹ Even the honest operation of the new social, political, and economic processes requires a strong adherence to high ethical norms. The Vivian Bose Commission investigated the Dalmia Jain group of firms in 1963, and its report revealed how the major industries engage in fraud, falsification of accounting, record tampering, and other illegal activities for personal benefit and tax avoidance.

Fraud and corporate scandals are as old as the hills in India. The notorious LIC/Mundhra scam, the first significant financial fraud of the independent India, occurred in the 1950s. Following that, frauds occurred alarmingly frequently in every decade; just a few examples include the well-known Harshad Mehta, Ketan Parekh, Sahara, and Satyam scams. In accordance with the pertinent sections of the Indian Penal Code, 1860, these scams were looked into by the law enforcement agencies (IPC). Fraud was not specifically defined in the Companies Act of 1956. Legally, having a separate one was unnecessary because Lord Macaulay's IPC sufficiently addressed all such crimes. Based on the Dr. J.J. Irani Committee Report, the Companies Bill, 2008 was the initial legislative proposal to replace the Companies Act, 1956. (Irani Report).

Research Objectives

The research objectives are:

- 1) To understand the meaning of corporate frauds.
- 2) To analyse various corporate frauds of India which effectuated changes in company law.
- 3) To analyse the new amendments made in company law and suggest the changes for improvement of it.

Research Question

The research questions are:

- 1) What is the meaning of corporate frauds?

¹ Sanjeev Gupta, India: Corporate frauds in India – perceptions and emerging issues, *Emerald's Journal of Financial Crime* (2015).

- 2) What are changes made in company law due to the various scams that happened in India?
- 3) What are the new amendments made in company law to tackle the challenges of frauds and scams?

Research Hypothesis

Alternative Hypothesis: Corporate scams have not effectuated changes in company law in any way.

Null Hypothesis: Corporate scams have effectuated changes in company law.

Definition of Fraud under Section 447 of the Act

“Section 447 of the Act is an amalgam of several sections of the IPC including Section 405 dealing with Criminal Breach of Trust, Section 415 dealing with Cheating, Section 463 dealing with Forgery and Section 477A dealing with falsification of accounts.”

Without prejudice to any liability, including repayment of any debt under this Act or any other law, the terms "without prejudice to" in Section 447 of the Act mean without negatively impacting any other legal processes. In the context of the aforementioned section, it means that actions taken in accordance with Section 447 of the Act will not be barred as long as they do not negatively impact an action or a proceeding involving any liability. This covers the payment of debts started in accordance with any other Act clauses or currently in effect laws.

The explanation lists the following as the many components of fraud: a) any act, or

(b) an omission,

(c) hiding any information or

(d) misusing one's power

Committed by someone or anyone else with their knowledge in any case with the purpose of misleading, taking advantage of, harming, or impairing the company's, its shareholders', creditors', or other parties' interests, whether or not there is any unjust gain or loss.

Judges have considered the phrase "intent to deceive" in light of Section 463 of the IPC. In the case of *Vimla v. State*, it was determined that while the concept of deceit is a fundamental component of fraud, it does not exhaust it. Deception and harm to the one who was duped are two components of the term "fraud." Injury includes any harm committed to a person's health, intellect, reputation, or any aspects of their personhood other than economic loss, which is the deprivation of property, whether it be mobile or immovable, or of money. A gain or advantage for the deceiver nearly always results in a loss or disadvantage for the victim. The second requirement is met even in the uncommon situations where the deceiver receives a profit or advantage without a corresponding loss for the victim. "Section 447 of the Act has been invoked in a few recent corporate scandals which are still at different stages of trial. Given that it is a relatively new provision, there are no direct pronouncements on this provision so far either by NCLT or the High Courts or the Supreme Court (SC). This provision has been invoked by the SFIO in a few recent corporate scandals."

"The Act has introduced stringent punishment for the persons who are found to be guilty of fraud. Fraud, if it involves an amount of at least INR 10 lakh or 1% of the turnover of the company, whichever is lower, is an offence punishable by imprisonment not less than six months and can go up to maximum of 10 years. The provision for fine cannot be less than the amount of fraud and may extend up to three times the fraud amount. However, if the fraud in question involves public interest, the term of imprisonment shall not be less than three years."

"The offence under Section 447 of the Act is cognisable, non-bailable and non-compoundable. Section 446A of the Act lays down five factors to be considered by the Court while deciding the amount of fine or imprisonment under the Act: (a) size of the company; (b) nature of business carried on by the company; (c) injury to public interest; (d) nature of the default; and (e) repetition of the default."

Company Bill 2011: The beginning of Changes and Improvements

The case *Salomon v. Salomon* serves as the introduction to company law. Indian history usually draws attention to English history and the well-known South Sea Bubble case with its destructive Bubble Act 1720 since the term has its roots in the English language. According to history, there was a time when businesses behaved like bubbles—they form quickly and burst

quickly. The aforementioned Act utterly destroyed this practise by introducing disclosure standards into a company's legal framework for the first time.²

The 1956 Companies Act, which proved to be incompatible with the business climate in India, served as the model for our nation. A variety of frauds starting in 1956 caused India's economy to be unstable, and many changes were tried to address the problem. Unfortunately, the Sahara scam's emergence forced the Act to relinquish all of its regulatory, enforcing, and administrative authority. "Due to this, the Companies Bill, 2011 was passed with the provisions listed below:

1. E-Governance by maintenance and inspection of documents by companies in the electronic form being allowed for the first time.
2. The concept of Corporate Social Responsibility is being introduced.
3. Enhanced accountability of the companies by introducing independent directors, CSR committee, remuneration committee, shareholder relationship committee, and audit committee.
4. Additional disclosure norms.
5. Facilitate the raising of capital by companies.
6. Audit accountability.
7. Managerial remuneration.
8. Facilitates mergers and acquisitions.
9. Protection of minority shareholders and small shareholder along with investor protection.
10. Introducing woman director and Serious Fraud Investigation Officer.
11. Introducing National Company Law Tribunal and mediation and conciliation panel."

² Ankush Banga, India: The Journey of Companies Act from 1956 to 2021, *The Taxman Journal* (2021)

The Sahara scandal, which alarmingly declared the need for disclosure and corporate control, led to the creation of the Companies Act of 2013. A J.J. Irani Committee was established to draught the 2013 Act, which included stringent disclosure requirements.³ With regard to compliance, disclosure, administration, penalties, and proceedings, the Act painted a radically new image. The audience has been compelled to quickly accept, adapt, and adjust themselves, forgetting the 1956 Act in the process. The Company Law Tribunal, which has extraordinary powers, has effectively supplanted the Company Law Board. For the purpose of enforcing disclosure standards, it is necessary to isolate the Act's disclosure-related sections from its other components.

Companies Act 2013: Is it really effective?

The purpose of the Companies Act 2013, which replaces the Companies Act 1956, is to support the best corporate governance and the upkeep of discipline through disclosure. The Satyam to Sahara case was carried out in the presence of the Companies Act of 1956, which made politicians and the public aware that there is no need for a law to govern businesses in the country. Because of this, the Companies Act 2013 was carefully drafted by the legislators to guarantee that there won't be any fresh Satyam to Sahara partnerships following its passage. When compared to the 1956 Act's history, the 2013 Act has seen some of the most intricate and well-known schemes involving numerous legal infractions, particularly involving foreign businesses. Scams are currently moving toward the banking industry. Is it depicting a loosely connected structure between the laws of other corporations and those of banks? It has been observed that scams frequently take place within SEBI's network, but the institution always waits until it is too late to recognise them and take action.

Some scams that took place are enactment of Companies Act 2013 are:

Shardha Chit Funds Scam – 2013

Millions of depositors invested money in West Bengal's Ponzi scheme, which was backed by political favouritism and promised to yield unbelievable profits. SEBI and RBI caught the defaults. The scam's financial stakes were estimated to be between Rs. 2060 and Rs. 2400 crores. The Enforcement Directorate and SFIO have been granted custody of the Shardha

³ Madhu Bala, India: Corporate frauds and legal mechanism in india-an overview, Journal IJCAR (2018)

Group's chairman and managing director in order to investigate money laundering. 1000 depositors have received compensation to date.⁴

2014- HAL and Rolls-Royce Defence Scam

According to the allegations, Rolls-Royce, a British business, bribed HAL out of Rs. 10,000 crores in exchange for the deal to provide aircraft engines to the state-owned HAL company. The Defense Ministry had filed a complaint after receiving information that led to the allegation. HAL has been instructed to halt all further negotiations pending the outcome of the CBI investigation, which was launched in this regard. The Vigilance division later claimed that Rolls-Royce had contracted a third party for the transaction. As the CBI investigation intensified, the British company Rolls-Royce wrote to state-owned HAL to say that it had paid its agent Ashmore Pvt. Ltd. a commission of Rs. 18 crore and was willing to repay the money to the government.

2017- Mining Scam by Essar Group, Reliance Group, and Adani Group

A Public Interest Litigation brought against the Adani Group, Essar Group, Reliance Anil Dhirubhai Ambani Group, and other mining corporations for over-invoicing coal extracted in Indonesia brought the scandal to light. The businesses were charged with diverting extra money into accounts abroad. 40 firms that were charged with raising the price of Indonesian coal are thought to have contributed an estimated Rs. 290 billion to the scheme. This made it difficult for the businesses to evade taxes. The situation is still open.

2018- Punjab National Bank Scam

The act of issuing massive loans with advances is where the problem started. Due to its allure, more borrowers began making defaults, which caused banks' NPA to increase. The same prevented it from turning a profit. This has also caused share prices to decline. In the past year, it has also experienced serious governance problems. RBI published a rehabilitation plan in which SBI will contribute money to buy a 49% interest. Customers whose salaries are connected to accounts with this bank will be significantly impacted. The bank was also given a 30-day moratorium, and since the RBI now controls all aspects of it, its board has no further

⁴ Akansha Tomar, India: Corporate Frauds - The Analysis, Mondaq Journal (2018)

authority. Several compliance experts remarked that promoter-driven banks require special regulatory attention and that corporate governance flaws need to be remedied.

Major Amendments in Companies Act 2013

Due to various scams even after the enactment of the Companies Act 2013, the government in 2019 made about 40 amendments in companies act to improve ease of doing business and mainly to tightening the noose around unscrupulous businesses.

It can be observed that, through amendments the government is trying to make the execution very strict. They are increasing the penalties and offences bringing them in line with foreign laws.⁵ “The major amendments out of 40 are:

- Govt can ask a tribunal to pass disgorgement order against management personnel found involved in fraud.
- National Financial Reporting Authority can ban CAs from any audit or valuation related activities for a period of 6 months to 10 years.
- Non-compliance of CSR laws can land officials in jail.
- Any unspent CSR money has to be transferred into a special account. The money in this account has to be spent within 3 financial years.
- Companies can issue DVRs with voting rights up to 74% of the post-issue paid up capital from the existing 26%.
- More offences can be resolved at the level of Regional Director (instead of approaching NCLT, which is an adjudicatory body).
- Mandatory for shareholders of unlisted companies to hold or transfer securities only in dematerialised form.

⁵ Dipak Mondal, India: Companies Act amendments aim to curb fraud, increase accountability, Business Today (2019)

- Non-compliances with requirements of prohibition on issuances of shares at discount, and timely filing of annual return, no longer attract imprisonment.”

Conclusion

Corporate fraud is not a new issue in India. Several corporate frauds have been exposed, and the offenders have occasionally been punished. The government and investors have paid a high price for these financial crimes. The public that invested their money suffers a long-term considerable loss even while the offenders are punished. Corporate financial fraud victims do not have simple access to their money. Years are needed to make up for lost time. Numerous laws impose severe fines and strict corporate requirements, yet as we can see, new corporate frauds are uncovered every year, indicating that laws alone won't be sufficient to halt these crimes. Corporate fraud is expensive and socially unwelcome. The collapse of ethical values at both the individual and organisational levels is the root cause of this awful illness. The only way out of the mess may require both a genuine social transformation that affects people on a deep level and strong leadership capable of establishing discipline at all levels.

In the Post-COVID era, the new normal is in charge of the future. The digitization of all industries is pushed quickly and readily during the pandemic. Nowadays, there are a lot of digitally conducted transactions, contracts, contacts, meetings, etc., which present several opportunities for manipulation. There are more opportunities to be duped, so the vigil mechanism needs to be strengthened to overcome these challenges. False identity and other offences listed in the Information Technology Act 2000 must be tied to corporate governance for the digital business sector to experience the least amount of stress. Although the Companies Act of 2013 incorporates several ideas, implementation is often postponed. People from all industries have already experienced irreparable hurt as a result of it. I firmly believe that now is the ideal time to alter the Companies Act 2013's execution and implementation procedures in order to give every business in the nation a solid foundation and promote national development. Additionally, it is necessary to consider "whether we need an alternative SEBI authority or a highly specialised wing to tackle concerns relevant to the present and the future”.

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