

ALL THE VERY BEST FOR YOUR EXAMS

SHORT NOTES FOR CAIIB BANKING REGULATIONS AND BUSINESS LAWS

Though we had taken enough care to go through the notes provided here, we shall not be responsible for any loss or damage, resulting from any action taken on the basis of the contents. Creation of these short notes is the efforts of so many persons. First of all we thank all of them for their valuable contribution. We request everyone to go through the Macmillan book and update yourself with the latest information through RBI website and other authenticated sources. In case you find any incorrect/doubtful information, kindly update us also (along with the source link/reference for the correct information).

Dr. K Murugan, DMS, MBA (Finance), MBA (HR), MCA, MSc (IT), CAIIB

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CAIIB – GENERAL INFORMATION

Consists of 4 papers :

I. Compulsory Paper

1. Advanced Bank Management
2. Bank Financial Management
3. Advanced Business & Financial Management
4. Banking Regulations and Business Laws

II. Elective Papers (Candidates to choose any one of their Choice)

1. Rural Banking
2. Human Resources Management
3. Information Technology & Digital Banking
4. Risk Management
5. Central Banking

- Only existing employees of banks who had cleared JAIIB can appear for CAIIB Exam.
- CAIIB exams are conducted in on-line mode only.
- The examination will be conducted normally twice a year in May / June and November / December on Sundays.
- The duration of the examination will be of 2 hours.
- **Examination Pattern :**
 - (i) Question Paper will contain 100 objective type multiple choice questions for 100 marks including questions based on case studies/ case lets. The Institute may however vary the number of questions to be asked for a subject.
 - (ii) There may be some numerical questions in some of the CAIIB subjects where, no options will be provided. These questions will not be in the MCQ pattern and the answer has to be keyed in by the candidate.
 - (iii) The examination will be held in Online Mode only.
 - (iv) There will be no negative marking for wrong answers.
 - (v) Questions for the examination will be asked for:
 - a. Knowledge testing
 - b. Conceptual grasp
 - c. Analytical/ logical exposition
 - d. Problem solving
 - e. Case analysis

➤ **Passing Criteria :**

1. Minimum marks for pass in the subject is 50 out of 100.
2. Candidates securing at least 45 marks in each subject with an aggregate of 50% marks in all subjects of examination in a single attempt will also be declared as having completed the Examination.
3. Candidates will be allowed to retain credits for the subject they have passed in an attempt till the expiry of the time limit for passing the examination.

Note : A candidate will be given 5 attempts for completion of exam (CAIIB) but, within a maximum period of three years, whichever is earlier, from the time he/she registers for the exam. These 5 attempts need not be consecutive.

➤ **"Class of Pass" Criteria :**

- ❖ **First Class** : 60% or more marks in aggregate and pass in all the subjects in the FIRST PHYSICAL ATTEMPT.
- ❖ **First Class with Distinction** : 70% or more marks in aggregate and 60% or more marks in each subject in the FIRST PHYSICAL ATTEMPT.
- ❖ Candidates who have been granted exemption in the subject/s will be given "**Pass Class**" only.

➤ **Cut-off Date of Guidelines /Important Developments for Examinations :**

- ❖ In respect of the exams to be conducted by the Institute for the Period from February to July of a calendar year, instructions/guidelines issued by the regulator(s) and important developments in banking and finance up to 31st December will only be considered for the purpose of inclusion in the question papers.
- ❖ In respect of the exams to be conducted by the Institute for the period from August to January of a calendar year, instructions/guidelines issued by the regulator(s) and important developments in banking and finance up to 30th June will only be considered for the purpose of inclusion in the question papers.

➤ **Exam Fees**

Description	Fees*
First attempt fee	5,000
Second attempt fee	1,300
Third attempt fee	1,300
Fourth attempt fee	1,300
Fifth attempt fee	1,300

* Plus Convenience charges and Taxes as applicable.

Please Note: Candidates are required to Register for every attempt separately

SYLLABUS

The details of the prescribed syllabus which is indicative are furnished in the booklet. However, keeping in view the professional nature of examinations, all matters falling within the realm of the subject concerned will have to be studied by the candidate as questions can be asked on all relevant matters under the subject.

Candidates appearing for the examination should particularly prepare themselves for answering questions that may be asked on the latest developments taking place under the various subject/s of the said examination although those topics may not have been specifically included in the syllabus. Further, questions based on current developments in banking and finance may be asked. **Candidates are advised to refer to financial news papers / periodicals more particularly "IIBF VISION" and "BANK QUEST" published by IIBF.**

MODULE A: REGULATIONS AND COMPLIANCE

Legal Framework of Regulation of Banks

Business of Banking, Constitution of Banks, Reserve Bank of India Act, 1934, Banking Regulation Act, 1949, Reserve Bank as a Central Bank and Regulator of Non-Banking Financial Institutions/Banks, Government as a Regulator of Banks, Control over Co-operative Banks, Regulation by Other Authorities

Control over Organisation of Banks

Licensing of Banking Companies including RBI Licencing Policy for Universal Banks and Small Finance Banks/Branch Licensing, Paid-up Capital and Reserves, Shareholding in Banking Companies, Subsidiaries of Banking Companies, Board of Directors, Chairman of Banking Company, Appointment of Additional Directors, Restrictions on Employment, Controls over Management, Corporate Governance, Directors and Corporate Governance

Regulation of Banking Business

Power to Issue Directions, Acceptance of Deposits, Nomination, Loans and Advances, Regulation of Interest Rates, Regulation of Payment Systems, Internet Banking Guidelines, Regulation of Money Market Instruments, Banking Ombudsman, Regulation to Strengthen Financial Stability

Returns, Inspection, Winding Up, Mergers & Acquisitions

Annual Accounts and Balance Sheet, Audit and Auditors, Submission of Returns, Preservation of Records and Return of Paid Instruments, Special Audit, Inspection and Scrutiny, Board for Financial Supervision, Acquisition of Undertakings, Amalgamation of Banks, Winding up of Banks, Penalties for Offences

Public Sector Banks, Private Sector Banks, Regional Rural Banks, Differentiated Banks and Co-operative Banks, Local Area Banks

State Bank of India, Regional Rural Banks, Other Public Sector Banks, Application of Banking Regulation Act to Public Sector Banks, Disinvestment of Shares by Government, Co-operative Banks, Private Sector Banks, Differentiated Banks, Local Area Banks

Non-Banking Financial Companies (NBFCs)

Regulators of NBFCs, Role of NBFC in promoting Inclusive Growth, Registration, Revised Scale Based Regulatory Structure, Nomenclature and Regulatory Norms, Capital Guidelines, Prudential Guidelines, Corporate Governance, Fair Practices Code for applicable NBFC, Bank Finance to NBFCs registered/not requiring registration with RBI, Co-Lending by banks and NBFCs to PSA

Financial Sector Legislative Reforms and Financial Stability and Development Council

Narasimham Committees 1/2, Banking Sector Reforms, Reforms in Monetary Policy, Reforms in Financial Markets, Reforms in Forex Market, Financial Sector Development Council (FSDC), Function of the FSDC, Wings of FSDC

MODULE B: IMPORTANT ACTS/LAWS & LEGAL ASPECTS OF BANKING OPERATIONS – PART A

The Prevention of Money Laundering Act, 2002

Offence of Money Laundering, Punishment for Money Laundering, Obligations of Banking Companies, Financial Institutions and Intermediaries, Enhanced Due Diligence, Rules Framed, Records to be Maintained, Information Contained in the Records, Procedure for Maintaining Information, Procedure for Furnishing Information to the Director, Verification of Records of the Identity of Clients, Maintenance of Records of Identity of Clients, Some Cases pertaining to the Act

Negotiable Instruments Act, 1881

Negotiable Instruments, Types and Characteristics, Drawer/Acceptor, Payment of Cheques – Protection to Bankers' /Customers', Material Alteration, Where Alteration is not apparent, Protection to the Collecting Banker

Foreign Exchange Management Act, 1999

Meaning of Certain Important Terms Used in FEMA, Regulation and Management of Foreign Exchange, Powers of RBI with Respect to Authorized Persons, Contravention, Penalties, Adjudication and Appeals, Directorate of Enforcement, Special Provisions relating to Assets held outside India

Payment & Settlement Systems Act, 2007

Definitions, Designated Authority/Authorization, Regulation and Supervision by the RBI, Settlement and Netting, Power of RBI to make regulations

Law Relating to Securities and Modes of Charge – I

Mortgage, Document of Title to Immoveable Property – Meaning, Copy of Document of Title to Immoveable Property Where Acceptable

Law Relating to Securities and Modes of Charge – II

Appropriation, Assignment, Pledge, Hypothecation, Bankers lien, Set-off

Creation/Registration and Satisfaction of Charges

What is a Charge?, Procedure for Registration of Charge, Effect of Registration of Charges, Effect of Non- registration of Charges, Provisions of Companies Act 2013 Relating to Registration of Charges

MODULE C: IMPORTANT ACTS/LAWS & LEGAL ASPECTS OF BANKING OPERATIONS – PART B

Reserve Bank – Integrated Ombudsman Scheme, 2021

Coverage and Definitions, Ombudsman–Appointment/Location of Offices/Establishment of a Centralized Receipt and Processing Centre, Procedure for Redressal of Grievance, Procedure for Filing a Complaint / its Initial Scrutiny and Resolution, Passing of an Award and Right to Prefer to Appeal, Suspension of the Scheme

The Micro, Small and Medium Enterprises Development Act, 2006

Coverage and Definitions, Summary of Regulation, National Board for Micro, Small and Medium Enterprises (NBMSME)/Advisory Committee, Memorandum of Micro, Small and Medium Enterprises, Delayed Payments to Micro and Small Enterprises, Micro and Small Enterprises Facilitation Council and Reference to the Council in case of Disputes, Disclosures and Penalty for Contravention of the Provisions of the Statute

Introduction to Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (SARFAESI Act, 2002)

Constitutional Validity of the Act

Definitions Under SARFAESI Act, 2002

Preamble, Appellate Tribunal, Asset Reconstruction, Bank, Board, Borrower, Central Registry, Debt Recovery Tribunal, Default, Financial Assistance, Financial Asset, Financial Institution, Hypothecation, Non-performing Asset, Originator, Obligor, Property, Qualified Institutional Buyer, Scheme, Securitization, Security Agreement, Secured Asset, Secured Creditor, Secured Debt, Security Interest, Security Receipt, Sponsor

Regulation of Securitisation and Reconstruction of Financial Assets of Banks and Financial Institutions

Registration of Asset Reconstruction Company, Cancellation of Certificate of Registration, Acquisition of Rights of Interest in Financial Assets, Notices to Obligor and Discharge of Obligation of Such Obligor, Issue of Security Receipts and Raising of Funds by Securitization or Reconstruction Company, Exemption from

Registration of Security Receipt, Measures of Assets Reconstruction, Other Functions of the Securitization Company or Reconstruction Company, Resolution of Dispute, Powers Available with RBI

Enforcement of Security Interest

Enforcement of Security Interest, Chief Metropolitan Magistrate or District Magistrate's Assistance for Taking Possession of Secured Asset, Manner and Effect of Takeover of Management, No Compensation to Directors for Loss of Office, Application against Measures to Recover Secured Debt, Appeal to Appellate Authority, Right of the Borrower for Compensation and Costs

Central Registry

Central Registry, Central Registrar, Register of Securitization, Reconstruction and Security Interest Transactions, Filing of Transactions of Securitization, Reconstruction and Creation of Security Interest, Modification of Security Interest Registered, Satisfaction of Security Interest, Right to Inspect Particulars of Securitization, Reconstruction of Security Interest Transactions

Offences and Penalties

Penalties, Penalties for Non-compliance of Directions of Reserve Bank of India, Offences, Cognizance of Offences, Power of Adjudicating Authority to Impose Penalty/Appeals against Penalty and Adjudicating Appellate Authority

Miscellaneous Provisions

Non-Applicability of the Provisions of the SARFAESI Act in Certain Cases, Exemption of Certain Classes of Banks /Financial Institutions, Protection of Action Taken in Good Faith, Offences by Companies, Civil Court not to have Jurisdiction, Overriding Effect on Other Laws, Limitation, Power of the Central Government to Make Rules, Amendments to Certain Other Enactments

Registration of Security Interest by Secured Creditors and Other Creditors/ Rectification by Central Government in Some Cases

Registration by Secured Creditors and Other Creditors, Rectification by Central Government in Matters of Registration, Effect of the Registration of Transactions, Right of Enforcement of Securities and Priority Allowed to Secured Creditors

The Recovery of Debts and Bankruptcy Act, 1993

Constitutional Validity of the Act, Extent, Commencement, Application and Definitions

Establishment of Tribunal and Appellate Tribunal

Establishment of Tribunal, Composition of Tribunal, Qualification for Appointment as Presiding Officer and Term of Office, Staff of Tribunal, Establishment and Composition of Appellate Tribunal, Qualification for Appointment as Chairperson of the Appellate Tribunal and Term of Office, Filling up of Vacancies at Tribunal and Appellate Tribunal, Finality of Orders Constituting Tribunal or an Appellate Tribunal

Jurisdiction, Powers & Authority of Tribunals

Jurisdiction, Powers and Authority of Tribunals, Bar of Jurisdiction of Civil Courts

Procedure of Tribunals

Application to the Tribunal, Appeal to the Appellate Tribunal, Deposit of Amount of Debt Due for Filing

Appeal, Procedure and Powers of the Tribunal and the Appellate Tribunal, Limitation

Recovery of Debts Determined by Tribunal and Miscellaneous Provisions

Modes of Recovery of Debts, Validity of Recovery Certificate and Amendment Thereof, Stay and Amendment for Recovery Proceeding and Certificate, Other Modes of Recovery, Application of Certain Provisions of the Income Tax Act, Appeal against the Order of Recovery Officer, Transfer of Pending Cases, Power of Tribunal to Issue Certificate of Recovery in Case of Decree or Order, Chairperson, Presiding Officer and Staff of Appellate Tribunal and Tribunal Public Servants, Protection of Action Taken in Good Faith, Overriding Effect of the Act, Powers to Make Rule

Introduction to the Insolvency and Bankruptcy Code, 2016

Definitions, Coverage, Pillars of IBC, 2016, The Insolvency Resolution Process for Companies and Limited Liability Entities, Corporate Insolvency Resolution Process (CIRP), Initiation of Corporate Insolvency Resolution Process by a Financial Creditor, Suspension of Initiation of CIRP, Persons not Entitled to Make Application, Time – Limit for completion of Insolvency Resolution Process and withdrawal of application admitted under the Code, Declaration of Moratorium and Public Announcement by the Adjudicating Authority, Appointment/Tenure of the Interim Resolution Professional, Committee of Creditors, Appointment of Resolution Professional, Liquidation, Order of Priority of Payment of Debts, Fast Track Insolvency Resolution Process, Voluntary Liquidation of Corporate Person

The Bankers' Books Evidence Act, 1891

Applicability and Definitions, Conditions in the Printout, Mode of Proof of Certain Entries in Bankers' Books, Case in which Officer of Bank not Compellable to Produce Books, Inspection of Books by Order of Court or Judge, Costs of Application

The Legal Services Authorities Act, 1987: Lok Adalats

Organization of Lok Adalats, Jurisdiction of Lok Adalats, Cognizance of Cases by Lok Adalats, Disposal of Cases by Lok Adalats, Nature of Award of the Lok Adalats and Powers

The Consumer Protection Act, 2019

Definitions, Unfair Contract and Unfair Trade Practice, Central, State and District Consumer Protection Councils, Central Consumer Protection Authority, District, State and National Consumer Disputes Redressal Commission, Ministry of Consumer Affairs, Food and Public Distribution

(Department of Consumer Affairs) Notification dated 30th December, 2021, Finality of Orders and Limitation Period, Consumer Mediation Cell

The Law of Limitation

Definitions, Limitation and Its Computation, Computation of the Period of Limitation, Acts Giving Rise to Fresh Period of Limitation, Certain Important Provisions in Schedule to the Limitation Act

Tax Laws

Income Tax, Commodity Transaction Tax, Goods and Services Tax

MODULE D: COMMERCIAL & OTHER LAWS WITH REFERENCE TO BANKING OPERATIONS

Meaning and Essentials of a Contract

Meaning of Contract, Key Components to Form a Contract Essentials of a Valid Contract, Contract Act and Banking

Contracts of Indemnity

Rights of Indemnity Holder, Implied Indemnity, Enforceability of Contract of Indemnity

Contracts of Guarantee

Parties to the Contract, Basic Principles of Contract to be complied, Consideration, The Liability of the Surety, Continuing Guarantee, Death of Surety, Variance in Terms of the Contract, Discharge of Principal Debtor, Forbearance to Sue, Release of One Co-surety does not Discharge Other, Surety can Claim His Dues from the Principal Debtor, Security, Misrepresentation made by the Creditor, Implied Promise by the Principal Debtor to Indemnify the Surety, Co-sureties for the Same Debt, Revocation of a Continuing Guarantee

Contract of Bailment

Meaning of Bailment, Essential Features of Bailment, Bailor Bound to Disclose to the Bailee, Bailee to take care of Goods, Effects of mixing of Goods and Expenses, Duties of the Bailee with regard to Goods, Bailee's Lien

Contract of Pledge

Ingredients of Pledge, Nature of Pledge, Pledge by Way of Hypothecation, Pledge by Pledgee

Contract of Agency

Definition, Contract of Agency, Essential Characteristics of a Contract of Agency, Rules of Agency, Types of Agents, Rights and Duties of the Agent and Principal

Meaning and Essentials of a Contract of Sale

Meaning of some of the Important Terms Defined Under the Sale of Goods Act, 1930, Meaning of Contract of Sale of Goods, Features of Contract of Sale of Goods, Sale and Agreement to Sell, Distinction between a Sale and an Agreement to Sell

Conditions and Warranties

Meaning of Condition and Warranty, Implied Conditions and Warranties

Unpaid Seller

Rights of an Unpaid Seller

Definition, Meaning and Nature of a Partnership

Meaning and Definition of Partnership, Essential Characteristics, Types of Partnership, Limited Liability Partnership (LLP)

Relations of Partners to One Another

General Duties of Partners, Duty to Indemnify the Loss caused by Fraud, Determination of Rights and Duties of Partners by Contract between the Partners, The Conduct of the Business, Mutual Rights and Liabilities, The Property of the Firm, Profits Earned by Partners, Rights and Duties of Partners

Relations of Partners to Third Parties

Partner is an Agent of the Firm, Implied Authority of Partner as Agent of the Firm, Extension and Restriction of Partner's Implied Authority, Partner's Authority in an Emergency, Mode of Action to Bind Firm, Liability of a Partner for Acts of the Firm, Liability of the Firm for Wrongful Acts of a Partner, Liability of Firm for Misapplication by Partners, Holding Out, Rights of Transferee of a Partner's Interest

Minor Admitted to the Benefit of a Partnership

Minor cannot be a Partner, Legal position after the Minor attains majority, Retirement of a Partner, Insolvency of a Partner

Dissolution of a Firm

Dissolution, Dissolution by Agreement, Compulsory Dissolution, Dissolution on the Happening of Certain Contingencies, Dissolution by the Court, Liability for Acts of Partners Done after Dissolution

Effect of Non-Registration

Registration

Definition and Features of a Company

Definition of a Company, Features of a Company, Distinction between a Company and Partnership

Types of Companies

Classifications of Companies on the basis of mode of Incorporation, Classifications of Companies on the basis of Liability, Classifications of Companies on the basis of Public Interest, Holding and Subsidiary Companies

Memorandum of Association and Articles of Association

Memorandum of Association, Articles of Association, Effect of Memorandum and Articles, Distinction between the Memorandum of Association and Articles of Association

Doctrines of Ultra Vires/ Constructive Notice/ Indoor Management

Doctrine of Ultra Vires, Effects of Ultra Vires Transaction, Constructive Notice of Memorandum of Association and Articles of Association, Effect of the Doctrine of Constructive Notice, Doctrine of Indoor Management

Membership of Company

Who is a Member of a Company? Various Modes of Becoming Member of a Company, Who can be Members of a Company?, Cessation of Membership in a Company, Register of Members, Place of Keeping and Inspection of Register of Members, Rights and Duties (Liabilities) of Members of a Company, Rights of Members

Prospectus

What is a Prospectus? Compliance with Respect to Prospectus, Mis-statements in a Prospectus and Remedies

Directors

Minimum Number of Directors, Appointment of Directors and Proportion of those who are to Retire by Rotation, Ascertainment of Directors Retiring by Rotation and Filing of Vacancies, Right of Persons other than Retiring Directors to stand for Directorship, Additional Directors, Filling of Casual Vacancies among Directors, Consent to the Company, Consent to be filed with Registrar of Companies, Whole-time Director, Qualification Shares, Maximum Number of Directorships, Vacation of Office by Directors, Certain Powers can be exercised only at Meetings of the Board, Restrictions on Powers of Board, Loan to Director, Contracts in which Directors are Interested, Alternate Director, Compensation for Loss of Office.

Limited Liability Partnership Act, 2008

Definitions, A Body Corporate, Partner/Designated Partner, Liabilities of and changes in Designated Partners, Incorporation of a Limited Liability Partnership, Partners and their Relations, Conversion

Transfer of Property Act, 1882

Sale of Immoveable Property, Mortgage of Immoveable Property, Types of Mortgage, Sale without Court Intervention, Enforcement of Mortgages through Court, Leases of Immoveable Property, Actionable Claims

The Right to Information Act, 2005

Applicability, Definitions

Right to Information and Obligations of Public Authorities

Obligations of Public Authorities, Procedure for obtaining Information, Disposal of Request, Appeal, Orders in Appeal, Penalties

Information Technology Act, 2000

Definitions, Electronic Governance, Certifying Authorities, Digital Signature Certificates, Penalties, Appeal, Investigation, Critical Information Infrastructure –Protected System, Application of the Act to Electronic Cheque and Truncated Cheque,

Prevention of Corruption Act, 1988

Definitions, Special Judges, Offences and Penalties, Fixing of Fine, Persons authorized to investigate, Powers to inspect 'Bankers Books', Appeal and Revision

APPENDIX

Important Provisions / Sections of certain Acts

MODULE - A : REGULATIONS AND COMPLIANCE

Unit 1 : Legal Framework of Regulation of Banks

- ❖ Banking means acceptance of deposits of money from the public for lending or investment.
- ❖ Such deposits may be repayable on demand or may be for a period of time as agreed to, by the banker and the customer, and may be repayable by cheque, draft or otherwise.
- ❖ Apart from banking, banks are authorised to carry on other business as specified in Section 6 of the Banking Regulation Act.
- ❖ Banks are, however, prohibited from undertaking any trading activities.
- ❖ Banks are constituted as companies registered under the Companies Act, 1956, statutory corporations constituted under Special Statutes or Co-operative societies registered under the Central or State Co-operative Societies Acts. The extent of applicability of the regulatory provisions under the Banking Regulation Act and the Reserve Bank of India Act to a bank depends on the constitution of the bank.
- ❖ Reserve Bank of India is the central bank of the country and the primary regulator for the banking sector.
- ❖ The government has direct and indirect control over banks. It can exercise indirect control through the Reserve Bank and also act directly in appeals arising from decisions of the Reserve Bank under the various provisions of the Banking Regulation Act.
- ❖ In public sector banks like the State Bank of India and its subsidiaries, nationalised banks and the regional rural banks, 50% or more of their shares are held by the Central Government. Central Government has substantial control over the management of these banks. Only certain provisions of the BR Act are applicable to these banks as indicated in that Act.
- ❖ Co-operative banks operating in one state only are registered under the State Co-operative Societies Act and are subject to the control of the State Government as also the Reserve Bank.
- ❖ In the case of non-banking business of the banks, they are subject to control by other regulatory agencies.

Constitution of Bank

Banks in India fall under one of the following categories:

1. Banks in India fall under one of the following categories:
2. Body corporate constituted under a special statute
3. Company registered under the Companies Act, 1956 (Companies Act 2013) or a foreign company
4. Co-operative society registered under a Central or State enactment.

Public Sector Banks (other than SBI)

These Public Sector Banks are constituted under the Banking Companies (Acquisition) and Transfer of Undertakings) Act, 1970 and the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1980.

State Bank of India (SBI)

The State Bank of India was constituted under the State Bank of India Act, 1955 while the seven associate/subsidiary banks were constituted under the State Bank (Subsidiary Banks) Act, 1959.

Regional Rural Banks (RRBs)

The RRBs were constituted under the Regional Rural Banks Act, 1976. These banks are governed by the statutes creating them as also some of the provisions of the Banking Regulation Act and the Reserve Bank of India Act.

Private Sector Banks/Foreign Banks

Most Private Sector Banks (including Micro and Small Finance Banks) are Companies' constituted under Section 3 of the Companies Act, 1956 or incorporated under the Companies Act, 2013. Foreign Banks are basically foreign companies constituted as per statutes abroad and treated as such under section 2(42) of the Companies Act, 2013.

Co-operative Banks

A co-operative bank conducts ordinary banking business but is established on a co-operative basis. If a co-operative bank is operating in more than one state, the Central Act i.e. Multi State Cooperative Societies Act applies. In other cases, the respective State Co-operative Societies Act would apply.

Reserve Bank of India Act, 1934

- ❖ The Reserve Bank of India Act, 1934 was enacted to constitute the Reserve Bank of India and came into force from 6th March 1934.
- ❖ The general superintendence and direction of the affairs and business of the bank have been vested with the Central Board of Directors which consists of –
 - ❖ A governor and not more than four deputy governors appointed by the central government.
 - ❖ Four directors nominated by the central government, one from each of the local boards.
 - ❖ Ten directors nominated by the central government
 - ❖ Two government officials nominated by the central government.
- ❖ Section 17 of the of RBI Act 1934 t defines the manner in which the RBI can conduct business. The RBI Act 1934 deals with the constitution, powers and functions of the Reserve Bank.
- ❖ Section 18 of RBI Act 1934 deals with emergency loans to banks. The section 19 of the Reserve Bank of India Act, 1934 states that the Reserve Bank of India has been prohibited from (a) making

loans or advances; (b) drawing or accepting bills payable otherwise than on demand ; (c) allowing interest on deposits or current accounts.

- ❖ Section 20 of RBI Act 1934 narrates obligation of the RBI to transact Government business.
- ❖ Section 21 of RBI Act 1934 states that the RBI must conduct banking affairs for the central government and manage public debt .
- ❖ Section 22 of RBI Act 1934 states that only the RBI has the exclusive rights to issue currency notes in India.
- ❖ Section 24 of RBI Act 1934 states that the maximum denomination a note can be is ₹10,000.
- ❖ Section 26 of RBI Act 1934 describes the legal tender character of Indian bank notes.
- ❖ Section 26 (2) deals with withdrawal of legal tender of notes.
- ❖ Section 27 of RBI Act 1934 states that the RBI shall not re-issue bank notes which are torn, defaced or excessively soiled.
- ❖ Section 28 of RBI Act 1934 allows the RBI to form rules regarding the exchange of damaged and imperfect notes.
- ❖ Section 31 of RBI Act 1934 states that in India, only the RBI or the central government can issue and accept promissory notes that are payable on demand. However, cheques , that are payable on demand, can be issued by anyone.
- ❖ Section 42 of RBI Act 1934 states that Cash Reserves of Scheduled Banks to be kept with the Bank (RBI).
- ❖ Section 42(1) of RBI Act 1934 says that every scheduled bank must have an average daily balance with the RBI. The amount of the deposit shall be a certain percentage of its net time and demand liabilities in India.
- ❖ Section 45 U of RBI Act 1934 defines Repo, Reverse Repo, Derivative, Money Market Instruments and Securities.

Banking Regulation Act, 1949

- ❖ Banking Regulation Act, 1949 is a legislation in India that regulates all banking firms in India. Passed as the Banking Companies Act 1949, it came into force from 16 March 1949 and changed to Banking Regulation Act 1949 from 1 March 1966. It is applicable in Jammu and Kashmir from 1956.
- ❖ Initially, the law was applicable only to banking companies. But, in 1965 it was amended to make it applicable to cooperative banks and to introduce other changes. In 2020 it was amended to bring the cooperative banks under the supervision of the Reserve Bank of India.
- ❖ Section 5 of BR Act interprets the terms Bank and Banking Company.
- ❖ Section 6 of BR Act deals with the forms of business a bank can undertake.
- ❖ Section 7 of BR Act deals with usage of word bank, banker , banking or banking company. No company other than a banking company shall use as part of its name in connection with its business] any of the words "bank", "banker" or "banking" and no company shall carry on the business of banking in India unless it uses as part of its name at least one of such words.
- ❖ Section 8 of BR Act prohibits a Bank from engaging directly or indirectly in any trading.

- ❖ Section 9 of BR Act deals with disposal of non banking assets
- ❖ As per Section 10 B of BR Act a Banking company to be managed by whole time chairman.
- ❖ Section 10BB of BR Act deals with Power of Reserve Bank to appoint Chairman of the Board of directors appointed on a whole-time basis or a managing director] of a banking company.
- ❖ As per Section 14 of BR Act, no banking company shall create any charge upon any unpaid capital of the company, and any such charge shall be invalid.
- ❖ As per Section 15 of BR Act, no banking company shall pay any dividend on its shares until all its capitalised expenses have been completely written off.
- ❖ In terms of Section 16 of BR Act (prohibition of common directors) - no banking company incorporated in India shall have as a director in its Board of directors any person who is a director of any other banking company.
- ❖ As per Section 17 of BR Act, every banking company shall create a reserve fund and out of the balance of profit of each year as disclosed in the profit and loss account and before any dividend is declared, transfer to the reserve fund a sum equivalent to not less than 20% of such profit.
- ❖ Section 18 of BR Act deals with Cash reserves to be maintained by Banks.
- ❖ Section 20 of BR Act deals with the Restrictions on loans and advances
- ❖ Section 20 A of BR Act stipulates Section 20A - Restrictions on power to remit debts by Banks.
- ❖ As per Section 20 of BR Act banking company shall not
 - (a) grant any loans or advances on the security of its own shares, or-
 - (b) enter into any commitment for granting any loan or advance to or on behalf of-
 - (i) any of its directors,
 - (ii) any firm in which any of its directors is interested as partner, manager, employee or guarantor.
- ❖ RBI exercise control advances by banking companies as per Section 21 of BR Act.
- ❖ As per Section 21A of BR Act, Rates of interest charged by banking companies not to be subject to scrutiny by Courts.
- ❖ Section 22 of BR Act deals with Licensing of banking companies.
- ❖ As per Section 26 of BR Act, Banks have to submit a Return of unclaimed deposits (accounts which have not been operated upon for ten years, within thirty days after the close of each calendar year.
- ❖ Section 26A of BR Act deals with establishment of Depositor Education and Awareness Fund (DEAF).
- ❖ Section 35 of BR Act empowers RBI to inspect any banking company and its books and accounts.
- ❖ Section 35A of BR Act empowers Reserve Bank to give directions to Banking Companies.
- ❖ Section 44A of BR Act deals with the Procedure for amalgamation of banking companies.
- ❖ Section 44B of BR Act imposes Restriction on compromise or arrangement between banking company and creditors.
- ❖ Section 45 of BR Act deals with the Power of Reserve Bank to apply to Central Government for suspension of business by a banking company and to prepare scheme of reconstitution or amalgamation.

- ❖ Section 45Z of BR Act deals with the Return of paid instruments to customers.
- ❖ Section 45ZA of BR Act deals with Nomination in Deposit Accounts.
- ❖ Section 45ZC of BR Act deals with the Nomination for Safe Custody Articles.
- ❖ Section 49A of BR Act imposes restriction on acceptance of deposits withdrawable by cheque. No person other than a banking company, the Reserve Bank, the State Bank of India or any other banking institution shall accept from the public deposits of money withdraw able by cheque.

This Act shall not apply to:

- ❖ A primary agricultural credit society; or
- ❖ A Co-operative society whose primary object and principal business is providing of long-term finance for agricultural development.

The objectives of the Banking Regulation Act is to:

- ❖ Provide specific legislation to the business of banking in India
- ❖ Prevent bank failures by prescribing minimum capital requirements
- ❖ Ensure balanced development and growth of banking companies
- ❖ Give specific powers to RBI
- ❖ Safeguard the interest of Depositor.

Reserve Bank as Central Bank

The Reserve Bank was constituted under Section 3 of RBI Act. The Central Govt holds the whole capital of RBI.

- ❖ Regulating the issue of bank notes
- ❖ Keeping of reserves for ensuring monetary stability
- ❖ Generally to operate the currency and credit system of the country to its advantage.

Major Powers of RBI in the different roles as regulator and supervisor

- ❖ Power to issue banking licenses
- ❖ Power of appointment and removal of banking boards/personnel
- ❖ Power to regulate the business of banks
- ❖ Power to give directions
- ❖ Power to inspect and supervise banks
- ❖ Power regarding audit of banks
- ❖ Power to collect, collate and furnish credit information
- ❖ Power relating to moratorium, amalgamation and winding up
- ❖ Power to impose penalties

Government as a Regulator of Banks

The Reserve Bank is the primary regulator of banks. But the Central Government has also been conferred extensive powers under the RBI Act and BR Act to regulate banks either directly or indirectly.

The Governor and the members of the Central Board of the RBI are appointed by the Government of India (GOI) who also has powers to remove them. The GOI is the sole shareholder of the RBI.

A few areas where the power lies with the Government to do certain acts to regulate/supervise Banks are as follows:-

- ❖ Appeal against removal of managerial personnel of a Bank exercised by RBI, under Section 10B and 36AA of the Banking Regulation Act.
- ❖ Similarly appeal against, cancellation of banking license (under Section 22) and refusal of certificate regarding floating charge on assets (under Section 14A), may be preferred by the aggrieved banks, with the Government
- ❖ Suspension of operations and exemption from any of the provisions of the BR Act (under Section 4 and 53 respectively of the Act) may be permitted by the GOI on representation/recommendation of the RBI.
- ❖ Under Section 6(1) of the Act the GOI notifies which other business a banking company may engage, in addition to the business of banking.

Control Over Co-operative Banks

- ❖ A co-operative bank is a co-operative society engaged in the business of banking and may be a primary Co-operative bank, a district central Co-operative bank or a State Co-operative bank.
- ❖ With the introduction of Section 56 in the Banking Regulation Act, 1949 with effect from 1965, Co-operative banks came under the regulatory purview of the Reserve Bank. While the formation and management of Co-operative societies operating in one state only are under the control of the State Government while licensing and regulation of banking business rests with the Reserve Bank. Thus, there is a dual control of State Governments and the Reserve Bank over these banks.
- ❖ The Banking Regulation (Amendment) Act 2020 was enacted with effect from 26th June 2020 to give more powers to the RBI to restructure Co-operative Banks,
- ❖ Co-operative Banks have also been permitted to raise capital through public/private issues, preferential shares, debentures etc. The amendments however do not affect the existing powers of the State Registrars of co-operative societies under the State laws.
- ❖ In the case of Co-operative banks which are registered under the Deposit Insurance and Credit Guarantee Corporation Act, the Reserve Bank has the power to order their winding up.

Unit 2 : Control over Organisation of Banks

- ❖ A company wanting to commence banking business requires prior licence from the Reserve Bank.
 - ❖ The Reserve Bank has the discretion to reject licence or approve the licence on such conditions as it thinks fit. Before granting licence, Reserve Bank has to be satisfied by inspection or otherwise of the suitability of the company for licence.
 - ❖ A licence once given may also be cancelled after giving the bank an opportunity to be heard. Further, for opening new branches or shifting branches outside a city, town or village, permission of the Reserve Bank is required.
 - ❖ Banking companies have to have minimum capital and reserves as specified in the Banking Regulation Act. The shareholders of a banking company are entitled to dividends only after all the capitalised expenses are written off.
 - ❖ The commission or brokerage payable on selling shares is restricted to two and half per cent of the paid-up value of the shares.
 - ❖ The board of directors of a bank has to be constituted with persons having special knowledge or experience in accountancy, banking, economics, law, etc., as stipulated. The directors should not have substantial interest in other companies or firms.
 - ❖ The maximum period of office is limited to eight years continuously.
 - ❖ Authorized Capital the maximum limits of share capital which a company is authorised to have under its Memorandum.
 - ❖ Paid-up Capital The amount of share capital of a company is subscribed and paid-up.
 - ❖ Subscribed Capital The amount of share capital of a company, which is issued and subscribed.
 - ❖ The Reserve Bank is empowered to reconstitute the board, if the board is not properly constituted. Every banking company should have a full-time chairman (or a full-time managing director, if there is no fulltime chairman) with the specified qualifications.
 - ❖ The Reserve Bank has powers to remove the chairman and appoint a suitable person in his place in certain cases. The Reserve Bank also has powers to remove the directors or managerial personnel or other employees of banking companies.
 - ❖ The principles of corporate governance including the 'fit and proper' criteria for directors apply to banking companies as well as public sector banks.
 - ❖ A Temporary branch for less than 30 days in a town where a bank has an existing branch does not require permission from RBI.
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Unit 3 : Regulation of Banking Business

- ❖ The Banking Regulation Act empowers the Reserve Bank to issue directions to banking companies in public interest, in the interest of banking policy and in the interest of depositors.
- ❖ **Section 21** provides for the issue of directions to regulate loans and advances by banking companies. This may be done by regulating the purposes of lending, margins in respect of secured loans, rate of interest and terms and conditions of lending.
- ❖ **Section 35A** gives wide general powers to issue directions. The Reserve Bank issues directions from time to time under Section 21 (read with Section 35 A) regulating acceptance of deposits and lending.
- ❖ Under **Section 21A** of the Act, the rate of interest on loans and advances contracted between a bank and its customer is not liable to be reopened by a court of law.
- ❖ **Section 20** of the Act imposes restrictions on loans and advances to directors, and companies and firms in which directors are interested as director, partner, etc.
- ❖ A banking company which is a scheduled bank has to maintain a certain percentage of the time and demand liabilities as cash reserve with the Reserve Bank under Section 42 of the Reserve Bank of India Act, as notified by the Reserve Bank from time to time.
- ❖ Failure to do so renders the banking company liable to penalty. For non-scheduled banking companies, Section 18 of the BR Act provides for cash reserve.
- ❖ Banking companies have also to maintain a certain percentage of their demand and time liabilities in liquid assets as stipulated under **Section 24** of the BR Act. These assets may be maintained to the extent and in the form and manner as notified by the Reserve Bank. Apart from this, banking companies are required to maintain such assets in India at not less than seventy five per cent of demand and time liabilities as at the close of business of the last Friday of every quarter.
- ❖ Banking companies also have to transfer to the reserve fund twenty per cent of their annual profits as disclosed in the profit and loss account.
- ❖ Regulation of credit to different sectors of the economy is known as Selective Credit Control. While General Credit Controls operate on the cost and volume of credit, Selective credit controls aim at regulating the distribution or direction of bank resources to particular sectors of the economy.

Selective Credit Control seeks to influence the demand for credit by

- ❖ Making borrowing costly for certain purposes, which are relatively inessential
- ❖ By imposing stringent conditions on lending for such purposes
- ❖ By giving concessions for certain desired types of activities

The tools employed for exercising selective credit control are

- ❖ Minimum margins for lending against selected commodities
- ❖ Ceiling on the levels of credit

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- ❖ Charging minimum rate of interest on advances against specified commodities Scheduled Banks

A scheduled bank is a bank included in the second schedule of the RBI Act. **Section 42(6)** of the Act. RBI may include any bank in the second schedule if it satisfies the following requirements.

- It has paid-up capital and reserves of an aggregate value of not less than Rs. 5 Lakhs.
- It satisfies the Reserve Bank that its affairs are not conducted in a manner detrimental to the interests of depositors; and
- It is
 - ❖ State cooperative Bank
 - ❖ A company defined in section 3 of the companies act
 - ❖ An institution notified by central govt

Cash Reserve : The penalty which is payable by a banking company which is scheduled bank for failure to maintain cash reserve in any week for the first time is 3% of over bank rate. For 2nd time 5% over bank rate.

Unit 4 : Returns, Inspection, Winding Up, Mergers & Acquisitions

- ❖ Every banking company has to prepare its balance sheet and profit and loss account annually as at the end of the calendar year or at the end of twelve months as on a date notified by the Central Government.
- ❖ The accounts have to be audited by auditors duly qualified to be auditors of companies.
- ❖ Three copies of the balance sheet, profit and loss account and the auditor's report have to be submitted as returns to the Reserve Bank and to the Registrar of Companies.
- ❖ Banking companies have also to furnish other returns like return on maintenance of cash reserve, maintenance of liquid assets, etc.
- ❖ The Reserve Bank is authorised to inspect or conduct, scrutiny of banking companies, their books and accounts.
- ❖ The Board for Financial Supervision set up by the Reserve Bank by statutory regulations framed under the Reserve Bank of India Act supervises the affairs of banking companies.
- ❖ The Government may acquire the undertakings of banking companies in certain circumstances based on a report from the Reserve Bank.
- ❖ The Central Government may also order moratorium on banking companies on the application of the Reserve Bank. During moratorium, the Reserve Bank may prepare a scheme for amalgamation, which may be sanctioned by the Central Government. Such an amalgamation scheme will have overriding effect on any laws, agreements, etc.
- ❖ The Reserve Bank may also apply to the High Court for winding up of a banking company when it is not able to pay its debts and also in certain other circumstances.
- ❖ The Reserve Bank of India Act and the Banking Regulation Act impose certain penalties for contravention or default committed by banking companies or other persons.

Board for Financial Supervision

- ❖ It is constituted by RBI. The board consists of Chairman (Governor of RBI), Vice Chairman (one of the Dy. Governor of RBI), Four directors from the Central Board. The board performs functions and exercises the powers of supervision and inspection under the RBI Act and the BR Act.
 - ❖ The board meets at least once in a month. Three members of whom one Chairman / vice-chairman shall form a quorum for the meeting.
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Unit 5: Public Sector Banks, Private Sector Banks, Regional Rural Banks, Differentiated Banks, Co-operative Banks and Local Area Banks

The public sector banks are statutory corporations (or body corporate) established under special statutes.

The State Bank of India and the Nationalised banks also act as agents of the Reserve Bank to transact the banking business of the Central Government.

State Bank of India

- State Bank of India was established under Section 3 of the State Bank of India Act, 1955 for taking over the undertaking of the Imperial Bank and to carry on the business of banking.
- State Bank has its corporate centre in Mumbai and local head offices at Mumbai, Kolkata, Chennai and other places as decided by Central Government in consultation with the Central Board of the State Bank. The Central Government can give directions to the bank on matters of policy involving public interest in consultation with the Governor of the Reserve Bank and the Chairman of State Bank.
- The Board shall consist of Chairman, not more than four Managing Directors appointed by the Central Government and other directors.
- The Chairman and Managing Directors are appointed for a period not exceeding five years and are eligible for reappointment. Their services can be terminated by the Central Government by giving a three months' notice after consultation with the Reserve Bank.
- The State Bank shall act as an agent of the Reserve Bank at the places where it has a branch and where Reserve Bank has no branch, if so required, by the Reserve Bank, for transacting Government business and other business entrusted to it by the Reserve Bank.
- The State Bank has to close its books and balance accounts each year as on 31 March or such other date as may be specified by the Central Government. Within three months of the closing date, it has to furnish to the Central Government and the Reserve Bank its balance sheet and profit and loss account together with auditors' report and a report by the Central Board on the working and activities of the bank.
- All the five subsidiaries along with Bharatiya Mahila Bank have been merged with SBI w.e.f. 1st April 2017.

Regional Rural Banks

- The Regional Rural Banks (RRBs) are public sector institutions, regionally based, rural oriented and engaged in commercial banking. They were first set up in 1975 under the Regional Rural Banks Ordinance, 1975. The ordinance was later replaced by the Regional Rural Banks Act, 1976.
- 'Sponsor Bank' is a bank by which a regional rural bank is sponsored and it holds 35 per cent of the issued capital of the RRB, while the Central Government holds 50 per cent and the State Government holds the remaining fifteen per cent of the issued capital.

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- The board consists of a chairman appointed by the sponsor bank from among its officers in consultation with NABARD, or otherwise in consultation with the Central Government.
 - Regional rural banks may transact the business of banking as defined in Section 5(b) of the Banking Regulation Act and any other business permissible for a bank to undertake under Section 6(1) of that Act.
 - Every RRB has to close and balance its accounts as on 31 March or such other date as the Central Government may specify. The auditors have to be appointed with the approval of the Central Government.
 - There are presently 43 RRBs and there are further plans to amalgamate RRBs, in a road map prepared in consultation with NABARD, to bring down the number of RRBs pan India. The amalgamations have been/is being carried out with a view to enable the RRBs to minimize their overhead expenses, optimize the use of technology, enhance the capital base and area of operation and increase their exposure.

Other Public Sector Banks

- The other public Sector Banks (apart from SBI) are called Nationalized Banks since they came into being consequent to the enactment of the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1970 and Banking Companies (Acquisition and Transfer of Undertakings) Act, 1980 also called the "Bank Nationalization Acts".
- As per the statute the Central Government is required to hold, at all times, not less than fifty one per cent of the equity of these banks. No equity shareholder other than the Central Government can exercise voting rights in excess of one per cent of the total voting rights of all the shareholders.
- The Board in a nationalized Bank consists of directors who could either be nominated/ appointed by the Government of India or elected from among the shareholders.
- Meetings of the Board shall ordinarily be held at least six times in a year and at least once in each quarter. The quorum of a meeting of the Board shall be one- third of the number of directors holding office as such directors of the Board on the day of the meeting.
- The Board in a nationalized Bank consists of directors who could either be nominated/ appointed by the Government of India or elected from among the shareholders. Not more than four* other whole-time directors (Executive Directors), (*increased from 3 to 4 by GOI in August 2019)

Nationalised Banks

The Bank Nationalisation Act 1970 and Banking companies (Acquisition and Transfer of Undertaking) Act 1980. Transferred the undertaking of existing private banks to the corresponding new banks popularly known as Nationalised banks.

Paid-up Capital – Originally entire Paidup Capital was held by Central govt., some of these banks have recently made public issue of shares, but the Central Govt. still holds majority of shares in all these banks. The Shares other than those held by the Central Govt. are freely transferrable.

Disinvestment of Shares by Government

Merger of Nationalized banks:

The government in August 2019 unveiled a mega plan to merge 10 public sector banks into four as part of plans to create fewer and stronger global-sized lenders as it looks to boost economic growth from a six-year low. These mergers have been driven mainly by the following factors:

- ❖ The low level of capital, which has led to frequent requests for capitalization
- ❖ The high level of NPAs prevailing
- ❖ The poor profitability for the entire sector
- ❖ The low growth rate for the entire sector

The mega merger of the following PSBs have come into force with effect from 1st April 2020

- ❖ Oriental Bank of Commerce (OBC) and United Bank of India merged into Punjab National Bank (PNB)
- ❖ Syndicate Bank merged into Canara Bank.
- ❖ Allahabad Bank merged with Indian Bank.
- ❖ Andhra Bank and Corporation Bank merged with Union Bank of India
- ❖ Vijaya Bank and Dena Bank merged with Bank of Baroda

After the merger, there are 12 PSBs. There is now a move in the Government of India, to privatize certain Public Sector Banks.

Co-operative Banks

- ❖ Co-operative banks are registered either under the State laws governing co-operatives or under the multi-state Co-operative Societies Act. If a co-operative bank operates only in one state, the State law applies and in the case of co-operative banks operating in more than one state, the Central Act applies.
- ❖ The Banking Regulation Act is applicable to co-operative societies subject to the modifications stipulated in Part V (Section 56) of the Act.
- ❖ A primary cooperative bank is a co-operative society other than a primary agricultural credit society, which satisfies the following criteria
 - The primary object or principal business is the transaction of banking business.
 - The paid-up share capital and reserves are not less than Rs. 1 lakh.
 - The byelaws do not permit admission of any other co-operative society as a member
- ❖ A state co-operative bank is the principal co-operative society in a state with the primary objective of financing other societies.
- ❖ A central co-operative bank is the principal co-operative society in a district with the primary objective of funding other co-operative societies in the district.

Loans And Advances:

Section 20 of the Banking Regulation Act lays down certain restrictions on loans and advances by co-operative banks. Co-operative bank shall not grant loans and advances as under:

- ❖ Loans and advances on the security of its own shares
- ❖ Unsecured loans or advances to any of its directors.
- ❖ Unsecured loans or advances to firms or private companies in which any of its directors are interested as partner, managing agent or guarantor

License:

- Every co-operative society requires a licence from the Reserve Bank under Section 22 of the Banking Regulation Act (as applicable to co-operative societies) to carry on banking business in India. However, primary credit societies are exempt from the requirement.

Liquid Assets:

- ❖ Co-operative banks have to maintain liquid assets as provided in Section 24(1) of the Banking Regulation Act
- ❖ In the case of state co-operative banks, which are scheduled banks, the balances required under Section 42 of the RBI Act will also be accounted.
- ❖ In the case of the Central co-operative banks, balances maintained with the state co-operative bank concerned and in the case of primary co-operative banks the balances maintained with Central co-operative banks or the state co-operative bank concerned shall be accounted.
- ❖ The co-operative banks have also to maintain as specified in Section 24(2A) liquid assets being not less than 25 per cent or such other percentage not exceeding forty per cent as the Reserve Bank may stipulate.
- ❖ Co-operative banks other than scheduled Co-operative Banks and scheduled state co-operative banks have to maintain in India by way of cash reserve with itself or by way of balance in current account with the Reserve Bank or the state co-operative bank of the state concerned or district Co-operative Bank a sum equivalent to at least three per cent of its total demand and time liabilities in India.

Accounts and Audit:

- ❖ Every co-operative bank has to prepare a balance sheet and profit and loss account of its business as on the last working day of the year. Three copies of such balance sheet and accounts, along with statutory auditor's report have to be submitted to the Reserve Bank within six months.
- ❖ A state co-operative bank and a central co-operative bank have to submit such return to NABARD also.

Inspection:

- ❖ The provisions of Section 35 relating to inspection are applicable to co-operative banks with minor modifications.
- ❖ It is also open to Reserve Bank to call for inspection of a primary cooperative bank by one or more officers of the state co-operative bank in the State where the primary co-operative bank is registered.
- ❖ The Reserve Bank may supply a copy of the report of any inspection or scrutiny to the state co-operative bank or the Registrar of Co-operative Societies concerned.

Registration with DICGC:

The Deposit Insurance and Credit Guarantee Corporation Act, 1961, which provides for insuring deposits of banks, is applicable to co-operative banks also. Accordingly, under Section 13C of the Act, co-operative banks have to be registered with the corporation for this purpose. The registration of a co-operative bank may be cancelled if:

- ❖ it is prohibited from accepting deposits
- ❖ its licence is cancelled
- ❖ it has been ordered to be wound up
- ❖ it has ceased to be a co-operative bank under the sub-Section (2) of Section 36A of the BR Act
- ❖ it has converted into a non-banking co-operative society
- ❖ it has been amalgamated with any other co-operative society

The Banking Regulation (Amendment) Act 2020

The salient details of the changes brought about by this amendment were inter-alia as follows:

- ❖ It allowed the RBI to initiate a scheme for reconstruction or amalgamation of a bank (including a Cooperative Bank) (Section 45)
- ❖ Where the Central Bank imposes a moratorium on a Bank, it thereafter cannot grant any loans or make investments in any credit instruments during the tenure of the moratorium.
- ❖ Co-operative banks may issue equity, preference, or special shares on face value or at a premium to its members, or other persons residing within their area of operations. They may also issue unsecured debentures or bonds or similar securities with maturity of ten or more years to such persons. However, a prior approval from RBI is mandatorily required for such issuance.
- ❖ No person will be entitled to demand payment towards surrender of shares issued to him by a cooperative bank.
- ❖ RBI has been given powers as per the amendment to supersede the board of directors of a multistate co-operative bank for up to five years under certain conditions which includes cases where it is in the public interest and to protect depositors.

Private Sector Banks

- ❖ The Private Sector Banks are those Banks where the majority stake, in all cases, is held by private entities/individuals. These Banks are mostly incorporated under the Companies Act 1956 and are also bound by the other statutes such as the Banking Regulation Act 1949, RBI Act 1934 etc.
- ❖ In India, private sector banks are classified into two categories. These are those called “Old Private Sector Banks” which came into existence before 1968 and “New Private Sector Banks that were incorporated after the 1990s.
- ❖ As of now there are 21 private sector banks in the country.

Payment Banks

RBI, based on the recommendations of the Nachiket Mor Committee (2013) issued the key features of the Payments Banks guidelines.

Eligible Promoters:

- Existing non-bank Pre-paid Payment Instrument (PPI) issuers; and other entities such as individuals/ professionals, NBFC, BCs, mobile telephone companies, super-market chains, companies, real sector cooperatives; that are owned and controlled by residents; and public sector entities may apply to set up payments banks.

Local Area Banks (LAB)

It was in the year 1996 that a decision was taken to allow the establishment of Local Area Banks in the private sector.

- ❖ **Area of operation:** The area of operation of an LAB is usually restricted to a maximum of three geographically contiguous districts. The activities of an LAB are also focused on local customers predominantly in rural and semi-urban areas so as to bridge the credit gap in these areas.
- ❖ **Scope of activities:** LABs are normally required to finance agriculture and allied activities, MSME, agro-industrial activities, trading activities and non-farm sector.
- ❖ **Registration/Licensing:** Such banks are registered as a public limited company under the Companies Act, 1956/ the Companies Act, 2013/partnership firms under The Partnership Act, 1932. Those are licensed under the Banking Regulation Act, 1949 and may be included in the Second Schedule of the Reserve Bank of India Act, 1934.
- ❖ **Supervision over LABs:** Supervision over LABs lies with the relevant department of the RBI. Thus they have accounting policies, prudential norms, and other policies as laid down by the RBI.
- ❖ **Branches:** Normally, at the time of granting a license, a LAB is granted permission to open a branch in a single urban center in each district and the remaining branches are to be opened in rural and semi-urban centers.
- ❖ RBI approved established of only 10 Local Area Banks but out of them only 2 (January 2022) are in existence today functioning as Non-Scheduled Banks. They are Coastal Local Area Bank Ltd and Krishna Bhima Samruddhi Local Area Bank Ltd.

Unit 6 : Non - Banking Financial Companies (NBFCs)

Non Banking Finance Companies (NBFCs)

A Non-Banking Financial Company (NBFC) is a company registered under the Companies Act, 1956.

It is engaged in the business of -

- Loans and advances
- Acquisition of shares/ stocks/ bonds/ debentures/ securities issued by Government or local authority
- Leasing, hire purchase, insurance business, chit business etc.

NBFC does not include any institution whose principal business is that of agriculture activity, industrial activity, purchase or sale of any goods (other than securities) or providing any services and sale/ purchase/ construction of immovable property.

- The Department of Non-Banking Supervision (DNBS) of RBI is entrusted with the responsibility of regulation and supervision of NBFCs.
- NBFC-MFIs provide access to basic financial services such as loans, savings, money transfer services, micro-insurance etc. to poor people and attempt to fill the void left between the mainstream commercial banks and money lenders.
- NBFCs' role in financial inclusion indicate the fact that they have been game changers in certain areas like financial inclusion especially micro finance, affordable housing, second-hand vehicle finance, gold loans and infrastructure finance.

NBFCs aid economic development in the following ways

- Mobilization of Resources - It converts savings into investments
- Capital Formation - Aids to increase capital stock of a company
- Provision of Long-term Credit and specialized Credit
- Aid in Employment Generation
- Help in development of Financial Markets
- Helps in Attracting Foreign Grants
- Helps in Breaking Vicious Circle of Poverty by serving as government's instrument.

Registration

- In terms of Section 45-IA of the RBI Act, 1934, it is mandatory that every NBFC should be registered with RBI to commence or carry on any business of non- banking financial institution.
- RBI to obviate dual regulation, certain categories of NBFCs which are regulated by other regulators are exempted from the requirement of registration with RBI viz. Venture Capital Fund/Merchant Banking companies registered with SEBI, Insurance Company holding a valid Certificate of Registration issued by IRDA, Nidhi companies as notified under Section 620A of the Companies Act, 1956, Chit companies as defined in clause (b) of Section 2 of the Chit

Funds Act, 1982, Housing Finance Companies regulated by National Housing Bank, or a Mutual Benefit company.

Applicable NBFCs

- Systemically Important Non-Deposit taking Non-Banking Financial Company (NBFC-ND-SI) registered with the Bank.
- Deposit taking Non-Banking Financial Company (NBFC-D)
- NBFC–Factor registered with the RBI under section 3 of the Factoring Regulation Act, 2011 and having an asset size of Rs. 500 crore and above
- Infrastructure Debt Fund – NBFC (IDF-NBFC) [Net Owned Fund of Rs. 300 crore or more and which invests only in Public Private Partnerships (PPP)]

NBFC– Micro Finance Institution (NBFC-MFI) registered with the RBI and having an asset size of Rs. 500 crore and –

- Minimum Net Owned Funds of Rs. 5 crore.
- Not less than 75 per cent of its total assets are in the nature of “microfinance loans”.

NBFC- Infrastructure Finance Company (NBFCIFC) registered with the RBI and having an asset size of Rs. 500 crore and above and which fulfills the requirements as-

- A minimum of 75 per cent of its total assets deployed in “infrastructure loans”;
- Net owned funds of Rs. 300 crore or above;

Net Owned Funds and Capital Requirement

- Reserve Bank has specified two hundred lakh rupees (Rs. two crore) as the net owned fund (NOF) required for a non-banking financial company to commence or carry on the business of non-banking financial institution, except wherever otherwise a specific requirement as to NOF is prescribed by the RBI.
- Every applicable NBFC shall maintain a minimum capital ratio consisting of Tier I and Tier II capital which shall not be less than 15 per cent.
- The Tier I capital in respect of applicable NBFCs at any point of time, shall not be less than 10 per cent.
- NBFCs primarily engaged in lending against gold jewellery (such loans comprising 50 per cent or more of their financial assets) shall maintain a minimum Tier I capital of 12 per cent.

Revised Scale Based Regulatory Structure

The NBFCs have been divided into 4 layers based on their size, activity, and perceived riskiness namely

- Base Layer
- Middle Layer
- Upper Layer

➤ Top Layer

Base Layer (BL): The Base Layer would comprise of –
Non-deposit taking NBFCs below the asset size of Rs. 1000 crore and

NBFCs undertaking the following activities-

- NBFC-Peer to Peer Lending Platform (NBFC-P2P),
- NBFC-Account Aggregator (NBFC-AA),
- Non-Operative Financial Holding Company (NOFHC) and
- NBFCs not availing public funds and not having any customer interface

Middle Layer (ML): The Middle Layer would consist of

- All deposit taking NBFCs (NBFC-Ds), irrespective of asset size
- Non-deposit taking NBFCs with asset size of Rs. 1000 crore and above and

NBFCs undertaking the following activities

- Standalone Primary Dealers (SPDs),
- Infrastructure Debt Fund - Non-Banking Financial Companies (IDF-NBFCs),
- Core Investment Companies (CICs),
- Housing Finance Companies (HFCs) and
- Infrastructure Finance Companies (NBFC-IFCs).

Upper Layer (UL):

The Upper Layer would comprise of those NBFCs which are specifically identified by the RBI as warranting enhanced regulatory requirement based on a set of parameters and scoring methodology as devised by them.

Top Layer (TL):

The Top Layer would ideally remain empty and may be populated if the RBI is of the opinion that there is a substantial increase in the potential systemic risk from specific NBFCs in the Upper Layer.

Regulatory Norms

Provisioning for Standard assets:

The RBI has w. e. f. 01-10 2022 decided that NBFCs classified as NBFC-UL shall maintain provisions in respect of 'standard' assets at the following rates for the funded amount outstanding:

NPA Classification:

The extant NPA classification norm stands changed to the overdue period of more than 90 days for all categories of NBFCs. A glide path is provided to NBFCs in Base Layer to adhere to the 90 days NPA norm.

Ceiling on IPO Funding:

There shall be a ceiling of Rs. 1 crore per borrower for financing subscription to Initial Public Offer (IPO).

Prudential Guideline

- Concentration of credit/ investment – The extant credit concentration limits prescribed for NBFCs separately for lending and investments shall be merged into a single exposure limit of 25% for single borrower/ party and 40% for single group of borrowers/ parties.
- An applicable NBFC may exceed the concentration of credit/investment norms, by 5 per cent for any single party and by 10 per cent for a single group of parties, if the additional exposure is on account of infrastructure loan and/ or investment.

Infrastructure Finance Companies may exceed the concentration of credit norms

- In lending to:
 - ❖ Any single borrower: by ten per cent of its owned fund; and
 - ❖ Any single group of borrowers: by fifteen per cent of its owned fund;
- In lending to and investing in:
 - ❖ A single party: by five percent of its owned fund; and
 - ❖ A single group of parties: by ten percent of its owned fund.

Corporate Guidelines

- Risk Management Committee – In order that the Board is able to focus on risk management, NBFCs are required to constitute a Risk Management Committee (RMC) either at the Board or executive level. The RMC would be responsible for evaluating the overall risks faced by the NBFC including liquidity risk and will report to the Board.
- Loans to directors, senior officers and relatives of directors – NBFC-BL are required to have a Board approved policy on grant of loans to directors, senior officers and relatives of directors and to entities where directors or their relatives have major shareholding.
- Chief Compliance Officer – In order to ensure an effective compliance culture, it is necessary to have an independent compliance function and a strong compliance risk management framework in NBFCs.
- Core Banking Solution – NBFCs with 10 and more branches are mandated to adopt Core Banking Solution.

NBFC Activities Not Eligible for Bank Finance

- Bills discounted/ rediscounted by NBFCs.
- Investments of NBFCs both of current and long-term nature, in any company/entity by way of shares, debentures
- Unsecured loans/ inter-corporate deposits by NBFCs to/ in any company.
- All types of loans and advances by NBFCs to their subsidiaries, group companies/ entities.

-
- Finance to NBFCs for further lending to individuals for subscribing to IPOs and for purchase of shares from secondary market.
 - Shares and debentures cannot be accepted as collateral securities for secured loans to NBFC.

Co-lending Model Between Banks and NBFCs

- The banks and NBFCs shall formulate Board approved policies for entering into the Co-Lending Model (CLM) and place the Board approved policies on their websites.
 - Banks are permitted to co-lend with all registered NBFCs (including HFCs) based on a prior agreement. Co-lending banks will take their share of the individual loans on a back-to-back basis in their books. NBFCs shall be required to retain a minimum of 20% share of the individual loans on their books.
 - Banks shall not be allowed to enter into co-lending arrangement with an NBFC belonging to the promoter Group.
-

Unit 7 : Financial Sector Legislative Reforms & Financial Stability and Development Council

Narasimham Committee

Narasimham Committee 1 (1991)

- ❖ The Committee was set up in August 1991, to examine all aspects relating to the 'Structure, Organization, Functions and Procedures' of the financial system. It was also called the 'Committee on Financial Systems'.
- ❖ High CRR & SLR: The Committee found that the CRR and SLR required to be kept by Banks was very high (aggregating to 53.5% at that time) that led to a continuous loss in potential income to banks, which in turn adversely affected their profitability. The Committee termed the high SLR/SLR as a 'Tax on the Banking System' and recommended its lowering.
- ❖ Directed Credit Program: The Committee was generally critical of the directed lending to priority sector and felt that this resulted in overlooking of the qualitative aspects of credit and deterioration in the quality of the loan portfolio besides no proper appraisal of credit applications, no insistence on collateral and very weak post credit supervision and monitoring.
- ❖ Interest subsidy: The Committee was of the view that interest subsidy being offered in various schemes, especially government sponsored ones, was loss of precious profits for the Banks and that timely credit was more important than this charging of subsidized interest.
- ❖ Other findings: The Committee also brought to focus the other factors plaguing the PSBs some of which have been brought out below –
 - Opening of large number of branches without considering in many cases need and potential viability.
 - The lines of command and control had stretched too far and central office supervision, internal inspection and audit weakened.
 - Deterioration in staff quality due to rapid recruitment and promotion without proper training and experience.
 - Excessive bank credit to agriculture and small industry, where the unit cost of administering the loans tend to be high, increasing staff requirements/ staff costs and impacting profitability.

Narasimham Committee 2 (1998)

The Narasimham Committee 2 was termed "Committee on Banking Sector Reforms" and set up in December 1997 to review the progress of implementation of financial sector reforms recommended by the Committee on Financial Systems (CFS) (1991).

The major recommendations of the Committee were those regarding

- ❖ Strengthening of the 'Banking System' in India (Capital Adequacy measures/concept of Risk Weights)
- ❖ Introduction of stringent 'Asset Quality' norm

- ❖ Interest subsidy for priority sector to be eliminate
- ❖ Introduced concept of Asset Reconstruction Companies (ARCs) etc.
- ❖ Need for strict implementation of IRAC norms and Disclosure requirements, changes in systems and procedures etc.

Banking Sector Reforms

Competition enhancing measures

- ❖ Granting of operational autonomy to public sector banks, reduction of public ownership in public sector banks by allowing them to raise capital from equity market up to 49 per cent of paid-up capital.
- ❖ Transparent norms for entry of Indian private sector, foreign and joint-venture banks and insurance companies, permission for foreign investment in the financial sector in the form of Foreign Direct Investment (FDI) as well as portfolio investment.
- ❖ Roadmap for presence of foreign banks and guidelines for mergers and amalgamation of private sector banks and NBFCs.
- ❖ Foreign banks being permitted to operate in India through any one of three channels.
- ❖ Licensing of banks in the private sector/part divestment in PSBs: The RBI has also more recently given an impetus and encouraged setting up for differentiated banks/small finance banks etc.
- ❖ After nationalization of 14 large banks in 1969 and the onset of globalization and liberalization in 1991, it was recognized that there is urgent need for introducing greater competition in the Indian money market which could lead to higher efficiency of the financial system.
- ❖ Migration to CBS
- ❖ Introducing VRS (year 2001), etc.

Resultantly by the year 2008, banks' balance sheets were much stronger/growth was strong/ NPAs had come down from the peak of around 12% to slightly over 2%.

Measures enhancing role of market forces

- ❖ Market determined pricing for government securities, disbanding of administered interest rates.
- ❖ Introduction of pure inter-bank call money market, auction-based repos, reverse- repos for short term liquidity management, facilitation of improved payments and settlement mechanism.
- ❖ Significant advancement in dematerialization and markets for securitized assets.
- ❖ More recent RBI introduction of the 'Targeted Long Term Repo Operations
- ❖ Scheme' whereby Banks are allowed to borrow, on tap, at Repo Rates for periods up to 3 years for investing in specific assets/sectors, thereby infusing liquidity in the market.

Prudential Measures

- ❖ The Statutory Liquidity Ratio (SLR) which was 38.5 per cent in 1991-1992 was brought down to some 28 per cent in five years. Similarly, the CRR brought down from 14 per cent to 10 per cent by 1997. This has been further reduced to SLR - 18% and CRR 4.50% currently (November 2022). The Capital to Risk Weighted Assets Ratio (CRAR) of scheduled commercial banks (SCBs),

introduced in 1992, stood at 14.2 per cent as of March 2019 remained well above the regulatory requirement of 9.0%

- ❖ Measures to strengthen risk management through recognition of different components of risk, assignment of risk-weights to various asset classes and connected norms.
- ❖ Lending, risk concentration, application of marked-to-market principle for investment portfolio and limits on deployment of fund in sensitive activities started.
- ❖ 'Know Your Customer' and 'Anti Money Laundering' guidelines, introduction of Basel II/III guidelines, introduction of capital charge for market risk, higher graded provisioning for NPAs.
- ❖ The RBI introduced, in a phased manner, prudential norms for income
- ❖ recognition, asset classification and provisioning for the advances portfolio of the banks so as to move towards greater consistency and transparency in the published accounts.
- ❖ Deregulation of credit processes and interest rate structures: The structure of administered rates have been almost totally done away with in a phased manner under reform

Institutional and legal measures

- ❖ Setting up of Lok Adalats (people's courts), debt recovery tribunals, asset reconstruction companies, settlement advisory committees, etc. for quicker recovery/ restructuring.
- ❖ Promulgation of Securitization and Reconstruction of Financial Assets and Enforcement of Securities Interest (SARFAESI) Act, 2002
- ❖ Setting up of Credit Information Bureau of India Limited (CIBIL) for information sharing on defaulters as also other borrowers.
- ❖ Setting up of Clearing Corporation of India Limited (CCIL) to act as central counter party for facilitating payments and settlement system.
- ❖ Enacted the Insolvency and Bankruptcy Code in 2016 to amend the laws relating to reorganization and insolvency resolution of corporate persons, partnership firms and individuals in a time bound manner.

Supervisory measures

- ❖ Establishment of the Board for Financial Supervision as the apex supervisory authority for commercial banks, financial institutions and NBFCs.
- ❖ Introduction of CAMELS supervisory rating system, move towards risk-based supervision.
- ❖ Strengthening corporate governance, enhanced due diligence on important shareholders, fit and proper tests for directors, etc. introduced.
- ❖ The Government of India introduced the 'Enhanced Access & Service Excellence'.1 (EASE) in January 2018 which represented a comprehensive reforms agenda required to be put in place in a time bound manner by PSBs thereby institutionalizing clean and smart banking.

Technology Related measures

- ❖ Setting up of INFINET as the communication backbone for the financial sector, introduction of Negotiated Dealing System (NDS) for screen-based trading in government securities

- ❖ Promulgation of Payment & Settlement System Act, 2007
- ❖ Introduction of RTGS, NEFT, ECS, ATMs, Mobile Banking, Internet Banking, E-commerce, "Immediate Payment Service (IMPS), Unified Payments Interface (UPI), etc.
- ❖ Many Banks, have since 2020, also embraced enthusiastically the use of new age technologies such as Artificial Intelligence, Machine Learning, Robotics and Digital Banking.
- ❖ Banks are also increasingly getting into tie ups with Fintech companies to expedite their digital transformation.
- ❖ The use of blockchain technology/AI /ML etc.

Reforms In Monetary Policy

- ❖ Emphasis has been put on development of multiple instruments to transmit liquidity and interest rate signals in the short-term in a flexible and bi-directional manner.
- ❖ Move from direct instruments (such as, administered interest rates, reserve requirements, selective credit control) to indirect instruments (such as, open
- ❖ market operations, purchase and repurchase of government securities) for the conduct of monetary policy.
- ❖ LAF has emerged as the tool for both liquidity management and also as a signaling device for interest rate in the overnight market. RBI has introduced Standing Deposit facility (SDF) which is the floor limit of the Policy corridor.
- ❖ Use of open market operations (OMO) to deal with overall market liquidity situation especially those emanating from capital flows; Introduction of Market Stabilization Scheme (MSS) as an additional instrument to deal with enduring capital inflows without affecting short-term liquidity management role of LAF, etc.

Reforms In Financial Markets

- ❖ Repos/CBLO: With steps towards making call market a pure inter-bank market, turnover progressively switched from call money market to repo and CBLO market as daily average volumes in call market got Substantially reduced. Volumes in case of market repo and CBLO, on the other hand, rose manifold.
- ❖ Government Securities Market: As a part of reforms, concessionary financing was eliminated with introduction of market auction system and phasing out of automatic monetisation with Ways and Means Advances (WMA).
- ❖ Capital Market: Primary market witnessed a significant movement away from Controller of Capital Issues (CCI) regime imposing primary issuance at sub-market rates to free pricing and book-building system along with mandatory disclosures as prescribed by SEBI. In the secondary market, corporatization of exchanges, screen-based trading replacing open outcry system, introduction of options and futures replacing erstwhile Badla System.

Financial Sector Development Council

- ❖ Financial Sector Development Council (FSDC) was constituted in Dec. 2010.

- ❖ The primary objective of FSDC is to strengthen and institutionalize the mechanism for maintaining financial stability, promoting financial sector development and enhancing internal regulatory coordination. There should be coordination among these financial sector regulators to ensure better efficiency as well as for avoiding overlapping of functions.
- ❖ Government of India set up Financial Stability and Development Council (FSDC) in December 2010 with the Finance Minister as the Chairman. It is not a statutory body.

Composition of FSDC

The Chairman of the Council is the Finance Minister and its members include:

- ❖ Heads of financial sector Regulators (RBI, SEBI, IRDAI, & PFRDA)
- ❖ Finance Secretary and/or Secretary
- ❖ Secretaries from Department of Economic Affairs (DEA), Department of Financial Services (DFS), Revenue Department and Ministry of Information Technology (MeitY)
- ❖ Chairman of the Insolvency and Bankruptcy Board of India (IBBI)
- ❖ Chief Economic Adviser.

Function Of The FSDC

The functions of FSDC include:

- ❖ To strengthen and institutionalize the mechanism for maintaining financial stability and development;
- ❖ Monitoring of macro-prudential supervision of the economy including the functions of large financial conglomerates;
- ❖ To enhance inter-regulatory coordination;
- ❖ Focus on financial literacy and financial inclusion.

Wings of FSDC

- ❖ FSDC Sub-Committee
- ❖ Inter regulatory technical group (IR – TG)
- ❖ Inter Regulatory Forum for monitoring Financial Conglomerates (IRF-FC)
- ❖ Working Group on resolution regime for financial institutions
- ❖ Macro Financial Monitoring Group (MFMG)
- ❖ Early Warning Group

MODULE B : IMPORTANT ACTS/LAWS & LEGAL ASPECTS OF BANKING OPERATIONS – PART A

Unit 8 : The Prevention of Money Laundering Act, 2002

Offence of Money Laundering

The Prevention of Money Laundering Act, 2002 was enacted to prevent money laundering and to provide for the confiscation of property derived from, or involved in, money laundering.

A person shall be guilty of offence of money-laundering if such person is found to have directly or indirectly attempted to indulge or knowingly assisted or knowingly is a party or is actually involved in one or more of the following processes or activities connected with proceeds of crime:

- ❖ Concealment
- ❖ Possession
- ❖ Acquisition
- ❖ Use
- ❖ Projecting as untainted property
- ❖ Claiming as untainted property

Punishment For Money Laundering

In terms of Section 4 of the Act “Whoever commits the offence of money-laundering shall be punishable with

- ❖ Rigorous imprisonment for a term which shall not be less than three years but
- ❖ Which may extend to seven years and
- ❖ Shall also be liable to fine.

Obligations of Banking Companies, Financial Institutions and Intermediaries

- ❖ Maintenance of Records
- ❖ Every information maintained, furnished or verified, shall be kept confidential.
- ❖ The records referred to in clause (a) of sub-section (1) shall be maintained for a period of five years from the date of transaction between a client and the reporting entity.
- ❖ The records referred to in clause (c) of sub-section (1) shall be maintained for a period of five years after the business relationship between a client and the reporting entity has ended or the account has been closed, whichever is later.
- ❖ The Central Government may, by notification, exempt any reporting entity or class of reporting entities from any obligation under this Chapter.

Enhanced Due Diligence

According to Section 12AA “(1) Every reporting entity shall, prior to the commencement of each specified transaction,—

- ❖ Verify the identity of the clients undertaking such specified transaction by authentication under the Aadhaar Act, 2016.
- ❖ Where the client fails to fulfill the conditions laid down under sub-section (1), the reporting entity shall not allow the specified transaction to be carried out.
- ❖ Where any specified transaction or series of specified transactions undertaken by a client is considered suspicious or likely to involve proceeds of crime, the reporting entity shall increase the future monitoring of the business relationship with the client, including greater scrutiny or transactions.
- ❖ The information obtained while applying the enhanced due diligence measures under sub-section (1) shall be maintained for a period of five years from the date of transaction between a client and the reporting entity.

Records To Be Maintained

In terms of Rule 3, Every reporting entity shall maintain the record of all transactions including, the record of—

- ❖ All cash transactions of the value of more than ten lakh rupees or its equivalent in foreign currency
- ❖ All series of cash transactions integrally connected to each other which have been individually valued below rupees ten lakh or its equivalent in foreign currency where such series of transactions have taken place within a month and the monthly aggregate exceeds an amount of ten lakh rupees or its equivalent in foreign currency.
- ❖ All transactions involving receipts by non-profit organizations of value more than rupees ten lakh, or its equivalent in foreign currency.
- ❖ All cash transactions where forged or counterfeit currency notes or bank notes have been used as genuine or where any forgery of a valuable security or a document has taken place facilitating the transactions.
- ❖ All suspicious transactions whether or not made in cash.
- ❖ All cross border wire transfers of the value of more than five lakh rupees or its equivalent in foreign currency where either the origin or destination of fund is in India
- ❖ All purchase and sale by any person of immovable property valued at fifty lakh rupees or more that is registered by the reporting entity.

Note: As per Rule 4 of the Rules: The records shall contain all necessary information specified by the Regulator to permit reconstruction of individual transaction, including:

- ❖ The nature of the transactions;
- ❖ The amount of the transaction and the currency in which it was denominated;
- ❖ The date on which the transaction was conducted; and
- ❖ The parties to the transaction.

Procedure for Maintaining and Furnishing Information to the Director

As per the requirements of Rule 6 the information as to the transactions should be maintained in hard and soft copies in accordance with the procedure and manner as may be specified by the RBI or SEBI.

As per Rule 8

- ❖ The Principal Officer of a reporting entity shall furnish the information in respect of transactions referred to in clauses (A), (B),(BA),(C) and (E) of sub-rule (1) of rule 3 every month to the Director by the 15th day of the succeeding month.
- ❖ The Principal Officer of a reporting entity shall furnish the information in respect of transactions referred to in clause (D) of sub-rule (1) of rule 3 not later than seven working days on being satisfied that the transaction is suspicious.
- ❖ The Principal Officer of a reporting entity shall furnish, the information in respect of transactions referred to in clause (F) of sub-rule (1) of rule 3, every quarter to the Director by the 15th day of the month succeeding the quarter.
- ❖ For the purpose of this rule, delay of each day in not reporting a transaction or delay of each day in rectifying a mis-reported transaction beyond the time limit as specified in this rule shall constitute a separate violation.

Verification Of Records Of The Identity Of Clients

Individual

One certified copy of an officially valid document containing details of his permanent address, current address including in respect of the nature of business and financial status.

Company

- ❖ Certificate of incorporation
- ❖ Memorandum and articles of association
- ❖ Board resolution or the power of attorney
- ❖ Officially valid document in respect of the person, operating the account.

Partnership Firm

- ❖ Registration certificate
- ❖ Partnership deed
- ❖ Officially valid document in respect of the person acting in the transaction.

Trust

- ❖ Registration certificate
 - ❖ Trust deed
 - ❖ Officially valid document in respect of the person acting in the transaction.
-

Unit 9 : Negotiable Instruments Act, 1881

Introduction

- ❖ The Negotiable Instruments Act came into force from 1st March 1882 and presently extends to the whole of India.
- ❖ This is the law in the country governing the making, negotiation and payment of negotiable instrument including a customer's cheque by a banker, and the respective rights, obligations of the parties to a negotiable instrument including protections available to the parties thereto.
- ❖ The Act has been amended a number of times the latest being in 2018 (w e f from 01-09-2018) whereby Section 143A and 148 was introduced which deal primarily with providing interim compensation during the pendency of the criminal complaint and criminal appeal.

Effect of insertion of Section 143A

- ❖ With the insertion of Section 143A, the new provision was introduced wherein a competent Court while trying a cheque dishonour offence is empowered to order the drawer of the cheque to pay interim compensation not exceeding 20% of the cheque amount to the complainant, where the drawer pleads not guilty to the accusation made in the complaint.
- ❖ However, if the drawer of the cheque is acquitted, the Court shall direct the complainant to repay to the drawer, the amount of interim compensation, with interest at the bank rate as published by the RBI, prevalent at the beginning of the relevant financial year, within 60 days from the date of the order, or within such further period not exceeding 30 days as may be directed by the Court

Negotiable Instruments

As per Section 13 "(1) A negotiable instrument means a promissory note, bill of exchange or cheque payable either to order or to bearer.

Characteristics

- ❖ Those are contracts between two or more persons.
- ❖ Those are always in writing.
- ❖ Those have an amount expressed in a particular currency.
- ❖ Those have a tenor after which they become payable or are payable on sight.
- ❖ Those are payable to 'order' or 'bearer'.
- ❖ Where those are payable to order those are transferable by endorsement and delivery and where payable to bearer by simple delivery.
- ❖ Those are always signed by the issuer.
- ❖ Those usually have a beneficiary if payable to order.
- ❖ Those are dated.

Types

Promissory Note

According to Section 4: "Promissory note" is an instrument in writing (not being a bank-note or a currency-note) containing an unconditional undertaking, signed by the maker, to pay a certain sum of money only to, or to the order of, a certain person, or to the bearer of the instrument."

Illustrations: A signs instruments in the following terms:

- (a) "I promise to pay B or order Rs. 500."
- (b) "I acknowledge myself to be indebted to B in Rs. 1,000, to be paid on demand, for value received."

Bill of Exchange

According to Section 5: "A Bill of Exchange is an instrument in writing containing an unconditional order, signed by the maker, directing a certain person to pay certain sum of money only to or to the order of a certain person or to the bearer of the instrument."

There are 3 parties involved

- ❖ Drawer: The party that issues a bill of exchange "creditor"
- ❖ Drawee: The party to which order to pay is sent "debtor"
- ❖ Payee: The party to which bill of exchange is payable "beneficiary"

Thus the essential characteristics of a 'Bill of Exchange' are:

- ❖ It must be in writing.
- ❖ It must be signed by the drawer.
- ❖ The drawer, drawee and payee must be certain.
- ❖ The sum payable must also be certain.
- ❖ It should be properly stamped.
- ❖ It must contain an express order to pay money and money alone.

Cheque

According to Section 6: "A cheque is a bill of exchange drawn on a specified banker and not expressed to be payable otherwise than on demand and it includes the electronic image of a truncated cheque and a cheque in the electronic form."

Banker has legal duty to make payment of a cheque if:

- ❖ The cheque is properly drawn.
- ❖ There is sufficient balance in the account.
- ❖ There is no legal restraint on the bank's duty to pay. It includes cheque in electronic form and truncated cheque

Payment of Cheques – Protection to Bankers' /Customers'

Bankers' Duty to Pay in terms of Section 31 of the Negotiable Instruments Act (NI ACT) 1881 "The drawee of a cheque having sufficient funds of the drawer, in his hands, properly applicable to the payment of such cheque, must pay the cheque when duly required so to do, and, in default of such payment, must compensate the drawer for any loss or damage caused by such default".

In case of wrongful dishonor, the drawee is only liable to the drawer for compensation and not to the payee, any holder or endorsee, except in the following circumstances –

- ❖ Winding up of the bank. Here the holder would become a creditor as far as the Bank is concerned and entitled to make a claim
- ❖ The bank does not heed the crossing on the cheque, pays and consequently.

Payment in Due Course:

- ❖ Protection to a paying Banker is however available under the NI Act provided payment of a cheque is made in 'due course'.
- ❖ Payment in due course is defined in Section 10 of the NI Act. In terms of Section 10," 'Payment in due course' means payment in accordance with the apparent tenor of the instrument in good faith and without negligence to any person in possession thereof under circumstances which does not afford a reasonable ground for believing that he is not entitled to receive payment of the amount therein mentioned".

Additional Protection to the Paying Banker:

- In terms of Section 85 of the NI Act, additional protection to the paying banker is available against fraudulent endorsements of the payee/other endorsees in an order or bearer cheque provided payment is made in due course.

Material Alterations

A materially altered cheque may be declared null and void. Banker has to be very careful whenever there is a material alteration in the cheque presented for payment. It should be ensured that any material alteration is made with the consent or authority of the drawer and is confirmed by his/her signature.

The following instances of material alteration may be considered important

- ❖ Alteration in the date of the instrument which might have the effect of hastening or delaying the time of payment.
- ❖ Alteration of the name of the payee (beneficiary)
- ❖ Alteration of the amount which is the most common form of fraudulent alteration.
- ❖ Alteration of an order cheque to a bearer cheque.

Where Alteration is not Apparent

In terms of the amended Section 89 “(1) Where a promissory note, bill of exchange or cheque has been materially altered but does not appear to have been so altered, or where a cheque is presented for payment which does not at the time of presentation appear to be crossed or to have had a crossing which has been obliterated, payment thereof by a person or banker liable to pay, and paying the same according to the apparent tenor thereof at the time of payment and otherwise in due course, shall discharge such person or banker from all liability thereon; and such payment shall not be questioned by reason of the instrument having been altered, or the cheque crossed”.

Protection to the Collecting Banker

Sec. 131 grants protection to a collecting banker. This is applicable to both cheques and drafts.

Conditions for Protection

- ❖ The collecting banker acts in good faith.
 - ❖ It acts without negligence.
 - ❖ It receives payment for a customer.
 - ❖ The cheque is crossed generally or specially to the collecting bank
 - ❖ It verifies the prima facie genuineness of the cheque for collecting payment under CTS clearing.
 - ❖ It looks for any fraud, forgery or tampering that can be verified with due diligence and ordinary care, and is apparent on the face of the cheque to be truncated.
-

Unit 10 : Foreign Exchange Management Act, 1999

Introduction

- ❖ Foreign Exchange Management Act (FEMA) was enacted to replace FERA, effective from June 1, 2000.
- ❖ The objective was to consolidate and amend the law relating to foreign exchange with the objective of facilitating external trade and payments and for promoting the orderly development and maintenance of foreign exchange market in India.
- ❖ The provisions of the FEMA extends to all over India and also applies to all branches, offices and agencies outside India owned or controlled by a person resident in India.
- ❖ By maintaining sufficient reserves, India's foreign exchange policy marked a shift from Import Substitution to Export Promotion.

Important Terms

Capital account transaction

Means a transaction by which there may be a change (either an increase or decrease) in the assets or liabilities outside India of persons resident in India or assets or liabilities in India of persons resident outside India.

Current account transaction

Means a transaction other than a capital account transaction.

Foreign currency

- ❖ It is defined to mean any currency other than Indian currency.
- ❖ The term "foreign exchange" is much wider than the term foreign currency.
- ❖ It includes amounts payable in any foreign currency, drafts, travelers' cheques, letters of credit or bills of exchange, expressed or drawn in Indian currency but payable in any foreign currency.
- ❖ Under the FEMA, a "person" is defined to include the following entities an individual, a Hindu Undivided Family (HUF), a company and a firm.

Person resident in India

Means A person residing in India for more than 182 days in the preceding financial year but does not include a person who has gone out of India or who stays outside India for taking up employment outside India, or for carrying on a business or vocation outside India.

Repatriate to India

Means bringing into India the realized foreign exchange and the selling of such foreign exchange to an authorized person in India in exchange for rupees

RBI has the following powers under FEMA

- ❖ To appoint authorized persons and to inspect the authorized persons.
 - ❖ If any person contravenes any provision of this Act, or contravenes any rule, regulation, notification, direction or order issued in exercise of the powers under this Act, he will be liable to a penalty up to thrice the sum involved in such contravention where such amount is quantifiable, or up to two lakh rupees where the amount is not quantifiable, and where such contravention is a continuing one, further penalty which may extend to five thousand rupees for every day after the first day during which the contravention continues.
 - ❖ The Central Government establishes a directorate of enforcement with a director and other officers, called officers of enforcement. (Section 36)
 - ❖ The Central Government can (subject to conditions and limitations), authorize any customs officer/central excise officer/any police officer/any other officer of the Central Government or a State Government to exercise the powers and discharge the duties of the director of enforcement or any other officer of enforcement. (Section 38)
-

Unit 11 : Payment And Settlement Systems Act, 2007

Introduction

- ❖ The Payment and Settlement Systems Act, 2007 came into effect on August 12, 2008.
- ❖ It extends to the whole of India.
- ❖ The PSS Act, 2007 provides for the regulation and supervision of payment systems in India and designates the Reserve Bank of India as the authority for that purpose and all related matters.
- ❖ The Reserve Bank is authorized under the Act to constitute a Committee of its Central Board known as the Board for Regulation and Supervision of Payment and Settlement Systems (BPSS), to exercise its powers and perform its functions and discharge its duties under this statute.

Designated Authority/Authorization

Designated Authority

- ❖ RBI is the authority designated under the statute for supervision of payments etc.
- ❖ The Reserve Bank shall exercise the powers, perform the functions and discharge the duties conferred on it under this Act through a Board to be known as the "Payments Regulatory Board".

The Board shall consist of the following members, namely:–

- ❖ The Governor of the Reserve Bank-Chairperson, ex officio
- ❖ The Deputy Governor of the Reserve Bank in-charge of the Payment and Settlement Systems Member, ex officio
- ❖ One officer of the Reserve Bank to be nominated by the Central Board of the Reserve Bank Member, ex officio
- ❖ Three persons to be nominated by the Central Government-Members.

Authorization

- ❖ According to Section 4 "(1) No person, other than the Reserve Bank, shall commence or operate a payment system except under and in accordance with an authorization issued by the Reserve Bank under the provisions of this Act.
- ❖ The Reserve Bank may, under sub-section (1) of this section, authorize a company or corporation to operate or regulate the existing clearing houses or new clearing houses of banks in order to have a common retail clearing house system for the banks throughout the country: Provided, however, that not less than fifty-one per cent of the equity of such company or corporation shall be held by public sector banks.

Regulation and Supervision by the RBI

Changes in the Payment System/Charges that may be levied

Section 11 states - No system provider shall cause any change in the system which would affect the structure or the operation of the payment system without–

- ❖ The prior approval of the Reserve Bank and

- ❖ Giving notice of not less than thirty days to the system participants after the approval of the Reserve Bank
- ❖ Where the Reserve Bank has any objection, to the proposed change for any reason, RBI shall communicate such objection to the systems provider within two weeks of receipt of the intimation of the proposed changes from the system provider.
- ❖ The system provider shall, within a period of two weeks of the receipt of the objections from the Reserve Bank forward his comments to the Reserve Bank and the proposed changes may be effected only after the receipt of approval from the Reserve Bank.

Section 10 A of the Act stipulates that “no bank or system provider shall impose, whether directly or indirectly, any charge upon a person making or receiving a payment by using the electronic modes of payment prescribed under section 269SU of the Income-tax Act, 1961 (43 of 1961).

Power to access information/inspect:

- ❖ Section 12/13 and 14 deals with RBI powers to call for returns/access information and carry out inspections of any payment system and the premises from where the system is being operated.
- ❖ RBI has also powers to carry out audit and inspections of a payment system or participants (Section 16)

Power to issue directions:

The RBI powers to issue directions is covered in Section 17 to 19 of the Act. Section 17 states as follows “Where the Reserve Bank is of the opinion that,

- (a) a payment system or a system participant is engaging in, or is about to engage in, any act, omission or course of conduct that results in systemic risk being inadequately controlled; or
- (b) any action is likely to affect the payment system, the monetary policy or the credit policy of the country, the Reserve Bank may issue directions in writing to such payment system
 - To cease and desist from engaging in the act, omission or course of conduct or
 - To perform such acts as may be necessary, in the opinion of the Reserve Bank, to remedy the situation.

Settlement And Netting

Settlement can be defined as the process of transferring of funds through a central agency, from payer to payee.

- ❖ Gross settlement is where transactions are settled on a one to one basis, i.e. without bunching with other transactions or by not netting receipts and payments between 2 parties.
- ❖ Net settlement is where a large number of transactions between counterparties are accumulated and offset against each other, with only the net differential being transferred at predetermined times.
- ❖ RBI has powers to stipulate at the time of granting authorization whether the settlement among the system participants shall be determined in accordance with the gross or netting procedure.

Unit 12 : Law Relating to Securities and Modes of Charge – I

Introduction

- ❖ A 'charge' is an interest or right which a borrower or guarantor creates on his/her/its assets as a security in favour of the lender/Creditor to fall back to in case the borrower/guarantor fails to pay back the debt.
- ❖ There are two different types of charge fixed charge and floating charge, and different modes of charging securities.

Section 58(a) of the Transfer of Property Act, 1882 defines A mortgage is the transfer of interest in specific immoveable property, for the purpose of securing the payment of money advanced or to be advanced by way of loan, on existing or future debt.

The transferor is called the 'mortgagor' and the transferee a 'mortgagee'.

The principal money and interest of which payment is secured is called 'mortgage money' and the instrument by which the transfer is affected is called 'mortgage deed'.

The Transfer of Property Act contemplates 6 different kinds of mortgage.

(A) Simple mortgage: According to Section 58(b) of the Transfer of Property Act, a simple mortgage is a transaction whereby, 'without delivering' possession of the mortgaged property, the mortgagor binds himself personally to pay the mortgage money and agrees, expressly or impliedly, that in the event of his failing to pay according to his contract, the mortgagee shall have a right to cause the mortgaged property to be sold by a decree of the Court in a suit and the proceeds of the sale to be applied so far as may be necessary in payment of the mortgage money.'

(B) Mortgage by way of conditional sale: As per Section 58(c) of the Transfer of Property Act, a mortgage by way of a conditional sale of the property is a transaction whereby the mortgagor ostensibly sells the mortgaged property on the condition that On default of payment of the mortgage money on a certain date, the sale shall become absolute, or On such payment being made the sale shall become void or On such payment being made, the buyer shall transfer the property to the seller.

(C) Usufructuary mortgage: According to Section 58(d) of the Transfer of Property Act, 'a Usufructuary mortgage' is a transaction in which the mortgagor delivers possession expressly, or by implication and binds himself to deliver possession of the mortgaged property to the mortgagee and Authorises the mortgagee to retain such possession until payment of the mortgage money and to receive the rents and profits accruing from the property in lieu of interest and partly in payment of the mortgage money.

(D) English Mortgage: According to Section 58(e) of the Transfer of Property Act, an 'English Mortgage' is a transaction in which, the mortgagor binds himself to repay the mortgage money on a

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certain date and transfers the mortgaged property absolutely to the mortgagee, but subject to the provision that he will retransfer it to the mortgagor upon payment of the mortgage money as agreed.

(E) Equitable mortgage or mortgage by deposit of title deeds: According to Section 58(f) of the Transfer of Property Act, 'Where a person in any of the following towns - namely, the towns of Kolkata, Chennai and Mumbai and in any other town which the State Government concerned may, by notification in the official gazette, specify in this behalf- delivers to a creditor or his agent documents of title to immoveable property, with intent to create a security there on, the transaction is called a mortgage by deposit of title deeds. Documents of title or title deed in case of mortgage by deposit of title deeds shall be documents or instruments which evidence ownership of the mortgagor over the property.

(F) Anomalous mortgage: According to Section 58(g) of the Transfer of Property Act, 'a mortgage which is not a simple mortgage, a mortgage by conditional sale and usufructuary mortgage and English mortgage or a mortgage by deposit of title deeds within the meaning of this Section, is called an 'Anomalous Mortgage.'

Article 62 of the Indian Limitation Act, 1963 provides limitation period for filing of suit for recovery of mortgaged debt and sale of mortgaged property in the event of non-payment of the mortgaged debt.

Article 63(a) of the said Act provides a limitation period, in case of foreclosure of the mortgaged property.

The limitation period for filing suit for foreclosure is THIRTY YEARS from the date the money secured by mortgage becomes due.

The limitation period for filing a suit for sale of mortgaged property is TWELVE YEARS, from the date when the money sued for becomes due.

CERSAI: Central Registry of Securitization Asset Reconstruction and Security Interest of India: At the same time there are always cases where the original is lost and the chances of that document being made use of for any purpose becomes remote.

In the absence of the original, the next best proof of the owner's title to the property, is a certified copy of that document.

Thus, unless and until the original title deeds are lost, under no circumstances can a certified copy of a document be considered to be a document of title for the purposes of section 58 (1) of the TP Act.

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Unit 13 : Law Relating to Securities and Modes of Charge – II

Appropriation

- ❖ The Indian Contract Act, 1872 lays down the rules for appropriation which is applicable to a creditor who receives payment from a debtor
- ❖ Appropriation is the application of a particular payment, received from a debtor, for the purpose of repayment of a particular debt.
- ❖ Section 59 of Indian Contract Act states that right of appropriation is vested in the hands of debtor. He can appropriate payment by an express intimation.
- ❖ Sec 60 of Indian Contract Act states that In case the customer has deposited amount in bank without giving any specific direction, the bank can exercise its right of appropriation and apply it in payment of any loan account.
- ❖ Sec 61: Where neither party makes any appropriation, the payment shall be applied in discharge of debts, in order of time. If the debts are of equal standing, the payment shall be applied in discharge of each proportionately.

Assignment

- ❖ The term 'Assignment' means the process by which a person called the assignor prefers to transfer rights or benefits to another person called the assignee.
- ❖ In terms of Section 130 of the Transfer of Property Act: The transfer of an actionable claim, whether with or without consideration, shall be effected only by the execution of an instrument in writing signed by the transferor or his duly authorized agent, shall be complete and effectual upon the execution of such instrument.
- ❖ In banking practice, a borrower may assign the book debt, money due from Government department, and life insurance policies as security for an advance.
- ❖ The assignee can only have rights equal to that of the assignor and cannot have better rights.

Pledge

Pledge means bailment of goods for purpose of providing security for payment of debt or performance of promise' (as per the Section 172 of Contract Act 1872).

Three requirements are to be satisfied for a valid pledge:

- ❖ There must be bailment of goods (bailment means delivery of goods)
- ❖ The bailment must be, by or on behalf of the debtor and
- ❖ The bailment, must be for the purpose of providing security for the payment of a debt or performance of promise.

The person, whose goods are bailed is called the Pawnor, the person who takes the goods as security is called the Pawnee.

- ❖ Delivery may be physical, when goods are physically transferred or symbolic as in the case of handing over the key to the godown, where the goods are stored so as to be out of the control of the pawnor.
- ❖ Pledge can be created only in the case of existing goods which are in the possession of the pawnor himself.
- ❖ Possession of goods is the most important characteristic of pledge and therefore, pledge is lost when possession of the goods is lost. However, the pawnee may release the goods after obtaining a letter of trust from the pawnor.

Rights of Pawnee

- ❖ Rights of retainer
- ❖ Right to claim extraordinary expenses
- ❖ No right to retain in respect of the other debts
- ❖ Pawnee's right where Pawnor makes default in payment
 - He may sue the pawnor upon the debt or promise
 - He may retain the pawned goods as collateral security
 - He may sell it after giving the pawnor reasonable notice of the sale.

Duties of Pawnor:

- ❖ He must disclose to the pawnee any material faults or extra-ordinary risks in the goods to which the pawnee may be exposed.
- ❖ The pawnor must reimburse the pawnee for any expenses incurred for the preservation of the goods.
- ❖ In the case of forced sale, if the amount realised is less than the debt due from the pawnor, he is liable to make good the balance.
- ❖ When the goods are pledged, there is the implied condition that the pawnor has title to the goods pledged. However, in practice the banker obtains the pawnor's signature to a document known as an agreement of pledge.

Advantages of Pledge

- ❖ The goods are in the custody of the pawnee and, therefore, it is easy to sell in case of default.
- ❖ Because of close supervision, it will not be possible for the pawnor to manipulate the stocks.
- ❖ Even if the goods are unfortunately lost due to any reason, the banker can recover the amount under the insurance policy.
- ❖ The formalities connected with the pledge are simpler than in the case of mortgage.

Hypothecation

- ❖ The term came to be defined in the SARFAESI Act, 2002. As per Sec. 2 of the Act, 'Hypothecation' means a charge in or upon any moveable property, existing or future, created by a borrower in favor of a secured creditor, without delivery of possession of the moveable property to such

creditor, as a security for financial assistance and includes floating charge and crystallization of such charge into fixed charge on moveable property.

- ❖ Where the borrower is a company registered under the Companies Act, the charge by way of hypothecation must be registered within a period of 30 days of its creation.

Drawbacks of Hypothecation

- ❖ The fundamental difficulty about this charge is that goods remain in the possession of the borrower and therefore the creditor's control over such goods is almost negligible
- ❖ The borrower may realise stocks hypothecated and pay to other creditors. He may even sell marketable stocks and keep only obsolete and slow moving stocks for the banker to realise.
- ❖ The borrower may hypothecate the same stock with more than one banker or having previously hypothecated, the goods may subsequently be pledged to another creditor.
- ❖ The realisation of the assets in case of default of payment is a difficult, prolonged and costly affair. The banker may find only obsolete and slow-moving items.
- ❖ According to Section 332 of the Companies Act, 2013 any floating charge on the undertaking or property of the company created within a period of twelve months preceding the commencement of the winding up, becomes invalid under certain circumstances.

Note: While lending against hypothecation of goods, bankers obtain a letter of hypothecation which serves as the hypothecation agreement and contains several clauses to protect the banker's interest under all contingencies.

Banker's Lien

- ❖ Lien is the right of the banker to retain possession of the goods and securities owned by the debtor until the debt due from the latter is paid.
- ❖ The banker's lien is an implied pledge. A banker acquires the right to sell the goods which came into his possession in the ordinary course of banking business, in case the debt is not paid.
- ❖ Section 171 of the Indian Contract Act, 1872, gives to the banker an absolute right of general lien on all goods and securities received by the banker.

In order for the right of lien to be exercised-

- ❖ The property must come into the hands of the Bank in normal course of banking business
- ❖ It should not have been entrusted for a particular purpose inconsistent with the lien.
- ❖ The possession with the Bank must be lawful.
- ❖ There should be no agreement inconsistent with the lien

Set-off

In the case of a banker, the right of set-off enables him to adjust a debit balance in a customer's accounts, with any balance outstanding to his credit in the books of the bank.

Salient Features

- ❖ Both debts must be for certain sums. A debt-accruing due cannot be set-off against the debt already due.
- ❖ The banker cannot set-off the credit balance in the account of guarantor till the liability of the guarantor is determined.
- ❖ The credit balance in the current account cannot be set-off against a contingent liability of a bill discounted but not yet due.
- ❖ A banker cannot set-off a debt due to him upon a loan account repayable on demand or at a specified date against a credit balance in the current account until the demand is made or due date arrives.
- ❖ The parties must be mutually indebted in the same right.
- ❖ When the right set-off is available to the bank, lien right cannot apply. These two different rights cannot be exercised simultaneously at the same time.

The right of set-off available to a banker under different situations can be understood better after going through the following chart.

Unit 14 : Creation/Registration and Satisfaction of Charges

Charge

'Charge' has been defined in section 2 (16) of the Companies Act 2013. As per section 2(16) a 'charge' would be

- ❖ An interest or lien
- ❖ Created on the property or assets of a corporation or any of its undertakings or both as security and
- ❖ Includes a mortgage.

It is mandatory for every company to register with the Registrar of Companies (ROC) specific charges created by it on its assets as well as on modification of the charge or its satisfaction. No registration of the charge deprives the creditor the benefit of the security under such circumstances such as when the company is wound up.

Charges requiring registration

The following charges were required to be filed with the ROC

- ❖ A charge for the purpose of securing any issue of debentures
- ❖ A charge on uncalled share capital of the company
- ❖ A charge on any immovable property, wherever situated.
- ❖ A charge on any book debts of the company
- ❖ A charge, not being a pledge, on any movable property of the company
- ❖ A floating charge on the undertaking or any property of the company including stock in trade
- ❖ A charge on calls made but not paid
- ❖ A charge on a ship or any share in a ship
- ❖ A charge on goodwill, on a patent or a license under a patent, on a trade mark, or on a copyright or a license under a copyright.

Rule for registration is that all types of charges are required to be registered with the ROC, within stipulated period, irrespective of whether the charge created is

- ❖ Within or outside India
- ❖ On its property or assets or any of its undertakings
- ❖ Whether tangible or otherwise, fixed or floating
- ❖ Situated in or outside India.

Charges not requiring registration

- ❖ Corporate Guarantee
- ❖ Arising due to the operation of some specific law where registration is not required
- ❖ Hundi, which is a Negotiable instrument

Types Of Charges

Fixed charge:

- ❖ 'Fixed charge' is also called 'specific charge'. It extends over a specific property or properties of the company.
- ❖ It may be noted, that charges specified in Section 77 of the Companies Act, 2013, created in conformity with the provisions of the said Act over a specific property gives right to the creditor so secured, to sell the said property through a Court of Law/ Tribunal (DRT) or under the provisions of SARFESAI Act and claim and appropriate the proceeds towards the dues payable by the company.

Floating charge:

- ❖ A 'floating charge' means a 'charge' that is general and not specific.
- ❖ That floats over the present and future property of the company, which means it does not fasten on or attach to any particular property.
- ❖ That does not restrict the company from assigning the property, subject to charge to third persons, whether by way of sale or security
- ❖ That on happening of an event or contingency, crystallizes as a fixed charge.

When floating charge becomes fixed or crystallized/attached

When the debtor company ceases to carry on business or goes into liquidation or some other act which affects the powers of the company to dispose the assets charged. A floating charge may also crystallize on the happening of an event specified in a charge deed.

Effect of floating charge becoming fixed or crystallized

When a floating security upon all the property or assets of the company becomes fixed, it constitutes a charge upon all the property or assets then belonging to the company. It has priority over the subsequent equitable charges and over unsecured creditors.

Procedure for Registration of Charge

- ❖ A charge created by a company is required to be registered with the Registrar within thirty days of its creation in such form and on payment of such fees as may be prescribed.
- ❖ The application for delay has to be made to the registrar in Form No. CHG-10 and supported by a declaration from the company signed by its secretary or director that such delay in filing shall not adversely affect the rights of any other intervening creditors of the company.
- ❖ Where a charge is registered successfully with the ROC under sub-section (1), he/she would issue a certificate of registration of such charge to the company and to the person/entity in whose favor the charge is created. It is issued by the ROC in Form CHG 2.

Effect of Registration of Charges

- ❖ In terms of Section 80 of the Companies Act 2013 “Where any charge on any property or assets of a company or any of its undertakings is registered under section 77, any person acquiring such property, assets, undertakings or part thereof or any share or interest therein shall be deemed to have notice of the charge from the date of such registration”.
- ❖ The date of registration of charge is important for considering priority and the charge registered first will get the priority over all charges registered later, in the absence of any agreement between the charge holders to the contrary (for example a pari - passu charge agreement).
- ❖ In terms of section 77(3) of the Act amended vide Companies (Registration of Charges) Amendment Rules, 2019: No charge created by a company shall be taken into account by the liquidator appointed under the Act or the Insolvency and Bankruptcy Code (IBC), 2016, or any other creditor unless it is duly registered under sub-section (1) and a certificate of registration of such charge is given by the Registrar under sub-section (2).

Provisions of Companies Act 2013 relating to Registration of Charges

Chapter VI comprising of Sections 77 to 87 of the Companies Act, 2013 provides for the registration of charges. They can be stated briefly as follows:

- ❖ Section 77: This Section has already been dealt with in detail hereinabove
- ❖ Section 78: This Section provides that in case the charge is not registered by the Company within the period referred to in Section 77, the charge- holder may apply for filing of charge in the prescribed manner and “the Registrar may, on such application, within a period of fourteen days after giving notice to the company, unless the company itself registers the charge or shows sufficient cause why such charge should not be registered, allow such registration on payment of such fees, as may be prescribed”.
- ❖ Section 79: In terms of Section 79 “The provisions of section 77 relating to registration of charges shall, so far as may be, apply to— (a) a company acquiring any property subject to a charge within the meaning of that section; or (b) any modification in the terms or conditions or the extent or operation of any charge registered under that section.”
- ❖ Section 80: This Section provides that after registration of charge created, any other person acquiring such property charged or any party thereof, shall be deemed to have notice of the charge registered and shall take the property subject to such charge.
- ❖ Section 81: It is provided under this Section that Registrar of Companies shall keep a register of charges containing particulars of all charges requiring registration. This Section further provides that a copy of particulars contained in the register of charges can be obtained by any person on payment of fee.
- ❖ Section 82: This section provides that the Company shall intimate the Registrar of any payment/ satisfaction in full of any charge registered within a period of 30 (thirty) days.

MODULE C : IMPORTANT ACTS/LAWS & LEGAL ASPECTS OF BANKING OPERATIONS – PART B

Unit 15 : Reserve Bank – Integrated Ombudsman Scheme, 2021

Introduction

- ❖ The 'Banking Ombudsman Scheme 2006' was a scheme which became operative from January 01 2006, for providing an expeditious and inexpensive forum for bank customers for resolution of complaints relating to certain services rendered by banks.
- ❖ The Scheme was introduced under Clause 35A of the Banking Regulation Act, 1949 by RBI.
- ❖ RBI had also introduced two more ombudsman schemes, viz. The Ombudsman Scheme for Non-banking Financial Companies, 2018 (for customers of larger NBFCs), and Ombudsman Scheme for Digital Transactions, 2019 (for grievances related to digital transactions).
- ❖ In November 2021, RBI integrated all the three Schemes into one omnibus Ombudsman Scheme, viz. The Reserve Bank - Integrated Ombudsman Scheme, 2021 (IOS 2021) to cover all entities regulated by RBI.

Coverage

The Scheme covers the following regulated entities:

- ❖ All Commercial Banks, Regional Rural Banks, Scheduled Primary (Urban) Cooperative Banks and Non-Scheduled Primary (Urban) Co-operative Banks with deposits size of Rupees 50 crore and above as on the date of the audited balance sheet of the previous financial year
- ❖ All Non-Banking Financial Companies (excluding Housing Finance Companies) which (a) are authorized to accept deposits; or (b) have customer interface, with an assets size of Rupees 100 crore and above as on the date of the audited balance sheet of the previous financial year.

Ombudsman – Appointment/Location Of Offices/ Establishment Of A Centralized Receipt And Processing Centre

Appointment and Tenure of Ombudsman and Deputy Ombudsman

- ❖ In terms of Clause 4 of the scheme: The Reserve Bank may appoint one or more of its officers as Ombudsman and Deputy Ombudsman, to carry out the functions entrusted to them under the Scheme.
- ❖ The appointment of Ombudsman or the Deputy Ombudsman, as the case may be, shall be made for a period not exceeding three years at a time.

Location of the Office

Clause 5 of the scheme provides information about the location of offices of the ombudsman under the revised scheme. According to Clause 5 "(1) The offices of the Ombudsman shall be at such places as may be specified by the Reserve Bank.

Establishment of a Centralized Receipt and Processing Centre (CRPC)

- ❖ Clause 6 of the scheme envisages the setting up of a Centralized Receipt and Processing Centre for processing of customer complaints relevant to the scheme.
- ❖ Clause 6 states “The Reserve Bank shall establish the Centralized Receipt and Processing Centre at any place as may be decided by it to receive the complaints filed under the Scheme and process them”.
- ❖ The complaints under the Scheme made online shall be registered on the portal (<https://cms.rbi.org.in>). Complaints in electronic mode (E-mail) and physical form, including postal and hand-delivered complaints, shall be addressed and sent to the place where the Centralized Receipt and Processing Centre of the Reserve Bank is established, for scrutiny and initial processing.

Procedure for Redressal of Grievance

Complaint: As per clause 9 “Any customer aggrieved by an act or omission of a Regulated Entity resulting in deficiency in service may file a complaint under the Scheme personally or through an authorized representative as defined under clause 3(1)(c)”

Circumstances where a complaint is not maintainable:

Commercial judgment/commercial decision of a Regulated Entity

- ❖ A dispute between a vendor and a Regulated Entity relating to an outsourcing contract
- ❖ Grievances not addressed to the Ombudsman directly
- ❖ General grievances against Management or Executives of a Regulated Entity
- ❖ Disputes in which action is initiated by a Regulated Entity in compliance with the orders of a statutory or law enforcing authority
- ❖ Services not within the regulatory purview of the Reserve Bank
- ❖ Disputes between Regulated Entities
- ❖ Disputes involving the employee-employer relationship of a Regulated Entity.

Moreover as per Clause 10(2) “A complaint under the Scheme shall not lie unless:

(a)The complainant had, before making a complaint under the Scheme, made a written complaint to the Regulated Entity concerned and –

- ❖ The complaint was rejected wholly or partly by the Regulated Entity, and the complainant is not satisfied with the reply; or the complainant had not received any reply within 30 days.
- ❖ The complaint is made to the Ombudsman within one year after the complainant has received the reply from the Regulated Entity to the complaint or, where no reply is received, within one year and 30 days from the date of the complaint.

(b)The complaint is not in respect of the same cause of action which is already–

- ❖ Pending before an Ombudsman or settled or dealt with on merits, by an Ombudsman
- ❖ Pending before any Court, Tribunal or Arbitrator or any other Forum or Authority

(c)The complaint is not abusive or frivolous or vexatious in nature

(d)The complaint to the Regulated Entity was made before the expiry of the period of limitation prescribed under the Limitation Act, 1963, for such claims

(e)The complainant provides complete information as specified in clause 11 of the Scheme

(f)The complaint is lodged by the complainant personally or through an authorized representative other than an advocate unless the advocate is the aggrieved person.

Procedure for Filing a Complaint

Filing:

The complaint may be lodged online through the portal designed for the purpose (<https://cms.rbi.org.in>).The complaint may also be submitted through electronic or physical mode to the Centralized Receipt and Processing Centre as notified by the Reserve Bank.

Initial Scrutiny:

- ❖ According to Clause 12 dealing with initial scrutiny of complaints received: Complaints which are in the nature of offering suggestions or seeking guidance or explanation shall not be treated as valid complaints under the Scheme and shall be closed accordingly with a suitable communication to the complainant.
- ❖ Complaints which are non-maintainable under clause 10 shall be separated to issue a suitable communication to the complainant.
- ❖ The remaining complaints shall be assigned to the offices of the Ombudsman for further examination under intimation to the complainant. A copy of the complaint shall also be forwarded to the Regulated Entity against whom the complaint is filed with a direction to submit its written version.

Resolution:

- ❖ The Ombudsman/Deputy Ombudsman shall endeavor to promote settlement of a complaint by agreement between the complainant and the Regulated Entity through facilitation or conciliation or mediation.
- ❖ The Regulated Entity shall, on receipt of the complaint, file its written version, enclosing therewith copies of the documents relied upon, within 15 days before the Ombudsman for resolution.
- ❖ In case the Regulated Entity omits or fails to file its written version and documents within the time as provided in terms of sub-clause (3), the Ombudsman may proceed ex-parte based on the evidence available on record and pass appropriate Order or issue an Award.
- ❖ If any amicable settlement of the complaint is arrived at between the parties, the same shall be recorded and signed by both the parties.

The complaint would be deemed to be resolved when:

- ❖ It has been settled by the Regulated Entity with the complainant upon the intervention of the Ombudsman; or
- ❖ The complainant has agreed in writing or otherwise (which may be recorded) that the manner and the extent of resolution of the grievance is satisfactory; or
- ❖ The complainant has withdrawn the complaint voluntarily.

Award By Ombudsman

The Award shall contain following rulings:

- ❖ Direction to the regulated entity for specific performance
- ❖ Amount to be paid by the regulated entity to the complainant as compensation for loss suffered.

Following ceilings apply to payments by the regulated entity to the complainant:

- ❖ Actual amount involved in the dispute - without any ceiling.
- ❖ Compensation for consequential loss (directly out of the act or omission of the bank) - to the extent of actual loss, with ceiling of Rs. 20 lakh
- ❖ Compensation for loss of time, expenses incurred, harassment and mental anguish suffered - up to the ceiling of Rs. 1 lakh.

- ❖ A copy of the Award is sent to the complainant and the regulated entity. The complainant should give a letter accepting the Award in full and final settlement to the regulated entity, within 30 days of receiving the award copy.
- ❖ The regulated entity should comply with the Award and intimate compliance to the ombudsman, within 30 days of receiving acceptance letter from the complainant.
- ❖ The Appellate Authority (AA) is the Executive Director in-Charge of the RBI Department administering the Scheme. An appeal can be made by either of the parties against the award or an order of rejection made by the Ombudsman. A Regulated Entity can appeal only with prior sanction of the Chairman or the MD/ CEO or, in their absence, the ED/Official of equal rank.

Unit 16 : The Micro, Small and Medium Enterprises Development Act, 2006

Introduction

The Micro, Small and Medium Enterprises Development Act, 2006 was enacted to facilitate the promotion and development and enhancing the competitiveness of micro, small and medium enterprises

The Act became operational from October 2nd 2006. In accordance with the provision of MSME Act, 2006 the Micro, Small and Medium Enterprises (MSME) are classified in two classes:

- ❖ Manufacturing Enterprises: The enterprises engaged in the manufacture or production of goods pertaining to any industry specified in the First Schedule to the Industries (Development and Regulation) Act, 1951.
- ❖ Service Enterprises: The enterprises engaged in providing or rendering of services.

Classification

National Board For Micro, Small And Medium Enterprises (NBMSME)

- ❖ The Board provides representation to all sections/segments connected to MSMEs including Associations of Micro, Small and Medium manufacturing and service enterprises, women enterprises, Central Ministries, States representing different regions of the country, trade unions, etc.
- ❖ The NBMSME normally consists of 47 members of which 18 are ex-officio members. The head office of board is in Delhi.

Functions of the Board

- ❖ Examining the factors affecting the promotion and development of MSMEs and review the policies & programs of the Central Government in regards to facilitating the promotion & development & enhancing the competitiveness of such enterprises and the impact thereof on such enterprises.
- ❖ Making recommendations on matters referred to it by the Central Government which, in the opinion of that Government, is necessary or expedient for facilitating the promotion and development and enhancing the competitiveness of the micro, small and medium enterprises.
- ❖ Advise the Central Government on the use of the Fund or Funds constituted under section 12 which states "There shall be constituted, by notification, one or more Funds to be called by such name as may be specified in the notification and there shall be credited thereto any grants made by the Central Government under section 13"

Advisory Committee

- ❖ Section 7(2) of the MSME Act, 2006 provides for constitution of Advisory Committee for MSME, under the Chairmanship of the 'Secretary, Ministry of Micro, Small and Medium Enterprises.'
- ❖ The Advisory Committee usually comprises of five officers of the Central Government having experience in matters relating to Micro, Small and Medium Enterprises, three representatives of

State Governments and one representative each from Micro, Small and Medium Enterprise associations.

- ❖ The Member Secretary of NBMSME is also the Member Secretary of Advisory Committee.

Functions of the Advisory Committee

- ❖ To examine matters referred by the NBMSME concerning promotion and development of MSME sector and enhancing its competitiveness.
- ❖ To provide advice to the Central Government on issues related to the promotion, development and enhancement of competitiveness of micro, small and medium enterprises, which include issues concerning Credit Facilities, Procurement Preference Policy, Constitution and Administration of Funds, etc.
- ❖ To provide advice to the State Governments on issues relating to notifying any rule made to carry out the provisions of the MSME Act-2006 including the composition of Micro, Small Enterprises Facilitation Councils etc. as provided under section 30.
- ❖ Recommend or advice Central Government or State Governments or the Board, in connection with the classification of a class/es of enterprises after taking into consideration the level of employment, investments, need of higher investment in plant and machinery or equipment for technology upgradation, employment generation and enhanced competitiveness and international standards for classification of small and medium enterprises.

Memorandum of Micro, Small And Medium Enterprises

- ❖ Section 8 of the statute provides for filing of the memorandum of micro, small or medium enterprise with such authority as may be specified by the State or the Central Government, by the person desirous of commencing such enterprise.
- ❖ The form of the memorandum, the procedure of its filing and other matters shall be such as may be notified by the Central Government after obtaining the recommendations of the Advisory Committee in this behalf.
- ❖ The authority with which the memorandum shall be filed by a medium enterprise shall be such as may be specified, by notification, by the Central Government.
- ❖ The State Government shall, by notification, specify the authority with which a micro or small enterprise may file the memorandum.

Delayed Payments To Micro And Small Enterprises

Chapter 5 of the statute deals with the issue of delayed payment by buyers of products/ services from MSMEs.

- ❖ Liability of buyer to make payment: As per the provisions of Section 15 "Where any supplier supplies any goods or renders any services to any buyer, the buyer shall make payment on or before the date agreed upon between him and the supplier in writing, Provided that in no case the period agreed upon between the supplier and the buyer in writing shall exceed forty-five days from the day of acceptance or the day of deemed acceptance.

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- ❖ Date from which and rate at which interest is payable. As per Section 16, where a buyer fails to make payment to the supplier, the buyer shall, be liable to pay compound interest with monthly rests to the supplier on that amount from the appointed day or from the date immediately following the date agreed upon, at three times of the bank rate notified by the Reserve Bank.

Micro And Small Enterprises Facilitation Council

The Micro and Small Enterprise Facilitation Council is set up under Section 20 of the Act and is required to be established by State Governments. 'at such places, exercising such jurisdiction and for such areas, as may be specified in the notification.'

Composition of the Council

The composition of the members of the council shall consist of not less than three but not more than five members to be appointed from amongst the following categories, namely:

- ❖ Director of Industries, or any other officer not below the rank of such Director, in the Department of the State Government having administrative control of the small scale industries
- ❖ One or more office-bearers or representatives of associations of micro or small industry or enterprises in the State.
- ❖ One or more representatives of banks and financial institutions lending to micro or small enterprises
- ❖ One or more persons having special knowledge in the field of industry, finance, law, trade or commerce.

The person appointed under clause (i) of sub-section (1) shall be the Chairperson of the Micro and Small Enterprises Facilitation Council.

Reference to Council

- ❖ Where any amount due to a Micro or Small Enterprise is not paid in time or there is a dispute involving such transactions, the parties may refer the matter to the 'Facilitation Council' under the provisions of Section 18 of the Act.
- ❖ On receipt of a reference under sub-section (1), the Council shall either itself conduct conciliation in the matter or seek the assistance of any institution or center providing alternate dispute resolution services.
- ❖ Micro and Small Enterprises Facilitation Council or the center providing alternate dispute resolution services shall have jurisdiction to act as an Arbitrator or Conciliator in a dispute between the supplier located within its jurisdiction and a buyer located anywhere in India.
- ❖ Every reference made under this section shall be decided within a period of ninety days from the date of making such a reference.

Setting aside decree, award or order

In Section 19 of the statute, there are provisions that, No application for setting aside any decree, award or other order made either by the Council itself or by any institution or center providing alternate dispute resolution services, shall be entertained by any court unless the appellant has deposited with it seventy-five per cent of the amount in terms of the decree, award.

Disclosures And Penalty For Contravention Of The Provisions Of The Statute

Disclosures

Any buyer, who is required to get his annual accounts audited under any law for the time being in force, is required to furnish additional information in his annual financial statements.

This additional information would pertain to

- ❖ The principal amount and the interest due thereon (to be shown separately) remaining unpaid to any supplier as at the end of each accounting year.
- ❖ The amount of interest paid by the buyer in terms of section 16, along with the amount of the payment made to the supplier beyond the appointed day during each accounting year.
- ❖ The amount of interest due and payable for the period of delay in making payment (which have been paid but beyond the appointed day during the year) but without adding the interest specified under this Act
- ❖ The amount of interest accrued and remaining unpaid at the end of each accounting year
- ❖ The amount of further interest remaining due and payable even in the succeeding years, until such date when the interest dues as above are actually paid to the small enterprise.

Penalty

In terms of Section 27

Whoever intentionally contravenes or attempts to contravene or abets the contravention of any of the provisions contained in sub-section (1) of section 8 or sub-section (2) of section 26, shall be punishable :

- ❖ In the case of the first conviction, with fine which may extend to rupees one thousand; and
- ❖ In the case of second or subsequent conviction, with fine which shall not be less than rupees one thousand but may extend to rupees ten thousand.

Where a buyer contravenes the provisions of section 22, he shall be punishable with fine which shall not be less than rupees ten thousand.

Unit 17A : Introduction to Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (SARFAESI Act, 2002)

SARFAESI Act, 2002

Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (SARFAESI Act 2002) came into force from June 21st 2002 and extends to the whole of India.

It has brought a legal framework for the following important activities in the credit market:

- ❖ Securitization of financial assets
- ❖ Reconstruction of financial assets.
- ❖ Recognition of any 'interest' created in the security for due repayment of a loan as a 'security interest', irrespective of its form and nature but when it is not in the possession of the creditor.
- ❖ Power to enforce such a security for the realization of money due to banks and the financial institutions in the event of a default, without the intervention of the Courts.
- ❖ Enabling provisions for the setting up a central registry for the purpose of registration of transactions of securitization, reconstruction and the creation of the security interest.

There is an obligation on the part of the borrowers to repay loans and if they are unable to repay, then the securities for the loans can be sold without intervention of the Courts of Law or Tribunals, by following the procedure as provided in the Act and the Rules framed there under, for recovery of the loans.

- ❖ The Act is applicable to cases where security interest for securing repayment of any financial asset is more than Rs.1 Lakh and the amount due is 20% or more of the principal amount and interest thereon.
- ❖ The Act is not applicable to any security interest created on agricultural land and certain properties not liable to attachment under some specified Acts.
- ❖ Creditors other than secured creditors not eligible to exercise right of enforcement of securities under this Act.
- ❖ The borrower can file an appeal to the DRT only after depositing seventy-five per cent of the amount claimed by the lender. The Supreme Court declared this condition of the deposit of seventy five per cent of the claim amount as unreasonable, oppressive, arbitrary and violative of the Article 14 of the Constitution. The Act has since been suitably amended by deleting the condition of pre-deposit of the amount for filing an application/appeal under Section 17. CAIIB Paper (BRBL) Module C Unit 4: Definitions Under SARFAESI Act, 2002

Unit 17B : Definitions Under SARFAESI Act, 2002

Preamble

The preamble of a statute indicates the purpose of the statute. The SARFAESI Act as per its preamble is 'an Act to regulate securitization and reconstruction of financial assets and the enforcement of security interest and to provide for a Central database of security interests created on property rights

Appellate Tribunals

As per the SARFAESI Act, any person aggrieved by the order passed by the 'Debt Recovery Tribunal' can file an appeal to the authority called as the 'Appellate Tribunal' i.e. Debts Recovery Appellate Tribunal (DRAT) within 45 days from the date on which a copy of the order aggrieved has been passed or deemed to have been passed by the Tribunal is received upon depositing 50% of the claim amount. (It can be reduced to 25% if considered on justifiable grounds by DRAT).

Asset Reconstruction

- ❖ The Asset Reconstruction is the acquisition by any Asset Reconstruction Company of any right or interest, of any bank or financial institution, in any financial assistance, for the purpose of realization of such financial assistance.
- ❖ Asset Reconstruction Company" means a company registered with Reserve Bank under section 3 for the purposes of carrying on the business of asset reconstruction or securitization, or both and having net owned fund of not less than Rs. two crore or such other higher amount as the Reserve Bank, may, by notification, specify.

Central Registry

- ❖ Central Registry means the registering office, set up or caused to be set up by the Central Government. With this proposed set up, all the transactions of asset securitization, reconstruction as well as transactions of creation of security interests, will have to be registered with this authority.
- ❖ All creditors including secured creditors may file particulars of transactions by which security interest is created with central registry. Such registration or filing of attachment orders will be deemed to be public notice from the date of filing with the Central Registry. The time limit of 30 days to file particular of securitization, Asset reconstruction or creation of security interest with CERSAI has been done away with.

Debt Recovery Tribunal

- ❖ The Recovery of Debts Due to Banks and Financial Institutions Act (RDDBFI Act), 1993 provides for establishment of Debts Recovery Tribunals (DRTs) and Debts Recovery Appellate Tribunals (DRATs) with for expeditious adjudication and recovery of debts due to banks and financial institutions, insolvency resolution and bankruptcy of individuals and partnership firms and connected matters therewith.

- ❖ The Act is applicable to cases where the amount of debt due to any bank or financial institution defined under the Act or a consortium of banks or financial institutions is Rs. 20 Lakh or more.
- ❖ Recently the e-DRT project has been implemented in all DRTs and DRATs. e-DRT provides access to e-filing, e-payment of fees, cause list generation and a case information system that enables viewing of case status, orders and judgments.

Default

- ❖ When the borrower does not pay any principal debt or any interest on the principle debt or any other amount payable to the secured creditor and due to such non-payment the account of such a borrower is classified as a non-performing asset (NPA) in the books of accounts of the secured creditor, as per the RBI guidelines, it is called default.
- ❖ For getting the right of security enforcement, under this Act, there should be a default committed by the borrower. The creditor must also be a secured creditor.

Hypothecation

Hypothecation (Section 2 (n)) means: a charge in or upon any moveable property, existing or future, created by a borrower in favor of a secured creditor without delivery of possession of the moveable property to such creditor as a security for financial assistance and includes floating charge and crystallization of such charge into fixed charge on moveable property.

Securitisation

- ❖ Securitization means acquisition of financial asset by the Asset reconstruction company from the originator. Such an acquisition may be by raising of funds by such an Asset reconstruction company from the qualified buyers by issue of security receipts.
- ❖ This is a process where non-liquidated financial assets are converted into marketable securities, i.e., security receipts that can be sold to the investors.

Security Interest

“Security interest” means right, title or interest of any kind, upon property created in favor of any secured creditor and includes :

- ❖ Any mortgage, charge, hypothecation, assignment or any right, title or interest of any kind, on tangible asset, retained by the secured creditor as an owner of the property, given on hire or financial lease or conditional sale or under any other contract which secures the obligation to pay any unpaid portion of the purchase price of the asset or an obligation incurred or credit provided to enable the borrower to acquire the tangible asset; or
- ❖ Such right, title or interest in any intangible asset or assignment or licence of such intangible asset which secures the obligation to pay any unpaid portion of the purchase price of the intangible asset or the obligation incurred or any credit provided to enable the borrower to acquire the intangible asset or licence of intangible asset”.

Security Receipt

- ❖ The security receipt evidences the purchaser's undivided right, title and interest in the security. These receipts are transferable in the market. By this Act, a new type of transaction in the financial market has been created for transfer of the security interest.
- ❖ The ARC shall issue SRs only to QBs; and hold and administer the financial assets for the benefit of the QBs.

Sponsor

Sponsor is an entity holding not less than ten per cent of the paid-up equity capital of Asset Reconstruction Company.

Unit 17C : Regulation of Securitisation and Reconstruction of Financial Assets of Banks and Financial Institutions

Registration of Asset Reconstruction Company

The Asset Reconstruction company can commence or carry business, only after complying with the following two conditions:

- ❖ It obtains certification of registration from the Reserve Bank of India by applying in prescribed format
- ❖ It has the owned funds at the time of registration not less than Rupees two crore or such other higher amount as Reserve Bank may, by notification, specify.
- ❖ Such registered companies can raise money for their acquisition activities by issue of security receipts for formulating schemes. This Act has provided the legal framework for this activity.
- ❖ Depending on the nature of security asset, the Reserve Bank of India has the powers to specify different amounts of owned funds for different class or classes of securitization companies or reconstruction companies.
- ❖ If any Asset Reconstruction Company wants to make any substantial change in its management or a change in the registered address or change in the name, then that needs prior approval of the Reserve Bank of India.

Following conditions are required to be fulfilled by ARCs as per Section 3(3) of the act:-

- ❖ That the ARC has not incurred losses in any of the three preceding financial years
- ❖ That such ARC has made adequate arrangements for realization of the financial assets acquired for the purpose of securitization or asset reconstruction and shall be able to pay periodical returns and redeem on respective due dates on the investments made in the company by the qualified buyers
- ❖ That the directors of ARC have adequate professional experience in matters related to finance, securitization and reconstruction
- ❖ That any of its directors has not been convicted of any offence involving moral turpitude.
- ❖ That a sponsor of an asset reconstruction company is a fit and proper person in accordance with the criteria as may be specified in the guidelines issued by the Reserve Bank for such persons.
- ❖ That asset reconstruction company has complied with or is in a position to comply with prudential norms specified by the Reserve Bank
- ❖ That asset reconstruction company has complied with one or more conditions specified in the guidelines issued by the Reserve Bank for the said purpose.

Cancellation of Certificate of Registration

As per Section 4 of the SARFAESI Act 2002, the registration granted to the Asset Reconstruction Company by the Reserve Bank of India is cancellable on following grounds:

- ❖ The company ceases to carry on the business of securitization or asset reconstruction, or

- ❖ The company ceases to receive or hold any investment from a qualified institutional buyer, or
- ❖ The company fails to comply with any of the conditions subject to which the certificate of registration was granted, or

The company fails to-

- ❖ Comply with any of the directions issued by RBI.
- ❖ Maintain accounts in accordance with the requirements of any law or any direction or order issued by the RBI, or
- ❖ Submit or offer for inspection its books of accounts or other relevant documents when so demanded by RBI or
- ❖ Obtain prior approval of the Reserve Bank of India for change in management or change in registered office or change of name.

Acquisition of Rights of Interest in Financial Assets

The Asset Reconstruction Company can acquire the financial asset of any bank or financial institution by any of the following ways:

- ❖ By issuing a debenture or bond or any other security in the nature of debenture for the agreed consideration and agreed terms and conditions between the bank/financial institution and the ARCs.
- ❖ By entering into an agreement with such bank or financial institution for the transfer of financial asset to such company on terms and conditions as may be agreed between them.

Any document executed by any bank or financial institution under sub-section (1) in favor of the asset reconstruction company acquiring financial assets for the purposes of asset reconstruction or securitization shall be exempted from stamp duty in accordance with the provisions of section 8F of the Indian Stamp Act, 1899.

Notices to Obligor and Discharge of Obligation of such Obligor

- ❖ When the bank or financial institution decides, that the financial asset be now acquired by the ARC, a notice may be given about such an acquisition to the obligor. Giving of such notice is optional and not compulsory under the Act.
- ❖ In case, the obligor is a company and creation of charge has been registered, then also the giving of notice to the respective registrar is optional. Thus, there is no need of modification of charge with the Registrar of Companies
- ❖ However, if the bank or financial institution decides to give notice to the obligor, then notice to the ROC is required to be given when the obligor is a company.
- ❖ If notice of acquisition as said above is given to the obligor, it is necessary that the obligor should make payments to the concerned Asset Reconstruction Company.

Such payments amount to a valid discharge of liability of the obligor making the payment.

If notice of acquisition, as said above is not given, the money or property received by the bank or financial institution from the obligor shall be held by such bank or financial institution in trust and shall be handed over to the concerned Asset Reconstruction Company. (Section 6)

Issue of Security Receipts and Raising of Funds by ARC

- ❖ ARC raises funds for acquisition of an asset by issue of security receipts. Only the qualified institutional buyers or such other category of investors including non-institutional investors as may be specified by the Reserve Bank in consultation with the Board, from time to time, can buy these security receipts.
- ❖ In the event of non-realization under sub-section (2) of financial assets, the qualified buyers of an asset reconstruction company, holding security receipts of not less than 75% of the total value of the security receipts issued under a scheme by such company, shall be entitled to call a meeting of all the qualified buyers and every resolution passed in such meeting shall be binding on the company.

Measures Oof Asset Reconstruction

ARC may, for the purposes of asset reconstruction, provide for any one or more of the following measures, namely:-

- ❖ The proper management of the business of the borrower, by change in, or takeover of, the management of the business of the borrower
- ❖ The sale or lease of a part or whole of the business of the borrower
- ❖ Rescheduling of payment of debts payable by the borrower
- ❖ Enforcement of security interest in accordance with the provisions of this Act
- ❖ Settlement of dues payable by the borrower
- ❖ Taking possession of secured assets in accordance with the provisions of this Act
- ❖ Conversion of any portion of debt into shares of a borrower company

Powers available with RBI

- ❖ To Determine Policy & Issue Directions: The powers available with the RBI under the SARFEASI Act 2002 is detailed in Sections 12, 12A and 12B of the statute.
- ❖ To call for Statements and Information: In terms of Section 12 A The Reserve Bank may at any time direct a asset reconstruction company to furnish it within such time as may be specified by the Reserve Bank, with such statements and information relating to the business or affairs of such asset reconstruction company
- ❖ To carry out Audit and Inspection: Section 12 B details the powers available with the RBI to carry out audits and inspections in an Asset Reconstruction Company.

Unit 17D : Enforcement of Security Interest

Enforcement of Security Interest

- ❖ Under the SARFAESI Act a secured creditor can enforce the security interest created in his favor without the intervention of the Court or Tribunal. This power given to the secured creditor, has an overriding effect over the provisions related to mortgage in the Transfer of Property Act, 1882, as in that Act Court intervention is required.
- ❖ Section 13(2) of the SARFAESI Act speaks about the notice to be given by the secured creditors to the borrower, who has defaulted in making the repayment and whose account is classified as NPA. The notice should be given asking the borrower to discharge in full his liabilities to the secured creditors within sixty days from the date of notice.
- ❖ The notice should give the details of the amount payable by the borrower and the secured asset intended to be enforced by the secured creditor in the event of non-payment of secured debt by the borrower.
- ❖ Though the requirement for classification as NPA is a precondition for serving of the notice as per Section 13(2), such a requirement is dispensed with in case of secured debt raised by borrowers through debt securities as per amendment to Section 13 (2).
- ❖ If the borrower on receipt of the notice under Section 13(2) from the secured creditor makes any representation or raises any objection, the reasons for overriding the objections of the borrower must be communicated to him by the secured creditor within 15 days of the receipt of such representation.
- ❖ While directing that the reasons for the rejection must be conveyed to the borrower, the Supreme Court has clarified that the communication to the borrower giving the reasons for not accepting the objections of the borrower does not give an occasion to resort to any proceedings.

If the borrower does not pay in full as per the notice such non-payment by the borrower gives the secured creditor right to take recourse to one or more of the following measures to recover his secured debt:

- ❖ Take possession of the secured assets of the borrower including the right to transfer by way of lease, assignment or sale for the realisation of money from the secured asset.
- ❖ Takeover the management of the secured asset of the borrower
- ❖ Appoint any person as manager to manage the security assets, the possession of which has been taken over by the secured creditor.
- ❖ If the borrower pays the entire dues, costs charges and expenses incurred by the creditor at any time before the date fixed for sale or transfer, the secured creditor shall not sell or transfer the secured asset and no further steps shall be taken for sale or transfer.
- ❖ In cases of joint finance or consortium finance by two or more secured creditors, no secured creditor can take any action of taking possession of secured asset, unless exercise of such right is agreed upon by the secured creditors representing not less than 60% in value of the outstanding dues on the record date.

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- ❖ In case the borrower is a company under winding up process, the dues payable to the workmen have pari passu charge with the secured creditors as provided in Sections 325 and 326 of the Companies Act, 2013.
 - ❖ When the borrower receives the notice from the creditor under Section 13(2), the borrower shall not transfer by way of sale, lease or otherwise, other than in the ordinary course of business, any of his secured assets referred to in the notice without prior written consent of the secured creditor. Non-compliance with this provision attracts penal provisions under the SARFAESI Act that provides for punishment of imprisonment of one year or fine or both.
 - ❖ The authorized officer is authorized to issue the sale certificate. Such a certificate is conveyance of immoveable property and requires stamping, as may be required under the relevant State laws.
 - ❖ Section 13(5A), (5B) and 5(C) allows a Secured Creditor to itself buy the immoveable property of a borrower, subject to certain terms and conditions. As per these sections” (5A) Where the sale of an immovable property, for which a reserve price has been specified, has been postponed for want of a bid of an amount not less than such reserve price, it shall be lawful for any officer of the secured creditor, if so authorized by the secured creditor in this behalf, to bid for the immovable property on behalf of the secured creditor at any subsequent sale.

Chief Metropolitan Magistrate Or District Magistrate’s Assistance for Taking Possession of Secured Asset

- ❖ When the secured creditor is required to take possession or control of the secured asset or when the secured asset is required to be sold or transferred under the provisions of the SARFAESI Act, the secured creditor can take the help of the Chief Metropolitan Magistrate or the District Magistrate or any officer authorized by the Chief Metropolitan Magistrate or District Magistrate.
- ❖ On such request being made the Chief Metropolitan Magistrate or the District Magistrate or authorized officer, as the case may be, shall take possession of the security asset and documents relating thereto and forward such asset and documents to the secured creditor. DM/CMM/ authorized officer has to pass order for taking possession of the secured assets within 30 days

Manner and Effect of Take Over of Management

- ❖ When the secured creditor/Asset Reconstruction Company takes over the management of business of a borrower, he may publish a notice in a newspaper published in the English language and in a newspaper published in an Indian language in circulation in the place where the principal office of the borrower is situated.
- ❖ On publication of such a notice, the directors of the company, immediately before the publication of the notice, shall be deemed to have vacated their offices. As an effect of this, any management contract between the borrower and any directors or manager thereof shall be deemed to be terminated.
- ❖ On publication of the above said notice and then after the appointments of directors or administrators as stated above, all the property and effects of the business of borrower are

deemed to be in the custody of the directors or the administrators so appointed, as the case may be. They are empowered to take such steps as may be necessary to take into their custody or under their control all the property, effect and actionable claims to which the borrower is entitled.

Where the management of the business of a borrower which is a company as defined in the Companies Act, 1956, is taken over by the secured creditor, then following effects shall apply:

- ❖ The shareholders of the company can not lawfully appoint any person to be a director of the company.
- ❖ No resolution passed by the shareholders of the company shall be given effect to, unless approved by the secured creditor.
- ❖ No proceeding for the winding up of such company or for the appointment of a receiver for the company shall lie in any Court, except with the consent of the secured creditor.

Application against Measures to Recover Secured Debt

Any person, including the borrower, aggrieved by any of the measures taken by the secured creditor or his authorized officer for taking possession of the security may make an application along with the prescribed fees, to the Debts Recovery Tribunal having jurisdiction within forty-five days from the date on which such measures are taken.

If the Debts Recovery Tribunal declares the recourse taken by a secured creditor, is not in accordance with the provisions of this Act. person, it may, by order,

- ❖ Declare the recourse to any one or more measures taken by the secured creditor as invalid
- ❖ Restore the possession of secured assets or management of secured assets to the borrower; and
- ❖ Pass such other direction as it may consider appropriate and necessary in relation to any of the recourse taken by the secured creditor.

The Debts Recovery Tribunal has to dispose of the application, in accordance with the provisions of the recovery of debts due to Banks and Financial Institutions Act. The application has to be disposed of as early as possible, but within sixty days.

The delay should not be beyond four months from the date of filing of the application. If any such application is not disposed of within four months, the aggrieved party can prefer an application to the Appellate Tribunal for seeking directions for the early disposal of the application.

Appeal to Appellate Authority

- ❖ Any person aggrieved by any order made by the debts recovery tribunal can prefer an appeal along with the prescribed fees to the Appellate Tribunal within thirty days from the date of receipt of the order of debts recovery tribunal.

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- ❖ No appeal can lie unless the borrower deposits fifty per cent of the debt claimed by the secured creditor. The tribunal has powers for reasons to be recorded, to reduce this amount to twenty-five per cent of the claim amount

Right of the Borrower for Compensation and Costs

If the debt recovery tribunal or the appellate tribunal

- ❖ Holds that the possession of secured asset by the secured creditor is not in accordance with the provisions of the Act or Rules framed thereunder and
- ❖ Directs the secured creditor or any other aggrieved person, who has filed the application or appeal, to return the secured asset to the borrower, then such borrower shall be entitled to payment of such compensation and costs as may be determined by the tribunal or the appellate tribunal.

No pecuniary limit is fixed by the Act for filing application under Section 17 or filing appeal under Section 18. Therefore, application before DRT and appeal before the DRAT against the actions initiated by the secured creditors under Section 13(4), would be normally accepted in all legally valid cases irrespective of amount. CAIIB Paper 4 (BRBL) Module C Unit 7-Central Registry

Unit 17E : Central Registry

- ❖ Under the SARFEASI Act, there is a provision for the establishment of a Central Registry under Section 20 of the Act.
- ❖ The Central Government may, by notification, set up or cause to be set up from such date as it may specify in such notification, a registry to be known as the Central Registry with its own seal for the purposes of registration of transaction of securitization and reconstruction of financial assets and creation of security interest under this Act.
- ❖ The head office of the Central Registry shall be at such place as the Central Government may specify.
- ❖ The Central Government may, by notification, define the territorial limits within which an office of the Central Registry may exercise its functions.

The objective of setting up of Central Registry is to prevent frauds in loan cases involving multiple lending from different banks on the same immovable property. The Registry has become operational on March 31, 2011.

Transactions/charges required to be mandatorily registered by banks and financial institutions are:

- ❖ All particulars of creation, modification or satisfaction of security interest in respect of equitable mortgages created
- ❖ All particulars of creation, modification or satisfaction of security interest other than mortgage by deposit of title deed.
- ❖ All particulars of creation, modification or satisfaction of security interest in hypothecation of Plant & Machinery, stock, book debts whether existing or future
- ❖ All particulars creation, modification or satisfaction of security interest in intangible assets being know how, copy rights, trade marks, etc. or similar nature.
 - The charges will be effective from the date of registration of charge with CERSAI.
 - Creditors other than secured creditors are not eligible to exercise right of enforcement of securities under this Act.
 - Any person having order of attachment against the borrower shall file such order with Central registry. Such registration will be deemed to be public notice from the date of filing with the Central Registry.
 - No secured creditor shall be allowed to exercise right of enforcement of securities unless the security interest created has been registered with the Central Registry.
 - Secured creditor and creditors holding order of attachment shall have priority over all subsequent security interest created upon such property and any transfer by way of sale, lease or assignment or license of such property or attachment order subsequent to such registration.

Register of Securitisation, Reconstruction and Security Interest Transactions

A record shall be maintained at the central registrar at the head office of the central registrar in which transactions relating to:

- ❖ Securitization of financial assets
- ❖ Reconstruction of financial assets,
- ❖ Creation of security interests shall be maintained.

In terms of Section 22 of the SARFEASI Act 2002 The record of central registrar can be kept fully or partly on computer, floppies, diskettes, or any other electronic form. Any entry made with the central registrar shall be a reference to any such transaction.

Filing of Transactions of Securitisation, Reconstruction and Creation of Security Interest

- ❖ As per Section 23 of the SARFEASI Act 2002 (1)] the particulars of every transaction of securitization, asset reconstruction or creation of security interest shall be filed, with the Central Registrar in the manner and on payment of such fee as may be prescribed.
- ❖ The Central Government may, by notification, require the registration of transaction relating to different types of security interest created on different kinds of property with the Central Registry.
- ❖ The Central Government may, by rules, prescribe forms for registration for different types of security interest under this section and fee to be charged for such registration.

Satisfaction of Security Interest

- ❖ The asset reconstruction company or the secured creditors, shall give intimation to the Central Registrar of the payment or satisfaction in full, of any security interest relating to the asset reconstruction company or the secured creditors and requiring registration within thirty days from the date of such payment or satisfaction.
 - ❖ On receipt of intimation under sub-section (1), the Central Registrar shall order that a memorandum of satisfaction shall be entered in the Central Register.
 - ❖ If the concerned borrower gives an intimation to the Central Registrar for not recording the payment or satisfaction.
 - ❖ If no cause is shown, the Central Registrar shall order that a memorandum of satisfaction shall be entered in the Central Register.
 - ❖ If cause is shown, the Central Registrar shall record a note to that effect in the Central Register, and shall inform the borrower that he has done so.
 - ❖ The particulars of securitization or reconstruction or security interest entered in the central register are open for inspection by any person during office hours on payment of fees as may be prescribed. Same is applicable if the data is kept in the electronic form at the office of the central registrar.
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Unit 17F : Offences and Penalties

Penalties

- ❖ Section 23 of the Act provides for filing of the particulars of charge created. Section 24 provides for modification of the charge filed and the Section 25 provides that the satisfaction of the charge has to be intimated to the central registrar.
- ❖ If the securitization or reconstruction company or the secured creditor fails to perform any of the duties as stated above, the company and the officers concerned for the default, as per provisions of this section, are punishable with a fine that may extend to five thousand rupees for each day during which the default continues.
- ❖ These provisions were existing before amendment to the Act carried out in 2016 and have since been omitted.

Penalties for Non-compliance of Directions of Reserve Bank of India

- ❖ Under the Section 12 or 12A of the SARFAESI Act, the Reserve Bank of India is statutorily empowered to issue directions to the securitization or reconstruction company. If any such company fails to comply with any of the directions issued by the Reserve Bank of India, then such company is punishable with a fine not exceeding Rs. 5 lakh for the default. In case of further continuation of the offence, an additional fine up to Rs. 10,000 per day of the default can be imposed.
- ❖ These provisions were existing before amendment to the Act carried out in 2016 and have since been omitted.

Offences

If any person:

- ❖ Contravenes, or
- ❖ Attempts to contravene, or
- ❖ Abets the contravention

of the provisions of the SARFAESI Act or rules made there under, he shall be punishable with imprisonment for a term, which may extend to one year or with a fine or both.

The Act has made various provisions where duties are cast on the borrower, the secured creditor, the securitization and the reconstruction company.

Cognizance of Offences

- ❖ Section 30 provides that no court shall take cognizance of any offence punishable under section 27 in relation to non-compliance with the provisions of section 23, section 24 or section 25 or under section 28 or section 29 or any other provisions of the SARFAESI Act, except upon a complaint in writing made by an officer of the Central Registry or an officer of the Reserve Bank, generally or specially authorized in writing in this behalf.

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- ❖ Cognizance of the offence under the SARFAESI Act shall be taken by the Metropolitan Magistrate or the Judicial Magistrate of First Class only. No Court below the rank than this can take cognizance of such offences.

Power of Adjudicating Authority to Impose Penalty/Appeals

Where any asset reconstruction company or any person fails to comply with any direction issued by the Reserve Bank under this Act the adjudicating authority may, by an order, impose on such company or person in default, a penalty not exceeding one crore rupees or twice the amount involved in such failure where such amount is quantifiable, whichever is more, and where such failure is a continuing one, a further penalty which may extend to one lakh rupees for every day, after the first, during which such failure continues.

- ❖ Any penalty imposed under this section shall be payable within a period of thirty days from the date of issue of notice under sub-section (2).
- ❖ Where the asset reconstruction company fails to pay the penalty within the specified period under sub-section (3), the adjudicating authority shall, by an order, cancel its registration: Provided that an opportunity of being heard shall be given to such asset reconstruction company before cancellation of registration.
- ❖ No complaint shall be filed against any person in default in any court pertaining to any failure under sub-section (1) in respect of which any penalty has been imposed and recovered by the Reserve Bank under this section.
- ❖ Section 30B lays down the law for appealing against the decision of an adjudicating authority and states "A person in default, aggrieved by an order passed under sub-section (4) of section 30A, may, within a period of thirty days from the date on which such order is passed, prefer an appeal to the Appellate Authority: Provided that the Appellate Authority may entertain an appeal after the expiry of the said period of thirty days, if it is satisfied that there was sufficient cause for not filing it within such period."
- ❖ Section 30C identifies and defines the power of the appellant authority.
- ❖ Section 30D deals with 'recovery of penalties' Any penalty imposed under section 30A shall be payable within a period of thirty days from the date on which notice demanding payment of the recoverable sum is served upon the person in default and, in the case of failure of payment by such person within such period, the Reserve Bank may, for the purpose of recovery-
 - Debit the current account, if any, of the person in default maintained with the Reserve Bank or by liquidating the securities, if any, held to the credit of such person in the books of the Reserve Bank
 - Issue a notice to the person from whom any amount is due to the person in default, requiring such person to deduct from the amount payable by him to the person in default, such amount equivalent to the amount of the recoverable sum, and to make payment of such amount to the Reserve Bank. CAIIB Paper 4 (BRBL) Module C Unit 9-Miscellaneous Provisions.

Unit 17G : Miscellaneous Provisions

Non-applicability of the Provisions of the SARFAESI Act in Certain Cases

Section 31 gives the details of excluded securities to which the Act is not applicable.

- ❖ A lien, on any goods, money or security given by or under the Indian Contract Act, 1872 or the Sale of Goods Act, 1930
- ❖ A pledge of movable goods, within the meaning of Section 172 of the Indian Contract Act, 1872.
- ❖ Creation of security interest in any vessel as defined within the meaning of Section 3(55) of the Merchant Shipping Act, 1958.
- ❖ Any conditional sale, hire-purchase or lease or any other contract in which no security interest has been created.
- ❖ Any rights of unpaid seller under Section 47 of the Sale of Goods Act, 1930.
- ❖ Any properties not liable for attachment or sale under the first proviso to Section 60(1) of the Civil Procedure Code, 1908.
- ❖ Any security interest for securing repayment of any financial asset not exceeding one lakh rupees.
- ❖ Any security interest created in agricultural land.
- ❖ Any case, in which the amount due is less than twenty per cent of the principal amount and interest thereunder.

Protection of Action Taken in Good Faith

- ❖ The Reserve Bank or the Central Registry or any secured creditor or any of its officers are protected for actions taken in good faith by the provisions made in the Act. For actions taken or initiated under the Act no suit, prosecution or any other legal proceeding can be taken against the Reserve Bank or the Central Registry or any secured creditor or any of its officers.
- ❖ This protection is given so that actions contemplated and authorized under SARFAESI Act, can be taken without fear of counteraction from the borrower or any other person having interest in the property.

Offences by Companies

- ❖ As per Section 33 of the Act If a company and its officers commit any offence under the provisions of the SARFAESI Act the same is punishable.
- ❖ If any offence is committed under the provisions of this Act by a company, such company, as well as any person who is in charge of the business of the company, are deemed to be guilty of the offence and they are liable to be prosecuted and punished. It is permissible for a person acting for the company to prove that the offence was committed without his knowledge or that he had exercised due diligence to prevent the commission of such offence. In such cases and on proving his stand the person concerned shall not be punishable.

- ❖ If such offence is committed with the consent or connivance of any director or officer of the company, such director or officer shall be deemed to be guilty for the offences along with the company.
- ❖ The penal provisions are applicable to all categories of borrowers such as individuals, partnership firms, companies incorporated under the Companies Act or any other association of individuals.

Civil Court not to have Jurisdiction

- ❖ The SARFAESI Act has conferred jurisdiction on many matters to the debts recovery tribunal or the appellate tribunal. Therefore, for any such matters where empowerment and jurisdiction is given or vested with the debts recovery tribunal or the appellate tribunal, no Civil Court shall have jurisdiction to entertain any suit or proceedings relating to those matters.
- ❖ Similarly, any Court or authority cannot grant injunction in such matters and actions taken, or to be taken, under this Act as well as under Recovery of Debts Due to Banks and Financial Institutions Act, 1993.

Limitation

- ❖ The actions that secured creditor can take against the security under the SARFAESI Act are required to be taken within the limitation period as prescribed by the provisions of the Limitation Act (Section 36 of the SARFESAI Act.).
- ❖ That means, the action has to be taken within three years or twelve years as the case may be, from the date on which the cause of action arose.
- ❖ All secured creditors are required to take measures such as taking possession of the securities, provided their claim is within the period of limitation. It will be necessary for the banks and financial institutions to comply with the limitation aspect. If after sale of securities the claim is not fully satisfied and still there are any dues to be recovered from the borrower, the creditor is required to file civil suit before the Civil Court or a claim before the debt recovery tribunal within the limitation period.

Power of the Central Government to Make Rules

- ❖ For carrying out the provisions of this Act, the Central Government can frame rules and notify them in the Official Gazette. The Act also allows the Government to notify the rules in the Electronic Gazette as defined in the Information Technology Act, 2000, i.e. on the website of the Government.
- ❖ Whenever the Government makes a rule under the Act, the rule is required to be kept before each House of Parliament, while in session for a total period of thirty days. Both the Houses should agree to the rules as framed and they can make modifications therein. The rule gets the validity in the manner as decided by both the Houses.

Unit 17H : Registration of Security Interest by Secured Creditors and Other Creditors/Rectification by Central Government in Some Cases

Right of Enforcement of Securities

- ❖ Section 26D makes it compulsory for security interest to be registered with the Central Registry for it to be enforced.
- ❖ After the registration of security interest, the debts due to any secured creditor shall be paid in priority over all other debts and all revenues, taxes, cesses and other rates payable to the Central Government or State Government or local authority.

Rectification by Central Government in Matters of Registration

Sections 26A of the SARFEASI Act deals with the powers given under the statute to the Central Government to condone and set right omissions/errors in filing of creation /modification/satisfaction of charges, mandatorily required to be carried out.

- ❖ The Central Government, on being satisfied that the omission to file with the Registrar the particulars of any transaction of securitization, asset reconstruction or security interest or modification or satisfaction of such transaction was accidental or due to inadvertence or some other sufficient cause or it is not of a nature to prejudice the position of creditors.
- ❖ That on other grounds, it is just and equitable to grant relief, may, on the application of a secured creditor or asset reconstruction company or any other person interested on such terms and conditions as it may seem to the Central Government, just and expedient, direct that the time for filing of the particulars of the transaction for registration or modification or satisfaction shall be extended or, as the case may require, the omission or misstatement shall be rectified.
- ❖ Where the Central Government extends the time for the registration of transaction of security interest or securitization or asset reconstruction or modification or satisfaction thereof, the order shall not prejudice any rights acquired in respect of the property concerned or financial asset before the transaction is actually registered.

Effect of the Registration of Transactions

- ❖ The legal impact of registration of a charge with the Central Registry is detailed in Section 26C.
- ❖ As per Section 26C, Without prejudice to the provisions contained in any other law, for the time being in force, any registration of transactions of creation, modification or satisfaction of security interest by a secured creditor or other creditor or filing of attachment orders shall be deemed to constitute a public notice from the date and time of filing of particulars of such transaction with the Central Registry
- ❖ Where security interest or attachment order upon any property in favor of the secured creditor or any other creditor are filed for the purpose of registration under the provisions this Act, the claim of such secured creditor or other creditor holding attachment order shall have priority over any subsequent security interest created upon such property and any transfer by way of sale, lease or assignment or license of such property or attachment order subsequent to such registration.

Unit 18A : The Recovery of Debts and Bankruptcy Act, 1993

Introduction

- ❖ In 1991, the Recovery of Debts due to Banks and Financial Institutions Act, 1993 (DRT Act, as commonly known or called) was passed and it came into operation from 24 June 1993. This Act constituted the special, 'Debt Recovery Tribunals' for speedy recovery.
- ❖ Later in 2019 the name of the Act as stated above was changed to 'The Recovery of Debts and Bankruptcy Act, 1993' to also cater to insolvency resolution and bankruptcy of individuals and partnership firms.

Extent, Commencement, Application

- ❖ The Act is now applicable to the whole of India. and came into force on the 24th day of June, 1993.
- ❖ In terms of Section 1(4) of the Act , the provisions of this Act shall not apply where the amount of debt due to any bank or financial institution or to a consortium of banks or financial institutions is less than ten lakh rupees. However, the Government later raised the limit from Rs. 10 lacs to 20 lacs.

Important Definitions

- ❖ **Appellate Tribunal:** It is a body established for the purpose of preferring an appeal against the order passed by the tribunal. It is established under the sub-Section (1) of Section 8 of the Act.
 - ❖ **Chairperson:** means a chairperson of an appellate tribunal appointed under Section 9.
 - ❖ **Presiding Officer:** means the presiding officer of the Debts Recovery Tribunal appointed under sub-Section (1) of Section 4.
 - ❖ **Recovery Officer:** means a recovery officer appointed by the Central Government for each tribunal under the sub-Section (1) of Section 7. These officers are appointed under the Act for implementing the recovery orders passed by the Tribunal.
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Unit 18B : Establishment of Tribunal and Appellate Tribunal

Establishment of Tribunal

- ❖ The Central Government is empowered to establish tribunal, under Section 3 of the statute, to be known as Debt Recovery Tribunal to exercise the jurisdiction, powers and authority conferred on such tribunal by or under this Act.
- ❖ This section also empowers the Central Government to decide and specify the areas within which the tribunal may exercise jurisdiction for entertaining and deciding the applications filed before it. When the Government exercises these powers and takes such decisions they are notified in the Official Gazette of the Government.
- ❖ In terms of amendment to Section 3 of the Act in 2016 by adding sub-section 1(A), The Central Government shall by notification establish such number of Debts Recovery Tribunals and its benches as it may consider necessary, to exercise the jurisdiction, powers and authority of the Adjudicating Authority conferred on such Tribunal by or under the Insolvency and Bankruptcy Code, 2016.

Composition Of Tribunal

- ❖ The tribunal is made up of only one person called 'Presiding Officer' and the appointment is done by the Central Government by issuing a notification.
- ❖ The Central Government, by notification, has the powers to authorize the presiding officer of one tribunal to discharge also the functions of the presiding officer of another tribunal.

Qualification For Appointment As Presiding Officer And Term Of Office

- ❖ A person is qualified for appointment as presiding officer of a tribunal if he is, or has been, or is qualified to be appointed as a District Judge.
- ❖ The presiding officer of a tribunal holds office for a term of five years from the date on which he enters upon his office or until he attains the age of sixty-five years, whichever is earlier. (Section 6).

Note: The Central Government shall provide the tribunal with one or more recovery officer and such other officers and employees as the Government may think fit. The staff so appointed shall work under the general superintendence of the presiding officer. (Section 7)

Establishment and Composition of Appellate Tribunal

- ❖ The Central Government is empowered to establish one or more appellate tribunals, to be known as 'Debt Recovery Appellate Tribunal' to exercise the jurisdiction, powers and authority conferred on such tribunal by or under this Act. The Central Government is also empowered to decide and specify the areas within which the tribunal may exercise jurisdiction for entertaining and deciding the applications filed before it.

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- ❖ Appellate tribunal consists of only one person called as Chairperson and the appointment shall be done by the Central Government.
 - ❖ For administrative convenience, the Central Government has the powers to authorize the chairperson of one appellate tribunal to discharge also the functions of the chairperson of another appellate tribunal.

Qualifications for Appointment as Chairperson of the Appellate Tribunal and Term of Office

As per Section 10 of the Act a person shall not be qualified for appointment as the chairperson of an appellate tribunal unless he:

- ❖ Is, or has been, or is qualified to be a Judge of a High Court
- ❖ Has been a member of the Indian legal service and has held a post in Grade of that service for at least three years; or
- ❖ Has held office as the presiding officer of a tribunal for at least three years.
- ❖ The chairperson of an appellate tribunal shall hold office for a term of five years from the date on which he enters upon his office or until he attains the age of seventy years, whichever is earlier.

Finality of Orders Constituting Tribunal or an Appellate Tribunal

- ❖ No order of the Central Government appointing any person as the presiding officer of the tribunal or the chairperson of the appellate tribunal shall be called in question in any manner.
 - ❖ Presiding officer or chairperson can, by a three months written notice, resign his office. They cannot be removed, except by an order of the Central Government, on the ground of proved misbehavior or incapacity after inquiry.
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Unit 18C : Jurisdiction, Powers & Authority of Tribunals

Jurisdiction, Powers and Authority of Tribunals

- ❖ Whenever the Tribunal or the Appellate Tribunal is established from its appointed day, they exercise jurisdiction, powers and authority to entertain and decide applications or appeals, from the banks and financial institutions for recovery of debts due to them including deciding on applications under Part III of Insolvency and Bankruptcy Code, 2016.
- ❖ Chairperson of Appellate Tribunal is given general power of superintendence and control over the Tribunals under his jurisdiction. The chairperson can transfer any application from any Presiding Officer within his jurisdiction to any other Presiding Officer within his jurisdiction, on receiving application for transfer of case or even on his own motion. However before such transfer, he has to give notice to the parties and hear them. He also has power of appraising work of presiding officers, under his control - Section 17A (i).

As per Section 17A, for the purpose of exercise of general powers of superintendence and control over Tribunals under sub-section (1), the Chairperson may :

- ❖ Direct the Tribunals to furnish, in such form, at such intervals and within such time, information relating to pending cases both under this Act and the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (54 of 2002), number of cases disposed of, number of new cases filed.
- ❖ Convene meetings of the Presiding Officers of Tribunals periodically to review their performance.
- ❖ Where on assessment of the performance of any Presiding Officer of the Tribunal or otherwise, the Chairperson is of the opinion that an inquiry is required to be initiated against such Presiding Officer for misbehavior or incapacity, he shall submit a report to the Central Government recommending action against such Presiding Officer, and for reasons to be recorded in writing for the same.

Bar of Jurisdiction of Civil Courts

- ❖ From the date of establishing the Tribunal, i.e., the appointed day, no court or other authority shall have any jurisdiction, powers or authority to deal with cases i.e. claims of banks and financial institutions for recovery of Rs. 20 lakh and above. However, this is not applicable to High Courts and Supreme Courts exercising jurisdiction under Articles 226 and 227 of the Constitution.
 - ❖ The relevant date of bar of jurisdiction by the court or other authority is not the date when this Act came into application. The date is, since when the Tribunal is established having jurisdiction in that particular area. Order passed by the Civil Court, prior to establishment of a Tribunal but after commencement of DRT Act, was well within the jurisdiction of the Civil Court.
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Unit 18D : Procedure of Tribunals

- ❖ The institution can, with the DRT's permission, withdraw the application to take action under the SARFAESI Act 2002 (Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act).
- ❖ The DRT must process withdrawal applications promptly, ideally within 30 days from the date of application.
- ❖ Refusals require recorded justifications.
- ❖ Certain multi-state co-operative banks have the option to initiate debt recovery proceedings under the Multi-State Co-operative Societies Act, 2002, instead of the DRT route.
- ❖ If a bank or financial institution files an application under Section 19(1) for debt recovery, another bank or financial institution can join the proceedings at any stage before the final order by making an application.
- ❖ Applications filed under Sections 19(1) or 19(2) must comply with prescribed forms, documents, evidence, and fees.
- ❖ Upon receiving the application, the tribunal issues summons to the defendant with directions:
 - ❖ Show cause within thirty days of summons service as to why the relief should not be granted.
 - ❖ Disclose details of properties or assets not specified by the applicant.
 - ❖ The defendant, upon receiving the summons, cannot transfer assets with security interest or those disclosed without Tribunal approval.
- ❖ Sale proceeds from secured assets must be deposited into the account of the bank or financial institution holding security interest.
- ❖ Section 5(i) The defendant must present a written statement of defence within thirty days of summons service, including any claim for set-off or counter-claim.
- ❖ Hearing for admission or denial of documents produced by parties is done under sub-section 5A.
- ❖ If a defendant admits a debt, they are ordered to pay within 30 days.
- ❖ Failure to comply may result in the Tribunal issuing a recovery certificate for the admitted debt amount.
- ❖ Tribunals can issue conditional attachment orders on properties, wholly or partially, as necessary.
- ❖ Attachment orders must comply with the requirements stated in Sub-Section 13.
- ❖ Failure to do so renders the order void.
- ❖ Breach of tribunal orders may result in property attachment and civil detention for up to three months.
- ❖ Tribunals can appoint receivers, remove property custodians, and confer various property management powers to ensure debt recovery.
- ❖ Recovery Certificate and Amendments (Section 19(22) and (22A)): The Presiding Officer issues a recovery certificate for debt payment. These certificates are considered as court orders for various legal proceedings.

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- ❖ Affidavits may be accepted as evidence; witness cross-examination is only required if deemed necessary by the tribunal.
 - ❖ Property transfers violating court injunctions are considered void and confer no rights or interests.
 - ❖ Anyone affected by a Tribunal's order or a deemed order under the DRT Act has the right to appeal. Appeal to Appellate Tribunal allowed unless the original order was made with the parties' consent Within 30 days of receiving the order.
 - ❖ Strives to resolve the appeal within six months from the receipt of the appeal.
 - ❖ Writ Petition to High Court: Under Article 226, and supervisory jurisdiction of High Court under Article 227.
 - ❖ Defendant, subject to a recovery order by the Debt Recovery Tribunal, requires depositing 50% of the determined amount for an appeal to the Appellate Tribunal.
 - ❖ Tribunal holds the discretion to decrease or waive the payment, but not below 25% of the determined amount, with a written rationale.
 - ❖ The Tribunal and the Appellate Tribunal are deemed to hold the status of a Civil Court in accordance with Section 195 and Chapter XXVI of the Code of Criminal Procedure, 1973.
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Unit 18E : Recovery of Debts Determined by Tribunal and Miscellaneous Provisions

Modes of Recovery of Debts

As per Section 25 of the Act, on receipt of the copy of the recovery certificate issued under Section 19(22), the Recovery Officer has to proceed to recover the amount specified in the certificate by one or more of the following modes:-

- ❖ Attachment and sale of movable and immovable property of the defendants.
- ❖ Arrest of the defendant and his detention in prison.
- ❖ Appointment of a receiver for the management of the movable and immovable properties of the defendant.
- ❖ Taking possession of property over which security interest is created or any other property of the defendant and appointing receiver for such property and to sell the same; (Section 25 aa).
- ❖ Any other mode of recovery as may be prescribed by the Central Government. (Section 25d).

Validity of Recovery Certificate and Amendment Thereof

- ❖ The defendant is debarred from raising any dispute before the Recovery Officer about the correctness of the amount specified in the recovery certificate issued by the Tribunal.
- ❖ The Presiding Officer of the Tribunal who had issued the recovery certificate is authorized to withdraw the certificate or correct any clerical or mathematical error in the certificate.
- ❖ When any party wants to have a review of the order passed by the Tribunal or the recovery certificate issued by the Tribunal on the ground that error is apparent on the face of the record, he can make application for review within sixty days of passing the order or issuing the certificate. Such application needs to be supported by affidavit verifying the contents. It is also required that the opposite party is given notice and hearing before the application is granted.

Stay of Proceedings Under Certificate and Amendment or Withdrawal

As per Section 27 of the Act

- ❖ Notwithstanding that a certificate has been issued to the Recovery Officer for the recovery of any amount, the Presiding Officer, may by an order, grant time for payment of the amount, provided the defendant makes a down payment of not less than twenty-five per cent. of the amount specified in the recovery certificate and gives an unconditional undertaking to pay the balance within a reasonable time, which is acceptable to the applicant bank or financial institution holding recovery certificate.
- ❖ (1A) The Recovery Officer shall, after receipt of the order passed under sub-section (1), stay the proceedings until the expiry of the time so granted.
- ❖ (1B) Where defendant agrees to pay 1B the amount specified in the Recovery Certificate and proceeding are stayed by the Recovery Officer, the defendant shall forfeit right to file appeal against the orders of the Tribunal.

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- ❖ (1C) Where the defendant commits any default in payment of the amount under sub-section (1), the stay of recovery proceedings shall stand withdrawn and the Recovery Officer shall take steps for recovery of remaining amount of debt due and payable.
 - ❖ Where a certificate for the recovery of amount has been issued, the Presiding Officer shall keep the Recovery Officer informed of any amount paid or time granted for payment, subsequent to the issue of such certificate to the Recovery Officer.

Application of Certain Provisions of The Income Tax Act

- ❖ Provisions of Section 29 of this Act are linked to certain sections of the Income Tax Act, 1961.
- ❖ For its effective purpose and to avoid its repetition in this Act, it is stated that these provisions will apply as if provided in this Act and Rules framed there under. This also makes it possible that any amendment made in the Income Tax Act to those provisions will automatically become applicable for this Act without there being requirement to amend this Act.
- ❖ Due to this provision the debt due from the defendant to the bank or financial institution is treated on par with Income Tax arrears and can be recovered like the arrears under the income tax.

Appeal against the Order of Recovery Officer

- ❖ The Recovery Officer is given powers under Sections 25 and 28 to recover the amount mentioned in the recovery certificate. As per Section 26, the defendant cannot question or dispute before the Recovery Officer about the correctness of the amount mentioned in the recovery certificate.
- ❖ When the Recovery Officer attaches and sells the property it is possible that the third party having any interest in such property may get affected. Therefore, Section 30 provides that any person aggrieved by the order of Recovery Officer may appeal within thirty days to the Tribunal. The period of thirty days is to be counted from the date on which a copy of the order is issued to him. On receipt of the appeal, the Tribunal has to hear the appellant and make enquiries as it deems fit. Thereafter the order of the Recovery Officer may be either confirmed or modified or set aside.

Transfer of Pending Cases

- ❖ As per Section 31: Every suit or other proceeding pending before any court immediately before the date of establishment of a Tribunal under this Act, being a suit or proceeding the cause of action, if it had arisen after such establishment, within the jurisdiction of such Tribunal, shall stand transferred on that date to such Tribunal.
- ❖ Provided further that any recovery proceedings in relation to the recovery of debts due to any multi-State co-operative bank pending before the date of commencement of the Enforcement of Security Interest and Recovery of Debts Laws (Amendment) Act, 2012 under the Multi-State Co-operative Societies Act, 2002, shall be continued and nothing contained in this section shall apply to such proceedings.

Where any suit or other proceeding stands transferred from any court to a Tribunal under sub-section (1) :

- ❖ ✓ The court shall, as soon as may be after such transfer, forward the records of such suit or other proceeding to the Tribunal; and
- ❖ ✓ The Tribunal may, on receipt of such records, proceed to deal with such suit or other proceeding, in the same manner as in the case of an application made under section 19 from the stage which was reached before such transfer or from any earlier stage as the Tribunal may deem fit.

Power of Tribunal to Issue Certificate of Recovery in Case of Decree or Order

If there is a decree or order passed by any court before coming into operation the DRT Act and the decree or order is not yet executed, the decree-holder may apply to the Tribunal for issue of recovery certificate. There is no fresh hearing or trial, etc., in such cases and the tribunal has to directly issue the recovery certificate based on the decree of the Civil Court.

Chairperson, Presiding Officer and Staff of Appellate Tribunal

The Chairperson of an Appellate Tribunal, the Presiding Officer of a tribunal, the Recovery Officer and other officers of the Appellate Tribunal and Tribunal are deemed public servants within the meaning of Section 21 of the Indian Penal Code. (Section 32).

Protection of Action Taken in Good Faith (Section 33)

When anything is done in good faith under this Act or is intended to be done so, no suit, prosecution or other proceeding shall lie against the Central Government, the Presiding Officer of a Tribunal or the Chairperson of an Appellate Tribunal or against the Recovery Officer.

Overriding Effect of the Act

- ❖ As per Section 34 of the Act: the provisions of this Act shall have effect notwithstanding anything inconsistent therewith contained in any other law for the time being in force or in any instrument having effect by virtue of any law other than this Act.
- ❖ DRT proceedings cannot be stayed by Company Court nor can proceedings be transferred to Company Court.
- ❖ DRT Act overrides the Companies Act and, therefore, leave of the company court is not necessary even if the company is under winding up proceedings.
- ❖ Moneys realized under DRT Act, distribution between bank and other secured creditors, when winding up proceedings are pending in company court, priority of secured creditors is subject to provisions of 529A of Companies Act.
- ❖ In respect of moneys realized under DRT Act out of the assets not charged, distribution between Bank/ FIs and other creditors, when no winding up order is passed against the company, the priorities have to be decided subject to principles underlying Section 73 of CPC and principles of natural justice.

Unit 19 : Introduction to the Insolvency and Bankruptcy Code, 2016

Introduction

- ❖ Recognizing that reforms in the bankruptcy and insolvency regime are critical for improving the business environment and alleviating distressed credit markets, the Insolvency and Bankruptcy Code Bill (IBC) was enacted by the Government and the same came into force in December 2016.
- ❖ After its enactment, the statute has been amended a few times with the latest amendment being through the Insolvency and Bankruptcy (Amendment) Act, 2021 which come into force on the 4th of April, 2021.

Pillars of IBC, 2016

Insolvency Professionals

- ❖ The primary duty of the Insolvency Professionals (IPs) is to assist in the completion of insolvency resolution, liquidation and bankruptcy proceedings.
- ❖ Insolvency Professionals are regulated persons who maintain professional standards and code of ethics as first level regulators.
- ❖ The Limited Insolvency Examination is one of the mandatory conditions of getting registered as an Insolvency Professional with IBBI.
- ❖ “Insolvency professional agency” means any person registered with the Board under section 201 as an insolvency professional agency (Section 3(20)).

Information Utilities

- ❖ Information Utilities’ would collect, collate, authenticate and disseminate financial information.
- ❖ They would also maintain electronic databases on lenders and terms of lending, thereby eliminating delays and disputes when a default actually takes place.
- ❖ Information Utility is defined in Section 3 (21) as “information utility” means a person who is registered with the Board as an information utility under section 210.

Adjudicating Authorities

- ❖ The adjudicating authorities under the Code are National Company Law Tribunal (NCLT) and Debt Recovery Tribunal (DRT).
- ❖ The NCLT is the forum where cases relating to insolvency of corporate persons (limited liability entities) will be heard, while DRTs are the forum for insolvency proceedings related to individuals and partnership firms.
- ❖ These institutions, along with their Appellate bodies, viz., the National Company Law Appellate Tribunal (NCLAT) and the Debt Recovery Appellate Tribunal (DRAT), respectively, will seek to achieve smooth functioning of the bankruptcy process.
- ❖ An appeal can be preferred on the orders of NCLT to National Company Law Appellate Tribunal (NCLAT) within 30 days (15 days’ extension if there is sufficient ground). Orders of NCLAT are

appealable within 45 days before the Supreme Court only on question of law. Civil Courts or any other authorities do not have jurisdiction and also cannot grant any injunction.

The Insolvency and Bankruptcy Board of India (IBBI)

This body has regulatory oversight over insolvency professionals, insolvency professional agencies and information utilities.

The Insolvency Resolution Process for Companies and Limited Liability Entities

If the default is above Rs. 1 Lakh (minimum amount of default has been increased to Rs. 1 Cr by the Government, by a notification, with effect from 24th March 2020), the creditor may initiate insolvency resolution process.

The Code proposes two independent stages:

- ❖ Insolvency Resolution Process – during which financial creditors assess whether the debtor's business is viable to continue and the options for its rescue and resurrection.
- ❖ Liquidation– if the insolvency resolution process fails or financial creditors decide to wind down and distribute the assets of the debtor.

Initiation of Corporate Insolvency Resolution Process (CIRP)

- ❖ The initiation of Corporate Insolvency Resolution Process (CIRP) by a Financial Creditor is provided in Section 7 of the IBC.
- ❖ As per Section 7 (1): A financial creditor either by itself or jointly with other financial creditors, or any other person on behalf of the financial creditor, as may be notified by the Central Government may file an application for initiating corporate insolvency resolution process against a corporate debtor before the Adjudicating Authority when a default has occurred.
- ❖ An application for initiation corporate insolvency resolution process against the corporate debtor shall be filed jointly by not less than one hundred of such creditors in the same class or not less than ten per cent. of the total number of such creditors in the same class, whichever is less.

Time-limit for Completion of Insolvency Resolution Process

- ❖ As per Section 12, the corporate insolvency resolution process shall be completed within a period of 180 days from the date of admission of the application to initiate such process.
- ❖ The resolution professional shall file an application to the Adjudicating Authority to extend the period of the corporate insolvency resolution process beyond 180 days, if instructed to do so by a resolution passed at a meeting of the committee of creditors by a vote of sixty-six percent of the voting shares.
- ❖ On receipt of an application, if the Adjudicating Authority is satisfied that the subject matter of the case is such that corporate insolvency resolution process cannot be completed within 180 days, it may by order extend the duration, but not exceeding ninety days.

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- ❖ Provided further that the corporate insolvency resolution process shall mandatorily be completed within a period of 330 days from the insolvency commencement date.

Appointment of Resolution Professional

As per Section 22 which deals with the appointment of a 'Resolution Professional'

- ❖ The first meeting of the committee of creditors shall be held within seven days of the constitution of the committee of creditors.
- ❖ The committee of creditors, may, in the first meeting, by a majority vote of not less than 66% of the voting share of the financial creditors, either resolve to appoint the interim resolution professional as a resolution professional or to replace the interim resolution professional by another resolution professional.

Liquidation

In liquidation proceedings, the Code provides secured creditors the right to choose between

- ❖ Enforcing /realizing/settling/compromising/dealing with their security interests and applying the proceeds to recover the debts due to it, or
- ❖ Relinquishing rights on these assets to the liquidation trust and receiving the proceeds obtained from the liquidator's sale of assets.

The commencement of liquidation process takes place on account of:

- ❖ Failure to submit the resolution plan to the NCLT within the prescribed period, or
- ❖ Rejection of resolution plan for non-compliance with the requirements of the Code, or
- ❖ Decision of creditors' committee based on vote of majority, or
- ❖ Contravention of resolution plan by the debtor.

Liquidation Process

- ❖ During liquidation, no suit or other proceedings shall be instituted by or against the corporate debtor; except through the liquidator on behalf of corporate debtor with permission of the NCLT.
- ❖ The Resolution Professional shall act as liquidator unless replaced.
- ❖ The liquidator shall form an estate of all assets of corporate debtor called the liquidation estate.
- ❖ Liquidator shall receive, verify and admit or reject, as the case may be, the claims of creditors within the prescribed time. Creditor may appeal to the adjudicator within 14 days.
- ❖ Assets will be distributed by the liquidator in the manner of priorities of debts as laid down in Section 53 of the Code.
- ❖ All sums due to any workman or employee from the provident fund, the pension fund and the gratuity fund will be considered as priority dues and is not to be included in the liquidation estate and estate of bankrupt.
- ❖ Upon the assets of corporate debtor being completely liquidated and the liquidator making an application, the NCLT shall pass an order dissolving the corporate debtor.

Order of Priority of Payment of Debts

- ❖ Insolvency resolution cost and liquidation cost
- ❖ Workmen's dues (for 24 months before commencement) and debts to secured creditor (who have relinquished their security interest)
- ❖ Wages and unpaid dues to employees (other than workmen) (for 12 months before commencement)
- ❖ Financial debts to unsecured creditors and workmen's dues for earlier period
- ❖ Crown debts and debts to secured creditor following enforcement of security interest
- ❖ Remaining debts
- ❖ Preference shareholders
- ❖ Equity Shareholders or partners

Fast Track Insolvency Resolution Process

The Government of India has introduced a 'Pre- Packaged Insolvency Resolution Process'(Section 54 A) for MSME corporate debtors classified as such under sub-section (1) of section 7 of the Micro, Small and Medium Enterprises Development Act, 2006.

The Code has provided for a fast track insolvency resolution process in respect of the following corporate debtors (under Section 55)

- ❖ A corporate debtor with assets and income below a level as may be notified by the Central Government; or
- ❖ A corporate debtor with such class of creditors or such amount of debt as may be notified by the Central Government; or
- ❖ Such other category of corporate persons as may be notified by the Central Government.

The process, in such cases shall be completed in 90 days (extendable by maximum 45 days).

Unit 20 : The Bankers' Books Evidence Act, 1891

Introduction

- ❖ Banks maintain accounts of their customers (including borrowers and other persons) and other details in various ledgers, registers, etc. When any claim of the bank is required to be established or proved in the Courts of Law or any other such forums, these books are required to be produced in original. It is difficult to do so. Therefore, its extracts and statement of accounts are produced.
- ❖ To facilitate the production of such evidence in easy way and to have evidentiary value to the extracts and copies, 'The Bankers' Books Evidence Act, 1891 was enacted to amend the Law of Evidence with respect to bankers' books.

Applicability & Definitions

- ❖ The Act extends to the whole of India except the State of Jammu & Kashmir.
- ❖ 'Bankers' books' include ledgers, day books, cash books, account books and all other records used in the ordinary business of a bank. These records may be kept in written form or stored in a micro- film, magnetic tape or any other form of mechanical or electronic data retrieval mechanism. Such record can be either on site or at any off site location and includes a back-up or disaster recovery site.

'Legal proceeding' means

- ❖ Any proceeding or inquiry in which evidence is or may be given;
- ❖ An arbitration; and
- ❖ Any investigation or inquiry under the Code of Criminal Procedure, 1973

❖ Certified copy' means when the books of a bank;

If maintained in the written form, a copy of any entry in such books together with a certificate written at the foot of such copy mentioning that

- It is a true copy of such entry
- That such entry is contained in one of the ordinary books of the bank
- That such entry was made in the ordinary course of business
- That such book is still in the custody of the bank
- And if the copy was obtained by a mechanical or other process that in itself ensures the accuracy of the copy, a further certificate to that effect.

If maintained in the electronic form

- ❖ Consists of printouts of data stored in a floppy, disc, tape or any other electromagnetic data storage device, or
- ❖ A copy of such printout; and it should contain the certificate having all the applicable contents
- ❖ If maintained in the mechanical form
 - A printout of any entry in the books of a bank stored in a microfilm, magnetic tape, or

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- Any other form of mechanical or electronic data retrieval mechanism obtained by mechanical or other process, and it should contain the certificate having all the applicable contents.

Conditions in the Printout

As per Section 2A of the statute when the books of the bank are not handwritten and copies are taken by way of printout, the copy must accompany the following:

- ❖ A certificate by the principal accountant or the manager to the effect that it is a printout of such entry or a copy of such printout; and
- ❖ A certificate by a person in charge of computer system containing a brief description of the computer system and the particulars thereof
- ❖ A further certificate required is from the person in charge of the computer system to the effect that, to the best of his knowledge and belief, such computer system is operated properly at the material time, he was provided with all the relevant data and the printout represents correctly and is appropriately derived from the relevant data.

Case in which Officer of Bank Not Compellable to Produce Books

- ❖ According to Section 5 of the Act in any proceeding where the bank is not a party, no officer of a bank shall be compellable to produce any bankers' book, contents of which can be proved, under this Act by production of certified copies.
- ❖ Similarly, no officer of the bank shall be called as witness to prove the matters, transactions and accounts recorded in the certified copies. However, the Court may order otherwise for special cause.
- ❖ Even where a Bank has itself filed a suit for recovery of dues, the original documents need not be produced in the court unless the documents are disputed. The requirement of filing original documents ought to be insisted upon only when the parties actually dispute the documents which are on record.

Inspection of Books by Order of Court or Judge

- ❖ In terms of Section 6 of the Act "(1) On the application of any party to a legal proceeding, the Court or a Judge may order that such party be at liberty to inspect and take copies of any entries in a banker's book for any of the purposes of such proceeding,
 - ❖ or may order the bank to prepare and produce, within a time to be specified in the order, certified copies of all such entries, accompanied by a further certificate that no other entries are to be found in the books of the bank relevant to the matters in issue in such proceeding.
 - ❖ An order under this may be made either with or without summoning the bank, and shall be served on the bank three clear days (exclusive of bank holidays) before the same is to be obeyed.
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Unit 21 : The Legal Services Authorities Act, 1987: Lok Adalats

Organization of Lok Adalats

As per Section 19(1) of the Legal Services Authorities Act 1987, Lok Adalats are organized by the State Authority, District Authority or the Supreme Court Legal Services Committee or High Court Legal Services Committee or Taluk Legal Services Committee at such intervals and places for exercising jurisdiction and for such areas as it thinks fit.

As per the provisions of Section 19(2) (3) and (4), Every Lok Adalat organized for an area shall consist of such number of :

- ❖ Serving or retired judicial officers
- ❖ Other persons, of the area as may be specified by the State Authority or the District Authority or the Supreme Court Legal Services Committee or the High Court Legal Services Committee.
- ❖ The experience and qualifications of other persons for Lok Adalats organized by the Supreme Court Legal Services Committee shall be such as may be prescribed by the Central Government in consultation with the Chief Justice of India.
- ❖ The experience and qualifications of other persons referred to in clause (b) of sub-section (2) for Lok Adalats other than referred to in sub-section (3) shall be such as may be prescribed by the State Government in consultation with the Chief Justice of the High Court.

Jurisdiction of Lok Adalat

- ❖ The jurisdiction of the Lok Adalats is provided in Section 19(5) according to which Lok Adalats shall have jurisdiction to determine and arrive at a compromise or settlement between the parties to a dispute.
- ❖ The dispute should be either a pending case before any court for which the Lok Adalat is organized or a matter which is falling within the jurisdiction but not pending in any court. The offences, which are compoundable under any law cannot be brought within the purview of the Lok Adalats. The monetary ceiling of amounts regarding which civil disputes can be settled under this mechanism is presently Rs. 20 lakh.

Disposal of Cases of Lok Adalat

- ❖ The Lok Adalats shall arrive at a compromise or settlement between the parties. They shall act with utmost expedition to arrive at a compromise or settlement between the parties and shall be guided by the principles of justice, equity, fair play and other legal principles.
- ❖ Where no compromise or settlement could be arrived at between the parties, the records of the case shall be returned to the court from which the reference was received. The court shall proceed with the matter from the stage it had reached before making a reference to the Lok Adalat.
- ❖ In respect of disputes which were not before the court and in the absence of compromise or settlement between the parties in the Lok Adalat, can also seek remedy in a court.

Nature of Award of the Lok Adalats and Powers

Powers of the Lok Adalats is derived from Section 22 of the Legal Services Authorities Act 1987.

As per Section 22 – The Lok Adalat shall, for the purposes of holding any determination under this Act, have the same 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

- ❖ The summoning and enforcing the attendance of any witness and examining him on oath
 - ❖ The discovery and production of any document
 - ❖ The reception of evidence on affidavits
 - ❖ The requisitioning of any public record or document or copy of such record or document from any court or office such other matters as may be prescribed.
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Unit 22 : The Consumer Protection Act, 2019

Introduction

- ❖ The Consumer Protection Act 2019 was enacted on August 9th 2019.
- ❖ It aims to provide for protection of the interests of consumers and for the said purpose, to establish authorities for timely and effective administration and settlement of consumers' disputes and for matters connected therewith or incidental thereto.

Important Definitions

“Consumer” means any person who:

- ❖ Buys any goods for a consideration which has been paid or promised or partly paid and partly promised, or under any system of deferred payment and
- ❖ Includes any user of such goods other than the person who buys such goods for consideration paid, when such use is made with the approval of such person, but does not include a person who obtains such goods for resale or for any commercial purpose; or
- ❖ Hires or avails of any service for a consideration which has been paid or promised or partly paid and partly promised, and includes any beneficiary of such service, but does not include a person who avails of such service for any commercial purpose.

“Consumer Rights” includes:

- ❖ The right to be protected against the marketing of goods, products or services which are hazardous to life and property;
- ❖ The right to be informed about the quality, quantity, potency, purity, standard and price of goods, products or services, so as to protect the consumer against unfair trade practices;
- ❖ The right to be assured, wherever possible, access to a variety of goods, products or services at competitive prices;
- ❖ The right to be heard and to be assured that consumer's interests will receive due consideration at appropriate for a
- ❖ The right to seek redressal against unfair trade practice or restrictive trade practices or unscrupulous exploitation of consumers; and
- ❖ The right to consumer awareness.

Unfair Contract and Unfair Trade Practice

An Unfair Contract has been defined in detail in Section 2(46) and Unfair Trade Practice in Section 2(47).

In terms of Section 2(46) “unfair contract” means a contract between a manufacturer or trader or service provider on one hand, and a consumer on the other, having such terms which cause significant change in the rights of such consumer, including the following,

- ❖ Requiring manifestly excessive security deposits to be given by a consumer for the performance of contractual obligations; or
- ❖ Imposing any penalty on the consumer, for the breach of contract thereof which is wholly disproportionate to the loss occurred due to such breach to the other party to the contract; or
- ❖ Refusing to accept early repayment of debts on payment of applicable penalty, or
- ❖ Entitling a party to the contract to terminate such contract unilaterally, without reasonable cause; or
- ❖ Permitting or has the effect of permitting one party to assign the contract to the detriment of the other party who is a consumer, without his consent; or
- ❖ Imposing on the consumer any unreasonable charge, obligation or condition which puts such consumer to disadvantage;”
- ❖ Thus, an unfair contract is one which seeks to curtail rights which should normally be available to all consumers.

In terms of Section 2(47) “unfair trade practice” means a trade practice which, for the purpose of promoting the sale, use or supply of any goods or for the provision of any service, adopts any unfair method or unfair or deceptive practice including any of the following practices, namely :—

i) Making any statement, whether orally or in writing or by visible representation including by means of electronic record, which:

- Falsely represents that the goods are of a particular standard, quality, quantity, grade, composition, style or model
- Falsely represents that the services are of a particular standard, quality or grade;
- Falsely represents any re-built, second-hand, renovated, reconditioned or old goods as new goods.
- Represents that the goods or services have sponsorship, approval, performance, characteristics, accessories, uses or benefits which such goods or services do not have.
- Represents that the seller or the supplier has a sponsorship or approval or affiliation which such seller or supplier does not have.
- Makes a false or misleading representation concerning the need for, or the usefulness of, any goods or services;
- Gives to the public any warranty or guarantee of the performance, efficacy or length of life of a product or of any goods that is not based on an adequate or proper test.
- Materially misleads the public concerning the price at which a product or like products or goods or services, have been or are, ordinarily sold or provided.
 - ❖ Permitting the publication of any advertisement, whether in any newspaper or otherwise, including by way of electronic record, for the sale or supply at a bargain price of goods or services that are not intended to be offered for sale or supply at the bargain price.
 - ❖ Permitting the offering of gifts, prizes or other items with the intention of not providing them as offered or creating impression that something is being given or offered free of charge when it is fully or partly covered by the amount charged, in the transaction as a whole.

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- ❖ Permitting the sale or supply of goods intended to be used, or are of a kind likely to be used by consumers, knowing or having reason to believe that the goods do not comply with the standards prescribed by the competent authority.
 - ❖ Permitting the hoarding or destruction of goods, or refusal to sell the goods, if such hoarding or destruction or refusal raises or tends to raise or is intended to raise,
 - ❖ Manufacturing of spurious goods or offering such goods for sale or adopting deceptive practices in the provision of service.
 - ❖ Not issuing bill or cash memo or receipt for the goods sold or services rendered in such manner as may be prescribed
 - ❖ Refusing, after selling goods or rendering services, to take back or withdraw defective goods and to refund the consideration thereof, if paid, within the period stipulated in the bill or cash memo or receipt or in the absence of such stipulation, within a period of thirty days
 - ❖ Disclosing to other person any personal information given in confidence by the consumer.

Central Consumer Protection Council

Section 3, 4 and 5 of the statute details about the establishment, working and objects of the Central Consumer Protection Council.

According to the provisions of Section 3

- ❖ The Central Government shall, by notification, establish the Central Consumer Protection Council to be known as the Central Council.
- ❖ The Central Council shall be an advisory council and consist of the following members, namely:
 - (a) The Minister-in-charge of the Department of Consumer Affairs in the Central Government, who shall be the Chairperson; and
 - (b) Such number of other official or non-official members representing such interests as may be prescribed.

Section 4 states

- ❖ The Central Council shall meet as and when necessary, but atleast one meeting of the Council shall be held every year.
- ❖ The Central Council shall meet at such time and place as the Chairperson may think fit and shall observe such procedure in regard to the transaction of its business as may be prescribed.

Section 5 states

The object of the council would be to render advice on promotion and protection of the consumers' rights under the statute.

State Consumer Protection Council

The State Consumer Protection Council is established under Section 6 of the Act. As per Section 6

Every State Government shall, by notification, establish with effect from such date as it may specify in such notification, a State Consumer Protection Council for such State to be known as the State Council.

The State Council shall be an advisory council and consist of the following members, namely:—

- ❖ The Minister-in-charge of Consumer Affairs in the State Government who shall be the Chairperson
- ❖ Such number of other official or non-official members representing such interests as may be prescribed
- ❖ Such number of other official or non-official members, not exceeding ten, as may be nominated by the Central Government.

- ❖ The State Council shall meet as and when necessary but not less than two meetings shall be held every year.
- ❖ The State Council shall meet at such time and place as the Chairperson may think fit and shall observe such procedure in regard to the transaction of its business, as may be prescribed.
- ❖ Section 7 describes the object of the State Council to be to render advice on promotion and protection of consumer rights under this Act within the State.

District Consumer Protection Council

Section 8 and 9 of the Consumer Protection Act 2019 deals with the establishment and object of the District Consumer Protection Council. As per Section 8-

- ❖ The State Government shall, by notification, establish for every District with effect from such date as it may specify in such notification, a District Consumer Protection Council to be known as the District Council.
- ❖ The District Council shall be an advisory council and consist of the following members, namely:

The Collector of the district, who shall be the Chairperson; and

- ❖ Such number of other official and non-official members representing such interests as may be prescribed.
- ❖ The District Council shall meet as and when necessary but not less than two meetings shall be held every year.
- ❖ The District Council shall meet at such time and place within the district as the Chairperson may think fit and shall observe such procedure in regard to the transaction of its business as may be prescribed.

According to Section 8: The objects of every District Council shall be to render advice on promotion and protection of consumer rights under this Act within the district.

Central Consumer Protection Authority

Establishment

The Central Consumer Protection Authority is formed under Section 10 of the statute. As per Section 10

- ❖ The Central Government shall, by notification, establish with effect from such date as it may specify in that notification, a Central Consumer Protection Authority to be known as the Central Authority to regulate matters relating to violation of rights of consumers, unfair trade practices and false or misleading advertisements which are prejudicial to the interests of public and consumers and to promote, protect and enforce the rights of consumers as a class.
- ❖ The Central Authority shall consist of a Chief Commissioner and such number of other Commissioners as may be prescribed, to be appointed by the Central Government to exercise the powers and discharge the functions under this Act.
- ❖ The headquarters of the Central Authority shall be at such place in the National Capital Region of Delhi, and it shall have regional and other offices in any other place in India as the Central Government may decide.

Investigation Wing

The Central Authority has an Investigation Wing for the purpose of conducting inquiry or investigation under this Act as may be directed by the Central Authority.

Functions

- ❖ To protect, promote and enforce the rights of consumers as a class
- ❖ To prevent violation of consumers rights under the Act
- ❖ To prevent unfair trade practices
- ❖ To ensure no false or misleading advertisement is made
- ❖ To ensure no person publishes false or misleading advertisement.
- ❖ Inquiries/ investigations into violations of consumer rights, unfair trade practices
- ❖ Intervene in any proceedings before a District/ State/ National Commission in any matter
- ❖ Review the matters relating to, and the factors inhibiting enjoyment of, consumer rights
- ❖ Recommend adoption of international covenants and best international practices
- ❖ Undertake and promote research in the field of consumer rights
- ❖ Spread and promote awareness on consumer rights
- ❖ Issue notices to alert consumers against dangerous or hazardous or unsafe goods or services
- ❖ Issue necessary guidelines to prevent unfair trade practices and protect consumers' interest.

Note: The Central Authority has been given powers under the Act to issue directions and levy penalties under Section 20 and 21 and any person aggrieved by an order passed by the Central authority under the aforesaid sections' may file an appeal to the National Commission within a period of thirty days from the date of receipt of such order." Section 24.

District Consumer Disputes Redressal Commission

- ❖ As per Section 28 of the Act, The State Government, by notification establishes a District Consumer Disputes Redressal Commission in each district.
- ❖ It comprises president and at least two members and not more than prescribed number of members. One of the members or president must be woman.
- ❖ It shall have jurisdiction to entertain complaints where the value of the goods or services paid as consideration does not exceed Rs. 1 crore.
- ❖ The District Commission shall ordinarily function in the district headquarters and may perform its functions at such other place in the district, as the State Government may, in consultation with the State Commission, notify in the Official Gazette from time to time.
- ❖ A person may appeal against order of District Commission to the State Commission on the grounds of facts or law within 45 days from the date of the order, or extended period permitted.
- ❖ No appeal by a person, who is required to pay any amount in terms of an order of the District Commission, shall be entertained by the State Commission unless the appellant has deposited fifty per cent of that amount in the manner as may be prescribed.

State Consumer Disputes Redressal Commission

The State Consumer Disputes Redressal Commission is established under Section 42 of the Consumer Protection Act 2019.

- ❖ The State Government shall, by notification, establish a State Consumer Disputes Redressal Commission, to be known as the State Commission, in the State.
- ❖ The State Commission shall ordinarily function at the State capital and perform its functions at such other places as the State Government may in consultation with the State Commission notify in the Official Gazette.

Each State Commission shall consist of :

- ❖ A President; and
- ❖ Not less than four or not more than such number of members as may be prescribed in consultation with the Central Government

The functions of the state Commission has been detailed in Section 47 of the Act.

To entertain

- ❖ Complaints where the value of the goods or services paid as consideration, exceeds Rs. 1 crore, but does not exceed Rs. 10 crores, Provided that where the Central Government deems it necessary so to do, it may prescribe such other value, as it deems fit
- ❖ Complaints against unfair contracts, where the value of goods or services paid as consideration does not exceed Rs. 10 crores
- ❖ Appeals against the orders of any District Commission within the State.
- ❖ To call for the records and pass appropriate orders in any consumer dispute which is pending before or has been decided by any District Commission within the State, where it appears to the

State Commission that such District Commission has exercised a jurisdiction not vested in it by law, or has failed to exercise a jurisdiction so vested.

- ❖ As per Section 51 of the Act- Any person aggrieved by an order made by the State Commission in exercise of its powers, may prefer an appeal against such order to the National Commission within a period of 30 days from the date of the order in such form and manner as may be prescribed
- ❖ No appeal by a person, who is required to pay any amount in terms of an order of the State Commission, shall be entertained by the National Commission unless the appellant has deposited 50% of that amount in the manner as may be prescribed.

Term of Office of the President

- ❖ The President of the State Commission shall hold office for a term of four years or upto the age of sixty-seven years, whichever is earlier and shall be eligible for reappointment for another term of four years subject to the age limit of sixty-seven years, and such reappointment shall be made on the basis of the recommendation of the Selection Committee.
- ❖ Every member of the State Commission and the President and every member of the District Commission shall hold office for a term of four years or upto the age of sixty-five years, whichever is earlier and shall be eligible for reappointment for another term of four years subject to the age limit of sixty-five years, and such reappointment shall be made on the basis of the recommendation of the Selection Committee.

National Consumer Disputes Redressal Commission

Section 53 of the statute deals with the establishment of a National Consumer Disputes Redressal Commission. Section 53 states:

- ❖ The Central Government shall, by notification, establish a National Consumer Disputes Redressal Commission, to be known as the National Commission.
- ❖ The National Commission shall ordinarily function at the National Capital Region and perform its functions at such other places as the Central Government may in consultation with the National Commission notify in the Official Gazette.
- ❖ The National Commission shall also have a President plus not less than 4 members. The President and members of the National Commission hold office for such term as specified in the rules made by the Central Government but not exceeding five years from the date on which he enters upon his office and shall be eligible for re-appointment up to the age of 70 for the President and 67 for other members.

As per Section 58 of the statute which details the functions of the National Commission- the National Commission shall have jurisdiction—to entertain

- ❖ Complaints where the value of the goods or services paid as consideration exceeds Rs. 10 crores.

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- ❖ Complaints against unfair contracts, where the value of goods or services paid as consideration exceeds Rs. 10 crores
 - ❖ Appeals against the orders of any State Commission
 - ❖ Appeals against the orders of the Central Authority

As per Section 67: Any person, aggrieved by an order made by the National Commission, may prefer an appeal against such order to the Supreme Court within a period of 30 days from the date of the order

Jurisdiction of Commission

- ❖ Jurisdiction of District Commission: District Commission shall have jurisdiction to entertain complaints where the value of the goods or services paid as consideration does not exceed fifty lakh rupees.
- ❖ Jurisdiction of State Commission: The State Commission shall have jurisdiction to entertain complaints where the value of the goods or services paid as consideration exceeds fifty lakh but does not exceed two crore rupees.
- ❖ Jurisdiction of National Commission: The National Commission shall have jurisdiction to entertain complaints where the value of the goods or services paid as consideration, exceeds two crore rupees.

Finality of Orders and Limitation Period

- ❖ Section 68: states that every order of a District Commission or the State Commission or the National Commission, as the case may be, shall, if no appeal has been preferred against such order under the provisions of this Act, be final.
- ❖ Section 69: The District Commission, the State Commission or the National Commission shall not admit a complaint unless it is filed within two years from the date on which the cause of action has arisen.

Consumer Mediation Cell

- ❖ The Act envisages the establishment of a Consumer Mediation Cell by each state to be attached to each of the District Commissions and the State Commissions of that State.
 - ❖ The Central Government shall establish, by notification, a consumer mediation cell to be attached to the National Commission and each of the regional Benches.
 - ❖ A consumer mediation cell shall consist of such persons as may be prescribed.
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Unit 23 : The Law of Limitation

Period of Limitation

- ❖ The Recovery of Debts due to Banks and financial institutions Act, 1993 and the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 specifically state that actions under those Acts are permissible only if the claim is within the period of limitation.
- ❖ The Limitation Act, 1963 is an Act to consolidate and amend the law for the limitation of suits and other proceedings.
- ❖ It extends to the whole of India.
- ❖ It is absolutely necessary that every suit or application or appeal shall have to be filed within the period of limitation. Section 3 of the Limitation Act declares that every suit instituted, appeal preferred, and application made after the prescribed period shall be dismissed although limitation has not been set up as a defense.

A suit is said to be instituted when the plaint is presented to the proper officer in the court. In the case of set off or counter claim, those shall be treated as a separate suit and shall be deemed to have been instituted:

- ❖ In the case of a set off, on the same date as the suit in which the set off is pleaded;
- ❖ In the case of a counter-claim, on the date on which the counter-claim is made in court.

Computation of Period of Limitation

- ❖ When the period of limitation expires on a day when the court is closed, the suit, appeal or application may be instituted, preferred or made on the day when the court reopens. (Section 4)
- ❖ Any appeal or any application other than execution petitions may be admitted after the prescribed period, if the appellant or applicant makes out sufficient cause for not preferring the appeal or application within the period of limitation. (Section 5)
- ❖ The computation of the period of limitation, for filing appeal, shall exclude the day on which the judgement was pronounced and the time taken for obtaining a copy of the decree, sentence or order appealed.
- ❖ For an application for execution of decree, the period during which the institution or execution has been stayed by injunction or order, the day on which the order was issued or made and the day on which it was withdrawn shall be excluded
- ❖ For filing any suit for which notice has to be given, or for which the previous consent or sanction of the Government or any other authority is required, in accordance with the requirements of any law for the time being in force, the period of such notice, or the time required for obtaining such consent or sanction shall be excluded.
- ❖ In computing the period of limitation for any suit, the time during which the defendant has been absent from India and from the territories outside India under the administration of the Central Government shall be excluded.

Acts Giving Rise to Fresh Period of Limitation

There are two instances which will give rise to fresh period of limitation. In these cases the period of limitation will be computed as if the starting point is the happening of the instances.

- ❖ Where before the expiration of the prescribed period for a suit or application in respect of any property or right, acknowledgement of liability in respect of such property or right has been made in writing signed by the party against whom such property or right is claimed, or by any person through whom he derives his title or liability, a fresh period of limitation shall be computed from the time when the acknowledgement was so signed.
 - ❖ Where payment on account of a debt or of interest on a legacy is made before expiration of the prescribed period by the person liable to pay the debt or legacy or by his agent duly authorized in this behalf, a fresh period of limitation shall be computed from the time when the payment was made. In this case 'debt' does not include money payable under a decree or order of a court.
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Unit 24 : Tax Laws

Income Tax

The Income Tax Act 1961 came into force from April 1st 1962 and extends to the whole of India to govern the law relating to taxation on Income of individuals, corporates etc.

This Act envisages taxation of income of an assessee on the basis of his (a) Residence (b) Place of source of income.

- ❖ Assessment Year: The income accruing, or arising, to a person (called 'Assessee') is taxed on the basis of 'Assessment Year'. The term Assessment Year represents the period of 12 months beginning from 1st April every year. The income arising in the 'previous year' and the tax paid thereon including the tax deducted at source, self assessed tax paid thereon is assessed in the assessment year.
- ❖ Previous year has been defined in Section 3 of the Income Tax Act 1961 as "—for the purposes of this Act, "previous year" means the financial year immediately preceding the assessment year.
- ❖ Total Income: As per Section 5 of the statute "(1) Subject to the provisions of this Act, the total income of any previous year of a person who is a resident includes all income from whatever source derived which—
 - Is received or is deemed to be received in India in such year by or on behalf of such person; or
 - Accrues or arises or is deemed to accrue or arise to him in India during such year; or
 - Accrues or arises to him outside India during such year

Under IT Act – Other norms are:

- ❖ Quoting PAN for opening a/c, purchase of DD, Term Deposit above Rs. 50,000.
- ❖ Declaration in Form 60 and 61.
- ❖ Repayment of Term Deposit above Rs. 20,000 by pay-order/credit to a Bank Account.
- ❖ Limit of deposit of cash in a Savings Account up to Rs. 10 lacs and Rs. 50 lacs in a Current Account in a Financial Year.

Computation of income:

Income Tax Act, 1961 envisages taxation of income under following heads:

- ❖ Salaries
- ❖ Income from house property
- ❖ Profits and gains from business or profession
- ❖ Capital gains
- ❖ Income from other sources

Income Tax

Computation of Taxable income involves the following steps namely

- ❖ Income arising under various heads to income is computed separately as per the relevant sections covering such incomes.
- ❖ After having computed the income under each head separately, the 'gross total income' representing the sum of above amounts computed under such heads is arrived at.
- ❖ Chapter VIA etc. of the Income Tax Act provides for various deductions allowable from the gross total income. The deductions so allowed are reduced from the gross total income to derive the taxable income.
- ❖ Income Tax as per relevant slabs and cess, if any, applicable, and interest, if any, applicable, at given rates is calculated on the Taxable Income

Income not included in Taxable Income:

Certain categories of income are exempt from tax and such income is not taken into account in the computation of income. These exempt incomes have been described in Section 10 of the IT Act.

- ❖ Agricultural income
- ❖ Any sum received by an individual as a member of a Hindu Undivided Family, where such sum has been paid out of the income of the family,
- ❖ In the case of a non-resident, any income by way of interest on such securities or bonds as the Central Government may, by notification in the Official Gazette, specify in this behalf, including income by way of premium on the redemption of such bonds
- ❖ in the case of an individual, any income by way of interest on moneys standing to his credit in a Non-Resident (External) Account in any bank in India in accordance with the Foreign Exchange Management Act, 1999, Provided that such individual is a person resident outside India.
- ❖ In the case of an individual, being a citizen of India or a person of Indian origin, who is a non-resident, any income from interest on such savings certificates issued before the 1st day of June, 2002 by the Central Government.

Assessment Proceedings

- Every person whose total income in a previous year exceeds the maximum amount which is not liable to tax is required to file his return by the due date prescribed in section 139. A company or partnership firm has to file its return of income.
- Income Tax department has prescribed different forms known as ITRs applicable to various categories of assesses which are compulsorily required to be filed on-line except Super Senior Citizens are given option to submit 'return' in paper mode provided the computation does not have any income chargeable under head of 'Profits and Gains from Business or Profession'.
- Now with insertion of sub-section 5E to Section 139A in the IT Act, has made Aadhar and PAN interchangeable meaning that an individual having an Aadhar number but not having a PAN number will be able to file his/her return on the basis of the Aadhar number

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- The AO determines the total income and issues an assessment order along with the notice of demand. The demand if any, raised after scrutiny assessment is payable within 30 days of the service of the Assessment order and the demand notice on the assessee.

Payment of Taxes:

Advance tax is payable as per the provisions of section 210 of the Income Tax Act. Advance tax arises from the concept of 'pay as you earn'. In the case of corporate assessee, advance tax is payable in four instalments as given below:

- By June 15–15 per cent
- By September 15–45 per cent
- By December 15–75 per cent
- By March 15–100 per cent of the advance tax payable.

The advance tax which is paid by an assessee on the basis of estimation of income may at times fall short of the tax payable as per the return of income. Such a shortfall, if any, shall be paid by way of 'self-assessment tax' under Section 140A of the Income Tax Act.

Deduction/Collection of tax at source

Members of Co-operative bank are exempted from TDS. The following payments generally occur during the course of business activities of a bank and are covered under TDS under the Income Tax Act, 1961.

- Salaries – Section 192
- Interest on securities – Section 193
- Payment of interest, other than interest of securities – Section 194A
- Payment to contractors or sub-contractors – 194C
- Payment of brokerage and commission – Section 194H
- Payment by way of rent – Section 194I
- Payment of professional and technical fees - Section 194J
- Payment to non-resident – Section 195

Firstly, the person deducting tax at source is required to obtain Tax Deduction Account Number (TAN) by filing an application in Form 49B. Tax shall be deducted at source as per the rates given in the Finance Act of the respective years. The tax deducted at source is required to be deposited in the Government account, generally within one week from the end of the month in which tax is deducted at source.

The rate of deduction of tax on payments made to non-residents under Section 195 is also given in the Finance Act of the relevant year. The Government of India enters into agreements for avoidance of double taxation of income both on the basis of residence and source with other countries. The rate given in the Double Taxation Avoidable Agreement (DTAA) with the respective country where the

recipient is resident will have to be taken into account. The rates applicable as per the DTAA will have to be applied for the purposes of TDS, when it is lower than the rates given in the Finance Act.

Non-compliance with provisions relating to TDS attracts:

- ❖ Levy of interest @ 12 per cent p.a. on the amount on tax payable at source from the date on which it is deductible until the date of payment.
- ❖ Recovery of tax deductible at source from the person responsible for deduction.
- ❖ Non-payment of tax deducted at source into Government a/c attracts prosecution proceedings and imprisonment from 3 months to 7 years under Section 276B of the Income Tax Act.
- ❖ Any failure to file returns/statements in this regard attracts penalty @ of Rs. 200 per day for the period of default. (Sec 234 E). The amount of fee shall not exceed the amount of tax deductible or collectible, as the case may be.

Permanent Account Number (PAN):

- ❖ Quoting of PAN has become mandatory in certain transactions.
- ❖ PAN is required to be quoted when an account is opened where amount of Fixed deposit/time deposit purchased by a depositor in any bank exceeds Rs. 50,000/-. Opening of bank accounts also require quoting PAN.
- ❖ Cash payments for purchase of bank drafts or pay orders or banker's cheques from a banking company, for an amount aggregating to Rs. 50,000/- or more during any one day or cash deposits aggregating Rs. 50,000/- or more with any bank during any one day, require quoting of PAN.
- ❖ Payment in cash in connection with travel to any foreign country, of an amount exceeding Rs. 25,000/- at any one time, has also been prescribed.

Commodity Transaction Tax

- ❖ Commodities Transaction Tax is a tax levied on exchange-traded non-agricultural commodity derivatives in India. It taxes the commodity trading in India wherein both parties - buyer and seller - are taxed depending on the contract size.
- ❖ While agricultural commodities are exempted from CTT, non-agricultural commodities such as gold, silver, and other non-ferrous metals including copper will be taxed. Apart from this, energy products like crude oil and natural gas will also be taxed under the Commodity Transaction Tax.
- ❖ Section 119: The law makes the recognised stock exchange (assessee) dealing in commodity trading responsible for collection of the commodities transaction tax from the seller who enters into a taxable commodities transaction in that recognized stock exchange at the rate specified.
- ❖ The CTT collected during any calendar month in accordance with the provisions of sub-section (1) shall be paid by every assessee to the credit of the Central Government by the seventh day of the month immediately following the said calendar month.
- ❖ Section 117 deals with the rate of commodity transaction tax for various transactions.

Goods and Services Tax

- ❖ The Goods and Services Tax (GST) is one indirect tax for the whole nation which was enacted on April 12th 2017 and came into force in India from July 8th 2017.
- ❖ GST is a single tax on the supply of goods and services, right from the manufacturer to the consumer. Credits of input taxes paid at each stage will be available in the subsequent stage of value addition, which makes GST essentially a tax only on value addition at each stage.
- ❖ Advantages: Easy compliance, uniformity of tax rates and structures, removal of cascading of taxes, improved competitiveness, etc. The benefits to Central and State Governments are that GST is simple and easy to administer, there are better controls on leakage, higher revenue efficiency, etc. For the consumer, the benefits can be grouped under single and transparent tax proportionate to the value of goods and services, relief in overall tax burden.
- ❖ The GST subsumes taxes levied and collected by the Centre viz. Central Excise duty, Additional Excise Duty, Additional Duties of Customs (commonly known as CVD), Service Tax, etc. and at State level Entertainment Tax, Octroi and Entry tax, Luxury Tax, Purchase Tax, Taxes on lottery, betting and gambling, and other taxes levied by the State.
- ❖ The GST levied by the Centre on intra-State supply of goods and/or services called the Central GST (CGST) and that levied by the States/ Union territory is called the State GST (SGST)/ UTGST. Similarly, Integrated GST (IGST) is which is levied and administered by Centre on every inter-state supply of goods and services.
- ❖ GST is a destination based tax and received by state in which goods are consumed.

Imports in GST Regime

- ❖ The import of goods has been defined in the IGST Act, 2017 as bringing goods into India from a place outside India.
 - ❖ Import of goods under GST or import of services under GST will be treated as deemed inter-State supplies and would be subject to Integrated tax in addition to the applicable Custom duties.
 - ❖ As per the provisions contained in Section 21 of the IGST Act, 2017, all import of services made on or after the appointed day i.e 1st July, 2017 will be liable to integrated tax regardless of whether the transactions for such import of services had been initiated before the appointed day. However, if the tax on such import of services had been paid in full under the existing law, no tax shall be payable on such import under the IGST Act.
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MODULE D : COMMERCIAL & OTHER LAWS WITH REFERENCE TO BANKING OPERATIONS

Unit 25A : Meaning and Essentials of a Contract

Meaning of Contract

In India the law relating to contracts is provided by the Indian Contract Act 1872.

Contract means an agreement enforceable by law meaning thereby that the rights and obligations arising out of the contract must be enforceable in a court of law.

All agreements between two or more persons are contracts if those satisfy the following

- ❖ It is made by free consent of all the parties
- ❖ It is made by parties who are competent to contract.
- ❖ It is made for a lawful consideration
- ❖ It is made with a lawful object and
- ❖ It is not declared as void expressly in the Indian Contract Act

Therefore, a Contract = Agreement + Enforceability. Thus, all contracts are agreements but all agreements are not necessarily contracts.

Key Components to Form a Contract

- ❖ When one person signifies to another person, his willingness to do or not to do something, with a view to obtaining the consent of that other person, he is said to make a proposal.
- ❖ When a person to whom the proposal is made, signifies his assent (consent), the proposal is said to be accepted. A proposal becomes a promise when it is accepted.
- ❖ The person making the proposal is called the 'promisor'. The person accepting the proposal is called 'promisee'.

Essentials of a Valid Contract

Proposal and Acceptance

- ❖ A contract comes into being only when an offer of a proposal is made by one party known as the promisor and is accepted by another party known as the offeree.
- ❖ The offer should be without any qualification and be definite. It must be clear, definite, complete and final. It should be communicated to the offeree. The process of making a proposal is completed by the act of communicating it. The acceptance of the offer should be absolute and unconditional. Moreover, the offer and acceptance must be 'consensus ad idem' which means that both the parties must agree on the same thing in the same sense.

Intention to Create Legal Relationship

- ❖ The intention of the two or more parties entering into an agreement must be to create a legal relationship between them. If there is no such intention between them there is no contract.
- ❖ Agreements of social nature, as they do not contemplate legal relationship, are not contracts.

An Agreement may be oral or written

- ❖ Under certain laws such as The Transfer of Property Act certain agreements are required to be in writing only and are also required to be registered and/or attested. If such formalities are not complied with, then the agreement cannot be enforced before a court of law.
- ❖ This applies in the case of sale or mortgage of immoveable property, lease, etc. This is brought out in Section 10(2).
- ❖ As per this section wherever there is a statutory requirement that the contract must be in writing and also registered etc, the statutory requirements must be complied with. Otherwise an agreement may be oral also.

Lawful Consideration

There must be a lawful consideration for both the parties to enter into an agreement. Consideration here means 'something in return'.

The Contract Act (Section 2d) defines consideration as under:

- ❖ When, at the desire of the promisor, the promisee or any other person,
- ❖ Has done or abstained from doing, or
- ❖ Does or abstains from doing, or
- ❖ Promises to do or to abstain from doing something. Such act or abstinence or promise is called a consideration for the promise.
- ❖ An agreement not enforceable by law is said to be void. An agreement enforceable by law is a contract. An agreement which is enforceable by law at the option of one or more of the parties thereto, but not at the option of the other or others, is a voidable contract. A contract which ceases to be enforceable by law becomes void when it ceases to be enforceable

However, in the following cases an agreement without consideration is valid:

- ❖ An agreement made out of natural love and affection.
- ❖ Between parties standing in near relation to each other.
- ❖ Which is in writing and registered.

The object of a contract should be lawful

It must not be illegal or immoral or opposed to public policy. It is lawful unless it is forbidden by law. When the object of a contract is not lawful, the contract is void.

Free and Genuine Consent

Free and genuine consent of the parties to a contract is required. A consent is said to be free when the parties agree to the same thing in the same sense. Consent is said to be free when it is not caused by coercion, as defined in section 15, or undue influence, as defined in section 16, or fraud, as defined in section 17, or misrepresentation, as defined in section 18, or mistake, subject to the provisions of sections 20, 21, and 22.

Certainty and Possibility of Performance

The agreements, in which the meaning is uncertain is deemed void. The contract must be certain and not vague or indefinite (Section 29).

Agreement not declared void

The agreement must not have been expressly declared void by the law in force in the country. For example dealing in 'rhinoceros horn' is banned. An agreement for export of the horn between A and B is void.

Capacity to Contract

According to Section 11 dealing with 'who is competent to contract' "Every person is competent to contract who is of the age of majority according to the law to which he is subject, and who is of sound mind and is not disqualified from contracting by any law to which he is subject".

Contract Act and Banking

- ❖ The relationship between a banker and customer is the transactional relationship and depends on the type of transaction.
 - ❖ When money is deposited in a bank, the relationship that is constituted between the banker and the customer is one of debtor and creditor. The relationship between bank and customer becomes that of creditor-debtor when customer has borrowed money from the
 - ❖ When a bank accepts securities, valuables, bonds, or other documents with the bank for safe custody from a person, the bank, besides becoming trustee, becomes a bailee and the customer is the bailor. When ancillary services rendered by the bank such as remittance, collection of cheques, bills, etc. on behalf of the customers, it is acting as an agent of its customer. In respect of hiring of safe deposit lockers by the bank, the relationship is that of lessor and lessee, etc.
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Unit 25B : Contracts of Indemnity

Contract of Indemnity

- ❖ A Contract of Indemnity is a contract by which one party promises to save the other from loss likely to be caused to him. This loss can be, either by the conduct of the promisor himself or by the conduct of any other person.
- ❖ The promisor is called the indemnifier and the other person is called indemnified. The essence of any contract of indemnity is that the assured must prove a loss.

Rights Of Indemnity Holder

In terms of Section 125 of the Act which deals with extent of liability of the Indemnifier, the promisee is entitled to recover from the promisor/indemnifier, in respect of the matter to which the promise to indemnify applies:

- ❖ All damages which he may be compelled to pay in any suit, in respect of any matter to which the promise to indemnify applies.
- ❖ All costs which he may be compelled to pay in any suit if, in bringing or defending it, or if the indemnifier authorized him to bring or defend the suit.
- ❖ All sums paid in compromise, not contrary to indemnity.
- ❖ Right to sue for specific performance – the indemnity holder is entitled to sue for specific performance if he has incurred absolute liability and the contract covers such liability.

Implied Indemnity

- ❖ A contract of indemnity may be express or implied depending upon the circumstances of the case, though Section 124 of the Indian Contract Act does not seem to cover the case of implied indemnity.
- ❖ An act is done by one person at the instance of another and such an act is not in itself manifestly tortuous to the knowledge of the person doing it, and such act turns to be injurious to the rights of a third person, the person doing it is entitled to an indemnity from him who requested that it should be done.

Enforceability Of Contract Of Indemnity

Commencement of Liability

The Indian Contract Act 1872, does not specify, the actual time of commencement of the liability of the indemnifier. Therefore the judgements have been varied with some High Courts opining that the indemnifier is not liable till the actual loss has been incurred by the indemnity holder and others insisting that the indemnity holder can compel the indemnifier to make good the loss even before he actually discharges his liability by payment etc.

Unit 25C : Contracts of Guarantee

- ❖ A 'Contract of Guarantee' is a contract to perform the promise, or discharge the liability, of a third person in case of latter's default.
- ❖ A guarantee may be either oral or written.
- ❖ The question whether a particular contract is a contract of indemnity or guarantee has to be decided by examining the language of the documents entered into between the parties and the nature of transaction.
- ❖ The person who gives the guarantee is called the 'surety'. The person in respect of whose default the guarantee is given is called the 'principal debtor'. The person to whom the guarantee is given is called the 'creditor/beneficiary'.

Consideration

Anything done, or any promise made, for the benefit of the principal debtor, is a sufficient consideration to the surety for giving the guarantee (Sec. 127).

The Liability of the Surety

- ❖ The liability of the surety is co-extensive with that of the principal debtor unless it is otherwise provided by the contract (Sec. 128).
- ❖ A surety is regarded as a favoured debtor. This means that only if the principal debtor is unable to pay the debt, the surety takes the place of the principal debtor. Again, once the surety has paid the debt, he then occupies the place of the original creditor. He can then claim from the principal debtor, the entire sum he has paid to the original creditor.
- ❖ The surety has no right to restrain an action against him by the creditor on the ground that the principal debtor is insolvent and that the creditor may have relief against the principal debtor in some other proceedings.
- ❖ Similarly, if the creditor has obtained any decree against the surety and the principal debtor, the surety has no right to restrain execution against him just because the creditor has not exhausted his remedies against the principal. discharged.
- ❖ Even the death of the principal debtor does not release the surety from his obligation during his lifetime and against his legal heirs to the extent of estate (immovable and movable properties) inherited by them from the deceased surety.

Continuing Guarantee

- ❖ A guarantee which extends to a series of transactions, is called, a 'continuing guarantee'. This type of guarantee is not limited to only one transaction but to many transactions.
- ❖ Illustration Mr. A contracts with Mr. B, a shopkeeper to allow Mrs. A to take whatever goods she may need from his shop, up to the amount of Rs. 20,000. Mr. A will be liable for the debts incurred by Mrs. A up to the given amount. A continuing guarantee may at any time be revoked by the surety, as to future transactions, by notice to the creditor (Sec. 130).

Death of Surety

- ❖ Normally, when the surety dies, the guarantee ends from that date. However, this is not true in all cases. It depends upon the terms of the contract and the intention of the parties as regards future transactions.
- ❖ The death of the surety operates, in the absence of any contract to the contrary, as a revocation of a continuing guarantee, so far as future transactions are concerned. Generally all guarantees obtained by banks are continuing guarantees and in the case of death of a surety, the guarantee would stand revoked for future transactions. This is the precise reason when the information of a guarantor's death is received, banks prefer to break the running accounts of a borrower.

Variance In Terms of The Contract

- ❖ Any variance (change/modification) made, without the surety's consent, in the 'terms of contract', between the principal debtor and the creditor, discharges the surety as to transactions subsequent to the variance (Sec. 133).

Discharge of Principal Debtor

The surety is discharged by any contract between the creditor and the principal debtor, by which the principal debtor is released, or by any act or omission of the creditor, the legal consequence of which is the discharge of the principal debtor (Sec. 134).

Forbearance to Sue

Mere forbearance on the part of the creditor to sue the principal debtor or to enforce any other remedy against him, does not discharge the surety unless the parties had agreed for such discharge.

Release of One Co-surety Does Not Discharge Others

Where there are co-sureties, a release by the creditor of one of them does not discharge the others. Also, the surety released does not become free from his responsibility to the other sureties.

Surety Can Claim His Dues from The Principal Debtor

- ❖ Once the surety makes the payment or performs the act which the principal debtor has failed to pay/ perform, the surety steps into the shoes of the creditor and he can claim his dues from the principal debtor.
- ❖ Subrogation is the right of the surety to recover his money from the principal debtor (PD) on settlement of the liabilities of PD with the creditor. Subrogation is the legal doctrine whereby one person takes over the rights or remedies of a creditor against his/her debtor.

Security

- ❖ A surety is entitled to the benefit of every security which the creditor has against the principal debtor at the time when the contract of surety-ship is made, whether the surety knows of the existence of such security or not.
- ❖ If the creditor loses such security, then the surety is discharged to the extent of the value of the security.

Misrepresentation Made By The Creditor

- ❖ Any guarantee obtained by means of misrepresentation made by the creditor is invalid. Any guarantee which the creditor has obtained by keeping silent as to the material circumstance, is also invalid.
- ❖ Implied Promise By The Principal Debtor To Indemnify The Surety
- ❖ In every Contract of Guarantee there is an implied promise by the principal debtor to indemnify the surety. The surety is entitled to recover from the principal debtor whatever sum he has rightfully paid under the guarantee (but no sums which he has paid wrongfully) (Sec. 145).

Co-sureties for the Same Debt

Where two or more persons are co-sureties for the same debt or duty, either jointly or severally, and whether under the same or different contracts, and whether with or without the knowledge of each other, the co-sureties, in the absence of any contract to the contrary, are liable, as between themselves, to pay each an equal share of the whole debt, or of that part of it which remains unpaid by the principal debtor (Sec. 146).

Unit 25D : Contract of Bailment

- ❖ As per Section 148 of the Indian Contracts Act 1872 defines bailment, bailor and bailee. “A bailment” is the delivery of goods by one person to another for some purpose, upon a contract that they shall, when the purpose is accomplished, be returned or otherwise disposed of according to the directions of the person delivering them.
- ❖ The person delivering the goods is called the “bailor”. The person to whom they are delivered is called, the “bailee”.
- ❖ The contract of bailment will specify the time for which the goods will remain with the person taking them. Also, the person who gives the goods can direct the other, either to return the goods after the requisite time has expired or, direct him to dispose of the goods in a particular manner.

Essential Features of Bailment

- ❖ Contract – There must be a contract between the party who delivers the goods i.e. bailor and the party which receives the goods, i.e. bailee, which may be express or implied.
- ❖ Delivery of Goods – It is imperative that goods are delivered by one party to another. Delivery may be actual or constructive.
- ❖ Delivery of Possession – Bailment compulsorily involves the delivery of ‘possession’ of goods from bailor to bailee. Possession involves control and intention to exclude others.
- ❖ Purpose – There must be delivery of goods from the bailor to the bailee for some purpose and not by mistake.
- ❖ Return of Specific Goods – In a bailment contract, it is agreed between the bailor and bailee that as soon as the purpose of the contract is achieved, the goods shall be returned or disposed of as per the directions given by the bailor.
- ❖ No Transfer of Ownership- Goods as has been defined in Section 2(7) of the Sales of Goods Act 1930, includes every kind of movable property only excluding money and actionable claims. Bailment is the delivery of goods alone. In a contract of bailment the possession passes from the bailor to the bailee, the ownership does not. Thus in transactions where money is exchanged for something, there is sale and not bailment since ownership passes to the buyer.

Bailor Bound to Disclose to Bailee

The bailor is bound to disclose to the bailee faults in the goods bailed (Sec. 150):

- ❖ Of which the bailor is aware and
- ❖ Which materially interfere with the use of them or
- ❖ Expose the bailee to extraordinary risk

Bailee to Take Care of Goods

- ❖ The bailee is bound to take care of the goods bailed to him as he would do for his own goods. The bailee (in the absence of any special contract) is not responsible for the loss, destruction or deterioration of the thing bailed if he takes such care.

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- ❖ On the other hand, if the bailee does anything different or inconsistent with what was supposed to be done with the goods, the bailor can demand that the bailee must pay the damage suffered as a result of these acts. A contract of Bailment is voidable at the option of the bailor, if the bailee does any act with regard to the goods bailed, inconsistent with the conditions of the bailment.

Rights of Bailee with Regard to Goods

- ❖ The bailor is responsible to the bailee for any loss which the bailee may sustain because of the reason that the bailor was not entitled to make the bailment or to receive back the goods.
- ❖ If the bailor has no title to the goods and the bailee, in good faith delivers them to the bailor or according the directions of the bailor, the bailee is not responsible to the owner in respect of such delivery.
- ❖ If the goods are to be kept or to be carried, or to have work done upon them by the bailee for the bailor, and the bailee is to receive no remuneration, the bailor shall repay to the bailee the necessary expenses incurred by him for the purpose of the bailment.

Bailee's Lien

- ❖ If the bailee has rendered any service involving the exercise of labour or skill in respect of the goods bailed to him, he has a right to retain such goods until he receives due remuneration for the services he has rendered.
 - ❖ Bankers, factors (financiers who purchase receivables and also offer related services), Attorneys of a High Court and policy brokers can, in the absence of a contract to the contrary, retain any goods bailed to them as a security for a general balance of account. Others do not enjoy such right unless there is express contract to that effect.
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Unit 25E : Contract of Pledge

- ❖ As per Section 172 of the Indian Contract Act 1872 “the bailment of goods as security for payment of a debt or performance of a promise is called ‘pledge’.
- ❖ The bailor is in this case called ‘pawnor’. The bailee is called ‘pawnee’.

To constitute a valid pledge, there must be:

- ❖ A contract in relation to an identified chattel to be delivered to the pledgee as security
- ❖ Actual delivery of possession of the identified chattel in pursuance of the contract.

The essential ingredients of a valid pledge are:

- ❖ The property pledged should be actually or constructively delivered to the pawnee; and
- ❖ Pawnee has only a special property in the pledge while the general property remains with the pawnor and wholly reverts to him on discharge of debt.

The major distinction between a pledge and lien is :-

- ❖ In lien there is no power of sale or disposition of the goods whereas in case of pledge there is power to sell on default.
- ❖ In the case of a lien, there is no transfer of any interest; the person exercising the lien has only a right to retain the subject matter of lien until he is paid. A lien disappears the moment the possession is lost and there is no right of sale. While in case of pledge, sale can be made in the event of default. Apledge is assignable.

Nature of Pledge

- ❖ If the pawnor makes default in payment of the debt in respect of which the goods were pledged, the pawnee may bring a suit against the pawnor and retain the goods pledged as a security (or) he may sell the goods pledged, after giving notice of the sale to the pawnor.
- ❖ If the proceeds of such sale are less than the amount due, in respect of the debt, the pawnor is still liable to pay the balance. If the proceeds of the sale are greater than the amount so due, the pawnee shall pay over the surplus to the pawnor.
- ❖ Pledge is a type of bailment. The bailee, while he is in possession of the goods, steps into the shoes of the owner for the purpose of legal remedy. Thus, if any person were to deprive the bailee of the goods – by way of theft, etc. – the bailee, himself, would have the right to file a suit against such other person. If, any damages are received from such a suit, it would be split between the bailor and the bailee, according to the proportion of their losses or damages.
- ❖ The pawnee can retain the goods pledged, not only for payment of the debt/interest on the debt but also for all necessary expenses incurred by him in preservation of the goods pledged. (Section 173)
- ❖ Where person pledges goods in which he has only a limited interest, the pledge is valid to the extent of that interest. (Section 179)

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- ❖ If a third person wrongfully deprives the bailee of the use of possession of goods bailed, or does them any injury, the bailee is entitled to use such remedies as the owner might have used in the like case if no bailment had been made; and either the bailor or the bailee may bring a suit against a third person for such deprivation or injury.

Pledge Without Actual Possession

Sometimes despite a charge of pledge available to a creditor/bank, it allows the custody of the movable property pledged to remain with the debtor for a special purpose. But this does not vitiate the effectiveness of the pledge.

Pledge By Pledgee

- ❖ Where, under certain circumstances, the pledgee further pledges the movable property pledged, the pledge will be valid only to the extent of the interest of the pledgee, which is equivalent to the amount for which the property has been given to him as security.
 - ❖ It has been held in the case, that if the pledgee pledges the goods pledged to him for a larger amount, the original pledger will still be entitled to the goods on paying the amount for which he himself pledged the goods.
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Unit 25F : Contract of Agency

- ❖ A 'Contract of Agency' stems from the need which arises sometimes for a person to employ another person to do an act for him/her or to represent him/her in dealing with third persons.
- ❖ In terms of Section 182 of Indian Contract Act: "An 'agent' is a person employed to do any act for another, or to represent another in dealings with third persons. The person for whom such act is done, or who is so represented, is called the "principal".
- ❖ Contract of agency is created when right is given to a person to represent the principal in dealing with third persons or to do something for the principal.

Essential Characteristics of Contract of Agency

Principal should be Competent to Contract:

- ❖ In terms of Section 183 of the statute "Any person who is of the age of majority according to the law to which he is subject, and who is of sound mind, may employ an agent". Moreover whatever a person can do personally he can do through an agent.

Agent should also be Competent to Contract:

In terms of Section 184 "As between the principal and third persons, any person may become an agent, but no person who is not of the age of majority and of sound mind can become an agent, so as to be responsible to his principal according to the provisions in that behalf herein contained."

Consideration for appointment not Necessary:

- ❖ No consideration is necessary to create an agency. This is provided in Section 185 of the Act. According to Section 185 "No consideration is necessary to create an agency."
- ❖ Authority given to the Agent may be express or implied. An authority is express when it is given by words oral or written and the authority is said to be implied when it is inferred from the circumstances of the case.

Rules of Agency

The two important rules of agency are :

- ❖ The first rule of agency is that whatever a person can do personally can also be achieved through an agent, subject of course to certain exceptions such as when the act to be performed is personal (e.g. marriage) or official.
- ❖ The second rule is that he who does an act through another does it himself. This means the acts of an agent, subject to certain conditions, are acts of the principal. This has also been emphasized by Section 226 of the Act which states "Contracts entered into through an agent, and obligations arising from acts done by an agent, may be enforced in the same manner, and will have the same legal consequences, as if the contracts had been entered into and the acts done by the principal in person".

Types of Agents

There are two ways of classifying an agent

- ❖ On the basis of extent of their authority.
- ❖ On the basis of nature of work performed by them

Classification on the basis of extent of authority

- ❖ **Special Agent:** An agent appointed to perform a particular act for the principal or represent the principal in a particular transaction This agent cannot bind the principal in any other matter than that for which he has been appointed.
- ❖ **General Agent:** A general agent is one who is authorized to do all acts in respect of a particular line of business, trade or employment. Such authority of the agent generally continues until it is terminated. If the principal wants to restrict the authority of a general agent he may do so but has to put persons dealing with the agent to notice regarding the curtailment. If he does not do so the principal becomes bound by the action of the agent.
- ❖ **Universal Agent:** Universal agent is one whose authority to act for the principal is unlimited. He/ she has authority to bind the principal by any act which he/she does, provided the act is legal.

Classification on the basis of nature of work performed

- ❖ **Mercantile or Commercial Agent:** A Mercantile agent as defined in Section 2(9) of the Sale of Goods Act 1930, However the definition does not cover all types of mercantile agents such as Factors, Auctioneer, Broker, Commission Agent and Del Credere Agent who are also mercantile agents.
- ❖ **Banker:** The relationship between a banker and a customer is basically that of a debtor and creditor for most of the transactions.
- ❖ **Non-Mercantile Agent:** These type of agents include solicitors, attorneys, insurance agents, forwarding agents etc.

Duties of Agents

- ❖ To carry out the work undertaken as agent as per the directions given by the principal and in the absence of any special/specific directions, the agent must carry out the work in accordance to the prevailing practices in the line.
- ❖ To carry out the work rationally and with care, skill and diligence.
- ❖ To render proper accounts to the principal on demand and not cause loss due to misappropriation or fraud.
- ❖ To communicate with the principal if he/she faces any difficulty in the discharge of their function and seek instructions.
- ❖ To pay to the principal all sums received for him after deducting therefrom all moneys due to himself from the principal or expenses properly incurred by him as well as any remuneration payable to him for acting as agent. (Section 217)

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- ❖ In terms of Section 215 of the Indian Contract Act, 1872: If an agent, without the knowledge of his principal, deals in the business of the agency on his own account instead of on account of his principal, the principal is entitled to claim from the agent any benefit which may have resulted to him from the transaction.
 - ❖ To protect and preserve the interest of the principal in case of his/her death or insolvency.
 - ❖ Not to use information which may come to his knowledge in the course of his function, as an agent, against the principal.
 - ❖ Not to make undisclosed secret profit from the agency.
 - ❖ An agent must not set up his own title or that of a third party, to the goods that he receives from the principal. If he does he may become liable for conversion.
 - ❖ Not to put himself in a position where interest and duty suffer.
 - ❖ An agent cannot delegate his/her authority and depute another person to do what he has himself undertaken to do. However, sub agent can be appointed in accordance with the provisions contained in the Act.

Rights of Agents

- ❖ In terms of Section 217 of the statute “An agent may retain, out of any sums received on account of the principal in the business of the agency, all moneys due to himself in respect of advances made or expenses properly incurred by him in conducting such business, and also such remuneration as may be payable to him for acting as agent”
- ❖ As per Section 219 “In the absence of any special contract, payment for the performance of any act is not due to the agent until the completion of such act; but an agent may detain moneys received by him on account of goods sold, although the whole of the goods consigned to him for sale may not have been sold, or although the sale may not be actually complete.”
- ❖ In the absence of contract to the contrary, an agent may retain goods, papers etc. whether movable or immovable, belonging to the principal received by him or in his possession until the amount due to him in respect of such goods etc. has been paid or accounted for to him.
- ❖ An agent is indemnified against the consequences of all lawful acts done by him in exercise of the authority conferred upon him. (Section 222)
- ❖ The agent has to be compensated for injuries sustained by him due to neglect or want of skill on the part of the principal.

Duties of Principal

- ❖ To indemnify the agent against the consequences of all lawful acts (section 222).
 - ❖ To indemnify the agent against the consequences of all acts done in good faith (Section 223).
 - ❖ To indemnify the agent for any injury caused by the principal’s neglect (Section 225).
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Unit 26A : Meaning and Essentials of a Contract of Sale

Sale of Goods Act 1930

- ❖ The Sale of Goods Act, 1930, extends to the whole of India.
- ❖ The Sale of Goods Act is specially enacted to lay down the law relating to the sale and purchase of moveable goods in the country. A contract of sale of goods is a contract under which the seller transfers or agrees to transfer the property in goods to the buyer for a price. When the property in the goods is transferred from the seller to the buyer, the contract is called a sale.
- ❖ 'Goods' means every kind of moveable property (other than actionable claims and money) and includes
 - Stock and shares
 - Growing crops, grass
 - Things attached to or forming part of the land which are agreed to be severed before sale or under the contract of sale.

Features of Contract of Sale of Goods

- ❖ Bilateral contract: A sale involves two persons – The buyer and the seller.
- ❖ Money consideration: The consideration for a sale of goods must be money, called the price payable for the transfer of goods.
- ❖ Moveable property: The Sale of Goods Act covers only the sale of moveable goods and not immovable property like land and building. The contracts relating to transfer of immovable property are governed by the Transfer of Property Act
- ❖ No particular form: The Act does not make it mandatory to enter into written contracts for the sale of goods. However, if any particular law provides for sale of certain types of goods to be done by a contract in writing, then that law has to be complied and the contract has to be in writing

The contract may be oral or written or can be implied by the conduct of the parties. A contract of sale is made by an offer to buy or sell goods for a price and the acceptance of such offer.

The contract may provide for:

- ❖ Immediate delivery of the goods on immediate payment of the price.
 - ❖ For the delivery or payment by instalments.
 - ❖ Postponement of delivery or payment.
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Unit 26B : Conditions and Warranties

Meaning of Condition and Warranty

- ❖ Under Section 12(1) of the Sale of Goods Act, “A stipulation in a contract of sale with reference to goods which are the subject thereof may be a condition or a warranty”.
- ❖ Condition: If the stipulation agreed to between the parties is essential to the main purpose of the contract and is of such a nature that if the stipulation is breached (i.e. violated/not complied) then a party to the agreement would have a right to treat the contract as repudiated (cancelled) then such a stipulation is known as a condition.
- ❖ Warranty: It is a stipulation collateral to the main purpose of the contract. The breach of such a stipulation gives rise to a claim for damages only. The parties cannot reject the goods and treat the contract as repudiated.

Implied Conditions and Warranties

Implied conditions and warranties are those, which the law interprets to imply to every contract of sale of goods.

Title of the seller:

There is an implied condition on the part of the seller that,

- ❖ He has a right to sell the goods (in the case of a sale), or
- ❖ He will have a right to sell the goods at the time when the ownership is to pass to the buyer (in the case of an agreement to sell).

Sale of goods by description

In the sale of goods by description, there is an implied condition that the goods shall correspond with the description.

Sale by sample:

In case of a sale by sample there is an implied condition that the:

- ❖ Bulk shall correspond with the sample in quality
- ❖ Buyer shall have an opportunity to compare the bulk with the sample
- ❖ Goods shall be free from any defect, rendering them un-merchantable, which would not be apparent on reasonable examination of the sample.

Sale is by sample as well as by description:

If the sale is by sample as well as by description, the goods must correspond not only to the sample but also to the description given.

Quiet possession:

There is an implied warranty that the buyer shall have and enjoy quiet possession of the goods.

Goods are free from any charge or encumbrance:

There is an implied warranty that the goods shall be free from any charge or encumbrance in favour of any third party not declared or known to the buyer before or at the time when the contract is made.

Quality or fitness of goods for any particular purpose:

There is no implied warranty or condition as to the quality or fitness of goods for any particular purpose except in the following case: If the buyer discloses to the seller the purpose for which he wants the goods and he relies on the seller's skill/judgement and if the goods are in the course of the seller's business to supply, then in such case, there is an implied condition that the goods shall be reasonably fit for such purpose.

Caveat Emptor (Buyer beware)

- ❖ Caveat means a warning, a caution. According to the doctrine of caveat emptor, the person who buys goods must keep his eyes open, his mind active and be cautious while buying the goods. In other words, the buyer must examine the goods thoroughly
 - ❖ Later on, if the goods do not serve his purpose or he depends upon his own judgement and he makes a bad choice, he cannot blame the seller for selling him such goods. The Sale of Goods Act also enshrines doctrine by stating that 'There is no implied warranty or condition as to the quality or fitness of goods for any particular purpose' except in specific cases.
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Unit 26C : Unpaid Seller

The seller of goods is deemed to be an 'unpaid seller' (Sec. 45 of Sale of Goods Act, 1930)

- ❖ When the whole of the price has not been paid or tendered;
- ❖ When the payment for the goods is received in the form of a cheque or other negotiable instrument and the same is dishonoured for financial or other reasons.

Here, the term 'seller' includes any person who is in the position of a seller, e.g., an agent of the seller, to whom the bill of lading has been endorsed, or a consignor or agent who has paid for goods to the seller.

Rights of an Unpaid Seller (Sec. 46)

Unpaid seller's rights against the goods

- ❖ Lien on the goods for the price while he is in possession of them.
- ❖ In case of insolvency of the buyer, a right of stopping the goods in transit after he has parted with the possession of them.
- ❖ A right of resale. If the property in goods has not passed to the buyer, the unpaid seller also has a right of withholding delivery of the goods.
- ❖ If the property in goods has not passed to the buyer, the unpaid seller also has a right of withholding delivery of the goods.

Unpaid seller's lien (Sec. 47)

The unpaid seller of goods (who is in possession of them), is entitled to retain possession of them until payment of the price is made in the following cases:

- ❖ if the goods have been sold without any stipulation as to credit;
- ❖ if the goods have been sold on credit, but the term of credit has expired
- ❖ if the buyer becomes insolvent.

Where an unpaid seller has made part delivery of the goods, he may exercise his right of lien on the balance goods, unless he makes part delivery under circumstances to show that he would waive the right to lien on all goods.

Termination of lien:

The unpaid seller of goods loses his lien thereon:

- ❖ When he delivers the goods to a carrier or other bailee for the purpose of transmission to the buyer without reserving the right of disposal of the goods
- ❖ When the buyer or his agent lawfully obtains possession of the goods
- ❖ By waiver of lien.

Right of stoppage in transit:

When the buyer becomes insolvent, the unpaid seller who has parted with the possession of the goods has the right of stopping them in transit. He may retain them until payment of the price.

Duration of transit:

- ❖ Goods are deemed to be in course of transit from the time when they are delivered to a carrier or other bailee for the purpose of transmission to the buyer and the transit ends, when the buyer or his agent takes delivery of them from such carrier or other bailee.
- ❖ The unpaid seller may exercise his right of stoppage in transit either by taking actual possession of the goods, or by giving notice of his claim to the carrier or other bailee in whose possession the goods are.

Effect of sub-sale or pledge by buyer

- ❖ The unpaid seller's right of lien or stoppage in transit is not affected by a further sale or by other disposition of the goods, which the buyer may have made. Exception to this is when any person in good faith and for consideration takes documents of title to goods from a buyer; or transfer of goods is by way of pledge, where right of unpaid seller may get defeated.
- ❖ If the goods are of a perishable nature, or if the unpaid seller, who has exercised his right of lien or stoppage in transit gives notice to the buyer of his intention to re-sell, the unpaid seller may, if the buyer does not within a reasonable time pay the price, resell the goods.
- ❖ He can also recover from the original buyer, damages for any loss occasioned by his breach of contract. The buyer is not entitled to any profit which may occur on the resale.
- ❖ If the unpaid seller does not give a prior notice of sale to the buyer, then the unpaid seller is not entitled to recover damages from the buyer. On the contrary, the buyer becomes entitled to the profit on a resale.
- ❖ If the unpaid seller who has exercised his right of lien or stoppage in transit re-sells the goods, the, 'new' buyer acquires a good title to the goods as against the original buyer, even if no notice of the resale was given to the original buyer.

Unpaid seller's rights against the buyer personally:

These rights arise out of breach of contract and the seller can file a suit to claim damages, claim the price of goods with interest and he can also repudiate the contract.

Unit 27A : Definition, Meaning and Nature of a Partnership

Partnership Act, 1932

- ❖ The Partnership Act, 1932 lays down the important provisions relating to partnership contracts. However, the general principles of the Contract Act also continue to apply to the partnership contracts.
- ❖ A business can be carried on by a single individual by using his own funds (Sole Proprietorship) or by two or more persons together in which case some of them would bring in money and some of them would use their business skills (Partnership). In the latter type of organization persons agree to share the profits and losses of their venture and it amounts to a contract. The rights and liabilities arising out of such a mode of carrying on business are governed by the Partnership Act.
- ❖ Two partnership firms cannot enter into a partnership though all the partners of two separate firms may join together and form a partnership which would be distinct from the two firms.
- ❖ A Company being a legal person is an entity distinct from its members and is a 'person' as per Section 4. Hence a Company may enter into a contract of partnership if authorized by its Memorandum of Association.

Meaning and Definition of Partnership

Section 4 of the Partnership Act, 1932 defines a partnership, partner, firm and firm- name as follows : "Partnership" is the relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all."

Essential Characteristics

Agreement between two or more persons:

- ❖ At least two persons competent to contract are necessary to form a partnership
- ❖ In terms of Section 5 of the Act, "The relation of partnership arises from contract and not from status". The contract may be express (oral or written) or implied.
- ❖ The agreement may have its own characteristic like being for a fixed period or for a completion of a particular task etc. The partnership being a contract never arises from the operation of law or inheritance. Thus it must have all the characteristics of a valid contract.

Business

It is imperative that a partnership is formed for carrying on some business. Business has been defined in Section 2(b) of the act as "Business" includes every trade, occupation and profession. The term business also conveys some actions involving transactions. However, the business being carried out by the persons forming the partnership must be legal.

Profits

- ❖ It is also necessary that the object of carrying on the business is to make profits, which may be shared amongst the partners in a definite ratio, as agreed.
- ❖ If any person declared as a partner is deprived of a share in the profits, he/she will not be considered as a partner as the motive for carrying on the business, in such an eventuality, is not profit. However, the reverse is not necessarily true as one or more partners may contract out of sharing losses while sharing the profits and it is also possible that all persons sharing profits may not be partners.

Mutual Agency

Since the business of a partnership firm may be carried out by all the partners or any or few of them acting for all, a partner is both an agent and the principal. Agent, because a partner can bind by his acts the firm /other partners, and principal because a partner is bound by the act of any of the other partners. Thus, a contract of partnership is regarded as an extension of the contract of agency.

Types Of Partnership

Partnership at will (Sec. 7):

- ❖ Where no provision is made by a contract between the partners for the duration of their partnership or for the termination of the partnership – the partnership is known as ‘partnership at will’.
- ❖ A partnership at will can be dissolved by any partner by giving notice in writing to all the other partners of his intention to dissolve the firm. The firm gets dissolved from the date mentioned in the notice as the date of dissolution and if no date is mentioned, the/firm gets dissolved from the date of the commencement of the notice.

Partnership for a fixed period:

- ❖ When two or more persons enter into a partnership agreement for a fixed period of time, it is known as a partnership for a fixed term.
- ❖ In such a case, when the fixed period of partnership is over, it comes to an end. However, the partners can continue to carry on the business after the fixed period. In that case, the mutual rights and duties remain absolutely unaffected and the partnership is automatically transformed into a partnership at will.

Particular partnership

Such partnership is entered into, for completing a particular job or assignment taken up by two or more persons jointly and to share the profits arising there from. Hence, a person may become a partner with another person in particular adventures or undertakings.

Limited Liability Partnership (LLP)

- ❖ Limited Liability Partnership Act, 2008 came into effect by way of notification dated 31st March 2009. A LLP is a body corporate and a legal entity separate from its partners.
 - ❖ The mutual rights and duties of the partners of the LLP and those of the LLP shall be is governed by an agreement between the partners, subject to the provisions of the Act.
 - ❖ No partner is liable on account of the independent or unauthorized actions of other partners or their misconduct.
 - ❖ Every partner in a LLP is an agent of the LLP but not of other partners of LLP.
 - ❖ Every LLP has at least two partners and also has at least two individuals as Designated Partners having Designated Partner Identification Number (DPIN), of whom at least one should be resident in India.
 - ❖ The Central Government has powers to investigate the affairs of a LLP, if required, by appointment of competent inspector, for the purpose.
 - ❖ A firm, private company or an unlisted public company is allowed to be converted into a LLP in accordance with the provisions of the act.
 - ❖ Indian Partnership Act, 1932 is not applicable to LLPs unless as expressly provided in the LLP Act.
 - ❖ The winding up of LLP may be either voluntary or by the National Company Law Tribunal (NCLT) under certain circumstances, etc.
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Unit 27B : Relations of Partners to One Another

General Duties of Partners

- ❖ Partners are bound to carry on the business of the firm to the greatest common advantage. The partners are responsible to each other for the conduct of the business of the firm.
- ❖ A partnership is primarily a contract of 'uberrimae fidei' and Section 9 of the Indian Partnership Act, 1932 deals with the duty of a partner in this connection, as 'general duties'.
- ❖ In terms of Section 9 "Partners are bound to carry on the business of the firm to greatest common advantage, to be just and faithful to each other, and to render true accounts and full information of all things affecting the firm to any partner, his heir or legal representative."

Duty to Indemnify the Loss Caused By Fraud

- ❖ According to Section 10 of the Act "Every partner shall indemnify the firm for any loss caused to it by his fraud in the conduct of the business of the firm." This duty to indemnify is an absolute one and no partner can contract himself out of it in the agreement.
- ❖ The innocent partners while being liable to third parties for the fraud of one of the partners can claim damages from that partner who committed the fraud.
- ❖ For example, if a partner commits a fraud upon a customer of the partnership firm for which the firm is held liable then the partnership firm, is entitled to recover from the partner the damages that the firm is required to pay.

Determination of Rights and Duties of Partners

- ❖ Subject to the provisions of this Act Sec. (11), the mutual rights, and duties of the partners of a firm may be determined by contract between the partners, and such contract may be expressed or may be implied by a course of dealing.
- ❖ Notwithstanding anything contained in section 27 of the Indian Contract Act, 1872, contracts between partners may provide that a partner shall not carry on any business other than that of the firm while he is a partner, the agreement becomes an agreement in 'restraint of trade'.

The Conduct of the Business

Section 12 of the Indian Partnership Act sets the rules for conduct of business by partners in a partnership firm.

- ❖ Every partner has a right to take part in the conduct of the business (unless he or she is a sleeping partner)
- ❖ Every partner is bound to attend diligently to his duties in the conduct of the business
- ❖ Any difference arising as to ordinary matters connected with the business can be decided by a majority of the partners and every partner has a right to express his opinion before the matter is decided. However, no change can be made in the nature of the business without the consent of all the partner.
- ❖ Every partner has a right to have access to and to inspect and copy any of the books of the firm.

Mutual Rights and Liabilities

As per Section 13 of the Indian Partnership Act 1932 dealing with mutual rights and liabilities of partners "Subject to a contract between the partners-

- ❖ A partner is not entitled to receive remuneration for taking part in the conduct of the business.
- ❖ The partners are entitled to share equally in the profits earned and liable to contribute equally to the losses made by the firm.
- ❖ Where a partner is entitled to interest on the capital subscribed by him such interest is to be paid only out of profits of the firm.
- ❖ Interest at 6 per cent on extra amount paid by the partner.
- ❖ The firm has to indemnify a partner in respect of payments made and liabilities incurred by him
- ❖ In the ordinary and proper conduct of the business, and
- ❖ In doing such act in an emergency, for the purpose of protecting the firm from loss
- ❖ A partner has to indemnify the firm for any loss caused to it by his willful neglect in the conduct of the business of the firm.

However, the partners are free to have an understanding/ agreement amongst themselves, e.g. all or some of the partners may be allowed remuneration by way of salary in addition to share profits.

The Property of the Firm

- ❖ The property of the firm includes all rights in property originally brought into the firm or later on acquired by the firm for the purpose of business of the firm and includes also the goodwill of the business.
- ❖ Unless the contrary intention appears, the property acquired by the partners from the funds of the partnership business is deemed to be the property of the firm (e.g. the partners had decided to purchase a particular property from the partnership funds and give it to a partner towards his long due remuneration).
- ❖ The property of the firm has to be held and used by the partners exclusively for the purposes of the business. However, the partners can decide the use of the property by mutual consent. (Section 14/15)

Profits Earned by Partners

- ❖ If a partner derives any profit for himself from any transaction of the firm or from the use of the property/ business connection of the firm/ the firm name, he is bound to pay it to the firm.
- ❖ Also, if a partner carries on any business competing with the firm he is bound to pay to the firm all profits made by him in that business. The reason for this is that a partnership is a fiduciary relationship and no partner is entitled to make any personal profit.
- ❖ However on the matters stated hereinbefore, the partners are free to have an understanding other than in the manner stated above. However, if they have no specific understanding on these matters, the above applies to them. (Section 16)

Rights and Duties of Partners

- ❖ After a change in the partners of a firm the mutual rights and duties of the partners in the reconstituted firm remain the same as they were immediately before the change.
 - ❖ Similarly, after the expiry of the term of the firm, if a firm constituted for a fixed term, continues to carry on business, the mutual rights and duties of the partners remain the same as they were before the expiry. Where additional undertakings are carried out where a firm constituted to carry out one or more adventures or undertakings, the mutual rights and duties of the partners in respect of the other adventures or undertakings are the same as those in respect of the original adventures or undertakings.
 - ❖ On the matters stated above, the partners are free to have an understanding other than in the manner stated above. However, if they have no specific understanding on these matters, the above applies to them.
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Unit 27C : Relations of Partners to Third Parties

Partner is an Agent of the Firm

- ❖ Section 18 of the Act implies that a partner is an agent of the firm for the purpose of the business of the firm. A partner can make the firm liable by his acts, if done in the name of the firm and in the ordinary course of business of the firm.
- ❖ However a partner, who contracts in his own name, incurs only a personal liability and the firm is not liable for the contracts entered in to in his personal name.

Implied Authority of Partner as Agent of the Firm

Authority

- ❖ 'Authority' available to a partner in a firm is actually the capacity in which a partner can bind the firm, through his acts. The authority may be express or implied.
- ❖ Where the authority of a partner is conferred on him through an express agreement, it is called express authority. However, on the contrary, where there is no agreement or there is one which is silent about the authority of the partner, then "the act of a partner which is done to carry on, in the usual way, business of the kind, carried on by the firm, binds the firm" and is known to be done under the 'implied authority' of a partner.

Acts Included In Implied Authority

- ❖ Purchasing goods on behalf of the firm
- ❖ Selling goods to the clients of the firm
- ❖ Receiving repayments in respect of the debt of the firm and giving receipts for them
- ❖ Settling accounts with the stakeholders of the firm
- ❖ Engaging servants to help in the business
- ❖ Borrowing money on behalf of the firm.
- ❖ Receiving goods from suppliers to the firm on credit.
- ❖ Drawing, Accepting and endorsing negotiable instruments on behalf of the firm.
- ❖ Pledging goods of the firm as security for borrowed money
- ❖ Employing a solicitor or lawyer to defend an action against the firm in a court of law
- ❖ Submitting a dispute pertaining to the business of the firm for arbitration.
- ❖ Open a banking account on behalf of the firm
- ❖ Compromise or relinquish any claim filed on behalf of the firm
- ❖ Withdraw a suit or proceedings filed on behalf of the firm
- ❖ Admit a liability in a suit or proceedings in a court of law
- ❖ Acquire or dispose or transfer immoveable property on behalf of the firm
- ❖ Enter into partnership on behalf of the firm.

The aforesaid acts can however be carried out by a partner if a partner has express authority to do so from the other partners.

Extension and Restriction of Partner's Implied Authority

- ❖ The partners in a firm may by mutual agreement amongst themselves, extend or restrict the implied authority of any partner.
- ❖ Any act done by a partner on behalf of the firm within his implied authority binds the firm unless the person with whom he is dealing knows the restriction or does not know or believe that partner to be a partner. This has been provided in Section 20.
- ❖ Thus a third party is not affected by a secret restriction of the implied authority of a partner of which he does not know about or has no notice about.

Partner's Authority in an Emergency

Whatever may be the powers given to a particular partner, in case of an emergency, a partner has authority to do all acts to protect the firm from loss, as would be done by a person of ordinary prudence in his own case. The firm is bound by such acts. This has been provided in Section 21.

Mode of Action to Bind Firm

- ❖ In order to bind a firm, the partner must do the activities in the name of the firm and execute the documents on behalf of the firm or in any other manner expressing or implying an intention to bind the firm.
- ❖ A person cannot simply sign an agreement in his own name to purchase goods for the firm and say that since he is the partner in a firm ABC it is implied that the partners are bound to pay for the goods.
- ❖ Every partner is liable jointly with all the other partners and also severally for all acts of the firm done while he is a partner. This is a core principle of partnership business.

Liability of the Firm for Wrongful Acts of a Partner

Sec. 26 of the Act stipulate that if a partner commits some wrongful act or omits doing of something in the ordinary course of the business of the firm with or without the authority of other partners and consequently a loss or injury is caused to any third party, the firm is liable thereof to the same extent as the partner.

Liability of Firm for Misapplication by Partners

Misapplication by a partner is dealt with in Section 27 of the Indian Partnership Act 1932. This section of the statute states "Where :

- ❖ A partner acting within his apparent authority receives money or property from a third party and misapplies it or,
- ❖ A firm in the course of its business receives money or property from a thirty party, and the money or property is misapplied by any of the partners while it is in the custody of the firm, the firm is liable to make good the loss.

Holding Out

- ❖ Sec. 28 of the Act states that anyone who, by words spoken or written or by conduct, represents himself for knowingly permits himself to be represented to be a partner in a firm is as liable as a partner in that firm to anyone who has on the faith of any such representation given credit to the firm whether the person representing himself or represented to be a partner does or does not know that the representation has reached the person so giving credit. This is known as doctrine of holding out.
- ❖ Such a stranger is liable individually and personally for the debts of the firm as if he was a partner in the firm on the principle of holding out. However, legal heirs or estate of the deceased partner is not liable to the firm, who uses his name or when the business of the firm is carried on in the old name of the firm, after his death.

Rights of Transferee of a Partner's Interest

- ❖ A transfer by a partner of his interest in the firm does not entitle the person to whom the interest is transferred (transferee) to interfere in the conduct of the business but entitles the transferee only to receive the share of profits of the transferring partner and the transferee has to accept the account of profits agreed to by the partners.
 - ❖ On dissolution of firm or cessation of the partnership business, the transferee is entitled to a share in assets of the firm and verification of accounts to ascertain his share.
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Unit 27D : Minor Admitted to the Benefit of a Partnership

- ❖ A person who is a minor cannot be a partner in a firm but with the consent of all the partners, he may be admitted to the benefits of partnership (Section 30(1) of the Indian Partnership Act 1932)
- ❖ In no circumstances, the minor can be made a party for the liabilities of the firm, i.e. cannot be personally liable for the acts of the firm except to the extent of such minor's share in the partnership (Section 30(3)).
- ❖ The minor has a right to share the property and profits of the firm as may be agreed upon by the partners and the minor can have access to the accounts of the firm. only the minor's share is liable for the acts of the firm but the minor is not personally liable for the acts of the firm and the liabilities arising from there.
- ❖ The minor may or may not take legal action (by filing suit) against the partners for payment of his share of the property or profits of the firm except when severing (ending) his connection with the firm.
- ❖ This is provided in Section 30(4). As per this section "Such minor may not sue the partners for an account or payment of his share of the property or profits of the firm, when severing his connection with the firm, and in such case the amount of his share shall be determined by a valuation made as far as possible in accordance with the rules contained in section 48"
- ❖ However, all the partners acting together or any partner who is entitled to dissolve the firm by notice to other partners can elect (choose) in such a suit filed by the minor to dissolve the firm. Thereafter, the court proceeds with the suit as a suit for dissolution and for settling accounts between the partners. The share of the minor is then determined along with the shares of the other partners.

Legal Position after the Minor Attains Majority

- ❖ Section 30(5) of the Act stipulates that at any time within six months of his attaining majority, or of his obtaining knowledge that he had been admitted to the benefits of partnership (whichever date is later) the minor partner who has attained majority may give public notice informing whether he has elected to become a partner or not.
- ❖ This notice determines his position as regards the firm. However, if he fails to give such notice, he shall become a partner in the firm on the expiry of the said six months.

Where such a person becomes a partner:

- ❖ His rights and liabilities as a minor continue up to the date on which he becomes a partner but he also becomes personally liable to third parties for all acts of the firm done since he was admitted to the benefits of partnership
- ❖ His share in the property and profits of the firm shall be the share to which he was entitled as a minor.

If such person elects not to become a partner:

- ❖ His rights and liabilities shall continue to be those of a minor up to the date on which he has given public notice that he does not want to become a partner
- ❖ His share shall not be liable for any acts of the firm done after the date of the notice; and
- ❖ He shall be entitled to sue the partners for his share of the property and profits. (Section 30(7))

Retirement of a Partner

A partner may retire:

- ❖ With the consent of all other partners
 - ❖ In accordance with an express agreement by the partners, or
 - ❖ Where the partnership is at will, by giving notice in writing to all the other partners of his intention to retire.
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- ❖ The retiring partner and other partners shall be liable as partners to third parties for any act done by any of them which would have been an act of the firm if done before retirement until the public notice is given of the retirement.
 - ❖ A retiring partner is discharged of his liability to a third party for acts of the firm before his retirement if there is an agreement between the third party, the retiring partner and the remaining partners of the reconstituted firm. (Section 32)

Insolvency of a Partner

- ❖ If partner of a firm is adjudicated as an insolvent, he ceases to be partner from the date on which the order of adjudication is made.
- ❖ An order of adjudication of a partner may or may not dissolve the firm. If the firm is not dissolved pursuant to a contract upon adjudication of a partner, the estate of a partner so adjudicated is not liable for any act of the firm and firm is not liable for any act of the insolvent, done after the date on which the order of adjudication is made.

Unit 27E : Dissolution of a Firm

Dissolution

- ❖ When there is a “Dissolution of a Firm” there would be termination of the firm and end of business relationship among all the partners.
- ❖ When there is a “Dissolution of a Partnership” there is only a change in the business relationship among all the partners and the firm continues to run.
- ❖ ‘Dissolution of a firm’ means that there is a breakdown in the relationship between all the partners in the firm. However where there is a breakdown of relationship or understanding/ faith between a few and not all partners usually allowing the remaining partners to reconstitute the firm, it is called reconstitution (dissolution) of a partnership.

Modes of Dissolution

Dissolution by Agreement:

In terms of Section 40 of the Indian Partnership Act 1932, a firm may be dissolved with the consent of all the partners or in accordance with a contract between the partners.

Compulsory Dissolution:

A firm is dissolved:

- ❖ if all the partners (except one) are adjudicated insolvent; or
- ❖ by the happening of any event which makes it unlawful for the business itself to be carried on or the event makes the business unlawful if it carried on in partnership.
- ❖ However, if the partnership firm is carrying on more than one separate businesses, the illegality of one or more does not cause the dissolution of the firm. The firm can continue to carry on its lawful adventures and undertakings. (Section 41)

Dissolution on the Happening of Certain Contingencies

A firm is also dissolved under the statute (Sec. 42) under certain circumstances. To avoid dissolution in these cases, the partners should have expressly agreed/or should expressly agree that the firm shall not be dissolved in these circumstances

- ❖ if the partnership is constituted for a fixed term, then by the expiry of that term
- ❖ if the partnership is constituted to carry out one or more adventures or undertaking, then by the completion thereof;
- ❖ by the death of a partner; and
- ❖ by the adjudication of a partner as an insolvent.

Dissolution by the Court

Section 44 of the Act states that on the filing of a suit by a partner, the court may dissolve a firm on any of the following grounds:

- ❖ That a partner has become of unsound mind

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- ❖ That a partner has become permanently incapable of performing his duties as partner.
 - ❖ That a partner is guilty of conduct which is likely to affect prejudicially the carrying on of the business
 - ❖ That a partner wilfully or persistently commits breach of agreements in relation to the management of the affairs of the firm or the conduct of its business or it is not reasonably practicable for the other partners to carry on the business in partnership with him because of his conduct with respect to the business
 - ❖ That a partner has transferred the whole of his interest in the firm to a third party,
 - ❖ That the business of the firm cannot be carried on except at a loss
 - ❖ On any other ground which renders it just and equitable that the firm should be dissolved.

Liability for acts of partners done after dissolution

- ❖ Any or all partner of the firm must give a public notice to the effect that the firm is dissolved.
 - ❖ This is because even after the dissolution of a firm, the partners continue to be liable to third parties for any act done by any of them, until such public notice is given. This has been provided in Section 45 of the statute.
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Unit 27F : Effect of Non-Registration

Registration

- ❖ The partners may or may not enter into a partnership deed and may decide to have an oral partnership if they have a strong understanding amongst themselves. Further, even if a partnership deed is entered into by the partners they may not opt for registration of the partnership firm.
- ❖ However, the Partnership Act casts certain disabilities on a partnership firm that is not registered with the Registrar of Partnership Firms. Due to this provision which is stated in the Section 69, a majority of the partnership firms decide to register the firm to avoid future hassles and complexities on solving issues amongst the partners as well as with third parties.

Effect Of Non-registration

The provisions of Sec. 69 states as follows-

- ❖ No suit to enforce a right arising from a contract or conferred by this Act shall be instituted in any Court by or on behalf of any person suing as a partner in a firm against the firm or any person alleged to be or to have been a partner in the firm unless the firm is registered and the person suing is or has been shown in the Register of Firms as a partner in the firm.
- ❖ No suit to enforce a right arising from a contract shall be instituted in any Court by or on behalf of a firm against any third party unless the firm is registered and the persons suing are or have been shown in the Register of Firms as partners in the firm

The provisions of sub-sections (1) and (2) shall apply also to a claim of set-off or other proceeding to enforce a right arising from a contract, but shall not affect :

- ❖ The enforcement of any right to sue for the dissolution of a firm or for accounts of a dissolved firm, or any right or power to realize the property of a dissolved firm, or
- ❖ The powers of an official assignee, receiver or Court under the Presidency-towns Insolvency Act, 1909 (2 of 1909), or the Provincial Insolvency Act, 1920 (5 of 1920), to realize the property of an insolvent partner.

This section shall not apply :

- ❖ To firms or to partners in firms which have no place of business in the territories to which this Act extends, or whose places of business in the said territories are situated in areas to which, by notification under section 56, this Chapter does not apply, or
 - ❖ To any suit or claim of set-off not exceeding one hundred rupees in value which, in the Presidency towns, is not of a kind specified in section 19 of the Presidency Small Cause Courts Act, 1882 (15 of 1882), or, outside the Presidency-towns, is not of a kind specified in the Second Schedule to the Provincial Small Cause Courts Act, 1887 (9 of 1887), or to any proceeding in execution or other proceeding incidental to or arising from any such suit or claim.
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Unit 28A : Definition and Features of a Company

Definition of a Company

- ❖ Section 3 of the Companies Act, 1956 defined a company as ‘a company formed and registered under this Act, or an existing company’.
- ❖ An existing company means a company formed and registered under any of the former Companies Acts. Section 2(20) of the new Companies Act, 2013 similarly defines company as “a company incorporated under the Companies act, 2013 or under any previous company law” which also means that those companies that were incorporated under Section 3 of the Companies Act, 1956 or any previous Companies Act.

Features of a Company

Registration:

A company has to be compulsorily registered under the Companies Act, 2013. Companies registered under Companies Act, 1956 need not re-register.

Artificial Legal Person:

- ❖ A company is an artificial legal person which is created by law and can be dissolved by the law alone. It is invisible, intangible and exists only in the eyes of the law. It enjoys many rights of a natural person. A company may enter into contracts in its own name, and it can acquire and dispose of property and can be fined under the provisions of the law for violation of law.
- ❖ A company is not a natural citizen like an individual and courts have held that neither the provisions of the Constitution of India nor the provisions of the Citizenship Act apply to a company.

Independent corporate personality

By incorporation under the Companies Act, 1956/The Companies Act 2013, the company is vested with a corporate personality which is independent of and different from the members who compose it.

Limited liability

Limitation of liability is an advantage of incorporation of a company. Since under company law, the existence of a company is different from its own members and directors and a company has its own existence and is itself the owner of its assets and has its own liabilities, the members of the company are not bound to contribute anything more than the nominal value of the shares held by them and their liability ends there even though there may be creditors who may be claiming much larger sums from the company.

Perpetual succession

An incorporated company never dies unless wound up as per the applicable law. It is a legal entity with perpetual succession.

Separate property

On incorporation the company becomes the owner of its capital and assets. The company is capable of holding property in its own name.

Transfer of shares

The Companies Act, 1956 (now ICA 2013) states that shares or other interest of any member in a company shall be moveable property, transferable in the manner provided by the articles of association. A shareholder may sell his shares in the open market and get back his money without changing the capital of the company.

Common Seal

- ❖ As a company is an artificial legal person, it is not capable of signing documents for itself. It acts through natural persons who are the directors appointed by the shareholders of the company. Any document bearing the common seal of the company is legally binding on the company.
- ❖ As per the amendment to Sec. 46 of the Companies Act, 2013, dealing with issue of share certificates of a Company, the use of common seal has been made optional. All such documents which required affixing the common seal may now instead be signed by two directors or one director and a company secretary of the company.

Corporate veil

- ❖ Although a company is a separate legal entity distinct from shareholders, in reality it is an association of persons who are the beneficial owners of all the corporate property. Hence, it may sometime become necessary to look at the persons who are behind the corporate veil.
- ❖ The corporate veil is said to be lifted or pierced when the Court ignores the separate entity of the company and directly concerns itself with the members or directors of the company. Corporate veil is normally ignored and lifted by the Court when the persons managing the company have indulged in to fraudulent, illegal acts or have siphoned off the funds of the company for their own benefit.

Distinction Between a Company and Partnership

Registration

- Registration of a company is compulsory under the Companies Act, 2013. Registration of a partnership is not compulsory under the Indian Partnership Act, 1932.

Number of members/partners

As provided under Section 3(1)- A company may be formed for any lawful purpose by :

- ❖ Seven or more persons, where the company to be formed is to be a public company;
- ❖ Two or more persons, where the company to be formed is to be a private company;

Minimum number of two persons is required to form a partnership. The maximum number shall not exceed one hundred

- ❖ **Legal status:** A company has a legal existence separate from its own members and is viewed as a separate legal person from its members. A firm does not have a separate legal existence different from its own partners.
 - ❖ **Ownership of property:** The property of the company is owned by the company itself and not its members as the company has a separate legal existence. The property of the firm is owned by the by the firm through its partners as a firm does not have a separate legal existence different from its own partners.
 - ❖ **Management:** The company is managed by a board of directors elected by the shareholders. A partnership is managed by the partners except the dormant and sleeping partners.
 - ❖ **Perpetual existence:** A company has a perpetual existence. A partnership does not have a perpetual existence and may be dissolved on the happening of certain events or otherwise even with the consent of all partners.
 - ❖ **Contracts:** A member/shareholder of the company can contract with the company. A partner cannot contract with his/her own partnership firm.
 - ❖ **Liability:** Except in case of a company with unlimited liability, the liability of the members of the company is limited to their shareholding. The liability of partners in a partnership is unlimited.
 - ❖ **Transfer:** When shares of a company are transferred to someone, he/she i.e. the transferee becomes a member of the company and the consent of all members is not required to become a member. A person can become a partner in a partnership firm with the consent of all the partners.
 - ❖ **Death:** The death of any or all members of the company does not determine (end) the existence of the company. Death of a partner dissolves the partnership unless the partnership deed provides otherwise.
 - ❖ **Agency:** The members of a company are not the agents of each other or of the company. Every partner of a firm is an agent of the firm as well as other partners.
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Unit 28B : Types of Companies

On the basis of incorporation, companies could be of two types namely :

- ❖ Statutory Corporation
- ❖ Companies registered under the Companies Act, 1956/2013

Statutory Company: A statutory company is created or incorporated by a special Act passed by either the Central or the State Legislature. It enjoys powers, rights and privileges as laid down in the Act. Hence, the statutory companies are not required to have Memorandum of Association. Although each statutory company is governed by the provisions of the special Act, the Companies Act, 1956/2013 is also applicable to them in so far as the provisions of the Companies Act, are not inconsistent with the provisions of the special Act

Example: Reserve Bank of India incorporated under the Reserve Bank of India Act, 1934.

Registered under the Companies Act, 1956 and also Companies Act, 2013: Such companies are incorporated and registered under the prevailing Companies Act, e.g. Tata Iron and Steel Company Limited is incorporated and registered under the Companies Act prevailing before the enactment of the Companies Act, 1956, i.e. the Companies Act, 1913 etc. and continue as such.

Classifications of Companies on the Basis of Liability

Where Companies are classified on the basis of liability, they could be :

- ❖ Company limited by shares
- ❖ Company limited by guarantee
- ❖ Company with unlimited liability

Company limited by shares:

- ❖ In such companies there is a provision for 'share capital' divided into a certain number of shares, which forms the source of funds to the Company, and each share has a fixed nominal value also known as the face value which the shareholder is bound to pay either at a the time of allotment or sometimes in instalments.
- ❖ The member is not bound to pay anything more than the fixed amount on the share, whatever may be the liabilities in the books of the Company. In other words, the liability of the members of such a company is limited to the extent of amount unpaid on the shares.

Company Limited by Guarantee

- ❖ Where the liability of the members of the company is limited by the memorandum of association to such an amount as the members undertake to contribute to the assets of the company in the event of the liquidation of the company, the company is known as a company limited by guarantee.

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- ❖ In such a company each member promises to pay a fixed sum of money in case of its winding up. The amount is called the guarantee.
 - ❖ A company limited by guarantee may or may not have a share capital. However, such a company must have articles of association.
 - ❖ If such a company has a equity share capital then each member is required to pay the amount of the fixed share capital, as in the case of a company limited by shares in addition to the guarantee. Thus the liability is restricted to the amount of the share capital plus the amount of guarantee.

Company with Unlimited Liability

- ❖ Where the liability of the members of a company is unlimited it is known as an unlimited company. Every member of such a company is liable without any limit for its debts as in the case of a partnership firm in proportion to his/her interest in the company.
- ❖ If such a company has equity share capital, it may be a public company or private company. An unlimited company must have articles of association and it must state the number of members and the share capital (if any) with which it is proposed to be registered.

Classifications of Companies on the Basis of Public Interest

On the basis of public interest, companies can be classified as under

- Private company
- Public company
- Government company
- Foreign company
- One Person Company
- Small Company

Difference between a Private Company and a Public Company

- ❖ A private company can have only two members and two directors. A public company has to have a minimum of seven members and three directors.
 - ❖ A private company need not obtain a certificate of commencement of business from the Registrar of Companies which a public company has to obtain. A Private Company has to only get the certificate of incorporation.
 - ❖ A private company need not hold a statutory meeting and submit a statutory report to the Registrar of Companies while a public company has to do so.
 - ❖ Certain provisions of the Companies Act, with respect to requirements of appointment and remuneration payable to the directors applicable to a public company are not applicable to a private company.
 - ❖ Certain provisions of the Companies Act, with respect to annual general meetings of a company are not applicable to a private company.
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Unit 28C : Memorandum of Association and Articles of Association

Memorandum of Association

As per Section 4(1) "The memorandum of a company shall state :

- ❖ The name of the company with the last word—Limited in the case of a public limited company, or the last words - Private Limited in the case of a private limited company
- ❖ The State in which the registered office of the company is to be situated
- ❖ The objects for which the company is proposed to be incorporated and any matter considered necessary
- ❖ The liability of members of the company, whether limited or unlimited etc.

It is thus a document of great significance as it embodies the fundamental rules regarding the constitution and scope of activities of a company. The purpose is to enable the creditors and those who deal with the company to know the permitted scope of its activities.

Name Clause

- ❖ A company is a legal person and hence it must have a name to be identified. A company cannot have a name which in the opinion of Central Government is undesirable. A name is undesirable when it is identical with or too nearly resembles the name of another company.
- ❖ If the company is with limited liability the last word of the name should be "limited" and in case of a private company the last words should be "private limited".
- ❖ However, the Central Government has powers to permit by licence a company not to use the words private limited or limited as the case may be, if the company is formed for promotion of arts, commerce, science, religion, charity or any other useful objective and the company intends to apply its income, if any, in promoting its objects and to prohibit the payment of any dividend to its members.

Registered office clause

- ❖ This clause must mention the name of the State in which the registered office of the company is situated. It is to be noted that the address of the registered office is not to be mentioned. Only the name of the State is required to be mentioned.
- ❖ A company shall from the date on which it commences business or within thirty days after the date of incorporation, whichever is earlier, have a registered office to which all the communications and notices may be addressed.
- ❖ Notice of the situation of the registered office and of every change therein is to be given within thirty days after the date of incorporation of the company or after the date of the change as the case may be to the registrar of companies who shall record the same.

Objective clause

- ❖ It should clearly state the objectives for which the company is established (incorporated) and the nature of business it can undertake/carry on.

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- ❖ Choice of the objectives is left with the subscribers to the memorandum of association who incorporate the company. Although the ownership of the corporate capital is vested in the company itself, in reality the capital is contributed by the shareholders. It is therefore very essential that the objectives of the proposed company must be intimated to the shareholders so that they can decide in which business areas they want to invest their money.
 - ❖ A company can have any lawful objectives. This means that a company cannot have objectives to carry on activities prohibited under the law.
 - ❖ The objectives clause, of the memorandum of association of a company are to be classified and stated under two sub-clauses as 'main clause' and 'other objectives'.
 - ❖ The Main Objectives clause must contain the main objectives which are to be pursued by the company immediately on incorporation and objectives which are incidental or ancillary to the attainment of the main objectives of the company. The Other Objectives clause must contain other objectives which are not included in the above clause.

Liability Clause

If the company is to be incorporated with limited liability the liability clause must state that the liability of the members shall be limited by the unpaid amount on shares.

Capital clause

In case of companies having a share capital this clause must state that the amount of share capital which the company will be authorized to raise and the number and the value of shares into which it is divided.

Association or subscription clause

The memorandum of association concludes with a declaration of the subscription that the persons who have subscribed their signatures intend to form themselves into an association in accordance with the Memorandum of Association.

Articles of Association

- ❖ The Articles of Association, is the second important document of a company and is described in Section 5 of the Companies Act 2013.
- ❖ It consists of a set of rules/regulations and bye laws made by the company for internal management of the company and for carrying out the objects of the company embodied in its Memorandum of Association.
- ❖ As per Section 5(5) "Where the articles contain provisions for entrenchment, whether made on formation or by amendment, the company shall give notice to the Registrar of such provisions in such form and manner as may be prescribed"

Effect of Memorandum and Articles

- ❖ As per Section 10 of the Companies Act 2013, Subject to the provisions of this Act, the memorandum and articles shall, when registered, bind the company and the members thereof to the same extent as if they respectively had been signed by the company and by each member, and contained covenants on its and his part to observe all the provisions of the memorandum and of the articles.
- ❖ All monies payable by any member to the company under the memorandum or articles shall be a debt due from him to the company.

Distinction Between MOA and AOA

- ❖ The memorandum of association contains the fundamental activities (objects) for which the company is incorporated. The conditions are introduced for the benefit of the creditors, the shareholders, and the outside public. The articles of association are the internal regulations of the company and they provide the manner in which the company will be managed.
 - ❖ The memorandum of association is a dominant instrument as it states the purposes of the company and the reasons for which it has come into existence. The articles of association are always held to be subordinate to the memorandum of association because the articles of association are merely the internal regulations of the company while the memorandum of association states the objects of the company beyond which the company cannot go. Clauses in the memorandum of association (e.g. change of registered office in another State or the objects clause) can be altered only by a special resolution passed by the company and with the approval of the Central Government. Any terms of the articles of association can be altered by a special resolution and no approvals are required from the Central Government or any other authority.
 - ❖ If a company commits an act in contravention of the memorandum of association (e.g. a company having objects only to manufacture biscuits starts activities of bottling of milk without proper amendments in the objects clause) then the acts done and liabilities arising there from are not binding on the company and the same cannot be ratified by the company. If a company does something in contravention of the provisions of its articles of association, it is only a procedural irregularity and the same can be ratified by the shareholders at a general meeting and thus rectified.
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Unit 28D : Doctrines of Ultra Vires/Constructive Notice/Indoor Management

Doctrine of Ultra Vires

- ❖ The Doctrine of Ultra Vires is a fundamental rule of Company Law. It states that the objects of a company, as specified in its Memorandum of Association, can be departed from only to the extent permitted by the Act.
- ❖ When a company exercises its powers to promote and/or realize any of its objectives stated in the memorandum of association, it is intra vires (i.e. within the powers of) the company. However, any other act of the company which is outside the scope of the objects clause of the memorandum of association is known as ultra vires (i.e. beyond the powers of) the company. The company cannot sue on an ultra vires transaction. Further, it cannot be sued too.

Effects of Ultra Vires Transactions

- ❖ An ultra vires transaction is void ab initio and therefore cannot become intra vires by reason of ratification. No company can be held liable for obligations arising out of such a contract.
- ❖ If lending done by the company is ultra vires then the company is entitled to recover the money from the debtors because the debtors cannot say that the company had no power to lend.
- ❖ If the rendering of a particular service by the company is ultra vires the company is entitled to recover the charges for such services. If the property of the company is delivered to an outsider through an ultra vires act, the company can get back the property if such property can be traced.
- ❖ If the company borrows money from a lender beyond the limits which it is permitted to borrow, such borrowing would be ultra vires and the company may not be held to be liable for the same unless the money has been used for the purposes of the company.
- ❖ However, the lender can trace the assets created out of such borrowing and can proceed against those assets for recovery of the money due to him. This is popularly known as 'Doctrine of Tracing' which is well recognized by Foreign Courts as well as Indian Courts.
- ❖ If a company's money has been spent ultra vires in purchasing any property the company is entitled to the ownership of such a property because that asset though wrongly acquired represents the capital of the company.
- ❖ If a director of a company makes an ultra vires payment, he is personally liable to the company and he can be compelled to refund the money. In the case of deliberate misapplication, criminal action can also be taken for fraud.
- ❖ Directors are the agents of the company. Hence, they must act within the limits of the powers of the company. If they induce (however innocently) an outsider to contract with the company in a matter in which the company does not have power to act, they will be personally liable to such an outsider for his loss provided that the outsider had no knowledge of the fact that the act was ultra vires the company.

Constructive Notice of Memorandum of Association and Articles of Association

- ❖ The memorandum of association and articles of association of a company are registered with the Registrar of Companies at the time of incorporation. As the office of the registrar of companies is a public office, they become public documents. Hence, the act expressly guarantees the right of inspection of these documents to all. It is therefore the duty of every person who deals with a company to inspect its public documents.
- ❖ In other words, he will be presumed to have knowledge of the contents of these documents and to have understood them according to their proper meaning. This kind of presumed notice is known as constructive notice. This is known as the doctrine of constructive notice.

Effect of the Doctrine of Constructive Notice

- ❖ He who deals with the company is deemed to have notice of the public documents whether he has actually seen them or not.
- ❖ A person dealing with the company is not only deemed to have notice but is also presumed to have read those documents and to have understood not only the company's powers but also of its officers.
- ❖ The doctrine of constructive notice is of a negative nature in the sense that it stops a person from contending (arguing) that he had no notice of the contents of the public documents.
- ❖ In companies law the doctrine of constructive notice is a doctrine where all persons dealing with a Company are deemed (or "construed") to have knowledge of the company's articles of association and memorandum of association.

Doctrine of Indoor Management

- ❖ A person who deals with the company is deemed to have read and understood the registered public documents such as the memorandum of association and articles of association, etc., to see that his contract with the company is not inconsistent with them. But he is not bound to inquire into the regularity of the company's internal functioning or the internal management of the company. Hence, if his contract is consistent with the public documents, the company is bound by such contract. He will not be affected by any irregularity in the internal management of the company. This is known as the doctrine of indoor management.
- ❖ Doctrine of indoor management protects outsiders dealing with the company.

Exceptions to Doctrine of Indoor Management

- ❖ Knowledge of internal irregularity: Where a person dealing with the company has actual knowledge of the internal irregularity of the company he is not entitled to claim protection of this doctrine because he could have taken measures For self-protection.
 - ❖ Acts outside apparent authority of an officer of company: Finally, if an officer of the company makes a contract with an outsider and if the act of the officer falls outside the apparent authority of an officer, then the company is not bound by such a contract.
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Unit 28E : Membership of Company

Member of a Company

According to Section 2 (55) of the Companies Act, 2013, the term member of a company means:

- ❖ The subscriber to the memorandum of the company who shall be deemed to have agreed to become member of the company and on its registration shall be entered as member in its register of members
- ❖ Every other person who agrees in writing to become a member of a company and whose name is entered in its register of members
- ❖ Every person holding shares of the company and whose name is entered as beneficial owner in the records of the depository.

Various Modes of Becoming a Member of a Company

- ❖ By Subscribing to Memorandum of Association: The Companies Act, 1956 and The Companies Act, 2013 provides that a subscriber of the memorandum of association shall be deemed to have agreed to become a member of the company.
- ❖ Membership by Allotment of Shares: A person may become a shareholder if he agrees to take shares in the company by allotment.
- ❖ Transfer of Shares: If a person buys shares of a company in the open market and then applies to the company to register him as a member, he becomes a member on registration of his name
- ❖ Transmission of Shares: On a death of a member, if the member has not made a nomination for the shares then the surviving joint holder (if any) or his legal representatives have the right to register themselves as members.
- ❖ Membership by Acquiescence: A person is deemed to become a member of a company if he allows his name to be put on the register of the members or otherwise holds himself out as a member even if there is no agreement to become a member.
- ❖ Joint Membership: When two or more persons hold shares in a company in their joint names, it is called a joint membership. In such a case the name of the member appearing first is considered to be the main member for the purpose of sending notices, dividend, etc.
- ❖ Beneficial Owner in the Records of Depository: Every person holding shares of the company and whose name is entered as a beneficial owner in the records of the depository shall be deemed to be a member of the concerned company.

Who can be Members of a Company?

- ❖ Any Person competent to contract: The Companies Act, 1956 (now ICA 2013) has not prescribed any qualifications for acquiring membership of a company. Hence, every person who is competent to contract can become a member of a company. It, therefore, follows that a person who is incapable of entering into a contract cannot be a member.
- ❖ Minor and persons of unsound mind: Under the Indian Contract Act, 1872 minors and persons of unsound mind are incompetent at law to contract. Hence such persons cannot become

members of a company. However, if a minor has by mistake been recorded as a member of the company, the company and the minor have a right to rescind the transaction and remove the name from the register of members. However, if a minor has been allotted shares and his name is entered into the register of members he incurs no liability during minority.

- ❖ Company as a member: As a company is a legal person it can become a member of another company provided it is so authorized by its memorandum of association. A company cannot buy its own shares and become a member of it
- ❖ Partnership firm: Since a partnership firm is not a legal person it cannot buy any shares in its own name and thus become a member of a company. The shares have to be bought only in the name of the individual partners of the partnership firm even though such shares constitute a part of the assets of the partnership firm.
- ❖ Registered society: A society registered under the Societies Registration Act, 1860 can hold shares in a company
- ❖ Non-residents: A non-resident cannot become a member of a company without complying with the requirements of the Foreign Exchange Management Act, 1999.
- ❖ Fictitious Persons: The Companies Act provides that any person who: (i) makes in a fictitious name an application to a company for acquiring or subscribing shares therein, or (ii) otherwise induces a company to allot, or register any transfer of shares to him or any other person in a fictitious name, shall be punishable with imprisonment for a term which may extend to five years.
- ❖ Limited Liability Partnership: A LLP, being an incorporated body under the statute, can become a member of a company.
- ❖ Insolvent Person: An insolvent person may remain a member of a company as long as he is on the register of members. He is entitled to vote, but he loses all beneficial interest in the shares and company will pay dividend on his shares to the Official Assignee or Receiver.

Cessation of Membership in a Company

- ❖ If a member transfers his shares to another person.
- ❖ If a member's shares are forfeited.
- ❖ If the shares are sold pursuant to a decree of a Court.
- ❖ If the member surrenders his shares to the company where such surrender is permitted.
- ❖ If he rescinds the contract to take the shares, e.g. on the ground of misrepresentation in the prospectus.
- ❖ If a member is adjudicated insolvent
- ❖ On the death of a member
- ❖ If redeemable preference shares are redeemed.
- ❖ If the company is being wound up.

Register of Members

In terms of Section 88 of the Companies Act 2013

Every company shall keep and maintain the following registers

- ❖ Register of members indicating separately for each class of equity and preference shares held by each member residing in or outside India
- ❖ Register of debenture-holders
- ❖ Register of any other security holders.
- ❖ Every register maintained under sub-section (1) shall include an index of the names included therein.
- ❖ The register and index of beneficial owners maintained by a depository under section 11 of the Depositories Act, 1996, shall be deemed to be the corresponding register and index for the purposes of this Act.
- ❖ A company may, if so authorized by its articles, keep in any country outside India, in such manner as may be prescribed, a part of the register referred to in sub-section (1), called "foreign register" containing the names and particulars of the members, debenture-holders, other security holders or beneficial owners residing outside India.
- ❖ If a company does not maintain a register of members or debenture-holders or other security holders or fails to maintain them in accordance with the provisions of sub-section (1) or sub-section (2), the company shall be liable to a penalty of three lakh rupees and every officer of the company who is in default shall be liable to a penalty of fifty thousand rupees.

The Companies Act provides that every company shall keep a register of its members and enter following particulars:

- ❖ The name and address, and the occupation, if any, of each member
- ❖ In the case of a company having a share capital, the shares held by each member
- ❖ The date at which each person was entered in the register as a member
- ❖ The date at which any person ceased to be a member.

A company may, after giving not less than seven days previous notice by advertisement in some newspaper circulating in the district in which the registered office of the company is situated, close the register of members or the register of debenture holders for any period not exceeding in the aggregate forty-five days in each year.

Place of Keeping and Inspection of Register of Members

The register of members is to be kept at the registered office of the company. It may be kept at any other place within the city, town or village in which the registered office is situated, if:

- ❖ Such other place has been approved for this purpose by a special resolution passed by the company in general meeting and
- ❖ The Registrar of Companies has been given in advance a copy of the proposed special resolution.
- ❖ The registers are to be open during business hours to the inspection of any member or debenture holder without fee. Any other person has to pay a fee.

The liability of a member of a company depends upon the nature of the company.

- ❖ Unlimited Liability Company: The member is liable in full for all the debts of the company contracted during the period of his membership.
- ❖ Company Limited by Guarantee: The member is liable to contribute a sum of money agreed and specified in the liability clause of memorandum of association in the event of being wound up.
- ❖ Company Limited by Shares: The member is liable to pay the full nominal value of the shares and the liability of the member ends there. However, if the member has paid only a part of the amount of the shares then his liability is limited to the unpaid amount on the shares in respect of which he is a member.

Rights of Members

Statutory Rights:

These are the rights conferred by the Companies Act. These rights cannot be taken away or modified by the memorandum of association or the articles of association.

- ❖ Priority to have new shares offered, in case the company proposes to increase capital.
- ❖ To receive notice of meetings, attend and vote at meetings.
- ❖ Transfer shares
- ❖ Receive copies of annual accounts of the company.
- ❖ To inspect the register of members, register of debenture holders and copies of annual returns.
- ❖ To apply to National Company Law Tribunal (NCLT), for calling an annual general meeting if the board of directors fails to call such a meeting.
- ❖ To convene an extraordinary general meeting of the company.
- ❖ Appoint the directors and auditors at the general meetings of the company.
- ❖ To approach the NCLT to order an investigation into the affairs of the company.

Documentary Rights

These rights are conferred upon the members by the memorandum of association and the articles of association of the company.

Proprietary Rights:

- ❖ To be registered as a member in the company's register of members.
- ❖ No personal liability of a company's debts.
- ❖ To receive dividends (if declared by the board of directors and approved by the members at AGM).
- ❖ To participate in the distribution of assets in case of liquidation of the company.

Unit 28F : Prospectus

The Companies Act, 2013 {Sec. 2(70)} defines a prospectus as any document described or issued as a prospectus and includes a red herring prospectus (Sec. 32) or shelf prospectus (Sec. 31) or any notice, circular, advertisement or other document inviting offers from the public for subscription or purchase of any securities of a body corporate.

Red herring prospectus

Means a prospectus which does not include complete particulars of the quantum or price of the securities included therein. Shelf prospectus means a prospectus in which the securities or class of securities included therein are issued for subscription in one or more issues over a certain period without the issue of a further prospectus.

In the following cases, even though shares are offered to the public, issue of prospectus is not required:

- ❖ When a person is invited to enter into an underwriting agreement/arrangement to purchase/subscribe the shares.
- ❖ When the shares are offered only to the existing shareholders or debenture-holders of the company.
- ❖ When the shares or debentures offered are, in all respects, uniform with the shares or debentures previously issued and listed on a recognized stock exchange.

Compliance with Respect to Prospectus

- ❖ Time of issue of Prospectus: A prospectus can be issued only after the incorporation of the company.
- ❖ Contents of the Prospectus: Section 26 of the Companies Act, 2013 stipulates the mandatory provisions that are to be stated in the prospectus.
- ❖ Date of publication: It is stated that a prospectus must be dated and this ensures a prima facie evidence of the date of its publication.
- ❖ Signature of every director on the Prospectus: A prospectus must be signed by every person mentioned therein as a director or proposed to be a director.
- ❖ Application form with a Prospectus: Every application form for shares must be accompanied by a copy of the prospectus except for the application forms issued to underwriters and existing shareholders and debenture holders.
- ❖ Statements by Expert in Prospectus: A prospectus, including a statement purporting to be made by an expert, cannot be issued unless he has given his written consent to the issue thereof and he has not withdrawn such consent before the delivery of a copy of the prospectus for registration to the Registrar of Companies
- ❖ Registration of the Prospectus: Before the issue of a prospectus the same must be delivered to the Registrar of Companies for registration with the documents. No prospectus shall be valid if it

is issued more than ninety days after the date on which a copy thereof is delivered to the Registrar.

Misstatements in a Prospectus and Remedies

A person who has been induced to subscribe for shares or debentures on the faith of a statement in a prospectus which is untrue has a twofold remedy:

- ❖ Remedy against the company
- ❖ Remedy against the promoters and experts who were responsible for the issue of the prospectus. The liability can be civil or criminal.

Civil Liability

Remedies against the Company: If there are untrue statements or misstatements or omissions in a prospectus which have induced any shareholder or debenture holder to buy shares or debentures respectively, the person has two fold remedies:

- ❖ Rescind the contract
- ❖ Claim damages from the company whether the statement is a fraudulent one or innocent one.
- ❖ Claim remedies against the promoters and experts: who were responsible for or associated with the issue of the prospectus. A suit for damages can be filed for misstatements in the prospectus

Criminal Liability

- ❖ It is required that certain matters and reports must be stated in the prospectus. Failure to do so will render the director or any other person responsible for the issue of such prospectus to be punished with fine.
 - ❖ Section 34 provides that if prospectus contains an untrue statement, every person who is responsible for the untrue statement in the prospectus shall be punishable with a fine or imprisonment or with both.
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Unit 28G : Directors

Introduction

- ❖ The board of directors control the day-to-day working and management of the company as well as the long-term strategic planning of the company.
- ❖ No body corporate, association or firm can be appointed as director of a company, and only an individual can be appointed

Minimum Number of Directors

As per Sec. 149 of ICA, 2013 every company must have:

- ❖ A minimum number of three directors in the case of a public company, two directors in the case of a private company, and one director in the case of a One Person Company; and
- ❖ A maximum of fifteen directors
- ❖ Provided that a company may appoint more than fifteen directors after passing a special resolution: Provided further that such class or classes of companies as may be prescribed, shall have at least one-woman director.

Every company shall have at least one director who has stayed in India for a total period of not less than one hundred and eighty-two days in the previous calendar year.

Independent Director

Every listed public company shall have at least one-third of the total number of directors as independent directors and the Central Government may prescribe the minimum number of independent directors in case of any class or classes of public companies.

'Independent director' has been elaborately defined in Section 149 as "An independent director in relation to a company, means a director other than managing director or a whole-time director or a nominee director, :

- ❖ Who, in the opinion of the Board, is a person of integrity and possesses relevant expertise and experience
- ❖ Who is or was not a promoter of the company or its holding, subsidiary or associate company; and who is not related to promoters or directors in the company, its holding, subsidiary or associate company
- ❖ Who has or had no pecuniary relationship, other than remuneration as such director or having transaction not exceeding ten per cent. of his total income or such amount as may be prescribed, with the company, during the two immediately preceding financial years or during the current financial year.

None of whose relatives :

- ❖ Is holding any security of or interest in the company, its holding, subsidiary or associate company during the two immediately preceding financial years or during the current financial year: Provided that the relative may hold security or interest in the company of face value not

exceeding fifty lakh rupees or two per cent. of the paid-up capital of the company, its holding, subsidiary or associate company or such higher sum as may be prescribed.

- ❖ Is indebted to the company, in excess of such amount as may be prescribed during the two immediately preceding financial years or during the current financial year;
- ❖ Has given a guarantee or provided any security in connection with the indebtedness of any third person to the company, for such amount as may be prescribed during the two immediately preceding financial years or during the current financial year; or
- ❖ Has any other pecuniary transaction or relationship with the company, or its subsidiary, or its holding or associate company amounting to two per cent. or more of its gross turnover or total income singly or in combination with the transactions referred to in sub-clause (i), (ii) or (iii)

Who, neither himself nor any of his relatives-

- ❖ Holds or has held the position of a key managerial personnel or is or has been employee of the company in any of the three financial years immediately preceding the financial year in which he is proposed to be appointed.
- ❖ Is or has been an employee or proprietor or a partner, in any of the three financial years immediately preceding the financial year in which he is proposed to be appointed,
- ❖ Holds together with his relatives two per cent. or more of the total voting power of the company
- ❖ Is a Chief Executive or director, of any non-profit organization that receives twenty-five per cent. or more of its receipts from the company, or that holds two per cent. or more of the total voting power of the company; or
- ❖ Who possesses such other qualifications as may be prescribed

Appointment of Directors and Proportion of those who are to Retire by Rotation

The provisions for appointment of Directors is found in Section 152 of the Companies Act 2013.

- ❖ Where no provision is made in the articles of a company for the appointment of the first director, the subscribers to the memorandum who are individuals shall be deemed to be the first directors of the company until the directors are duly appointed
- ❖ No person shall be appointed as a director of a company unless he has been allotted the Director Identification Number
- ❖ A person appointed as a director shall not act as a director unless he gives his consent to hold the office as director and such consent has been filed with the Registrar within thirty days of his appointment in such manner as may be prescribed
- ❖ Unless the articles provide for the retirement of all directors at every annual general meeting, not less than two-thirds of the total number of directors of a public company shall—
 - Be persons whose period of office is liable to determination by retirement of directors by rotation; and
 - Save as otherwise expressly provided in this Act, be appointed by the company in general meeting.

Right of Persons other than Retiring Directors to Stand for Directorship

- ❖ Every individual intending to be appointed as director of a company shall make an application for allotment of Director Identification Number to the Central Government in such form and manner and along with such fees.
- ❖ The Central Government shall, within one month from the receipt of the application, allot a Director Identification Number to an applicant.
- ❖ Any person is eligible for appointment to the office of director at any general meeting, if not less than fourteen days before the meeting, he himself or some other member intends to propose that person be appointed as a director, gives a signed notice in writing to the company signifying that person's candidature for the office of director along with a deposit of one lakh rupees, which shall be refunded to such person or, as the case may be, to the member, if the person proposed gets elected as a director or gets more than twenty- five per cent. of total valid votes cast either on show of hands or on poll on such resolution.

Additional Director

The board of directors can appoint directors by passing a resolution if such a power exists in the articles. Such directors are known as additional directors and they hold office only up to the date of the next annual general meeting of the company.

Whole-time Director

A "whole-time director" includes a director in the whole-time employment of the company. No company can appoint or re-appoint any person as its managing director, whole-time director or manager for a term exceeding five years at a time: Provided that no re-appointment shall be made earlier than one year before the expiry of his term.

Qualification Shares

A director is required to hold certain shares as qualification shares if such requirement is there in the articles of association of the company. This requirement is not applicable to a private company, unless it is a subsidiary of a public company.

Maximum Number of Directorships

No person, after the commencement of this Act, shall hold office as a director, including any alternate directorship, in more than twenty companies at the same time. Provided that the maximum number of public companies in which a person can be appointed as a director shall not exceed ten. The members of a company may, by special resolution, specify any lesser number of companies in which a director of the company may act as directors.

Vacation of Office by Directors

In terms of Sec. 167 of Indian Companies Act, 2013, the office of a director shall become vacant in case:

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- ❖ He incurs any of the disqualifications as specified in Sec. 164
 - ❖ He absents himself from all the meetings of the Board of Directors held during a period of 12 months with or without seeking leave of absence of the Board
 - ❖ He acts in contravention of the provisions of Sec. 184 relating to entering into contracts or arrangements in which he is directly or indirectly interested
 - ❖ He fails to disclose his interest in any contract or arrangement in which he is directly or indirectly interested, in contravention of the provisions of Sec. 184
 - ❖ He becomes disqualified by an order of a court or the Tribunal
 - ❖ He is convicted by a court of any offence, whether involving moral turpitude or otherwise and sentenced in respect thereof to imprisonment for not less than 6 months.
 - ❖ He is removed in pursuance of the provisions of this Act
 - ❖ He, having been appointed a director by virtue of his holding any office or other employment in the holding, subsidiary or associate company, ceases to hold such office or other employment in that company.

Restrictions on Powers of Board

The board of directors of a public company, or of a private company which is a subsidiary of a public company can exercise the following powers only after a resolution is passed to that effect by the shareholders of the company in general meeting:

- ❖ Dispose of any undertaking of the company
- ❖ Remit or give time for repayment of, any debt due by a director
- ❖ Invest, otherwise than in trust securities, the amount of compensation received by the company in respect of the compulsory acquisition
- ❖ Borrow moneys in excess of aggregate of the paid-up capital of the company and its free reserves
- ❖ Contribute to charitable and other funds not directly relating to the business of the company or the welfare of its employees an amount more than Rs. 50 thousand or five per cent of its average net profits during the three immediately preceding, financial years whichever is greater.

Loan to Director

- ❖ No company shall, directly or indirectly, advance any loan to its Directors or any other person in whom the Director is interested, or give any guarantee or provide any security in connection with a loan taken by the Director or any other person in whom the director is interested.
 - ❖ However, any loan or guarantee given by a company to its wholly owned subsidiary, or a guarantee extended to its subsidiary are exempted provided certain conditions stipulated in Section 186 of the Act are complied.
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Unit 29 : Limited Liability Partnership Act, 2008

Limited Liability Partnership (LLP)

A limited liability partnership firm is a body corporate which has its existence separate from the partners of the firm and has certain characteristics which are similar to that which a company constituted under the Companies Act 2013 has.

These characteristics are available in Section 3 of the LLP Act 2008. As per Section 3

- ❖ A limited liability partnership is a body corporate formed and incorporated under this Act and is a Legal entity separate from that of its partners.
- ❖ A limited liability partnership shall have perpetual succession.
- ❖ Any change in the partners of a limited liability partnership shall not affect the existence, rights or liabilities of the limited liability partnership.

Partner / Designated Partner

According to Section 6

- ❖ Every limited liability partnership shall have at least two partners.
- ❖ If at any time the number of partners of a limited liability partnership is reduced below two and the limited liability partnership carries on business for more than six months while the number is so reduced, the person, who is the only partner of the limited liability partnership during the time that it so carries on business after those six months and has the knowledge of the fact that it is carrying on business with him alone, shall be liable personally for the obligations of the limited liability partnership incurred during that period.

Designated partners' required to be identified in each LLP Firm as per Section 7.

- ❖ Every limited liability partnership shall have at least two designated partners who are individuals and at least one of them shall be a resident in India.
- ❖ If the incorporation document specifies who are to be designated partners, such persons shall be designated partners on incorporation

An individual shall not become a designated partner in any limited liability partnership unless he has given his prior consent to act as such to the limited liability partnership in such form and manner as may be prescribed.

- ❖ Every limited liability partnership shall file with the registrar the particulars of every individual who has given his consent to act as designated partner in such form and manner as may be prescribed within thirty days of his appointment.
- ❖ An individual eligible to be a designated partner shall satisfy such conditions and requirements as may be prescribed.

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- ❖ Every designated partner of a limited liability partnership shall obtain a Designated Partner Identification Number (DPIN) from the Central Government and the provisions of sections 153 to 159 (both inclusive) of the Companies Act, 2013 (18 of 2013)] shall apply.

Liabilities of and Changes in Designated Partners

The responsibilities/ liabilities of the designated Partner have been detailed in Section 8. A designated partner shall be :

- ❖ Responsible for the doing of all acts, matters and things as are required to be done by the limited liability partnership in respect of compliance of the provisions of this Act including filing of any document, return, statement.
- ❖ Liable to all penalties imposed on the limited liability partnership for any contravention of those provisions.

As per Section 9 a limited liability partnership may appoint a designated partner within thirty days of a vacancy arising for any reason.

Incorporation Document

Section 11 states: for a limited liability partnership to be incorporated,

- ❖ Two or more persons associated for carrying on a lawful business with a view to profit shall subscribe their names to an incorporation document
- ❖ The incorporation document shall be filed in such manner and with such fees, as may be prescribed with the Registrar of the State in which the registered office of the limited liability partnership is to be situated.
- ❖ There shall be filed along with the incorporation document, a statement in the prescribed form, made by either an advocate, or a Company Secretary or a Chartered Accountant or a Cost Accountant, who is engaged in the formation of the limited liability partnership

The incorporation document shall :

- ❖ ✓ Be in a form as may be prescribed
- ❖ ✓ State the name of the limited liability partnership
- ❖ ✓ State the proposed business of the limited liability partnership;
- ❖ ✓ State the address of the registered office of the limited liability partnership
- ❖ ✓ State the name and address of each of the persons who are to be partners of the limited liability partnership on incorporation
- ❖ ✓ State the name and address of the persons who are to be designated partners of the limited liability partnership on incorporation

Registration

When the requirements have been complied with, the Registrar shall retain the incorporation document and, unless the requirement has not been complied with, he shall, within a period of fourteen days :

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- ❖ Register the incorporation document
 - ❖ Give a certificate that the limited liability partnership is incorporated by the name specified therein.
 - ❖ The Registrar may accept the statement delivered under section 11 as sufficient evidence that the requirement imposed by clause (a) of that sub-section has been complied with
 - ❖ The certificate issued shall be signed by the Registrar and authenticated by his official seal.
 - ❖ The certificate shall be conclusive evidence that the limited liability partnership is incorporated by the name specified therein

Effect of Registration

As per Section 14 of the statute On registration, a limited liability partnership shall, by its name, be capable of :

- ❖ Suing and being sued
- ❖ Acquiring, owning, holding and developing or disposing of property, whether movable or immovable, tangible or intangible
- ❖ Having a common seal, if it decides to have one; and
- ❖ Doing and suffering such other acts and things as bodies corporate may lawfully do and suffer

Cessation of partnership

As per Section 24

- ❖ A person may cease to be a partner of a limited liability partnership in accordance with an agreement with the other partners or, by giving a notice in writing of not less than thirty days to the other partners of his intention to resign as partner.
 - ❖ A person shall cease to be a partner of a limited liability partnership—
 - On his death or dissolution of the limited liability partnership;
 - If he is declared to be of unsound mind by a competent court;
 - If he has applied to be adjudged as an insolvent or declared as an insolvent.
 - ❖ The cessation of a partner from the limited liability partnership does not by itself discharge the partner from any obligation to the limited liability partnership or to the other partners or to any other person which he incurred while being a partner.
 - ❖ Where a partner of a limited liability partnership ceases to be a partner, the former partner or a person entitled to his share in consequence of the death or insolvency of the former partner, shall be entitled to receive from LLP:-
 - An amount equal to the capital contribution of the former partner actually made to the limited liability partnership
 - His right to share in the accumulated profits of the limited liability partnership, after the deduction of accumulated losses of the limited liability partnership, determined as at the date the former partner ceased to be a partner.
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Unit 30 : Transfer of Property Act, 1882

Sale of Immoveable Property

- ❖ Section 54 of the Transfer of Property Act defines sale as “Sale is a transfer of ownership in exchange for a price paid or promised or part-paid and part- promised”.
- ❖ The sale of tangible immoveable property for a consideration exceeding Rs. 100/- can be made only by a registered instrument.
- ❖ Delivery of tangible immoveable property takes place when the seller places the buyer (or such person as directed by the buyer) in possession of the property.

Mortgage of Immoveable Property

- ❖ A mortgage is the transfer of an interest in specific immoveable property to secure the payment of money given by way of loan or to secure the performance of an engagement which may give rise to a pecuniary (monetary) liability.
- ❖ The transferor is called a mortgagor. The transferee is called a mortgagee. The principal money and interest secured is called the mortgage-money. The instrument (if any) by which the transfer is effected is called a mortgage-deed. (Section 58a)

Simple Mortgage

According to Section 58(b) of the Transfer of Property Act, a simple mortgage is a transaction whereby, ‘without delivering possession of the mortgaged property, the mortgagor binds himself personally to pay the mortgage money and agrees, expressly or impliedly, that in the event of his failing to pay according to his contract, the mortgagee shall have a right to cause the mortgaged property to be sold by a decree of the Court in a suit and the proceeds of the sale to be applied so far as may be necessary in payment of the mortgage money.’

Features of simple mortgage

- ❖ The mortgagor does not deliver possession of the mortgaged property to the mortgagee.
- ❖ The mortgagor binds himself personally to pay the mortgage money.

The mortgagor agrees that in the event of his failing to pay according to his contract, the mortgagee shall have a right to get the mortgaged property sold and recover his dues.

Mortgage by way of conditional sale

As per Section 58(c) of the Transfer of Property Act, a mortgage by way of a conditional sale of the property is a transaction whereby the mortgagor ostensibly sells the mortgaged property on the condition that on default of payment of the mortgage money on a certain date, the sale shall become absolute, or on such payment being made the sale shall become void

Essential features

- ❖ The sale is ostensible and not real.
- ❖ If the money is not repaid on the agreed date, the ostensible sale will become absolute upon the mortgagee applying to the Court and getting a decree in his favour.
- ❖ On such payment being made the sale shall become void, or the buyer (mortgagee) shall transfer the property to the seller (mortgagor).

Usufructuary mortgage

According to Section 58(d) of the Transfer of Property Act, 'a Usufructuary mortgage' is a transaction in which

- ❖ The mortgagor delivers possession or expressly, or by implication binds himself to deliver possession of the mortgaged property to the mortgagee; and
- ❖ Authorises the mortgagee to retain such possession until payment of the mortgage money and
- ❖ To receive the rents and profits accruing from the property and
- ❖ Appropriate the same towards the payment of interest or mortgage-money or both.

English mortgage

Where the mortgagor binds himself to repay the mortgage money on a certain date, and transfers the mortgaged property absolutely to the mortgagee, but subject to a proviso that he will re-transfer it to the mortgagor upon payment of the mortgage money as agreed, the transaction is called an English mortgage. (Section 58e)

Essential features

- ❖ The mortgagor binds himself to repay the mortgage-money on a certain date, and transfers the mortgaged property absolutely to the mortgagee.
- ❖ Subject to a condition that he will re-transfer it to the mortgagor upon payment of the mortgage money.

Equitable mortgage

As per Section 58 (f) of the statute, where a person in any of the following towns, namely, the towns of Calcutta, Madras and Bombay and in any other town which the State Government concerned may by notification in the Official Gazette, specify in this behalf, delivers to a creditor or his agent documents of title to immovable property, with intent to create a security thereon, the transaction is called a mortgage by deposit of title deeds.

Essentials

- ❖ The mortgagor delivers to a creditor or his agent documents of title to immovable property.
- ❖ With intent to create a security thereon.

- ❖ The delivery of documents of title is done in the aforesaid towns or a town specified by the State Government.
- ❖ The property given as a mortgage may or may not be situated in the notified town

Anomalous Mortgage

According to Section 58(g) of the Transfer of Property Act, 'a mortgage which is not a simple mortgage, a mortgage by conditional sale and usufructuary mortgage and English mortgage or a mortgage by deposit of title deeds within the meaning of this Section, is called an 'Anomalous Mortgage.

Essential features

- ❖ It must be a mortgage as defined by Section 58 of the Transfer of Property Act.
- ❖ It is negatively defined and should not be anyone of the mortgages listed above.

Anomalous mortgages are usually a combination of two mortgages. Examples of such mortgages are:

- ❖ Simple and usufructuary mortgage, and
- ❖ An usufructuary mortgage accompanied by conditional sale.

Sale without Court Intervention

- ❖ Where the mortgage is an English mortgage, and neither the mortgagor nor the mortgagee is a Hindu, Mohammedan or Buddhist or a member of any other race, sect, tribe or class from time to time specified in this behalf by the State Government, in the official gazette
- ❖ Where a power of sale without the intervention of the Court is expressly conferred on the mortgagee by the mortgage-deed and the mortgagee is the Government
- ❖ Where a power of sale without the intervention of the Court is expressly conferred on the mortgagee by the mortgage-deed and the mortgaged property or any part thereof was, on the date of the execution of the mortgage-deed, situated within the towns of Kolkata, Chennai, Mumbai, or in any other town or area which the State Government may, by notification in the official gazette, specify in this behalf.

Enforcement of Mortgages through Court

After the enactment of the Recovery of Debts due to Banks and Financial Institutions Act, 1993, recovery of debts of Rs. 20 Lakh and above due to banks and financial institutions can be commenced in the Debts Recovery Tribunals. If the banks and financial institutions advance loans/facility below Rs. 20 Lakh, and if they were secured by a mortgage on the borrower's immovable properties, the lender has to file a civil suit for the recovery of his dues by enforcement of the mortgage.

While filing the civil suit the following aspects may have to be kept in view:

- ❖ The suit shall be instituted in the court of the lowest jurisdiction where it can lie.

- ❖ The suit shall be instituted in the jurisdiction of the court where the mortgaged properties are situated.
- ❖ All puisne mortgagees (subsequent mortgagees) shall be impleaded as defendants.
- ❖ If there is more than one mortgage in favour of the lender filing the suit, he shall sue on all debts unless a leave of the court is obtained for filing separate suits
- ❖ If personal covenant of the mortgage is to be enforced, it must be ensured that the claim is within limitation
- ❖ While executing the mortgage decree, the decree holder can bring the properties mortgaged to sale without first seeking an order of attachment from the Court.
- ❖ The lender can also prefer recourse against the mortgaged property under SARFAESI Act for recovery of dues above Rs. 1 lakh irrespective of the type of mortgage.

Leases of Immoveable Property

- ❖ A lease is a transfer of a right to enjoy the property for a certain time (express or implied) or in perpetuity (that is forever), in consideration of a price paid or promised or any other thing of value, to be given periodically to the transferor by the transferee.
- ❖ The transferor is called 'the lessor', the transferee is called the 'lessee', the price is called the premium, and the money or any other thing to be given is called the rent.
- ❖ A sale is an absolute transfer of property. A lease is a partial or limited transfer of property. In a lease, there is a transfer of the right to enjoy such property. Thus, in case of a lease, there is a separation between ownership and possession.

Duration of Certain Leases in Absence of Written Contract

In terms of Section 106 of the Transfer of Property Act 1882, In the absence of a contract or local law or usage to the contrary,

- ❖ A lease of immovable property for agricultural or manufacturing purposes shall be deemed to be a lease from year to year, terminable, on the part of either lessor or lessee, by six months' notice
- ❖ A lease of immovable property for any other purpose shall be deemed to be a lease from month to month, terminable, on the part of either lessor or lessee, by fifteen days' notice.

Actionable Claim

- ❖ Actionable claim' means a claim to any debt (other than a debt secured by mortgage, hypothecation or pledge). Or to any beneficial interest in movable property, not in possession, either actual or constructive, which the Civil Courts recognize as giving reliefs, whether such debt or beneficial interest be existing, accruing, conditional or contingent.
- ❖ The transfer of an actionable claim whether with or without consideration, can be done only by the execution of an instrument in writing signed by the transferor. There is no mandatory requirement of giving notice to the debtor before the transfer of the actionable claim.

Unit 31 : The Right to Information Act, 2005

- ❖ The Right to Information Act, 2005 was enacted with intent to provide for setting out the practical regime of right to information for citizens to secure access to information under the control of public authorities, in order to promote transparency and accountability in the working of every public authority.
- ❖ The Act aims at containing corruption and holding the Governments and their instrumentalities accountable to the governed by providing access to information. The Act also creates a machinery for ensuring effective implementation of the Act.

Applicability

- ❖ In terms of amendment made to the Act with effect from 31-10-2019, It extends to the whole of India.
- ❖ All public sector banks and other institutions owned and controlled by the Government are public authorities and are also required to comply with the provisions of the Act.
- ❖ As per the Act, the public authority has to publish certain particulars about its organization which are
 - Particulars of its organization, functions and duties, powers of its officers and employees
 - Procedure followed in the decision making process, including channels of supervision and accountability
 - Norms set by it for the discharge of its functions
 - Rules, regulations, instructions, manuals and records, held by it or under its control or used by its employees for discharging its functions etc.
- ❖ RTI provides for exemption from disclosure of information including commercial confidence trade secrets, the disclosure of which would harm the competitive position of a third party unless the competent authority is satisfied that larger public interest warrants the disclosure of such information.
- ❖ The Act exempts disclosure of personal information which has no relation to any public activity or interest or which would cause unwarranted invasion of the privacy of the individual.

Definitions

- ❖ 'Central Information Commission' (Section 2b) means the Central Information Commission constituted by the Central Government.
- ❖ 'Central Public Information Officer' (Section 2c) means the Central Public Information Officer designated by the public authority and includes a Central Assistant Public Information Officer.
- ❖ 'Information' (Section 2 f) means any material in any form, including records, documents, memos, e-mails, opinions, advices, press releases, circulars, orders, logbooks, contracts, reports, papers, samples, models, data material held in any electronic form and information relating to any private body which can be accessed by a public authority under any law for the time being in force.

‘Public authority’ (Section 2h) means any authority or body or institution of self-Government established:

- ❖ by or under the Constitution
- ❖ by any other law made by Parliament
- ❖ by any other law made by the State Legislature
- ❖ by notification issued or order made by the appropriate Government

‘Right to information’ (Section 2 j) has been defined in an inclusive manner. It means the right to information accessible under this Act which is held by or under the control of any public authority and includes the right to:

- ❖ Inspection of work, documents, records
- ❖ Taking notes, extracts or certified copies of documents or records
- ❖ Taking certified samples of material
- ❖ Obtaining information in the form of diskettes, floppies, tapes, video cassettes or in any other electronic mode or through printouts where such information is stored in computers or in other device.

‘State Information Commission’ (Section 2k) means the State Information Commission constituted by the State Government under this Act.

Unit 32 : Right to Information and Obligations of Public Authorities

Obligations of Public Authorities

As per Section 4 of The Right to Information Act 2005,

Every public authority shall :

Maintain all its records duly catalogued and indexed in a manner and the form which facilitates the right to information under this Act and ensure that all records that are appropriate to be computerized are, within a reasonable time computerized and connected through a network all over the country on different systems so that access to such records is facilitated

Publish within one hundred and twenty days from the enactment of this Act,

- ❖ The particulars of its organization, functions and duties
- ❖ The powers and duties of its officers and employees
- ❖ The procedure followed in the decision making process, including channels of supervision and accountability
- ❖ The norms set by it for the discharge of its functions
- ❖ The rules, regulations, instructions, manuals and records, held by it or under its control or used by its employees for discharging its functions
- ❖ A statement of the categories of documents that are held by it or under its control
- ❖ The particulars of any arrangement that exists for consultation with, or representation by, the members of the public in relation to the formulation of its policy or implementation
- ❖ A statement of the boards, councils, committees and other bodies consisting of two or more persons
- ❖ A directory of its officers and employees
- ❖ The monthly remuneration received by each of its officers and employees, including the system of compensation
- ❖ The budget allocated to each of its agency,
- ❖ The manner of execution of subsidy programs, including the amounts allocated and the details of beneficiaries
- ❖ Particulars of recipients of concessions, permits or authorizations granted by it
- ❖ Details in respect of the information, available to or held by it, reduced in an electronic form;

Procedure for Obtaining Information

- ❖ PIO shall deal with requests from persons seeking information and If the information requested for is held by or its subject matter is closely connected with the function of another public authority, the PIO shall transfer, within five days, the request to that other public authority and inform the applicant immediately.
- ❖ PIO may seek the assistance of any other officer for the proper discharge of his/her duties.

- ❖ PIO, within thirty days of the receipt of the request, either provide the information on payment of such fee as may be prescribed or reject the request for any of the reasons specified under the Act.
- ❖ Where the information requested for, concerns the life or liberty of a person, the same shall be provided within forty-eight hours of the receipt of the request.

Disposal of Request

If the PIO fails to give a decision on the request within the period specified, he shall be deemed to have refused the request. Where a request has been rejected, the PIO shall communicate to the requester :

- ❖ The reasons for such rejection
- ❖ The period within which an appeal against such rejection may be preferred
- ❖ The particulars of the appellate authority.

The application shall be accompanied by a fee of rupees ten. It may be paid in cash against proper receipt or by demand draft or a banker's cheque or by Indian Postal Order. The instrument is payable to the accounts officer of the public authority.

Appeal

- ❖ The Central Government has the powers to constitute a body known as the Central information commission. The State Governments have the power to constitute for the State a body known as the State Information Commission to administer the provisions of the Act where the State Government is the appropriate authority.
- ❖ Any person who does not receive a decision within the time specified (normally thirty days) or is aggrieved by a decision of the Central Public Information Officer may, within thirty days from the expiry of such period or from the receipt of such decision, prefer an appeal to the officer who is senior in rank to the Central Public Information Officer in each public authority.
- ❖ A second appeal will lie against the decision of the appellate authority before the Central Information Commission (or the State Information Commission) and the same shall have to be preferred within ninety days from the date on which the decision should have been made or was actually received.
- ❖ The appeal shall be disposed of within thirty days of the receipt of the appeal or within such extended time not exceeding a total of forty-five days from the date of filing thereof. The decision of the Central Information Commission is binding on the parties.

Orders in Appeal

In deciding the appeal, the Central Information Commission may pass the following orders:

- ❖ Require the public authority to take any steps necessary to secure compliance with the provisions of this Act including
 - By providing access to information in a particular form
 - By appointing a Central Public Information Officer; etc.

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- ❖ Require the public authority to compensate the complainant for any loss or other detriment suffered
 - ❖ Impose any of the penalties provided under this Act
 - ❖ Reject the appeal.

Penalties

- ❖ The Central Information Commission has the power to impose a penalty of two hundred and fifty rupees for each day till the information is furnished subject to a maximum of twenty-five thousand rupees.
 - ❖ The Commission shall give an opportunity to the parties of being heard before imposing any penalty.
 - ❖ The Commission has the power to recommend taking disciplinary action against the Central Public Information Officer under the service rules applicable to him when he is satisfied that the Central Public Information Officer:
 - Without reasonable cause persistently failed to receive an application for information; or
 - Has not furnished the information within the time specified; or
 - With mala fide intent denied the request for information; or
 - Knowingly given incorrect, incomplete or misleading information; or
 - Destroyed information which was the subject of request; or
 - Obstructed in furnishing the information.
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Unit 33 : Information Technology Act, 2000

Introduction

- ❖ Information Technology Act 2000, was enacted consequent to the adoption of the Model Law on Electronic Commerce adopted by the United Nations Commission on International Trade Law in 1997.
- ❖ This Act aims to provide the legal infrastructure for e-commerce in India which involves the use of alternatives to paper based methods of communication and storage of information and also to facilitate electronic filing of documents of Government agencies.
- ❖ The Information Technology Act, 2000 also aims to provide the legal framework so that legal sanctity is accorded to all electronic records and other activities carried out by electronic means.

Electronic Governance

- ❖ Chapter III of the Act deals with electronic governance and gives legal recognition to electronic records (section 4) and electronic signatures (Section 5) including in Government and its agencies (Section 6).
- ❖ It also provides that information or any other matter shall be in writing or in the typewritten or printed form, notwithstanding anything contained in such law, such requirement shall be deemed to have been satisfied if such information or matter is rendered or made available in an electronic form; and accessible so as to be usable for a subsequent reference.
- ❖ The Chapter also deals with Delivery of Services by Service Providers used for efficient delivery of services in electronic form by the Government (Section 6A) and retention of electronic records (Section 7).

Certifying Authorities

The Act envisages a Controller of Certifying Authorities who shall perform the function of exercising supervision over the activities of certifying authorities as also laying down standards and conditions governing the certifying authorities as also specifying the various forms and content of Digital Signature Certificates.

Section 18 enumerates the functions to be carried out by the Controller-

- ❖ Exercising supervision over the activities of the Certifying Authorities
- ❖ Certifying public keys of the Certifying Authorities
- ❖ Laying down the standards to be maintained by the Certifying Authorities
- ❖ Specifying the qualifications and experience which employees of the Certifying Authority should possess
- ❖ Specifying the conditions subject to which the Certifying Authorities shall conduct their business
- ❖ Specifying the contents of written, printed or visual materials and advertisements that may be distributed or used in respect of a electronic signature Certificate and the public key
- ❖ Specifying the form and content of a electronic signature Certificate and the key

- ❖ Specifying the form and manner in which accounts shall be maintained by the Certifying Authorities
- ❖ Specifying the terms and conditions subject to which auditors may be appointed and the remuneration to be paid to them
- ❖ Facilitating the establishment of any electronic system by a Certifying Authority either solely or jointly with other Certifying Authorities and regulation of such systems
- ❖ Specifying the manner in which the Certifying Authorities shall conduct their dealings with the subscribers
- ❖ Resolving any conflict of interests between the Certifying Authorities and the subscribers
- ❖ Laying down the duties of the Certifying Authorities
- ❖ Maintaining a data base containing the disclosure record of every Certifying Authority containing such particulars as may be specified by regulations, which shall be accessible to public.

Penalties

In terms of Chapter IX – Section 43 of the said Act, “if any person without the permission of the owner or any other person who is in charge of a computer, computer system or computer network:-

- ❖ Accesses or secures access to such computer, computer system or computer network or computer resource
- ❖ Downloads, copies or extracts any data, computer data base or information from such computer including information or data held or stored in any removable storage medium
- ❖ Introduces or causes to be introduced any computer contaminant or computer virus into any computer, computer system or computer network
- ❖ Damages or causes to be damaged any computer, computer system or computer network, data, computer data base or any other programs residing in such computer
- ❖ Disrupts or causes disruption of any computer, computer system or computer network
- ❖ Denies or causes the denial of access to any person authorized to access any computer by any means
- ❖ Provides any assistance to any person to facilitate access to a computer in contravention of the provisions of this Act
- ❖ Charges the services availed of by a person to the account of another person by tampering with or manipulating any computer, computer system, or computer network.
- ❖ Destroys, deletes or alters any information residing in a computer resource or diminishes its value or utility or affects it injuriously by any means
- ❖ Steal, conceal, destroys or alters or causes any person to steal, conceal, destroy or alter any computer source code used for a computer resource with an intention to cause damage, he shall be liable to pay damages by way of compensation to the person so affected. The Act provides for appointment of any officers not below the rank of a director to the Government of India or an equivalent officer who shall adjudicate whether any person has made a contravention of any of the provisions of the Act or rules framed there under. The said adjudicating officer has been given the powers of a Civil Court.

Appeal

- ❖ The Telecom Disputes Settlement and Appellate Tribunal established under section 14 of the Telecom Regulatory Authority of India Act, 1997 shall, be the Appellate Tribunal for the purposes of this Act
- ❖ Any person aggrieved by an order made by controller or an adjudicating officer under this Act may prefer an appeal to a Appellate Tribunal having jurisdiction in the matter.
- ❖ No appeal shall lie to the Appellate Tribunal from an order made by an adjudicating officer with the consent of the parties.
- ❖ Every appeal under sub-section (1) shall be filed within a period of forty-five days from the date on which a copy of the order made by the Controller or the adjudicating officer is received by the person aggrieved and it shall be in such form and be accompanied by such fee as may be prescribed.
- ❖ On receipt of an appeal under sub-section (1), the Appellate Tribunal may, after giving the parties to the appeal, an opportunity of being heard, pass such orders thereon as it thinks fit
- ❖ The Appellate Tribunal shall send a copy of every order made by it to the parties to the appeal and to the concerned Controller or adjudicating officer.
- ❖ The appeal filed before the Appellate Tribunal under sub-section (1) shall be dealt with by it as expeditiously as possible and endeavor shall be made by it to dispose of the appeal finally within six months from the date of receipt of the appeal.

Critical Information Infrastructure – Protected System

- ❖ In accordance with Section 70 of the statute, The appropriate Government may, by notification in the Official Gazette, declare any computer resource which directly or indirectly affects the facility of Critical Information Infrastructure, to be a protected system.
- ❖ The appropriate Government may, by order in writing, authorize the persons who are authorized to access protected systems notified under sub-section (1).
- ❖ Any person who secures access or attempts to secure access to a protected system in contravention of the provisions of this section shall be punished with imprisonment of either description for a term which may extend to ten years and shall also be liable to fine.
- ❖ The Central Government may, by notification published in the Official Gazette, designate any organization of the Government as the national nodal agency in respect of Critical Information Infrastructure Protection.

Application of the Act to Electronic Cheque and Truncated Cheque

- ❖ As per Section 81A of the Act, The provisions of this Act, shall apply to, electronic cheques and the truncated cheques subject to such modifications and amendments as may be necessary for carrying out the purposes of the Negotiable Instruments Act, 1881 by the Central Government, in consultation with the Reserve Bank of India, by notification in the Official Gazette.
- ❖ Every notification made by the Central Government under sub-section (1) shall be laid, as soon as may be after it is made, before each House of Parliament, while it is in session, for a total period

of thirty days, both Houses agree in making any modification in the notification or both Houses agree that the notification should not be made, the notification shall thereafter have effect only in such modified form or be of no effect, as the case may be.

- ❖ The Act (Section 88) also provides for the constitution of the Cyber Regulation Advisory Committee which shall advise the Government as regards any rules or for any other purpose connected with the said Act.

Documents or Transactions to which the Act Shall Not Apply

The First Schedule to the statute enumerates the documents or transactions to which the Act does not apply.

- ❖ A negotiable instrument (other than a cheque) as defined in section 13 of the Negotiable Instruments Act, 1881.
- ❖ A power-of-attorney as defined in section 1A of the Powers-of-Attorney Act, 1882
- ❖ A trust as defined in section 3 of the Indian Trust Act, 1882
- ❖ A will as defined in clause (h) of section 2 of the Indian Succession Act, 1925
- ❖ Any contract for the sale or conveyance of immovable property or any interest in such property.

However the Central Government has vide a notification dated September 26, 2022, amended the aforesaid schedule. The First Schedule has been amended to:

- ❖ Exclude demand promissory notes and bills of exchange issued in favour of or endorsed by an entity regulated by the Reserve Bank of India, National Housing Bank, Securities and Exchange Board of India, Insurance Regulatory and Development Authority of India and Pension Fund Regulatory and Development Authority from the entry relating to negotiable instruments, in addition to cheques which was already excluded from the first schedule.
- ❖ Exclude those powers-of-attorney which empower an entity regulated by the Regulatory Authorities to act for, or on behalf of, and in the name of the person executing them, from the entry relating to a power of attorney.
- ❖ Omit contracts for sale or conveyance of immovable property or any interest in such property.

Unit 34 : The Prevention of Corruption Act, 1988

Introduction

- ❖ The Prevention of Corruption (P C Act) Act was promulgated on the 9th September 1988 mainly to consolidate and amend the law relating to the prevention of corruption and for matters connected therewith.
- ❖ Thus, it is the main statute aiming to curb corruption among public servants and others in the country.
- ❖ The statute was amended in 2013/2018, and more recently on 3rd September 2021. The Government of India, Ministry of Personnel, Public Grievances and Pensions has introduced 'Standard Operating Procedures (SOP)' under Section 17A, for investigating agencies.

Special Judges

Appointment

- ❖ Section 3 of the P.C. Act gives powers to the Central and State Governments to appoint 'Special Judges' to try cases under the statute. It also specifies the offences which may be dealt with by these special judges and the minimum qualifications which are necessary for their appointment.
- ❖ A person shall not be qualified for appointment as a special Judge under this Act unless he is or has been a Sessions Judge or an Additional Sessions Judge or an Assistant Sessions Judge under the Code of Criminal Procedure, 1973 (2 of 1974).

Transfer of Suits

- ❖ A situation sometimes arises where one of the parties in the trial requires it to be transferred to another court in the same or another city or to the High Court.
- ❖ The transfer of a case from a Special Judge to the High court itself was prohibited and not the transfer of a case from one Special Judge to another Special Judge, whether appointed under the Prevention of Corruption Act or any other statute.

Offences And Penalties

Section 7 to 15 of the P.C. Act defines the offences falling under the provisions of the Prevention of Corruption Act and the punishment/fine prescribed thereto.

- ❖ Section 13 of the Act defines 'criminal misconduct'. As per sub-section 2, a public servant who is found guilty of criminal misconduct is punishable with imprisonment for a term which shall be not less than four years but which may extend to ten years and shall also be liable to fine
- ❖ Section 14 of the Act deals with the punishment for a habitual offender, who, is a person convicted initially of an offence under this Act and who subsequently commits another similar offence. Such a person is punishable with imprisonment for a term which shall not be less than five years but which may extend to ten years and shall also be liable to fine.

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- ❖ In terms of Section 15 which deals with punishment for 'attempting' to commit an offence under the Act Whoever attempts to commit an offence referred to in clause (a) of sub-section (1) of section 13 shall be punishable with imprisonment for a term which shall not be less than two years but which may extend to five years and with fine.

Fixing of Fine

- ❖ In Section 16 of the statute, the criteria to be taken in consideration by the court while determining the amount of fine is brought out.
- ❖ According to the section while fixing the fine the court shall take into consideration the amount or the value of the property, if any, which the accused person has obtained by committing or "where the conviction is for an offence referred to in clause (b)] of sub-section (1) of section 13, the pecuniary resources or property referred to in that clause for which the accused person is unable to account satisfactorily."

Persons Authorized to Investigate

As per Section 17 of the Act the persons authorized to investigate have been specified.

The persons so authorized are no police officer below the rank,

- ❖ In the case of the Delhi Special Police Establishment, of an Inspector of Police
- ❖ In the metropolitan areas of Bombay, Calcutta, Madras and Ahmedabad and in any other metropolitan area notified as such under sub-section (1) of section 8 of the Code of Criminal Procedure, 1973, of an Assistant Commissioner of Police
- ❖ Elsewhere, of a Deputy Superintendent of Police or a police officer of equivalent rank.
- ❖ Such persons are permitted to authorize without the order of a Metropolitan Magistrate or a Magistrate of the first class, as the case may be, or make any arrest therefor without a warrant.

Enquiry or Investigation of Offences

- ❖ In terms of Section 17A, which was inserted in the amendment of 2018, specifies the levels at which approval is required to be obtained where enquiry or investigation is to be carried out in respect of offences purported to have been committed by a public servant in discharge of official functions or duties.
- ❖ Provided that no such approval shall be necessary for cases involving arrest of a person on the spot on the charge of accepting or attempting to accept any undue advantage for himself or for any other person.
- ❖ Provided further that the concerned authority shall convey its decision under this section within a period of three months, which may, for reasons to be recorded in writing by such authority, be extended by a further period of one month.
- ❖ On 3rd September 2021, the Ministry of Personnel, Public Grievances and Pensions, Government of India, vide their circular given a set of 'Standard Operating Procedures (SOPs)

with a view to achieving uniform and effective implementation for prior approval processes under section 17A of the statute.

The SOPs provide for

- ❖ Stage wise processing of information received by a Police Officer.
- ❖ Specifying the rank of Police Officer to seek prior approval under Section 17A, in respect of different categories of public servants.
- ❖ Consideration of the proposals under section 17A of the Act by the appropriate Government or Authority.
- ❖ Laying down of Single - Window procedure to specify receipt stage of the proposal and
- ❖ Check list for submitting proposals under Section 17A.

Enquiry or Investigation of Offences

On 3rd September 2021, the Ministry of Personnel, Public Grievances and Pensions, Government of India, vide their circular given a set of 'Standard Operating Procedures (SOPs) with a view to achieving uniform and effective implementation for prior approval processes under section 17A of the statute.

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- ❖ Stage wise processing of information received by a Police Officer.
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- ❖ Check list for submitting proposals under Section 17A.

Powers to Inspect 'Bankers Books'

- ❖ Section 18 of the P.C. Act gives powers to a police officer who has reason to suspect that for the purpose of investigation or inquiry in an offence under Section 17 of the statute, it is necessary to inspect any bankers' books.
- ❖ The Bank so approached, has to provide certified copies of the relevant entries to assist the police officer in the exercise of his powers under this section.
- ❖ However such powers cannot be exercised by a police officer below the rank of Superintendent of Police, unless he is specially authorized in this behalf by a police officer of or above the rank of a Superintendent of Police.
- ❖ Appeal and Revision in judgements of a special judge under the Act normally lies with the High Court as brought out by Section 27

ALL THE VERY BEST FOR YOUR EXAMS

SHORT NOTES FOR CAIIB BANKING REGULATIONS AND BUSINESS LAWS

Though we had taken enough care to go through the notes provided here, we shall not be responsible for any loss or damage, resulting from any action taken on the basis of the contents. Creation of these short notes is the efforts of so many persons. First of all we thank all of them for their valuable contribution. We request everyone to go through the Macmillan book and update yourself with the latest information through RBI website and other authenticated sources. In case you find any incorrect/doubtful information, kindly update us also (along with the source link/reference for the correct information).

Dr. K Murugan, DMS, MBA (Finance), MBA (HR), MCA, MSc (IT), CAIIB
